The Most Common Ways to Finance a Laundromat

All right, so you have just found the perfect store and you got yourself a signed purchase agreement, Congratulations! But once the euphoria wears off, you get this feeling of, oh my gosh, I need to come up with some money to pay for this business. So what is the best way to do it? Should you pay all cash for the store or should you finance it? Well, that all depends on the terms of the financing, how much cash you have, and how much cash flow you need to pocket each month from the business. In most cases, it makes a lot of sense to finance the business. So, if you're looking at your financing options, here are a few choices for you to think about.

Owner Financing

Probably the best bet for financing a used coin laundry is to get the seller to hold a note for some or all of the purchase price. Now why would a seller agree to do this? I mean, come on, they want out and they want the money yesterday, right? Well, maybe not. There are some tax advantages for a seller to receive payments for the business over time. If the seller has a low W-2 income, getting paid all cash can throw the seller into a higher tax bracket and a good portion of the money would go to Uncle Sam. How do you think your tax bill will look if we added an extra $250,000 to your income this year? Wouldn't it look a lot better if you spread that out over, say 5 to 7 years? The other nice thing about owner financing for the owner is that they still receive a steady stream of income, but now without the "headaches" of having to run a business. For you, as the buyer, you don't have to try to "qualify" for a loan or deal with a mortgage company. In addition, this gives you more piece of mind that the business is really doing the numbers that the seller is claiming, because in a sense, the seller now has a vested interest in your success. I like to think of owner financing as a "Win-Win" and it makes for smart business!

Home Equity Line of Credit (HELOC)

With the run-up of home prices over the past several years, you may find yourself in the enviable position of having a substantial amount of equity in your own home or a piece of rental property that you own. If this is the case for you, you're in luck, because using some of that equity to purchase a business that generates monthly cash flow is a really smart idea. First of all, that equity is just sitting there, not making you a dime. By using it for a Laundromat, you are now going to turn that equity into a stream of income. I like HELOC's because the interest rates are usually lower than those of traditional business loans and the loans are easier to qualify for, especially if the property is your principle residence. Plus, many times, a HELOC will have the option of paying interest only on your payments, maximizing your Net cash flow after debt service and increasing your overall ROI. This is the option we used to purchase our 1st store.

Small Business Association Loans

Probably the most common loan for a business of any kind is an SBA loan. Generally, if you go for an SBA (Small Business Association) loan, you can expect to have the financing be a full documentation loan. They generally will require 2 to 3 years of your personal income tax returns and may require you to use your primary residence as additional collateral. They generally want to see at least 2 years financial records on the business (Profit & Loss and Balance Sheets), plus the tax returns of the seller. If the store has had declining revenue over that period, there is a good chance that they will decline to loan, or require more of a down payment. Many times if the numbers look good you can get by with putting down as little as 20%. The interest rates on SBA loans are usually 1.5 to 3 % above the prime rate depending upon your credit. A word of warning, SBA loans can take anywhere from 45 up to 60 days to close, so make sure your escrow period is long enough to account for the lengthy funding process of an SBA loan if this is your choice of funding. In addition, an SBA loan could become a problem if you own a lot of rental property because it is highly likely that you will have a lien put on all rental Real Estate you own.

Private Investor Financing

Sometimes you can obtain financing from private investors to help you with your purchase. This can come in several forms, but here are a few of the more common ones.

Hard Money Loan (HML) – these are loans made many times by private investors in the secondary loan market to those who may have a hard time qualifying for a traditional SBA loan. HML's generally are pretty expensive with interest rates ranging from 2 to 5% above the prime rate. In addition, they tend to be shorter in length; usually the terms are 24 months or less, and often less than a year. Also, it is not uncommon for the loan to cost from 1 to 5 points (or % of the face value of the loan) up front. Remember, I said it was expensive! However, these loans can fund in as little as 3 days so if you need the money fast, this could be an option.

Promissory Note (PN) – Another type of private investor funding is to offer a Promissory Note (Prom Note) to an individual or group of investors. In this case, the lender would hold a note for say 5 years, at maybe 10 to 15% interest. In most cases, you need only make the interest payments either monthly or quarterly, with a balloon payment at the end of the term of the loan. The problem that most buyers have is finding people to lend them the money. There are many investment groups out there looking for decent returns and many of the members have idle cash looking for investments, so you could start there. Also, think of all the people you know who might have some extra bucks lying around not making them much money. It is not always easy to find the investors but when you do, these investors could become your potential money partners for other projects you work on in the future, so start making a list of potential investors and begin educating them on this type of investment opportunity. For them it sure beats 5% in a money market fund and for you it is essentially a no or low documentation loan!

Direct Investor (DI) – The last private investor funding I will bring up is a direct limited partner in the business. Oh, did I say that? You mean give up a piece of the business and profits to get the project funded? You bet! Fifty percent (50%) of $4K a month is better than 100% of nothing! Besides, there are ways to structure it so the partner has no say in the operation of the business (I prefer it that way), essentially a silent partner, but one you know about and who gives you money up front. This can be a real smart way to go if you have a good plan to increase the business, as you will both profit well.

