

Business Examiner

Canadians
are **HOT**
for a cold American
real estate market

Community Feature ~ Osoyoos

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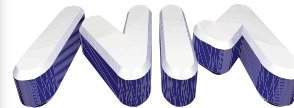
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Cover Feature

crisis of opportunity

By Devon Brooks

The annoying thing about old adages like 'buyer beware' is that they are both true and yet, often of no help to the people who have become statistics...

Two years ago, Dieter Gable a mortgage specialist with Intellichoice or Tom Caldwell of Brewer-Caldwell Property Management Services, both in Phoenix, Arizona could have told local buyers there to beware.

As Caldwell put it, "If you had a pulse, you qualified for a mortgage." Whenever a branch of industry, in this case the banking/mortgage industry stops performing the most elemental safety checks, buyers better beware.

What couldn't be known was just how big the fall would be. In 2006 the Center for Responsible Lending in the U.S. wrote a report predicting that up to 2.2 million borrowers would suffer from sub-prime mortgages to the tune of \$164 billion.

But the Center was wrong, very wrong. It vastly underestimated just how sweeping the influence of the sub-prime crisis would be.

By the end of 2007 John Atlas of the National Housing Institute and professor Peter Dreier at Occidental College wrote that that sub-prime mortgages worth \$1.5 trillion had been sold around the globe.

In 2006 14% of sub-prime mortgages were in

default. By last September approximately 20% of sub-prime mortgages were in default, worth \$300 billion and up to 2.2 million Americans will likely lose their homes.

Most recently doubts have hit Fannie Mae and Freddie Mac, the gargantuan, private but U.S. government backed mortgage brokers for half the nation.

Even the promise of American government backing couldn't stop the shares from taking a huge slide.

Scott Peckford is the president of Mortgage Architects in Kelowna and hosted two seminars on investing in U.S. real estate. He says, "If enough people believe something, whether or not it is true, it affects the market and the market adjusts to reflect that."

Yet Peckford believes the U.S. economy is still fundamentally strong. "I think the U.S. will work through this [sub-prime mortgage]. I think the war thing will be straightened out and it will rebound."

Meanwhile the defaulting debts, ladled out around the globe, have created near panic in the markets. In Canada the heaviest hit company was

PHOTOS BY DEVON BROOKS

The house in this inset photo went for \$3 million but the Arizona Acquisition Fund has a chance to pick it up for \$1.2 million. The other house (pictured above) sold for \$275,000 two years ago, but the AAF just acquired it for \$135,000.

the CIBC, which wrote down more than \$2 billion, after which the company's share price sagged from \$103.64 last year to \$54.35.

Compared to the 80 American mortgage companies, the huge investment house Bear Stearns and banker Indymac that disappeared within six months, the CIBC got off lightly.

Loss equals potential profit

More than 2,000 years ago Roman statesmen, Pliny the Elder wrote, "And the best plan is, as the popular saying was, to profit by the folly of others."

Modern business failures always represent opportunities for others. In Calgary, brothers Ron and Travis Cadman think they have found a vehicle for Canadian investors to have that opportunity.

They propose to buy up 175 properties on the Phoenix market from banks desperate to sell, rent them out for up to five years and sell them for handsome profits when the market comes back. Canadian investors won't buy the properties directly, but instead invest, in units of \$10,000, in a fund that the Cadman company, CBI Group, directs.

In Phoenix, they've partnered with the city's biggest property management firm, Brewer-Caldwell, to find the best properties with strict requirements for, and due diligence on each property.

Peckford gushes, "I think the idea is brilliant. That's my first thought. I wish I'd thought of it. Who knows the timeframe, but for Canadians I think this is the investment

opportunity of a lifetime."

The Arizona market

The Cadmans are real estate developers and investors with 23 years of experience. Looking at the mortgage crisis they realized that the losses would scare off buyers, banks and investors leaving houses under-valued, at least in the short term.

