THE CYCLE OF WEALTH

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INTRODUCTION

You have purchased a highly informational e-book to aid you in the process of finding and analyzing real estate investments, things to do before you get started, costly mistakes and how to avoid them and most importantly how to make real estate the profit center of your business. This manual was designed to show you the process of creating the cycle that will ultimately create wealth and give you financial freedom.

A word to the wise. Investing always carries with it an element of risk. I suggest that you consult with your CPA's, Legal Advisors, Real estate professionals and any other competent professional knowledgeable in the area of real estate investing before you attempt to try any of the techniques in the manual. Thank you.

OUTLINE

ACKNOWLEDGEMENT!

I would like to personally thank my family for their love and support throughout the years. They have been there for me through thick and thin. I would also like to thank my best friend and business partner Daniel F. Porter for encouraging me in the direction I’m going, for his friendship, loyalty and steadfast dedication. He is truly one of the greatest people I know. Lastly, I would like to thank my clients and business associates for the trust they’ve placed in me and for making my career one worth having. It has been a pleasure working with all of you.

WHERE DO I BEGIN?

The first step is always the most difficult. It is in this step that you will need to acquire the necessary knowledge and begin to lay the foundation of a successful business. It is not always easy and it certainly doesn't happen overnight but the good news is in the fact that once it has been created you can start the process of building wealth. It is important to remember that wealth is measured in time rather than in money. If you were to stop working today, how long could you survive?

Now we get down to brass tacks. Here is where you need to go through all of your finances to determine where you are today. You need to first list all sources of income, from your job or business, dividends, passive income from real estate, etc. Once you have your income listed per month from all sources you will need to figure out all of your expenses. Taxes, monthly payments on credit cards, car payments, mortgage payments, child support, utilities, etc. all the way down the list. Next you will need to list your assets. Now understand that an asset is (for our purposes) going to be defined as something that puts money in your pocket each month. So understand that we will not be listing your personal home as an asset, or your car. What we can list are stocks, savings, income producing real estate, royalties, businesses that make money without you (i.e. franchises, multi-level marketing (in some cases), etc.) Then you need to list your liabilities: full mortgage amount, full amount of credit card debt, total amount of student loans, amount owed on any vehicles. Even list the mortgage balances of your income properties.

Once you have those numbers (and be careful to categorize each credit or debit as income, expense, asset, or liability) then you need to total all passive income and put that as the top balance. (Remember passive means you don't work for it) Under that place your total income. Next go your total expenses and then your cash flow or what is left after expenses.

Congratulations! You have just created your personal financial statement. You can now see at a glance your overall financial position. You may find that all of your money goes to paying expenses. Later we will discuss how to fix this problem. You may see that your money is going to pay for your luxuries (i.e. cars, jewelry, vacations) or that you put your dollars to work for you in the investment/asset section of your financial balance sheet. This is where we want you to be.

So what if you are in the first category where your money is coming in and exiting straight through your expenses leaving very little to live on and nothing to save or invest? There is hope. Once you learn the principals of creating wealth you can become wealthy no matter what your situation. Do you remember the saying, "pay yourself first"? This is the fist principal to achieving financial freedom. Take 10% of your earned income and place it into an investment account. If you can, match it in a separate savings account. It may be that you need to create a budget. You've already listed all of your expenses and subtracted it from your total income. The amount left over, your cash flow, is where you take the 10% (or more) from. This will help you to "get a grip" on your finances. Think of it like an expense and learn to budget that 10% like you would any other monthly bill and you will get closer and closer to becoming wealthy. Remember, it's not what you make but what you keep that's important. Next you will need to evaluate your debt. Do you have good debt or bad debt? There is a difference. Not all debt is bad. If you have debt that you've used to invest in an asset (remember the definition of an asset) that is good debt. If you are making payments on a big screen TV, that would probably be considered bad debt. Bad debt is all we are concerned with.

So how do you move forward from here? You know where you're at, you understand which debt you will need to eliminate. Now you need to know how. Do I pay a debt off or purchase an asset? Here is the first of our formulas. This formula will help make this decision black and white. Here it goes.

