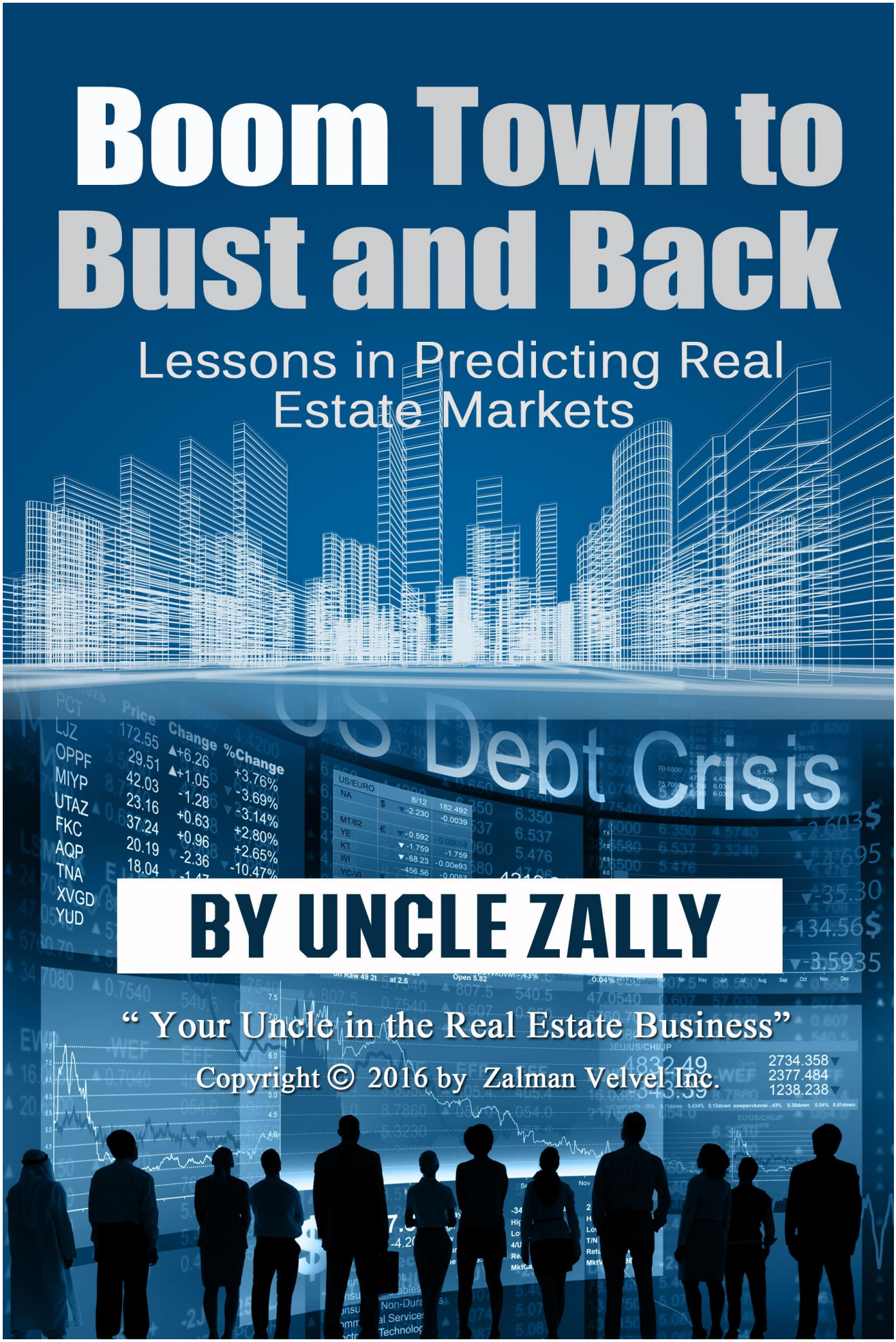
# Boom Town to Bust and Back

## Lessons in Predicting Real Estate Markets




**BY UNCLE ZALLY**

" Your Uncle in the Real Estate Business"

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## Acknowledgements

I want to thank my family and co-workers for encouraging me to write this book, the two Stevie's, The Deal Doctor and Nephew 9 Cup, and nephew Aran.

I also want to thank Rudy, who challenged me to make this better.