In fact they don't think the blood letting is finished just yet. Ron says, "We think property values may go down another 10%."

At the same time people still need somewhere to live and in a few years the Cadmans believe the market will turn around, because the Arizona economy is sound, it has a warm climate and the cost of living is cheap (and getting cheaper).

Moreover, newspaper hitting headlines like the sub-prime crisis and falling house prices ignore the obvious, which Gable observes, "The majority of people live in their homes and the reality is that even if the house is worth less than the mortgage, it's a footnote. The bank may not sleep as well, but they don't care."

The Cadmans chose Arizona because it is attracting big hi-tech companies like Honeywell and Yahoo, which want to set up enormously expensive complexes in a geologically safe area.

The answer they found was the county of Maricopa, which includes metropolitan Phoenix.

Greater Phoenix had a population of 3.2 million in 2000. The University of Arizona predicts that its

population will go up by an average of 125,000 people a year to 2020 before slowing slightly.

According to Brewer-Caldwell every 2.5 people moving there require a new housing unit of some type.

But to fund the program the Cadmans needed investors who were not scared off by real estate. The answer was the Canadian public who are seeing a levelling off

mortgage problems here."

Economic rationale

The key assumptions that will make this deal fly are the continued rapid growth of the Phoenix population and an eventual recovery of confidence in the economy and, more importantly, the housing market.

Chris Yeung, CBI's vice-president of sales and marketing, asks, "Realistically, will

promoter's corner on this.

The 2008 *Metro Phoenix Relocation Guide* shows that Arizona was the second fastest growing state in the U.S. More than 173,000 people moved there from July 2006 to the end of June 2007.

The 2006 increase was much larger than 2005 or 2007 when it increased by 140,000. Developers however jumped on the building boom and over built.

Caldwell's company saw that coming and got out of the market before it was overbuilt. What no one could see then was that in addition to overbuilding in Phoenix, the sub-prime crunch would also help to kick out the market's underpinnings.

But Caldwell believes the economic correction and the overbuilt market will be worked out of the Phoenix market within five years, but likely much sooner. "I think we'll be slow the rest of this year, but in 2009 my opinion is that we'll have a bit of a bounce [in the real estate market]."

For that reason he believes the best profits will come if the purchases are done very soon. "I don't know how long we have. I'm guessing 12 months maybe."

According to Peckford, whether Caldwell is right or not in his exact timing isn't all that important. He observes, "You can never tell where the bottom is. You might be buying before the bottom in three months, but in three years it won't matter."

What is equally important to the investment scheme is Brewer-Caldwell's accurate assessment of the Phoenix

market. As Gable says, "It requires a lot of due diligence to stay on top of the market."

This is where the Cadmans believe Caldwell-Brewer will give their investment the edge. A tour of properties either purchased or under consideration include one at 9444 W Jamestown Road in Phoenix. (pictured on page 4)

Caldwell says his company once owned and sold this house before in the \$275,000 range. Now it is back on the market for \$135,000 but he feels confident they'll get it for \$130,000. If the deal is completed they feel they'll be able to rent it out for \$1,250 a month. After closing costs, taxes, insurance, management and maintenance, and factoring in costs during vacancies plus mortgage payments they expect to get a cash flow of \$330 to \$360 a month.

The houses are being cherry picked from across the greater Phoenix market, carefully limiting exposure in any one neighbourhood. Ron says, "We only buy up to our quota in an area and then we're done."

The partners are not worried about Canadians going around them and buying up their own properties because individual buyers don't have local market savvy and, as Ron notes, "The lending environment down here is much more difficult."

Peckford says banks will only look at Canadian buyers if they have a down payment worth a minimum of 35% of the purchase price. At the same time, the buying prices that Brewer-Caldwell can extract from the banks is better than a private individual

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Tom Caldwell and Travis Cadman outside of one of the homes they want to purchase and rent in Phoenix before selling for huge profits once the U.S. economy recovers from the sub-prime mortgage crisis.

of real estate prices at high levels, leaving lots of space for leveraging and confidence for more.

