

# Wealth in Real Estate



## Building Wealth Through Real Estate

Why build wealth this way? The simple answer is that it is the **most powerful** way to accumulate wealth, and more people have become millionaires through real estate than any other means. A recent Wall Street Journal article indicated that 95% of Americans will face financial difficulties before or by retirement! There are several options for building wealth, but most of these options pale in comparison to real estate.



Cathy Staup is your key to start building wealth in real estate.

Consider options like savings accounts, CDs, bonds, and money market accounts. These are safer options, but you probably won't reach a goal of building significant wealth through these means. Although these are good options, they will barely keep pace with inflation. Think about it; not many millionaires became wealthy by investing in savings accounts? The stock market can bring you some interesting returns, but it can also lead to some big losses. You have very little control over the companies you invest in, and there are no significant tax advantages to owning stock.

Historically, real estate has provided investors with a stronger return than any other option. Think about the growth of the U.S. median home price from 1940 to July 2009 (a 69 year period): Even after adjusting for inflation, median home values nearly quadrupled over the 60-year period since the first housing census in 1940. Adjusted median values rose from \$30,600 in 1940 to \$119,600 in 2000, rising fastest (43 percent) in the 1970s and slowest (8.2 percent) in the 1980s.

While there have always been small inclines and declines along the way, the fact remains that real estate has had a strong history of steady appreciation over time. And even though most U.S. housing markets over the last few years have experienced larger than normal corrections during this down cycle, real estate has always recovered and will continue to outperform every other asset class.

Take this interesting thought: If you were to ask your parents what the best investment they ever made was, what would they say? More likely than not, they'll mention their home, and if they could do it all over again, I bet they wish they would have bought a few more.

Imagine you are able to purchase a brand new \$150,000 home with an investment of about \$30,000. If you rent this home and simply break even on your cash flow, you will have an asset that grows while someone else makes your mortgage, tax, and insurance payments. At a 5% per year, that home will be worth over \$611,000 in 30 years. A \$30,000 investment! Think of how you could use that money.

### **STRENGTH OF REAL ESTATE:**

This is the major strength of investing in real estate: **LEVERAGE!** With leverage, you can own something worth 5-10 times your initial investment and still be able to take advantage of 100% of the appreciation, cash flow and tax benefits.

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## Advantages of Real Estate

How can you benefit from investing in real estate?

**APPRECIATION:** Over the past 80 years, average real estate values have continually increased. There have, of course, been some periods where values decreased, but the overall trend has always gone up. What is it that has kept real estate in such high demand over the years? Like anything else, the value of real estate is determined by supply and demand. One of the main reasons is that shelter is a basic human need. People need a place to live, work, and shop where they are protected from the weather. Additionally, real estate is an investment that benefits from inflation. In periods of high inflation, real estate values go up.

**LEVERAGE:** One of the biggest advantages of real estate as an investment over any other asset class such as stocks, mutual funds, commodities, and government financial instruments is leverage. Leverage allows you to purchase and control a large amount of real estate with a relatively small amount of money.

For example, you could easily purchase a \$100,000 property with only a 20% (\$20,000) down payment. In some cases you can buy property for as little as 10% or less of the purchase price giving you even more leverage. To illustrate the power of this, use this as an example: Let's say you bought \$20,000 worth of gold, stocks, or some other investment. Then over the course of the year your investment went up 10%. Your investment is now worth \$22,000, and your total return on investment (ROI) is 10%.

Now let's take that same \$20,000 and use it as a down payment on an income property and buy a \$100,000 house. Once again, let's say it goes up 10% for the year. The property is now worth \$120,000, and your \$20,000 investment has now doubled due to the \$20,000 increase in your property's value. You have now made a return on investment of 100%! And remember, there is always equity in the property itself.

**FINANCING:** Unlike other investments such as stocks, bonds, mutual funds and commodities, you can get financing for the purchase of real estate. Lenders will loan up to 80% of the market value of your property, and in some cases as much as 90%. Up until a few years ago, lenders were even financing over 100% of the value, thereby giving you 100% leverage and an infinite return on your investment.

It is possible to finance the purchase of stock, however, purchasing stock on margin is not the same. You are typically limited to 50% of the principal value of the stock and if the stock's value drops you may be forced to pay those funds back immediately under a broker's margin call.