Let's say you have a credit card with a $2000.00 balance and a minimum payment of $40.00/mo. @ 15.78% interest and an asset you can purchase that gives you a net cash flow of $30.00/mo. with a $2000.00 investment or down payment. Which makes more sense to do?

First figure out the ROI (rate of return or cash on cash return) on the investment. Here's how:

$30.00/mo. X 12 mo. = $360.00/yr.

$360.00 / $2000.00 investment = 0.18 or 18% ROI

Now we analyze the credit cards RROI (reverse return on investment) Here's How:

$40.00/mo. X 12mo. = $480.00/total payments a year

$480.00/ $2000.00 investment = 0.24 or 24% RROI

So in this particular instance the credit cards RROI is greater than the assets ROI so you should pay off the debt. If it had been the other way around, and it often is, you should purchase the asset and let the asset pay for your debt. In the case above that investment would have more than likely been a real estate rental property. Although the numbers may have been slightly different depending on your location, the current market, etc. you can see how to determine whether to pay a debt off or acquire more debt to purchase a positive cash flow property and let the properties net rental income pay for the debt. (Net = Gross income – expenses)

Now you know where you are. It's time to make a plan for financial freedom. Familiarize yourself with the power of goal setting. Set goals that are obtainable but that will cause you to learn something new or step out and do something outside of your comfort zone. Set goals that encourage you to grow as an individual. As soon as you stop growing you become complacent and begin limiting the amount of success you can achieve and the person you could become.

One goal may be to retire ten years earlier. Another may be to support a ministry. The main thing is that they are your goals. You also need to know the "why" behind the goals. If you don't know why you've set a goal you are far less likely to fulfill it. Maybe spending time with your family is what motivates you to achieve financial freedom. Again though, these are your reasons.

Goal setting is extremely important. When a study was done on a graduating class at the esteemed academy of Yale, it was discovered that the three percent of students who set goals and committed them to paper actually outperformed the other ninety-seven percent in most areas of their lives.

Goal setting is powerful, but left alone is little more than good intensions often to be compromised or even forgotten. You need to create a plan to achieve those goals which have reasonable time frames attached to them. You need to not only determine the "why" but also the "how" of the goal. If your goal is to purchase a rental home in one year you may decide to save the 10% we talked about earlier until you have enough for a small down payment. You may have another plan to eliminate two-hundred dollars a month worth of monthly payments by selling your second financed vehicle and apply that two-hundred toward this rental purchase. You may decide to build credit over the next eight months to later obtain a more favorable loan for your rental property. We will discuss some ways of doing that later on. This is the second most crucial step to achieving the success you desire, goals being the first. Next, the plan.

ESTABLISHING YOUR BUSINESS!

What if I have bad credit? This is a common question and a very good one. I am a firm believer in being credit worthy. Unfortunately people, usually out of ignorance, abuse credit. Just remember, if your credit card limit is five thousand dollars and the most you can afford to spend (if you were purchasing an item with cash) is fifty dollars a month, it does not mean that you have five thousand dollars. Compound interest is probably the most incredible formula known to man. Don't abuse it or it WILL bury you. Just because you can afford the minimum payment on an item does not always mean you can afford to buy it. If you do this enough times and you are downsized, fired, get sick or hurt and can't cover the payments they will destroy you financially. This is one of the leading causes of bankruptcy which has become a very popular way of not taking responsibility for your actions. My thoughts on bankruptcy are that it may be necessary but only as a last resort. You took the responsibility of getting yourself in this position; you need to take the responsibility to get yourself out. With that said, credit can also be your most powerful tool in creating wealth. Leverage, if used responsibly, can be the quickest way to build wealth.

