

Investing in Rental Properties

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Why Rental Properties?

- Leverage: You can get a loan greatly reducing your cash investment and increasing returns.
- Cash flow: You make money every month your income is more than your expenses including the mortgage
- Tax Advantages: The IRS lets you depreciate rental properties every year for 27.5 years
- Mortgage pay down: When you get a loan, you will pay off principle every month increasing equity
- Appreciation: Home prices historically increase, which can negate or beat inflation

My 13th Rental Property

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What is Cash Flow?

- Cash flow is the money you make every month
- Rent –mortgage, taxes, insurance, maintenance, vacancies, utilities, HOAs
- Vacancies: 5 to 15 percent of rents (more for multifamily, higher vacancy rates)
- Maintenance: 5 to 15 percent of rents (age of home, condition, tenants are all factors)
- Property taxes: Vary greatly by state (\$500 a year to \$5,000 a year for same value property)

Why Leverage?

- Leverage allows a smaller investment than cash. 20 or 25 percent down is common for investment properties
- If you can cash flow with leverage in place your returns will be higher
- Leverage allows you to buy more properties, which magnifies advantages (tax, cash flow, appreciation)
- Difficult to finance more than four properties, but possible
- Mortgage payments stay the same, but rents will rise over time

Cash Flow on my 13th Rental

- Rent: \$1,300 a month
- Mortgage: \$530 (includes taxes and insurance)
- Vacancy allowance: 70
- Maintenance: 210
- Property management: \$112
- **Cash flow: \$378**

- **More information on the house here.**

Example of leverage

- Cash Purchase \$100,000
 - Cash needed \$101,000 (with closing costs)
 - Rent is \$1,200 a month and all expenses \$500 a month
 - Cash flow \$700 a month
 - Cash on cash return is 8.3%
- Financed Purchase \$100,000 with \$80,000 loan
 - Cash needed \$23,000 (with closing and loan costs)
 - Rent is \$1,200 a month and all expenses \$950 a month
 - Cash flow \$250 a month
 - Cash on cash return is 13%

How to get a loan

- Traditional bank will do 1-4 loans will do 20% down
- Traditional bank may do 4-10 loans with 25% down
- Portfolio lender will be very flexible and may lend on more than ten, twenty or have no limits
- Harder to qualify for investment loan, especially if you buy the most expensive personal house you can afford
- Saving down payments can be tough for multiple rentals

Is it Risky Leveraging Rentals?

- When you have great cash flow risk is much lower
 - Wait out the market drop because you have cash flow
 - You don't have to sell in a down market when you are making money
- When you have negative or little cash flow risk is high
 - Much harder to withstand down markets when prices drop and you lose money every month
- Buying below market value also protects against down markets because you have built-in equity

Tax advantages of Rentals

- Depreciate structure of the property
 - Structure of \$100,000 property worth \$80,000
 - Depreciate \$2,909 every year for 27.5 years
 - If you cash flowed \$3,000 a year you would only be taxed on \$91
- Capital gains taxes
 - When you hold the property as a long-term investment
 - Pay capital gains taxes which are much lower than earned income if you sell (20% versus 35%)

Mortgage Pay Down

- That \$80,000 mortgage is paid down \$1,300 the first year with minimum payments on 30 year amort.
- The amount paid down increases every year
- As property appreciates and mortgage decreases equity increases greatly
- Can refinance or sell to realize gain in equity
 - Be careful of recaptured depreciation when selling
 - 1031 exchange can be a great tax tool

Appreciation

- I never count on appreciation to make money. I count on cash flow and appreciation is a bonus
- Historic housing price increase over 100 years is 3.1%
- Historic return of stock market over 100 years is about 5%, with dividends 6 or 7%
- Is the stock market better? No!
 - Housing price index has nothing to do with investing. No cash flow, leverage or buying below market value is included.

Buying Below Market

- The greatest advantage of investing in real estate is buying below market value (you can't buy stocks below market value)
- If the house we bought for \$100,000 is worth \$120,000 we just gained \$20,000 in instant equity
- If you can buy below market value and leverage properties it increases your returns greatly
- This is the premise behind flipping as well. Only you buy cheap, fix up and rent instead of sell