Peckford notes, "We don't have the same potential for

all the U.S. housing markets be down for more than five years and will Maricopa county not come back?"

Statistics are solidly in the

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PROFILE 2008



Okanagan Nation Alliance

DOING BUSINESS WITH THE OKANAGAN NATION

Power Play

"The new Kelowna bridge was worth about \$150 million and everyone thought that was a mega-project. Across the member Bands and upcoming projects off-reserve, the Okanagan Nation has over \$3 billion in development projects going through various approval processes. Most business people in the Okanagan have no idea how many billions of dollars of development the Okanagan Nation as a whole has planned." - Geoff Greenwell, Senior Advisor - Business Development Unit of the Okanagan Nation Alliance (ONA).

Just how big a power play the Okanagan Nation's plans will be is just beginning to reach most business people in the Okanagan.

This fall the ONA is running its second, greatly expanded, annual business conference. Last year's was sold out, over-subscribed and an enormous success. This time The Thompson Okanagan Business Examiner will be covering, in depth, the huge range of business connections, opportunities and developments that this conference and the ongoing projects on band lands represent.

The large, special supplement will highlight how local, regional and national companies can effectively create, develop and enhance business opportunities with the Okanagan Nation and its member Bands.

Aside from regular distribution to the Examiner's 68,000 readers, decision makers, CEOs and business executives, a large press run will make sure the supplement will be available to everyone that attends the conference in October. In addition to extra print copies a PDF electronic copy will ensure that the sponsor and advertiser messages will reach fresh audiences over the coming year.

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crisis...

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could obtain because they are purchasing in bulk, in cash, from banks seeing hundreds of foreclosures.

The big picture?

Any investment has some risks, and the question here is whether the bigger picture in the U.S. could derail their plans and cause the Arizona economy to stall, which might delay or prevent the continued expansion of the Maricopa housing market that this deal depends on.

Potential threats include the continuation of the housing-mortgage crisis long term, increasing fuel costs and the wall going up along the Mexican border.

Phoenix, the country's fifth largest city, has very few high rises and virtually no transit system.

It is a city built to glorify the automobile. Suburbs are linked by excellent highways that stretch from one sprawling mini-city to the next, often with large undeveloped areas of raw desert in between.

If fuel costs continue their rapid rise it may slow the economic growth there more than in other, denser cities, but at the same time, it is hard to underestimate the American love affair with the automobile.

A more significant threat is the wall going up across the border to stop illegal Mexican immigrants from coming across.

While main stream Americans are upset about the huge flow of illegal aliens and the potential security issues, Arizona's economy has at least one foot resting on this illegal, and therefore very cheap, labour force.

For the mortgage crisis, Caldwell acknowledges that "Right now people have seen a fall and they're afraid." Neither he, nor the Cadmans believe this situation can last for any length of time and they're not alone.

For Canadian investors the

last possible monkey wrench is the Canadian dollar. Both Caldwell and Peckford believe the Canadian dollar will retreat back toward the 90¢ range. If they are correct it will provide an even richer payout for investors in the Arizona Acquisition Fund.

But that contention is unclear. In early July, CIBC World Markets economist Avery Shenfeld and Global Insight Canada economist Dale Orr stated that the Canadian dollar would inevitably follow the price of commodities, especially oil, to higher plateaux. Such a scenario, over a long period of time would work against returns for Canadian investors.

Summary of the Arizona Acquisition Fund offering

- Objective: raise \$12.5 million
- Sell investors bonds valued at \$10,000 each
- Purchase 175 homes in the greater Phoenix area at below market prices
- Rent out the properties to generate a cash flow for maintenance and carrying costs
- Pay investors 6% per annum
- Sell the properties when the market recovers
- Pay investors 60% of net profits
- In the event of a loss investors original investments are protected

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