So how do you build or restore credit? Credit needs at least six months of "on time" payments and usually three or four reliable sources reporting positively to the credit bureaus which I will list later on with their addresses. If you can't seem to get approved for credit cards unsecured you may want to try a secured card. They are more expensive but will help build credit. Cell phones are usually not the best source for building credit. The best credit reference is a bank. Call three separate banks and ask them what their lowest installment loan is. Let's say they are all a one thousand dollar minimum. Either purchase three CD's or open three passbook savings accounts in that amount one for each bank. Then ask for an installment loan in that amount secured by the accounts or CD's. When you receive the checks, make a payment a week for the first month on each loan with the money you've borrowed, then on time each month again for a minimum of six months until they are paid off. Once they are paid off, wait a few months and repeat this process. After the second time take the money from two of the banks and close the savings accounts. Open a checking account at the bank with the remaining savings account. Apply for overdraft protection. By this time you should have credit card applications pouring in. Wait another month or so and ask to borrow a thousand dollars unsecured. As long as you have remained current on all payments and paid the previous loans promptly this should not pose a problem. You are now looking good with three positive credit lines all reporting in your favor. Banks, no less, which as before mentioned are the best references. Coupled with a reasonable down payment, you may be in a position to obtain your first loan to purchase investment property.

The second step in developing your business is to build a team of professionals to whom you can seek advice pertaining to all aspects of your business. Do not make the mistake of thinking you are being smart and saving money doing everything yourself. I can't begin to tell you how many times I've seen people lose a dollar trying to save a dime. Hire competent professionals, CPA's, brokers, legal consultants or attorneys, financial planners and the list goes on. Their fees are so small in comparison to what they can save you in both time and money. Don't think you can be all these things yourself successfully. There just isn't time enough in a day to fill all these needs yourself. Trust me on this. You will be far better off if you do. Let these people know the goals you've set and the plans you've made. They will advise and support you in these things. If they don't, FIND SOMEONE ELSE!!!

Lastly, make sure you tell people you are in business. If you get the word out there that you are looking to purchase homes, you will find homes. Don't be afraid to compound your effectiveness by using other people's eyes and ears in addition to your own.

LOCATING INVESTMENT OPPORTUNITIES!

So you're ready to start the reason you began this whole process. I think it's important at this time to point out that there are many, many types of investments you can make. There are many kinds of stocks and ways of purchasing stock (i.e. margins, options, shorts, etc.). There are many other investments such as commodity trading, mutual funds, gold, and real estate Although they are all great investment strategies, real estate is what we will be focusing on for the purpose of this manual specifically because when a survey of millionaires was conducted, it was discovered that the vast majority of them either created their wealth through real estate or hold their wealth in real estate. It is also the investment vehicle that I am most familiar with in being both a licensed real estate agent and investor.

One of the most reliable sources of leads for investment opportunities can be a broker whether for stocks, commodities or real estate (if the agent is good and doesn't simply "hold" a license). Another is by searching the local newspaper. Websites are also a very popular search method. If it's not on the internet it is possible that it simply doesn't exist. You may also get a copy of the local tax roll. The tax rolls are of public record and many of them have phone numbers. Call and introduce yourself as a real estate investor wondering if they'd consider selling the property on the tax roll. Many scripts are available out there for this purpose. You can advertise in the paper "We buy houses" or "Investor seeking multi-residential property." One more and probably my favorite is to simply take a weekend, pick an area and drive up one street and down the next. Maybe park and walk your dog through a neighborhood you're interested in. What are you looking for? Real estate signs, For Sale By Owner signs, vacant property, rundown property that could be fixed up with paint and minor repairs, etc. Be creative. Successful people create more opportunities than they find. And simply put, luck is "When opportunity meets preparedness." Dolf DeRoos, a highly sought real estate investor/genius says, "The deal of a life time comes along about once a week." They are out there. At the end I am going to suggest a few books which are the foundation of my education and will expound on the points in this e-book. Don't let your education stop here. Never stop learning new things.

The next great thing to remember is that selfishness will bring you very little return. Find other investors. Work with them, learn from them and if a deal that you find will not work for you or does not make sense for your personal financial position or is not in line with your plan, pass it on. In return you may develop a never ending stream of leads and information based on others' experiences which may be the most valuable educational tool that you have. Others who have the same vision and passion are going to keep you focused and on track to achieving your own goals. Also, the more you can give to others the more that will come back to you.

THE CYCLE OF WEALTH!

Now it gets exciting. Here you will learn how to take what you earn and make it work for you instead of you constantly working for money. This is the chapter which caused me to right this e-book for you. Understand that there are whole books written on each section of each chapter of this e-book. This will give you an overview and hopefully a basic understanding of the process you will need to research and learn. This truly is only the beginning. The more you learn the more opportunities will begin to appear to you.

