

Bradley Laddusaw Presents: "The Evolution of the Hard Money Industry"

Private Money Comes Full Circle

ORANGE COUNTY, CA, USA, April 2, 2020 /EINPresswire.com/ -- The goal of this article is not to push any negativity among private lending operations that have started over the past few years. In fact, "mine is one of them". What we want to do is identify and explain how quickly the private/hard money lending industry evolved and why some companies had a firm stop as of last week.

In the [hard money industry](#), the rates that are offered, coupled with leverage are a direct result of "supply and demand" of capital. The active real estate investors that were acquiring distressed assets in 2010/2011 may remember a time when everything was priced comparable. Common structures in California, dependent on leverage, started at 12% interest and 2-3% origination, sometimes higher. During this time there was an abundance of properties and not a lot of free capital available for loans. The main source of capital for [Private Lending firms](#) was from Private Investors looking for a secured return against real estate, or Companies that had their own capital to lend out. Many [brokers](#) had borrower relationships but no capital. Brokers would refer these clients to Private Lending Firms.



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As the market continued to gain traction in 2012 and into 2013, Private Lending Companies heard whispers that "Institutional Money", "Private Equity", and/or "Wall Street" money was making an attempt to enter the marketplace. Who could blame them? At the time, there were really no comparable investments that had as strong of a risk/return profile as a secured, first trust deed against real estate. There was a hurdle they faced, SCALABILITY. Technology and resources did not allow them to deploy the capital they needed.

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From 2014-2016, another shift started to occur as technology began to improve, crowdfunding became more

mainstream, and Fintech started to make an appearance. Companies started to form mortgage pools, or funds, to allow for quicker closings and larger spreads. Online crowdfunding platforms started giving a huge group of retail investors access to loans secured against real estate. Family Offices were coming around to get more comfortable with lending. During this window as technology improved, "Institutional Money" started to make its push into the Hard Money Industry.

This newly available capital was great for the borrower. As access to capital improved, pricing, and leverage reached points that were not previously available. The Private Investors from 2011 and 2012 were now being pushed to compete with these new loan structures that arguably were "too rich for their blood" (ie: too risky). Remember from earlier, rates/leverage/and pricing are based on "supply" and "demand" of capital and there was an extreme "flood" of capital into the market, all while quality deals were becoming scarcer. I remember sitting down with investors in 2016, 2017 & 2018 and walking them through what was occurring. That was not the time to chase yield. Rather, stick to our parameters, even if it meant a reduction in volume. Leverage options were being increased while rates were being driven down. In investing, the term typically goes "More Risk, More Return." In this instance, we were seeing "More Risk, Less Return". The risk/return profile that attracted big money into the industry was being squeezed and this profile was no longer making sense.

In sitting down with investors, we discussed when "Big Money" sees an opportunity for arbitrage, they exploit that market until there is no way to gain an advantage on returns.

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Heading into 2019 there were great loan structures being offered to Fix and Flip investors. Fix and Flip investors were able to capitalize on the opportunities to borrow more money at lower costs than ever before. Correspondent lending programs exploded which helped resolve the scalability issue identified earlier. From a passive investor point of view, these structures did not appear to be sustainable at the pricing being offered. Again, "supply and demand" of capital.

The more money a firm raises over a short period of time, the faster it needs to get it to "work". We witnessed loan structures at 80%-90% LTP and 100% of the rehab. On paper, this netted over 100% of the purchase price. These were being priced anywhere from 1%-2% origination and rates starting in the low 8's%. A Private Lender was actually able to price out a bridge loan with substantially lower leverage, at an equal or slightly higher rate than a Fix and Flip Loan.

What happened?

Covid 19, Stock Market Sell Off, Liquidity dried up, and EXTREME Market Uncertainty.

How quickly can institutional money leave a market?

Overnight. That is what happened last week. Hard Money and Private Lending operations that started over the past few years, backed by this Big Money, put a pause on lending. Not all of them, but a good amount. They are in a wait and see position. In other words, this potentially means, "Wait and Re-Allocate."

What does this mean for Active Real Estate Investors going forward?

This is simply my opinion, but in the short term, pricing and leverage options are going to "revert back to the mean". If you want to call it that. The structures will drift to what was being offered before "Big Money" entered the space and the 85%/100% structure may not make a return. There will be a sticker shock on pricing and leverage, as a majority of the Lending Companies still lending will be pricing risk into their loans. Leverage may be reduced; pricing may increase. There will be liquidity in the marketplace and a majority of this liquidity will be in the form of Private Investors and Companies that have done this dance before.

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