Street Smart Buyer Session #3 Workbook

Let's review a bit from last week…. Ok we went over the Street Smart Analyzer and you all had a lot of great questions. The purpose of the analyzer was to add to your confidence level… You started looking at properties, then you took those properties, inserted the numbers such as rents, rates, mortgages, down payments, and amortizations, and plugged in the numbers. The purpose of this exercise is to get you extremely familiar with a property….

How are you doing with Goals?

You should also have at least one goal posted around the house in various places. Even if it is just one goal.. Maybe to buy ONE positive Cash flow property by June 1, 2016. I have my goals up and around the house INCLUDING on the upper right hand corner of my Fridge…. Why do I want to you to know that? Well I have a mentor, and he always says- You can't teach what you don't know.. And you can't lead where you won't go….. I've got goals just like you do. And I'm not going to tell you to post your goals all over your house and not do it myself!

Alright, well we are all living in Canada… and most of us have heard a lot about Alberta lately and the "Big Slow Down". Apparently there are thousands of people losing their jobs and going through some tough times…. Which is unfortunate. I have definitely been through tough times. And there were moments for sure where I would have done anything to get rid of properties… This was during the recession…. Well guess what, it's happening again.. Not on such a massive scale.. But there are definitely people who need help. Who are in over their heads. Who need a way out. This can create a huge opportunity for your as Street Smart Buyers…. The Chinese symbol for Crisis are two symbols together meaning Danger and Opportunity…So ultimately it is up to you how to see things. I chose to see Opportunity. I recommend you do the same.

Meanwhile, elsewhere in the world…. Some or all of you might think there are no opportunities…. Well I just had a no money down, no bank qualify right here in Kelowna… we are in a red hot market right now… But they are still there… I will give you a couple examples shortly….. First I want to go through some more numbers with you.. And it all comes down to the numbers.

I rushed a bit in the last session… I'm sorry about that. After I reviewed the recording, I realized yes the Analyzer is a great tool. I am so glad that it is there for you. But I think it is important just to take a quick step back and do some simple math for you.

Numbers and How to Calculate ROI (Return on Investment)

Let's take just one deal for example. Let's say it is a $300,000 property. Now with 25 percent down (and you can even buy investment property with less as low as 20 perceont down- but let's be conservative shall we? Better to overestimate things when it comes to real estate). With 25% down or $75,000 plus expenses- I am talking appraisals, inspections, legal fees and for those of us lucky enough to live in the Beautiful Province of British Columbia Land Transfer Tax- so lets say expenses of $5,000. You will have a total up front investment of $80,000.00

- EXAMPLE:
- $300,000.00 property
  - Down Payment: $ 75,000+ expenses $5,000 Total: $80,000.00 (Investment)

Alright, let's now say that you are looking at a <u>5 year term</u> and this is how the property performs:

$100 per month Cash flow or 1200 per year or $6000 over 5 years…. Let's say the property Appreciates or in other words it GOES UP IN VALUE 1% per year…. 1% of 300,000 is $3,000 per year times 5 years equals $15,000. Now we factor in my favourite part of Real Estate Investment PRINCIPLE REDUCTION…. This is the amount of money the loan will be paid down (by YOUR TENANT) over the next five years. At a rate of 2.39 over five years and a 25 year amortization, the balance of the mortgage or Principle reduction will be paid down by $34,942.00 That's a total of $55,941.00.

5 years:

- <u>Cash Flow</u> $100 per month= $1,200 x 5 = $6,000
- <u>Appreciation</u>: 1 % per year= $3,000 x 5= $15,000
- <u>PRINCIPLE reduction</u>= $34,942.00 (2.39% 25 year am)

Total: $55,941.00

Approx.