Here's the cycle of wealth. Earned income from your job (we are talking about what's left after all expenses, your cash flow) gets saved and then invested into assets (i.e. real estate, stocks, bonds, etc.) and turned into passive and portfolio income, passive being real estate rental income or money you don't work for, portfolio being income from paper assets in the form of dividends, etc. Then the passive income goes back into your investment account which goes back into assets, which buy more assets, which later pay your expenses which were listed on your financial statement and then as they continue to increase they buy your luxuries, your cars, your big house, TV and vacations. The best part is that because this is money that your money is earning you, you are not bound by your job because you can't afford to not work. Remember when I said wealth is measured in time not money? There it is. Each month your assets pay your bills, buy your luxuries, and buy more assets thereby increasing your wealth further. This is a compounding cycle much like the principle of compound interest. Your money makes more money which makes more money. An example of this might be for instance, let's say you have fifty thousand dollars to buy a BMW. Instead of buying the car, put the fifty thousand into an asset in the form of a down payment on a rental property which will produce five hundred dollars a month positive cash flow and let the asset buy your car. This way you still have the fifty thousand (in the form of available equity), you have a property which will appreciate in value plus give you added tax benefits and you will have your BMW. Picture this cycle as a circle being drawn which slowly gets larger and larger until it begins to exceed the borders of the paper being drawn on. This is the cycle of wealth. Think it, learn it, do it and you will become wealthy and if desired eventually you can become rich. I don't have a definition for rich. I'll leave that up to you.

Once you begin increasing your net worth and the income coming in to you, the “tax man” is probably going to be a concern for you. Keeping the money you make is often harder than making it ever was. There are many “legal” loop holes that are utilized by the rich that are often times not available or maybe simply overlooked by others. Some of these tactics may include the use of a IRC 1031 “Tax Deferred” real estate exchange to maximize your available equity and use the money you would otherwise pay taxes on up front, to increase your purchasing power. Another may be to incorporate or set up a real estate trust to protect your assets and filter expenses through the corporation in order to take additional write-offs and keep more money. These two examples are only the tip of the iceberg and in order to use them effectively advanced learning in these areas is important and probably unavoidable. Also, seek professional advice before making any decision that you are not fully competent to handle.

RULES TO INVESTING!

The following “rules” are nothing more that guidelines that I personally like to use. They help you to think through a decision and not act impulsively. They are by no means “set in stone” and there are always exceptions to every rule. They may help you avoid a costly mistake.

Rule #1. No Negative Cash Flow.

The reason for this is that you never want to put yourself in a position where you “have to” sell. There may be times when you do have a negative cash flow property but this can quickly begin to eat at your finances. An example of this might be a “flip-it” deal, where you can buy and sell quickly to create some quick capital gain. Another might be if the rents are low and can easily be raised to a point where the property becomes positive. As a general rule of thumb though, positive property supports itself and puts money in your pocket. Long term ownership is the best way to build net worth and passive income. You can refinance and free some equity without selling if you need to.

Rule #2. Never sell.

Again, an exception might be, if you can take a $200/mo. cash flow and “exchange” (through a 1031) up to a property that will produce a $600/mo. cash flow and increase your cash on cash return, then selling would be wise but it is really considered “exchanging.” There are probably other “good” examples but again, as a general rule of thumb, don’t put a time limit on your ownership of real estate. Refinancing will also free some of your available equity without selling the property. If a property is making you money, why sell it?

Rule #3. No Balloon payments.

Let’s say you have a balloon payment that is coming due in a year, you had planned to sell the property before this came due, (remember rule #2) but the market is now depressed. You can’t sell the property for what you’d like to get but the balloon is more than you can afford. Now you are forced to sell a good asset at less than you would like to. Well, can’t I just refinance and pay it off that way? Maybe. I’m sure that was part of the thought process when you bought it. But if the market is depressed that may be due in part to high interest rates. What if the higher interest rate causes you to loose your positive cash flow therefore breaking rule #1? Is there a time when they are ok? Of course, but think carefully before you do.