**TAX ADVANTAGES:** With investment property, you are allowed to deduct all of the mortgage interest, property taxes, insurance, maintenance, repairs, professional fees, and depreciation, etc. Do not confuse this deduction with that of your personal residence where you can deduct the mortgage interest on up to two properties. With investment property you are allowed to deduct these expenses on an *unlimited* number of income properties.



Are you  
currently  
paying  
someone  
else's  
mortgage?

**Depreciation** is a tremendous deduction that is often misunderstood and underappreciated. This is a “paper” deduction, which means that you do NOT need to spend any of your own cash in order to get this deduction. The IRS simply allows you to depreciate the structure (not the land) as if it would be worth nothing at the end of 27.5 years! Of course we all know that the property will be worth much more than what you paid for it in 27.5 years. Nevertheless, on a \$100,000 house you are allowed to write off nearly \$2,910 in depreciation alone each year for 27.5 years!

**CASH FLOW:** A properly purchased income property will provide its owner (you) a positive cash flow month after month, and year after year. Cash flow will vary from property to property based on variables such as the size of your down payment, the purchase price, market rent, and related expenses.

However, if you buy a property that makes sense the day you buy it, you will have a solid investment right from the beginning and for many years to come. Typically, it is wise to purchase property with a positive (or neutral) cash flow. There are only a few exceptions to this rule when carrying a (slightly) negative cash flow would make sense. The most common reason for purchasing a property with a (slightly) negative cash flow would be in situations where you are “deferring” a portion of your down payment in lieu of the negative cash flow.

**For example,** let’s say that a property purchased with 20% down would provide you a decent cash flow. However, you decide to increase the leverage on your investment by purchasing with a smaller 10% down payment thereby keeping the other 10% of the down payment. You have now lowered your down payment and doubled your leverage. In effect, you are paying for that “deferred” down payment through lower cash flows – similar to a payment plan.

**YOUR TENANT PAYS YOUR MORTGAGE:** A unique and very attractive feature of owning income property is that your tenants literally buy your investment property for you. Your tenants pay you rent every month that you then use to pay down your mortgage.

### **So what’s stopping you from purchasing your next property?**

Like many Americans who never reach their goals, you may be held back by some fear of the unknown. As I’m sure you know, the media loves to sensationalize bad information. Yes, there are many real estate markets around the country that have experienced price declines after one of the biggest booms in history. However, if you look closely, this was due to the fact that those areas were overbuilt, where the supply of homes exceeded demand. Savvy investors understand that the best places to buy real estate are in areas where demand exceeds supply. How do you find these areas?

By using Cathy Staup as your investment guru, you get access to exclusive investment opportunities in growth markets around the Puget Sound. I know the markets with job growth, low unemployment and positive migration which logically leads to a need for housing. Once you understand that **all real estate is local** and that **opportunities exist all the time**, all you have to do is make the decision to invest and keep building your real estate portfolio!

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## Getting Paid to Borrow Money

By now you know that income producing real estate is one of the best investments you can make. But, what is less well known is that income producing real estate allows you to **get paid to borrow money**.

The reason for this has to do with the reality of inflation. In times of inflation, your best protection against the declining value of the dollar is high quality, long-term, investment-grade, fixed-rate debt attached to a piece of income producing property. In a nutshell, the right kind of debt is good.

### Here's how it works:

Assume that you purchased a property back in 1979 and that a dollar actually was worth a full dollar. Then, thirty years later you find that same dollar worth only \$0.24 because of continued inflation driven by the government's absurd economic policy.

Although the overall purchasing power of the dollar has decreased over those thirty years due to inflation, the principal balance on your long-term debt is never adjusted in step with inflation. By paying down your fixed-rate debt with continually CHEAPER DOLLARS than those you originally borrowed with, you are effectively saving yourself a lot of money each and every year.