Here is how you calculate your Return on Investment. Now please keep in mind that I am a big fat MATH NERD. I seriously love Math. And believe you when I tell you that Calculating your Return on Investment is easy. It is just like it sounds. You take your return or How much money you make overall and DIVIDE it by what your original investment. So in this case. It is $55,941 that you made and you put up $80,000. That equals a 70% Return on Investment. Which equals a 14% return on investment PER YEAR!!! Which is huge.

Everybody knows that Investments can be Risky. Everybody says that in order to make a lot of money you have to take a lot of risk. However in real estate- Some people (in fact a lot of people) are able to make a really excellent amount of money AND be very safe and secure….. The best of both worlds.

Return On Investment:

$55,941.00 (Return)

$80,000.00 (Investment)

=

70% total ROI OR 14% annually

(70% divided by 5 years)

Let's sum this up as simply as possible. If you were to buy a property like this again, $100 monthly cash flow, appreciation of 1% per year (oh and by the way real estate has appreciated across North America on average 6% per year so this is a very conservative number).   So 1% appreciation per year AND principle reduction as calculated…. Your $80,000 will turn into approximately $135,941 in 5 years. Now that's big.

$80,000.00

$135,941.00

In 5 Years

You can actually invest in Real Estate with as little as 20% down conventionally in orther words going to the Bank and getting a mortgage…   Let's say it is a $300,000 property. Now with 20 percent down $60,000 plus expenses- I am talking appraisals, inspections, legal fees and for those of us lucky enough to live in the Beautiful Province of British Columbia Land Transfer Tax- so lets say expenses of $5,000. You will have a total up front investment of $65,000.00

- EXAMPLE:
- $300,000.00 property

– Down Payment: $ 60,000+ expenses $5,000 Total: $65,000.00 (Investment)

Your cash flow will decrease because you have a higher mortgage because you are putting less money down… So only $480 per month versus $100 (and we are assuming that you never raise rent in 5 years – which I am sure you will do). Again appreciation of 1% per year or $15k that stays the same… And the mortgage will go down even more $3K more over 5 years. So you end up with about the same profit at the end of the term (that is if you sell). But here's what you want to notice

5 years:

- <u>Cash Flow</u> $40 per month= $480 x 5 = $2,400
- <u>Appreciation</u>: 1 % per year= $3,000 x 5= $15,000
- <u>PRINCIPLE reduction</u>= $37,942.00 (2.39% 25 year am)

Total: $54,500.00

Approx.

You have put less money down as a down payment, made approximately the same amount of money. So instead of making a 14%ROI which is darn good, you're making more like a 17% ROI which is excellent!

Return On Investment:

$54,500.00 (Return)

$65,000.00 (Investment)

=

84% total <u>ROI</u> OR 17% annually

(84% divided by 5 <u>years</u>)

Now here's an example of a Low Money down deal. Let's say you can take over the financing for someone for $20,000 and yes let's say there are still some "other expenses of about $5K"… So you're in for 25% down, no bank qualify….. And you have agreed to pay $300,000 in 5 years (which is the value today).

- EXAMPLE:
- $300,000.00 property
  - Down Payment: $ 20,000+ expenses $5,000 Total: $25,000.00 (Investment)

Alright let's say you can make it cash flow $100 per month because of the way the financing is… And keep in mind you can use the Street smart Analyzer to do this…. So we have $6000 total cash flow over 5 years…. You plan to sell based on 1% appreciation per year.
Now, since it is over-leveraged a bit… The mortgage balance will only be paid down let's say $20,000… (In the two other cases it was over $30,000).

But in this case, you are working with a motivated seller, they have agreed to keep the financing in place, and you have calculated that the mortgage will be paid off by $20,000 over the next 5 years…. And you have it in your paperwork that YOU get to benefit from that $20,000 gain….. So that's a total of $41,400 in profit at the end of 5 years.

5 years:

- Cash Flow $100 per month= $1,200 x 5 = $6,000
- Appreciation: 1 % per year= $3,000 x 5= $15,000
- PRINCIPLE reduction= $20,000

Total: $41,400.00

Approx

Again this is where the power of Low Money Down real estate can be so powerful.
Your return is $41,000, your investment is $25,000, that's 163% over 5 years or 39% Return on Investment.. Which is MASSIVE.