Rule #4. No Variable interest rates.

Much for the same reason as rule #3. Everything is great now but if interest rates are low now and then go up to the point where the property is no longer positive… Again, there may be exceptions. Be careful and plan well though.

Rule #5. Get good tenants.

If you have to collect the rents with a gun or if you have to call the sheriff every month than the hassle of owning the property will probably exceed the joy of owning it. Don't get me wrong, there are great deals in bad areas but again, think it through and be careful.

One other point I feel is noteworthy is that of creative financing. I am not going to go into detail or lay out techniques to do this. There are entire books dedicated to this topic alone. They do work but can be extremely risky. I have found that you are often forced to give up a few things in return for them to work. No money down can be especially dangerous. Make sure you disclose everything you are doing and probably your intentions after you buy it. It is for these techniques that I created a system for myself with rules to follow. If a creative financing or no money down technique will cause me to break one or more of the rules, it may not be a good idea. Also, no money down deals are done all the time but the people who do them successfully on a regular basic are usually people who have a substantial cash reserve to back the deal incase the deal were to go bad on them.

FREQUENTLY ASKED QUESTIONS!

B*=Buyers*
S*=Sellers*

B

When is real estate investing risky?

As in all investments there is always some element of risk involved and usually the higher the risk the greater the return. This risk can be minimized by the level of knowledge you acquire about the investment you are making prior to making it. Retaining honest, knowledgeable professionals to aid you in the process can also prove to be a tremendous asset to you. There are instances where it may not be wise for an individual to invest. For instance, if your investment's success hinges on a strict time frame you may consider another investment. Also, I don't recommend "over leverage" meaning 100%+ leverage because it leaves, in most cases, virtually no room for error. I also don't suggest purchasing properties with substantial negative cash flow, balloon payments or variable interest rates unless you are in a position to weather the storm should the market turn against you. Gambling is not calculated risk. Keep in mind that sometimes a good investment for one person may not be so good for another. Bottom line is to know enough about what you are doing to make an educated decision. Don't speculate but rather analyze data and facts. Be careful not to put yourself out on a limb emotionally or financially and don't base anything off of opinion or wishful thinking alone.

B

How much money do I need to start?

The answer to this question is really based upon your goals along with your present situation. What are you looking for? Tax benefits? Cash flow? Equity build up? Capital gains? Or is your ultimate goal financial freedom? In a lot of real estate investments you can achieve all of these things at least in a small part but some investment are geared more specifically toward one benefit over the others. Personally, I recommend somewhere between 10%

and 15% down on a residential property and at least 20% for a commercial investment. There are techniques and in fact entire books written on "no down payment" real estate purchasing and it is possible. I still highly recommend some kind of a down payment. Leverage is a key element in building wealth through real estate but over leverage can at times be dangerous.

B

Why would I invest in real estate rather than in some other investment vehicle?

In my opinion real estate is by far the best wealth building vehicle available. Not only can an investment in real estate feed you through a low taxed passive rental income each month but you also have equity build up and depreciation write offs. Typically, real estate appreciates faster than the rate of inflation. Real estate is usually very stable as well as tangible unlike paper assets (i.e. stocks, bonds, etc.) and you can utilize the principle of leverage to maximize the cash on cash return on your investment. Another benefit is that there are literally hundreds of ways to increase the value of your investment and you can free your equity up to make other investments without selling the property. If you do sell you have the option of deferring the payment of taxes "legally" through the use of the IRC 1031 "Tax Free" exchange (a.k.a. Starker exchange) so that you can transfer "tax deferred" all of your equity into a larger, more profitable investment property allowing you increased purchasing power. I have found that with all these benefits combined, real estate drastically out performs every other investment vehicle available. These are but a few of the many benefits to investing in real estate. Others may include things like pride of ownership, income shelters and providing a service such as housing to a community.

B

It seems impossible to find properties where you can get a positive cash flow anymore. What do I need to do in order to gain a passive income from my real estate investments?