### Now, think about it another way:

Assume you purchased \$1 million worth of income producing real estate with a combined mortgage balance of \$800,000. And let's assume that over the course of one year you didn't pay down any principal and there was a 4 percent rate of inflation. Your loan balance of \$800,000 would now be worth only \$768,000 in terms of real dollars. That's a reduction of \$32,000 in one year! Effectively, you just got paid because of inflation. **And that's how you get paid to borrow money.**

Now if you believe that inflation has floated around 4% over the last few years, as the government would have you believe, then your \$800,000 loan would only be worth \$531,866 ten years from now. The fact is that "real" inflation has been much higher than that reported by the government. Many investors believe real inflation to be over 8% and some feel that we've seen as much as 12%.

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## How to Get Your Investment Down Payment

Real estate has always been the fastest and safest investment vehicle to acquire wealth and reach millionaire status. But you will need cash for a down payment or your real estate investment goals will be difficult to achieve.

**Every year that you don't invest is going to *cost* you money in lost opportunity.**

### So where do you get your down payment?

Most lenders require a 20% down payment because it provides them a level of comfort in case you default on your mortgage loan. It also happens to be the minimum equity required to avoid the addition of mortgage insurance premiums. Although a 20% down payment is considered by

You can  
still invest  
with  
practically  
no money!



Some practical tips on how to cash in on a down payment now!

many to be the norm, investors often look to increase their leverage in purchasing real estate by lowering their down payment. This reduces their initial cash requirement but increases their monthly carrying costs through higher mortgage payments and possible mortgage insurance.

#### **Here are some sources to help fund your next real estate investment:**

##### **Investment Savings**

For most investors, this is the best way to invest. Saving your money for the purpose of investing is the smartest use of your money and one of the best ways to achieve financial freedom.

##### **Tap Into Your 401(k)**

To get that down payment, you can tap into your 401(k), which you will have to pay back over a period of five years or more, with interest. This method, however, has both advantages and disadvantages. One of the advantages of getting a loan from your 401(k) is that it is not considered a debt by lenders when they assess your debt-to-income ratio. A major disadvantage of borrowing from your 401(k), however, is that should you leave your current job for whatever reason, you will have to pay the loan in full 90 days after you quit or are terminated.

##### **Self Directed IRAs**

Self directed IRAs are an excellent source of down payment funds. They can provide you the ability to build your retirement nest egg using real estate's excellent long-term rates of return, and depending on the type of IRA you use, you may be able to do it tax free.

##### **Business Lines of Credit**

Using business lines of credit can be a great source for your down payment needs. Each line of credit can range from \$25,000 to \$100,000 or more, and are available at very competitive interest rates. Business lines of credit make sense in situations where the property's cash additional monthly payments. You will need to run the numbers to determine if your cash positive or negative when financing part or all of your down positive, then you can effectively purchase with.

##### **Control Your Budget**

You can simply stick to a budget and save the funds.

Write down everything you spend money on. Don't leave anything out, even if it's a small candy bar that cost you a dollar. Assess your spending habits and see what you can improve and what expenses you can avoid. This may be a *slowest but best*.

##### **Partners, Partners, Partners!**

The *fastest* way to purchase your first (or next) property when you're short on funds is to use a cash partner be anyone who shares similar investing goals as you and investment capital available for the arrangement; you would be the credit partner and financing. You and your partner would split Partnerships are very easy to form and can be tweaked in any way you and your partner feel is mutually beneficial.

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## **A Plan for Simple Real Estate Wealth**

Now that you understand the power of real estate, you need a simple plan to build your wealth. The following is a **very simple plan** that will create long term wealth for you. The plan is very scalable, which means you can do more or less in order to achieve your wealth and income goals at your own pace. We are going to assume that you buy one new property per year; however, you can adjust it by purchasing more or less. So if you choose to purchase two per year, you will double your returns. We need to begin by making a few assumptions. So let's assume that the purchase price of each investment property will be \$150,000.



The  
benefits  
are  
literally  
unending!

Next, let's assume that the average appreciation rate in the local market you are investing in will be 5%. Again, this is an *average* as some years will be higher and others will be lower. Let's also assume that your mortgage interest rates are 7.0% on a 30-year fixed rate mortgage.

Finally, let's assume that you are purchasing each of your investment properties with a 20% down payment. There may be situations where you purchase with only 10% down or even less, but as a general rule-of-thumb, you can expect most lenders to require a 20% down payment.