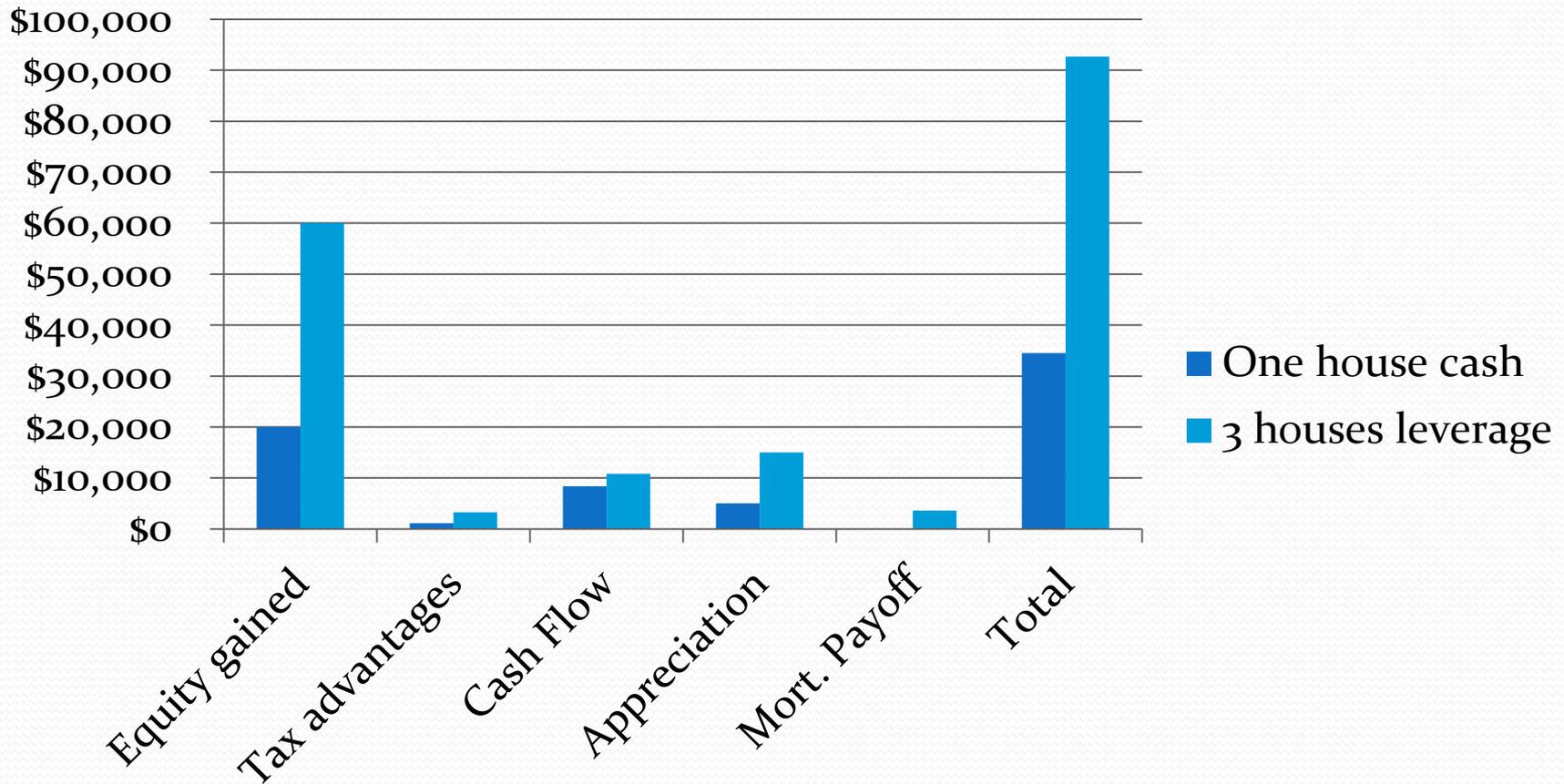
How to Buy Below Market?

- REO properties: Bank owned properties that went through foreclosure.
- Short sales: Have not gone through foreclosure, but bank must take less than they are owed
- Estate sales: Owner passes away and heirs want quick sale
- Distressed owners: divorce, money problems, relocation, jail, foreclosure, etc.
- All can be bought through MLS or auction process

How to buy the great deals

- Act fast! Good deals do not last long
- Cash purchases: many distressed homes need work and won't qualify for a loan
- Check auction sites like Homesearch.com, Auction.com, HUBZU, Williams and Williams, Hudson and Marshall
- Find local wholesalers or buy off market
 - Wholesalers buy houses cheap and resell them for a profit without making repairs

ROI Increases with Leverage



What is a Wholesaler?

- A wholesaler gets a house under contract or buys it and tries to assign the contract or sell the home as quick as possible
- Many wholesalers market to off market sellers who live out of state or are distressed. Good wholesalers will have great deals for flippers or rental property owners
- There are about 10 bad wholesalers for every good one so verify all information
- Find wholesalers at REI clubs/meet-ups, online or they will find you if you are a cash buyer

Buying off market properties

- Market to distressed or absentee owners
- “We Buy Ugly Houses” guys buy off market
- Billboards, bandit signs, direct mailing, word of mouth, websites
- Be careful if you are an agent
 - Full disclosure
 - Can list or buy their home as an agent if you follow the rules

Refinancing rental properties

- When you buy below market value you gain instant equity
- Common property I buy
 - Buy for \$100,000
 - Repair for \$15,000 for \$37,000 cash invested after down payment and closing costs
 - Worth \$145,000 to \$160,000 when done
 - Equity in home: \$160,000 - \$80,000 loan; \$80,000 equity
 - Refinance at 75 percent loan to value: \$120,000 loan
 - \$37,000 cash out after closing costs (no cash invested after refi)

1031 Exchange

- Sell rental property and buy another similar property
- No taxes paid on a qualifying exchange
- Great for properties that have been fully depreciated
- Cannot use on fix and flips
- Very short time frames to buy a new property after you sell your old property
- [More details here](#)

More information on rentals

- Investfourmore.com
 - Details on my properties
 - Over 350 free articles
 - Videos
 - Forum
 - Podcast
 - Cash flow calculator
 - Cash on cash return calculator
 - Coaching programs from me for investing in real estate
- Email: Mark@investfourmore.com
- Coaching: [Complete Blueprint for Successful Real Estate Investing](#)