In order to solve this problem often an investor is forced to invest in an unfamiliar market and often times even outside of their home state. Obviously, the ability to read markets is key in this decision making process and the analyzing of many investment opportunities is always the best way to educate yourself in order to make a smart purchasing decision. Is there risk? Always! Is there an advantage to this investment strategy? Yes! If the proper research is done to ensure that the investment you are making is a wise investment then the advantage can be substantial. The reason for this is simple because although in Northern California the market for multi-family apartment buildings may be at a peak and certainly would not be the best time to buy, San Antonio TX or Philadelphia, PA may be in a down but recovering market making a purchase there far more lucrative. This is the only way to eliminate "most" of the market trends investor's deal with. There should also be management fees figured into the expense column during the numbers analysis phase allowing someone else close to the property or even on site to manage the entire project for a very reasonable fee.

S

When should I sell my investment property?

If your cash on cash return is low and definitely if your losing money. These are signs that it may be time to trade that property up to a property with a substantially higher rate of return. Sometimes in order to accomplish this, an investor is forced to invest in an unfamiliar market and often times even outside of their home state. Obviously, the ability to read markets is key in this decision making process and the analyzing of many investment opportunities is always the best way to educate yourself in order to make a smart purchasing decision. Is there risk? Always! Is there an advantage to this? Yes! If the proper research is done to ensure that the investment you are making is a wise investment then the advantage can be substantial. The reason for this is simple because although in Northern California the market for multi-family apartment buildings may be at a peak and certainly would not be the best time to buy, San Antonio TX or Philadelphia, PA may be in a down but recovering market making a purchase there far more lucrative. This is the only way to eliminate "most" of the market trends investor's deal with. There should also be management fees figured into the expense column during the numbers analysis phase allowing someone else close to the property or even on site to manage the entire project for a very reasonable fee.

(Cash-on-Cash rate of return is Net Operating Income less Debt Service divided by Equity EXAMPLE: A property's Net Operating Income is $100,000, with a Debt Service of $70,000, giving a Cash Return of $30,000. The owner's Equity is $150,000. Cash on Cash rate of return = $30,000 divided by $150,000 = 0.2 or 20%)

S

What should I do in order to make sure that selling my property is a worthwhile move?

The absolute first thing you need to do is to set up a net sheet and figure all the costs of selling to determine how much equity you will have left to reinvest. Next, I suggest that you talk with a qualified real estate 1031 exchange company to see if you can trade your equity into a larger investment "tax deferred." Once you have optimized your equity and positioned yourself to make the most of your available equity (now including what you would have paid in taxes) you are then ready to identify the next investment.

S

Should I sell my bare land to purchase an improved property?

Again, it depends on your goals or what you plan to do with the property later on but if you simply plan to hold the property I would have to say "yes". "Buy land, they ain't makin' it anymore." This is in some circles a very popular saying, and it's true no doubt. However, I have never seen an improved real property that was not affixed to a piece of land and usually the land is at a cheaper price than if it were to be purchased separately. Below is a chart that shows how the two properties perform next to each other over time. This is only an estimate and is not necessarily reflective of all cases. It is simply for instructional purposes only.

	Bare Land	Improved Property (Single Family Rental)
Present Value	**$100,000**	**$100,000**
Appreciation Per Year (Estimated Example)	**3% @ 20 years$80,611**	**3% @ 20 years$80,611**
Gross Annual Income	**0**	**$7,200**
Annual Depreciation	**0**	**$2,500(x 37%)**
Approximate Property Earnings Potential (20 yrs)	**$180,611**	**$374,611**

CREDIT REPORT!

TransUnion
P.O. Box 390
Springfield, PA 19064-0390
800-916-8880

Equifax Information Service Center
P.O. Box 105873
Atlanta, GA 30348
800-685-1111

Experian
P.O. Box 2104
Allen, TX 75013-2104
800-643-3334

SUGGESTED READING!

"Rich Dad, Poor Dad"- Robert T. Kiyosaki

"Real Estate Riches"- Dolf De Roos, Ph.D.

"The Art Of The Deal"- Donald Trump

"Unlimited Riches"- Robert Shemin

"No Money Down"- Carleton Sheets

"Think and Grow Rich"- Napoleon Hill

"The 7 Habits of Highly Effective People"-Stephen R. Covey

NOTES!