And I'll tell you, yes, it can take a lot of digging to get deals like this… But you won't find them if you don't dig, if you don't look, and if you don't bring it up in conversations….. It works!

Return On Investment:

$41,400.00 (Return)

$25,000.00 (Investment)

=

163% ROI or 39% annually

(163% Divided by 5 years)

And the biggest factor in all three of these examples is the Wonderful aspect of Principal Reduction.. This is how much the Loan is Paid off over time. It's one of my favourite things about Real Estate…. Letting someone else pay down debt FOR YOU… Make me feel like a real Smarty Pants…..

Now the common thread that you will see when you talk to motivated Sellers will be that their properties are usually OVER- leveraged… This means that the debt on their home is more than the value. Sometimes It's by a little, and they don't the ins and outs of selling their home, and they can't pay a realtor so they just feel stuck……, sometimes it's by a lot and they feel like they are REALLY STUCK… like forever…..

This is where understanding mortgages and how they work and how you can use them to your advantage is so important… Yes the banks make the rules.. And he who owns the gold makes the rules. But if you understand the numbers… Then you will have an advantage that most people don't have. 9 out of 10 people I talk to don't know the balance of their mortgage. They don't know their rate, they don't know their term…. Most have an idea of their payment but even many of them don't know whether or not it includes their tax payment.

> Knowing the rules… understanding the numbers will give you a huge advantage… That's why I have spent 2 sessions on numbers… I learned this the hard way over time… And I tell you.. I left so much money on the table…. You don't have to!

For folks who are over- leveraged.. What you have to offer them is time… Time to let maybe a tough market recover… And most importantly… Time to pay the mortgage down. And the objective is to OF COURSE find someone Else to pay the mortgage down.

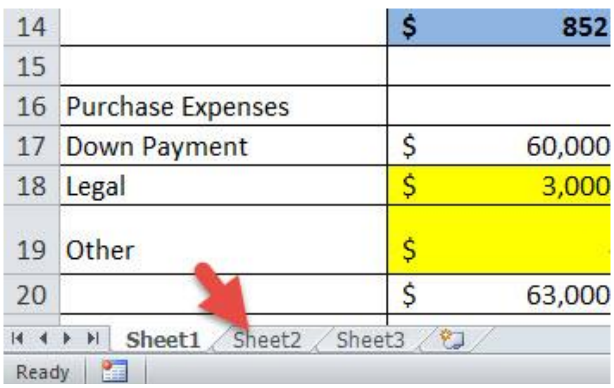
Example Property

This was one of the most complex deals I have ever done….. These poor people were desperate to move because they had simply outgrown their house. They had way more people than bedrooms. Plus there was a messy divorce involving a very angry Ex…. Needless to say there were many factors to this deal…

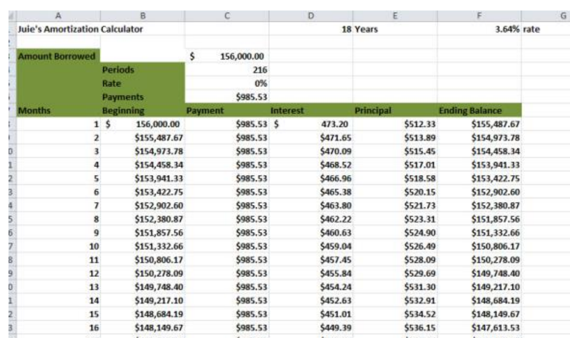
This property had mutliple issues "against" it… First of all the people who owned it together (angry exes) hated eachother.. Needless to say it was challenging to find a way for them to get along. Secondly they had bought extremely high in the market and the property value had not recovered. This was partly because the property was in a mobile home park……. So when I was dealing with it, it had 164, 000 worth of Debt on it and was only worth $125,000… that meant that IF they wanted to sell.. And they wanted to sell, they would have to PAY the bank $40,000 to be released from the mortgage….. So they were stuck. They were literally ready to walk away, let it go into foreclosure and declare bankruptcty…… But here's the thing… I got all the inofrmation that I needed about the property from the Motivated Seller Worksheet, I knew this property had been bought 8 years ago… And because I have analyzed so many deals and calculated so much financing… Which is why I recommend so strongly that you CONTINUE to practice looking at properties, and understanding numbers, I KNEW that EVENTUALLY some equity had to be there someday…..

