

New Trends In Bidding REOs Are Exciting!

The whole cycle of bidding on Bank Owned properties (REOs) is exciting and very frustrating for many reasons. Mostly the issue is about what the listing agent tells the perspective bidders and what the reality of the market – two very distinct differences.

The prices REOs have been sold at depend on the property's condition, location, willingness of the Asset Manager of the lender to sell the asset, and the bidding frenzy that the listing agent can stir up. This bidding process is often "compromised" by the fact that many wholesalers throw orders in on these REOs as soon as they come on the market with no intention of buying them, just re-selling them to other investors who are also caught up in the newbie frenzy of getting a deal at any cost.

To add insult to injury, rehabbers can pay the listing prices of these REOs when they first come on the market and sell them retail at substantial profits. So these competitive forces, rehabbers and wholesalers, are going head-to-head to get new offerings. The rehabbers are actually competing against themselves because the wholesalers are selling the deals they get to the rehabbers. So the rehabbers have to pay more since the wholesalers know the rehabbers will pay more and the wholesalers do not intend to close if they can't pre-sell the property.

Almost 60% of the time, the original offers on REOs do not close and come back to the market. The reason being that original buyer paid too much to flip the property to another investor or rehabber. This varies greatly because newbies are constantly coming into the market and get starry eyed at the prices based on old market values or what the property traded for a couple of years earlier. None of this matters and the market now is changing almost daily.

The pricing of the final sale is very interesting. Realtors will tell you that every one of their listing sells at or above their asking (listing) price. The reality is that the listing price drops to meet the sales price so only in about 15% of the actual sales are at the first offering price. The actual number of price reductions we see average four and we have seen as many as eleven before the property is sold. So which one of these prices did the realtor sell at full listing price – the first or the last?

How Asset Managers determine what final price they will allow the property to finally sell for is very interesting. In the northern United States we see Asset Managers just dropping the listing price on a regular basis about every ten days for 5% to 6% of the current listing price. So if the property started at \$100,000 the first price adjustment would be to \$94,000, then \$88,360, next \$83,058 and finally \$78,075 (if it sold here) – this assumes a 6% price reduction each time. Homeowners who have had to sell their property in a finite time (i.e., leaving the country and must sell in one month) can advertise they will be dropping the price every other day by \$3,000 until sold. It works very well because it attracts buyers believing they are getting a real bargain. So somewhere in the above chain of dropping listing prices, it is "true" that the property sold for full listing price.

One of our students did a survey of one full year's sales of REOs – approximate a few thousand, and plotted the final sale prices against each property's tax assessed land value ("TAV"). This assumes the value of the structure in the property was worthless. Obviously, this is not the real-life situation on any but a very few of these properties. Ironically, 80+% of the sales fell within 5% of the tax assessed land value. Statistically, this is a no-brainer that "proves" that the tax assessed value is what many of the Asset Managers keyed off. No one will ever admit that in the industry but it is hard to not acknowledge the facts. Check on the next ten properties you see sell and compare them with the TAV of the property. What muddies the waters is that land values (TAVs) have been dropping and investors are becoming more fanatic about getting in on the REO market, so you'll see some deals go way over this standard. This value may change in areas of the country so it should only be considered a guideline as to what the Asset Managers will actually accept.

The conventional method Asset Managers use are BPOs (Broker Price Opinions) that they pay realtors a measly \$35 - \$75 for instead of paying an appraiser \$250 to get a real evaluation. The actual sale price that will be accepted is a closely guarded secret, and it varies as the days on the market ("DOMs") gets longer and longer. Last week we had two of our offers accepted that amounted to a 40% price drop by the Asset Managers in one day.

Just today we had one realtor call and say that the price on a water-front property had been reduced by almost 50%! All we had to do was put in a contract before he listed it at the new price. Sounds like a real deal, right? Well after we sent in a contract the realtor called back and said "other offers had come in and we needed to give our HIGHEST AND BEST OFFER". We did just that and we got back a new response we haven't heard before, "You realize that this will be the only offer you can ever make?" Kind of intimidating, isn't it? This is especially true since the property was an ocean access rehabbed property that was worth three times the asking price.

The next question was, "Why such a bargain for us?" Actually, I suspect 100 other investors were told the same insider info, and when the property's price reduction was posted on the MLS® hundreds more would have been alerted. These MLS® watchers would have thrown in offers and the price would skyrocket – just as the Asset Manger expected. If the price hadn't gone crazy, he would have not taken any offers and relisted it possibly at a higher price than before! This method is yet another method of pricing REOs that takes advantage of investor greed.

Yet another way that deals are priced is what I called ordered chaos. These properties don't sell after many days on the market and the Asset Manager sends them to auction. The threat of sending the property to auction and canceling the agent's listing agreement moves and shakes the listing agent to get it sold. But usually the condition or the price won't allow an easy sale so the property is transferred to an auction house. The auction house attempts to sell the property and, if sold, the deal is done. However, at least 65% of the time the property is sold but doesn't close or isn't sold at all.

The big secret of the auction houses is they recycle the unsold properties at the end of the day. If you are thinking you didn't see anything that didn't sell, you are correct. What you don't know is the buyer may have been a "shill" or fake buyer that tried to drive bids up but couldn't on certain properties. These properties ultimately go back to the lender and are re-listed on the MLS®. The auction house doesn't get paid anything if the property doesn't sell, so if the recycle offer doesn't work, they may ask for "any bid". We have gotten deals for ¼ the original offering price using this inside technique to buy cast-off deals. Ironically, when they go back to the Asset Manager and are re-listed, they often go on at 50% over their original highest listing! They must think investors are really stupid but, unfortunately, sometimes they are right.

In summary, while it's nearly impossible to exactly tell what an REO property will ultimately sell for, our experience has been that most of our offers are accepted after months of letting them sit and waiting out the listing agent and his Asset Manager. Just look at the price history of each property to see what has really been happening with the property and govern yourself accordingly.