### **Putting it all together**

Now, if you purchase a new property at \$150,000 with a 20% down payment, you would be investing \$30,000 towards that property. Remember that your \$30,000 investment will be in your property in the form of equity. Additionally, there will likely be some closing costs which can range from 1% to 3% of the purchase price. Let's use 2%, or \$3,000, for our example here.

In order to calculate the return on investment we must also factor in the annual cash flow. We will assume your property generates an annual pre-tax cash flow of \$1,700 (approximately \$140 per month).

Calculating out the figures, this single income property is providing you a total return on investment of **35.6%** in your very first year of ownership! You will also note that your returns are increasing with each and every year.

Now take a look at your equity accumulation over the years. The equity adds to your overall net worth and is what we call *wealth*. The more equity you accumulate, the wealthier you become. The wealthier you are, the more freedom you enjoy. And remember that we are using a relatively conservative *average* appreciation rate of 5% per year.

**This isn't all** - This does not take into account the tremendous benefits provided by depreciation. Once you factor in the depreciation on your property your return on investment will be even higher. Depreciation is a tremendous tax benefit since it is a "paper" deduction – meaning that you don't have to spend actual cash-out-of-pocket in order to deduct it. The second part of your real estate wealth plan is to continue building your real estate portfolio by purchasing additional properties as often as you can.

## **Wealth Accumulation in Hyperdrive**

Now that you see the incredible wealth building potential of a single investment property, let's consider the **awesome wealth building power** of investing in multiple properties over time. Let's take the same example above and multiply our returns by simply purchasing one additional property per year over a 10-year period and see what happens. For this scenario we will assume that the purchase price of each new property will be 5% higher than the previous year in order to factor in the affect of price appreciation from year-to-year. Again, purchase price and appreciation are *averages*.

You could acquire over \$1,000,000 in equity over the course of only 10 years. By purchasing *only one* average priced property per year for ten straight years you will have built up enough equity to make you a millionaire (if you weren't already).



Cathy can help you start now on your way to building wealth in real estate!

In addition to the wealth you'd create for you and your family, you would also be benefiting from the growing annual cash flow being produced by your income properties. The income earned can help supplement your existing income, provide additional capital towards the purchase of additional income property, and eventually give you the freedom to quit your job and retire with *passive* income! Again, we are NOT factoring in the added benefits of depreciation here. The plan is simple and flexible. It is easy to follow and can be compressed into a **shorter period of time** if you have the resources to accumulate more than one property per year. If not, consider partnering.

**You are in control, but you must take action!**

## **What Should I Do Next?**

### **1. BUY INCOME PROPERTY!**

Start now! Don't wait to invest in real estate, invest in real estate and wait.

The sooner you purchase your next property, the sooner you will be accumulating equity and building up your net worth. The more property you buy, the wealthier you will become. The faster you build your real estate portfolio, the faster you will become **financially free!**

### **2. CONTINUE LEARNING**

Always be a student of real estate, business and finance, no matter how successful you become.

Continued learning increases your knowledge and improves your financial literacy ("financial IQ").

Continually feed your most useful tool – your brain!

## **Provided for you by Cathy Staup**

Tried, True and Trusted - Cathy Staup is an experienced real estate agent in Washington State, a member of the Northwest Multiple Listing Service and a prestigious member of the President's Club. She has represented clients as far away as Florida and Texas. Experienced in all phases of sales and marketing single family, multi-family, condominium properties, manufactured homes, improved and unimproved land, new construction and presales, Cathy is passionate about going the extra mile for her clients.

She is an approved instructor for the Washington State Housing Finance Commission which provides home buyer education services and down payment assistance for first time home buyers. Through teaching WSHFC classes she has gained a unique understanding of the challenges either first or third time home buyers face and is dedicated to making the experience as stress-free as possible. Cathy believes in the importance of informed and educated buyers or sellers.

Sellers have benefited from Cathy's marketing experience since 2002. Having lived in the greater Seattle area her entire life Cathy has lived in many neighborhoods and understands the local real estate market very well. This differentiates her from a lot of agents in the Northwest Multiple Listing Service. Cathy offers her experience, skills, motivation, attention to detail, follow through track record, and ability to provide the most service with the least amount of hassle for her clients.

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