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PropertyInvesting.com 'Insider'

Discover proven tips, strategies and techniques to dramatically increase your property investing profits

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Hi and welcome to your May 2004 edition of Insider - the e-zine outlining how to successfully invest in real estate - especially if you have a positive cashflow focus.

If you're receiving this newsletter for the first time then I'd like to warmly welcome you to the PropertyInvesting.com community! Remember that in addition to this free newsletter we also run a community forum board so you can share your knowledge or leverage off other people's ideas.

Here's what's on offer in this month's Insider:

Multiplication by Division

Back in early 2000, Dave and I set the financial goal of building $500,000 per annum in net (pre-tax) investment income by 9 May 2004 (the date of my 32nd birthday).

At the time both the date and achieving the target seemed a long way away - but at least we'd chosen a direction (financial independence) which gave us a basis for investing (positive cashflow properties). All that was left was building a bridge from here to there which was going to require hard work, discipline and commitment.

A strategy that has worked very well for us is multiplication by division.

We'd buy a property for $40,000, profit from the cashflow in the short-term and then, because the market had boomed, sell the property for $80,000 a year or so later (perhaps sooner!). Then, we would go back and buy two $40,000 properties (in the same region if we could find them or else another location).

Using this strategy allowed us to lock in our capital appreciation and then use to it secure another source of cashflow. This increased our yield at the same time as broadening our investment base, resulting in reduced credit and property risk.

Later we'd adopt the same multiplication by division principle as we traded out of single-family homes in Victoria and into higher yielding blocks of units in Tasmania.

When prices rose there we traded back into higher-yielding single family homes in an offshore location.

This constant realisation and reinvestment of profits is one of the secrets to our success. We began with a limited capital base which required us to keep working as accountants to fund deposits on further acquisitions. Then we started recycling deals as we turned one property into two, two into four etc. This was all possible so long as (1) we could find higher yielding positive cashflow properties and (2) so long as the real estate market continued to rise.

You may be wondering "why didn't you just refinance the equity instead of selling?'

Well it's true that selling triggered a capital gain (that is, we had to pay tax), but we wanted to avoid too much borrowing for two reasons. First, a lot of debt places you at the mercy of rising interest rates and second, lenders become nervous around highly leveraged property portfolios. In order to secure finance to fund ongoing expansion we needed to borrow no more than 80% of the purchase price while also being able to show our improving financial position on our tax returns.

Let's look at an example. Imagine you bought a $40,000 property using 80% interest-only finance. A year later that property had increased in value to $80,000. You would have the following two options:

1. **Refinance:** Assuming you could refinance your loan up to $64,000 (80% of $80,000), you'd unlock extra funds of $32,000. If you went and bought another $40,000 property then you'd need $10,000 (20% deposit + (say) $2,000 in closing costs) and have $22,000 ($32,000 - ($8,000 + $2,000)) in your back-pocket. Your total debt would be $96,000 [($64,000 + (80%*$40,000)].
2. **Selling:** Selling for $80,000 would mean you'd have to pay (say) $5,000 in sale costs and a tax of (say) $8,500. You'd pocket net funds of $34,500 ($80,000 - $5,000 [sale costs] - $8,500 [tax] - $32,000 [initial mortgage repaid]). If you bought two more $40,000 properties at 80% finance then you'd need $20,000 (2 * 20% deposits + 2* closing costs) and have total debt of $64,000 ($80,000 * 80%) leaving you with $14,500 ($66,250 - $20,000) of unencumbered cash in your back pocket to fund further acquisitions.

Under Option One (refinancing) you have $7,500 more cash but $32,000 more in borrowings PLUS a conditional liability for paying tax and sale costs at a date in the future when you decide to sell.

Option Two (selling) delivers less cash but also less risk because you have significantly less borrowings. You'll also earn more cashflow because you have less interest to pay.

Dave and I chose Option Two and used our other positive cashflow investment properties to fund the cash shortfall. We were able to legally defer the payment of tax for up to fourteen months as properties sold on the 1st of July were not taxed until the following year's income tax return was lodged; the government essentially gave us an interest-free loan.

My point is this... just like there's a predisposition to negatively gear to save tax, there is a tendency to avoid selling because it triggers a taxable capital gain. Yet don't be afraid to sell - see it as an essential part of locking in profits and reducing your exposure to unexpected events.

As the property market softens it would be wise to review your portfolio and seriously consider selling properties that you feel are underperforming while there are still purchasers looking to buy. In our case, we sold of some of our larger deals (like a block of 21 units) that only other largish / serious investors would consider buying. Our belief was it's better to take a guaranteed profit now rather than being left with an underperforming asset in an inhospitable real estate market.

When I began investing I was under the illusion that I'd own all my properties forever. This seemed reasonable at the time, but as I grew in knowledge and experience I saw that in order to achieve my goals I had to realise 100% of my gains and then take those profits and either reinvest in bigger deals with higher returns or else transform one property into two using multiplication by division.

In case you're wondering - on the face of enough evidence to suggest the property market was near its top, Dave and I changed our goal in September 2003. Our revised target was $350,000 per annum in net (pre-tax) investment income and $1,000,000 in the bank.

Thanks to multiplication by division and spot selling to recycle profits, we were able to achieve this goal and even went out to lunch to celebrate.

If you'd like to make a comment or discuss this topic then please visit this forum thread.