Because Mortgages are Amortized… Which means with every payment… a little more goes toward the principal or the BALANCE of the loan.

You can go to the Street Smart Analyzer and click on Sheet 2 in the bottom left hand Tab.



14		$ 852
15		
16	Purchase Expenses	
17	Down Payment	$ 60,000
18	Legal	$ 3,000
19	Other	$
20		$ 63,000



A	B	C	D	E	F
Juie's Amortization Calculator			18 Years		3.64% rate
Amount Borrowed		$ 156,000.00			
	Periods	216			
	Rate	0%			
	Payments	$985.53			
Months	Beginning	Payment	Interest	Principal	Ending Balance
1	$ 156,000.00	$985.53	$ 473.20	$512.33	$155,487.67
2	$155,487.67	$985.53	$471.65	$513.89	$154,973.78
3	$154,973.78	$985.53	$470.09	$515.45	$154,458.34
4	$154,458.34	$985.53	$468.52	$517.01	$153,941.33
5	$153,941.33	$985.53	$466.96	$518.58	$153,422.75
6	$153,422.75	$985.53	$465.38	$520.15	$152,902.60
7	$152,902.60	$985.53	$463.80	$521.73	$152,380.87
8	$152,380.87	$985.53	$462.22	$523.31	$151,857.56
9	$151,857.56	$985.53	$460.63	$524.90	$151,332.66
10	$151,332.66	$985.53	$459.04	$526.49	$150,806.17
11	$150,806.17	$985.53	$457.45	$528.09	$150,278.09
12	$150,278.09	$985.53	$455.84	$529.69	$149,748.40
13	$149,748.40	$985.53	$454.24	$531.30	$149,217.10
14	$149,217.10	$985.53	$452.63	$532.91	$148,684.19
15	$148,684.19	$985.53	$451.01	$534.52	$148,149.67
16	$148,149.67	$985.53	$449.39	$536.15	$147,613.53
17	$147,613.53	$985.53	$447.76	$537.77	$147,075.75

Click on Sheet 2 This is what the table looks like.

I knew that the property had an original mortgage 8 years ago… so it was getting paid off more and more quickly as time went on……

Here is an example… A $279,000 mortgages at 2.3 percent, amortized over 25 years will be paid down 7 k in the first year, 8600 in the 5th year and just to almost $10K in the 10th year…. So you can see, as the years go by… the mortgage gets paid off FASTER… By year 15, this $279,000 mortgage or Loan is paid down 126,0000- Hopefully by someone Else… Aka you tenant or your tenant buyer.