The point here is that you can be creative when it comes to financing your store. Of course there is always the option to just pay all cash, but what fun would that be?

The Laundromat Spring Bounce

The Laundromat business is a very cyclical one, meaning that there are times when we can always count on heavy months (the winter time) and other times when the collections are a bit lighter than we would prefer (the summer). In an established coin laundry, the gross revenue in the summer months is generally somewhere between 10 and 15% less than that of the winter months. Why, you ask? In most places in the US, the winter time has colder weather and it rains more. This means that customers wear thicker clothing and more of it. This is all good for filling up the washers and dryers.

So here we are in the spring time and getting ready for the summer, which is quickly approaching. Something interesting happens each year right around this time. There is what I like to call "The Spring Bounce". It is usually only one month and it changes every year. Sometimes it is April, sometimes it is May, but whenever it happens, we see that the business picks up and we have a great month.

There are a couple of reasons for this sudden increase in business, both of which makes complete sense. Firstly, when the weather breaks and the seasons change, away go all of the winter clothes and out come all the summer clothes. Many customers will wash all of the winter clothes before storing them for the summer. You will see them bringing in their comforters and blankets to clean them as well. Hurray!

Secondly, customers pull out of storage all of their summer clothes which have been stored all winter. In addition, graduations are here so there are plenty of graduation gifts like new summer outfits. All of this needs to be washed to be ready to wear. Hurray again! And bingo, we have a great month!

So, why is this a problem for potential investors? The reason is because if the investor is not careful they can easily over pay for a store. You see, many who seek to purchase a coin laundry do so in the spring time. I don't know why, maybe it is because they just got a big tax refund and want to invest it. Maybe it is because more Laundromats go on sale in the springtime than any other time of the year. But whatever the reason is, as an investor, you need to make sure that you don't just look at the numbers for the last six months of the business.

I always recommend to my clients, that you analyze the income of a store based upon the last 2 years of operations and to make sure that it includes the numbers for two summers if at all possible.

Last spring I knew a guy who purchased a Laundromat based upon the numbers from only the prior six-month period ending in May '06. So in other words, the seller only provided him 6 months of earnings and they were for the best six months of the year, rather than the average earning of the entire year. Now this store made a lot of money and the difference between the winter months and the summer months was well over $3,000. This translated to a net income difference about $1,500 a month and he overpaid for the store by over $75,000. When he realized his mistake, and came to me, it was too late to do anything about it.

So beware of "The Spring Bounce" if you are shopping right now for a store. In the world of Pooh, if you are not careful you might get pounced! And if you were wondering, yes this also happens in the Fall, right around Pumpkin time.

The Laundromat Spring Bounce

The Laundromat business is a very cyclical one, meaning that there are times when we can always count on heavy months (the winter time) and other times when the collections are a bit lighter than we would prefer (the summer). In an established coin laundry, the gross revenue in the summer months is generally somewhere between 10 and 15% less than that of the winter months. Why, you ask? In most places in the US, the winter time has colder weather and it rains more. This means that customers wear thicker clothing and more of it. This is all good for filling up the washers and dryers.

So here we are in the spring time and getting ready for the summer, which is quickly approaching. Something interesting happens each year right around this time. There is what I like to call "The Spring Bounce". It is usually only one month and it changes every year. Sometimes it is April, sometimes it is May, but whenever it happens, we see that the business picks up and we have a great month.

There are a couple of reasons for this sudden increase in business, both of which makes complete sense. Firstly, when the weather breaks and the seasons change, away go all of the winter clothes and out come all the summer clothes. Many customers will wash all of the winter clothes before storing them for the summer. You will see them bringing in their comforters and blankets to clean them as well. Hurray!

Secondly, customers pull out of storage all of their summer clothes which have been stored all winter. In addition, graduations are here so there are plenty of graduation gifts like new summer outfits. All of this needs to be washed to be ready to wear. Hurray again! And bingo, we have a great month!

So, why is this a problem for potential investors? The reason is because if the investor is not careful they can easily over pay for a store. You see, many who seek to purchase a coin laundry do so in the spring time. I don't know why, maybe it is because they just got a big tax refund and want to invest it. Maybe it is because more Laundromats go on sale in the springtime than any other time of the year. But whatever the reason is, as an investor, you need to make sure that you don't just look at the numbers for the last six months of the business.

I always recommend to my clients, that you analyze the income of a store based upon the last 2 years of operations and to make sure that it includes the numbers for two summers if at all possible.

Last spring I knew a guy who purchased a Laundromat based upon the numbers from only the prior six-month period ending in May '06. So in other words, the seller only provided him 6 months of earnings and they were for the best six months of the year, rather than the average earning of the entire year. Now this store made a lot of money and the difference between the winter months and the summer months was well over $3,000. This translated to a net income difference about $1,500 a month and he overpaid for the store by over $75,000. When he realized his mistake, and came to me, it was too late to do anything about it.

So beware of "The Spring Bounce" if you are shopping right now for a store. In the world of Pooh, if you are not careful you might get pounced! And if you were wondering, yes this also happens in the Fall, right around Pumpkin time.