Forum Post: The Best Learning Resource

This month's forum post comes from Coldy:

> Hey all,
>
> Excuse me - I'm very green in this game but also very eager. I'm just trying to learn what's the most effective learning resource on property investing for beginners, There are loads of books and I've been getting into Steve's book, "From 0 to

> 130 Properties..." (which is great) but what about seminars? Can anyone recommend an especially clear and inspiring one taking place within Melbourne?
>
> One more thing... I was just wondering whether it is legal to buy an apartment off the plan then sell it before completion. Thanks in advance. I'm finding the postings on this site very informative.
>
> Cheers,
> Coldy

I've picked Coldy's post as it raises the issue of wealth creation seminars, which has been a popular topic on the forums with American wealth creation expert Robert Allen in town.

Seminars are one of many ways to acquire 'up to the minute' relevant information. They are beneficial because you can gain a first-hand feeling for the presenter's message while also entering into a dialogue with experts and other attendees. In my seminars, I try hard to add a practical dimension to real estate theory by sharing examples of the way I invest and I also share ideas for how you can make immediate profits to recoup the attendance fee.

So-called 'get-rich-quick' or otherwise, it's reasonable to expect to pay up to $1,000 a day for a quality full-day seminar that includes meals, course notes etc. Just be mindful that the promoter doesn't pack the room to the rafters... I feel smaller numbers are better to ensure you get a chance to talk to the presenter and usefully network with other participants.

However, for all their good points, seminars are expensive educational resources. Often you can get a taste for the presenter from his/her other resources (books, tapesets etc.) that are priced more moderately. These are a great way to gain knowledge while also understanding more about a particular expert prior to forking out significant amounts of money to hear him/her speak.

Personally, I continue to routinely attend seminars to broaden my own investing knowledge. To gain value I make it a point to implement at least one idea gained from the event in order to recover the cost as soon as possible. Ultimately, seminars are only expensive for those who fail to use the information gained - for knowledge requires action to be effective.

Finally, to answer your second question - yes, you may legally resell your interest in a property purchased off the plan notwithstanding that it hasn't yet been completed. Be careful though, you might struggle to find a buyer as there may be more supply than demand and developers often discount in order to move sluggish stock.

Special Offer: WealthGuardian + An advance signed copy of my upcoming second book

Sadly, ignorance about the flexibility of our tax system means many Australians pay more income tax than they really have to. However, those who are properly structured not only legally minimise their tax, they also benefit from the peace-of-mind of knowing their assets are safeguarded too.

WealthGuardian is a fantastic resource that demystifies the complex topic of 'structuring'. It's an easy-to-read yet comprehensive guide (69-page workbook plus Audio CD) that you can work through at your own pace. It also includes a handy template to help you properly understand your current asset position.

Don't take my word for it... here's what previous WealthGuardian purchasers say:

> "I just received my copy of WealthGuardian... WOW! It's helped answer many of my questions and now when I go see my accountant, I can just tell him the structure that I want

which will save me both time and money! I thoroughly recommend this resource to all investors." - Ray C.

"Structuring is quite a complex subject and I'm really grateful that Steve and Paul have released a very useful resource that explains it in plain English. Thank you, guys!" - Rouvelee I.

If you want to minimise tax while safeguarding your assets then you'll really benefit from WealthGuardian. And here are two great reasons why RIGHT NOW is a great time to invest in this product:

1. Your window of opportunity to create (or change) your accounting structure is closing fast. Once the 2003/2004 financial year ends and 30 June ticks over, you will have missed the boat. This all means that you still have time to immediately benefit from the great information contained in WealthGuardian.
2. We are currently running a special offer to help PropertyInvesting.com members take control of their investing future by benefiting and profiting from WealthGuardian.

Our special offer is pretty simple... until June 30 (or earlier should our current stock of 63 units run out) we've knocked $70 off the recommended selling price PLUS we'll also send you a FREE copy of 'Tales from the Trenches' (an insightful 4-tape audio cassette package of Steve McKnight interviewing four successful property investors (value $95)).

Furthermore... **the first 10 buyers will also receive a personally signed and dedicated advance copy of my upcoming second book the moment it comes off the printing press** (currently expected to be ready in early October).

So, if you're quick to act, not only will you benefit from all the fantastic information in WealthGuardian (which we'll ship immediately), but you'll also be one of the first in the world to receive a copy of my upcoming second book which takes you deeper into the realm of achieving financial independence via positive cashflow property investing.

At just $225 (plus postage and handling), I'm sure you'll agree that this truly is a special offer. Find out more or purchase here.

Summary

Don't be afraid to take profits while you still can because an asset underperforming in a boom market will more than likely turn into a liability during turbulent times. It may be wise to sell why you still can and certainly don't be fooled into believing there'll always be a buyer willing to pay your top-dollar or "best case scenario" price.

Dave and I made a point of regularly spot selling properties using our 'multiplication by division' principle. Sure, selling triggered sale costs, income tax and additional closing costs as we bought back in, but selling allowed us to use profits rather than debt to fund expansion. Not only was this a less risky option, it allowed us to keep borrowing and to demonstrate (via tax returns) that our investing approach was profitable.

Seminars are a great way to broaden your investing knowledge but they can be expensive. Still, you'll end up ahead provided you gain and act on one piece of information to recoup the attendance fee.

Right! That's it for this May 2004 edition of Insider. I sincerely hope that you've been able to profit from the insights outlined in this resource. Until next month remember - *success comes from doing things differently!*

Sincerely,

Steve McKnight

P.S. Don't forget about the special offer we have on WealthGuardian for just $225 - a saving of $70 PLUS you'll receive Tales from the Trenches FREE + you'll receive an advanced signed copy of my upcoming second book (ready in Oct) FREE! Make your purchase now!