

# 8 TIPS



**TO HELP YOUR**

**DEVELOPMENT**

**BUSINESS**

**SURVIVE THE NEXT**

**RECESSION**

**Community**  
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# EVERYTHING IS

# GREAT UNTIL IT

# ISN'T.

You have cheap financing, you have a lot of buyers and you are selling houses faster than you can build them. Then you start to notice building material costs creeping up, interest rates starting to rise causing higher financing costs that squeeze profits and then buyers stop buying. It seems to come on all of a sudden while we are busy in our own world trying to keep up with the work of our business. The developers that make bets too late into the cycle get wiped out. Others can hold on and take advantage of the downturn to position themselves for the recovery. Here are some tips for how your development company can survive the next recession.

## Know where you are in the Cycle

The general economy follows the natural business cycle of ups and downs. Industries can have distinct cycles of their own that differ from the general economy. These cycles are what cause the boom and bust in real estate and the businesses connected to them. It's important to know where your industry is in its business cycle so you can prepare for what's ahead and not make the wrong investment moves that cost you money. I recommend ITR Economics ([www.itreconomics.com](http://www.itreconomics.com)). The information they provide is like having a superpower to see into the future and will help you gear up for upturns and more importantly better survive downturns.



## Strategy

What business are you really in? Are you a home developer or do you want to be a property manager?

As a developer you keep eye on executing your development schedule, on lowering construction inputs, improving financing, marketing and sales, working with municipal officials

and looking for your next development site. Starting a management arm can be a natural extension but as with any new business it takes your focus off your primary business. If you decide to provide management services can you lay off risk by subbing out some of the work and expense?

## Increase Cash Flow by Reducing Costs

The main cost of a service business is payroll. If you are trying to provide a new management service and take the leap to hire someone to help do some of the work it hits your pocket for a while. Do you feel like you are bringing on a property just to pay for staff as you grow? A person costs more on a monthly basis than you may bring on with 1, 2 or 3 new properties. My wife reminded me that earlier in my management business at the beginning of each year I was optimistic on our prospects for growth and more income but at the end of the year the money was not there. Growth eats cash.

The Institute of Real Estate Management (IREM) provides a report on management company costs says 21% of the expenses go to clerical and accounting personnel.

Robert Seibel, President of Seibel & Katz CPA in Cincinnati says: In order to compete with larger firms, smaller real estate development and property management firms often feel a great deal of pressure to offer their clients a more complete management solution. However, maintaining a modest size in house accounting department generally costs a minimum of \$357,750.

If you can save some portion of that expense you will significantly increase your cash flow. One way to do this is to use a sub-contracted accounting service to do the work. The main benefit is that you only pay for what you use. If you transition a property to board control you lose the corresponding expense if you add a new property you only add an incremental expense. You can use this extra money to improve your business, save money for unexpected expenses or pay yourself more.

## People on Demand

A best practice of construction companies is to have a core staff and then sub out the rest of your personnel needs. This technique helps you ride out the cyclicity of the development business. You can lay off project specific staff after the project is completed to reduce your overhead expense when times get lean. Keeping the majority of your personnel costs variable gives you more flexibility.

## Hold On to Key Staff

Holding on to your core staff during a recession is critical to your long term success. Having to build a team with each economic recovery is costly. One tactic to hold onto your key staff is to have them work on property management tasks during a recession. They are experts at the physical property and can handle maintenance and solve problems for homeowners for

the development. Rather than pay a management company you can pay your development company the fee to survive the downturn.

When I ran my management company during the Great Recession construction supervisors, home builders, architects and realtors were looking for a property management job to survive. Don't let your best people leave.

## Limit Liability

You can have the management function as a division of your development company or you have it be a standalone operation. Developers sometimes can get a bad rap and it may be beneficial to separate the management business to benefit marketing perception as well as a way of reducing liability. One technique could be to take a few key staff that would do the management and make them employees of the new entity. You could do this without any ownership interest and simply have the entity in an employee's name.

## Understanding Saves Time & Money

Have you worked with a management company that didn't understand your development? Did they have poorly educated staff that did things wrong? For example have they made a mess of architectural review items that ended up costing money? Your development staff has a much greater knowledge of your project and can do a job that is less frustrating and saves you time.

## Systems & Processes

If you decide to manage some of your development projects you will have to decide on what systems to use. As you add more properties at some point you will start to have problems and the problems are a sign that you are outgrowing the way you have done the work until now. The systems you use may start off as spreadsheets and paper files. Then you may use Quickbooks to do the accounting but it doesn't provide the best way to track information for unit owners like industry specific software.

If you want to add more properties to help cover some of your personnel costs you will have to go over the hurdle of improving your systems. You may not have the time or interest in becoming a systems expert to investigate and integrate systems – this took up a significant amount of my time and money when growing my business.

You can jump over the systems hurdle without being a systems nerd by using a service that provides the best systems for you. The systems work and you need some training. The benefits of going from old system to a new system that has all latest technology is: 1) it allows for growth, 2) it will streamline this part of your business and free up time, 3) your clients will be happier so you won't deal with complaints and you won't risk losing this revenue stream.

## Conclusion

Growing a development business is exciting, challenging, frustrating and can be very rewarding. You don't have to work at it alone. Books are great mentors. A few terrific business books that I recommend are: "The Rockefeller Habits of Success" by Verne Harnish and "Traction" by Gino Wickman

There are many benefits to subbing out the financial tasks associated with managing a development. You have a few options if you choose this route however, CPAs are too expensive, bookkeepers don't know this specialized area and a local management company may not have the best reputation. As a third party specialist Community Financials doesn't have these issues. To learn more about how Community Financials can help your development business survive schedule a consultation.