- $279,000 Loan or Mortgage
- Year 1: Paid down $7,000.00
- Year 5-6: $8,600.00

- Year 10-11: $9,700.00

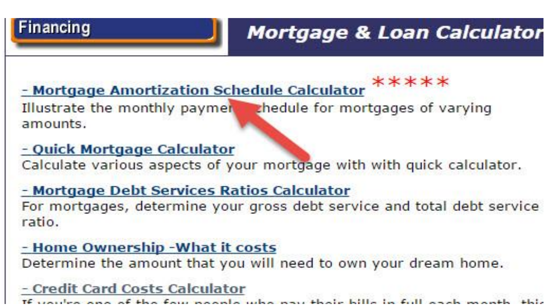
Year 15: $126,000.00

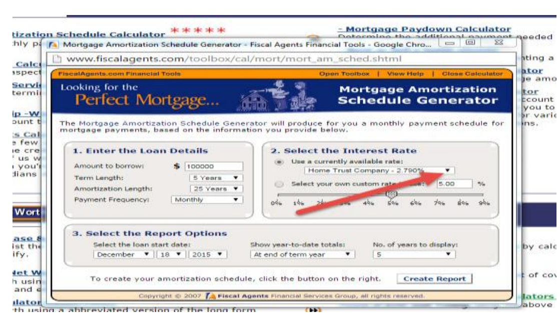
(approx)

Now back to my Deal…. Again, I knew that the mortgage had to be getting paid down faster and faster… I did my own calculation and determined that it would be paid off to a balance of 122K in 5 years… And here's something really interesting…. I had Dillon, the seller, contact the bank and confirm that these numbers were accurate… (That there would be no hidden fees). And at first the bank told Dillon that it would only be paid down about 10k over the next 5 years… I knew something didn't sound right about that… So I had him call back and get a second opinion… This time with a loan officer from the bank. And sure enough….. My estimation was correct! What we were able to do is get the property sold to a great Tenant buyer, we extablished an exit price of $132,000 PLUS $1200 per year cash flow.
So just by BUYING some time, and a little persistance… we were able to come up with a plan where instead of losing $40,000, they were able to profit over $15,000 including $3,000 up front!. That was a great day….

RATES

Rates are so important… They can really make a difference in Cash flow. You can search current rates Easily at www.FiscalAgents.com I will put the link on the site. You can follow the instructions below:





As you can see, a $240,000 mortgage at a rate of 2.39% will have a $1063 payment. The same loan at a rate of 4.64% costs $300 more per month. $3600 per year…. Over 5 years that is an added expense (or savings) of over $15,000. It is so important to pay attention to interest rates because they can drastically affect your profit at the end of the day.

Example

$240,000.00 at 2.39%= $1063.43

$240,000.00 at 4.64%= $1357.46

$300 per month Difference=

$3,600 per year

Over $15,000 over 5 Years….

Amortization

Now you can pick an amortization up to 35 years… But I'm just going to compare 20 to 25 year amortization. So a mortgage Now a 240K mortgage at 2.39 percent at a 25 year amortization will be paid down over 5 years about $35K…. And the payment will be about $1063. The same loan, 240K at 2,39 at a 20 year amortization will be paid down 46,600 over the same amount of time, but it will cost you more on a monthly basis… $1,258. So there is about a $12K difference in Debt reduction, it gets paid off faster with a 20 year amortization, but it will cost you $11,000 more in cash flow… This is where you need to have a talk with your accountant about tax strategy and cash flow. And you need to be sure and deal with an accountant who is well versed in tax law because things change can change a lot and they can certainly affect your bottom line!

$240,000.00 at 2.39% at <u>25 Year Amortization</u>

= **$34,942.00** Mortgage Reduction in 5 Years

Payment: **$1063.00**

$240,000.00 at 2.39% at <u>20 Year Amortization</u>

= **$46,611.00** Mortgage Reduction in 5 Years

Payment: **$1258.00**

Approx $12,000.00 Difference in 5 years in Debt Paydown

Approx $11,000.00 difference in CashFlow in 5 years

TAX STRATEGY… Talk to your accountant!

Your Homework…

- Keep Bringing Up Real Estate- "Great! I just learned a whole bunch about how to use mortgages to my advantage!"
- Keep looking at properties, looking for features, analyzing numbers (10- 20 PLUS) per week
- Practice Calculating Mortgage pay down in the Street Smart Analyzer
- Lookup and Compare Rates
- Compare Amortization
- Text me, email me if you think you Found Something….
- Questions about Low Money Down Ads…..
- We Are back in Session January 7, 2016.