## Dedication

**This book is, once again, dedicated to the true wealth in this world - our loved ones.**

# Forward


It's November 2013, and I'm sitting next to Steve McKnight on a Virgin Australia flight. We're heading back from the last leg of our book signing tour.

Steve is considered ***the*** expert on real estate in Australia, the "guru." He has a website with over 100,000 members, and he wrote the number one bestselling book on real estate there. He generously agreed to share writing credit with me on his newest book, Millionaire.

Steve and I had just completed a two hour presentation in Adelaide. We previously conducted similar sessions in Sydney, Melbourne, Brisbane, Perth, and Canberra. Steve began each presentation with a "market update," which I followed with a funny seminar on negotiation techniques. Steve then closed with an invitation to join him in the Fund he managed which invested in commercial real estate in the United States – which he considered the best opportunity on the planet.

Then we signed books ... lots and lots of books. More than 2,000 of 'em.

Believe me, I was well aware that it wasn't my signature that was coveted, but Steve's. He is a riveting speaker, and exudes integrity, which is a rare quality in the real estate seminar industry.

However, it was the "market update" portion of his presentation that interested me now on our flight back together. It detailed what the local real estate markets did in the last year, and what he predicted they would do in the coming year. I asked him to explain in greater detail how he arrived at his conclusions.

Normally, I wouldn't have paid much attention to what I termed "crystal ball" observations. During the first 20 years I had been investing in the United States, I didn't think predicting real estate markets was possible, or even necessary. My family had a ***foolproof system*** for making money in real estate.

Then we were thrown for a loop in 1999 until 2012.

Starting in 1999, and continuing for seven years, there was no other time that real estate market went **up** so quickly. It became a Boom, and we experienced the joy of making easy profits. All you had to do was buy something, and the next day it was worth more. It reminded me of Curt, a friend from high school, who said, "I can't wait for tomorrow. I get better looking every day."

Just like Curt, we awoke every day while the real estate market boomed, excited to be creating Financial Independence (perhaps we were a ***little*** better looking because we smiled so much.)

Then, for the next seven years, there was no time when the real estate market went **down** so quickly, and became a Bust, a part of the Global Financial Crisis. We experienced the pain of losing half the value of what we earned after 30 years of investing. We awoke every day, after the real estate market crashed, fighting to get back what we lost, while still holding on to what we had. Those times were not like Curt – it got uglier by the day.

We learned we were right at the center of one of the best and worst areas where all this took place: Fort Myers/Cape Coral, Florida. We became known as Ground Zero during the Bust that followed the Boom, because our real estate market felt like a nuclear bomb went off in it.

After listening to Steve's market updates, I was determined to study what happened in the U.S. market, and in Fort Myers/Cape Coral in particular. I wanted to know what the signposts of wealth and danger were, so if it ever happened again, I would be prepared, along with my family. In a way, we were lucky, because since we were at Ground Zero, what happened in our area was magnified, enabling us to see more easily what the signposts were, and then pass them along.

Wait a minute. I jumped right in without introducing myself. Sorry, I get that way when I am excited about something.

I go by the nickname of Uncle Zally. Think of me as your uncle in the real estate market.

I wrote this book to help you, my adopted nieces and nephews, who want to invest and profit from real estate.

***You will find this book is unique among real estate books.***

**It will show you how to Predict what your Real Estate market in the United States is going to do before it does it. It will give you the signs of wealth, so you can become Financially Independent. It will also give you the signs of danger so you can protect yourself.** The signs are a combination of supply and demand, economics, and human emotion. If you're not in investing in the U.S., you can adapt the method to your own real estate market. The method is adaptable.

It should be a great benefit to you because any time you can obtain wisdom about the best that can happen, and the worst, and know when the best and worst are getting ready to happen, that is extremely valuable information. **You will be able to double and quadruple your net worth faster than at any other time in your investing career - if you are aware.**

**If you are unaware, you may very well become a victim** of a Bust or Global Financial Crisis, which will send you back to square one, or worse, minus one, known as bankruptcy ... which many people were.

**Speaking of getting sent back to square one, do you know that more than 9 million homeowners lost their home during the 10 year period after 2005?**

If they had this book, they would have known the signs that indicated the best, and worst, were about to happen. They would have had strategies to reap huge rewards, and then shield themselves. That's what your Uncle Zally wants - to teach you, excite you, motivate you, and also **protect** you.

I am going to begin this book by offering you a healthy lifetime goal, Financial Independence, which will lead you to a happier, more secure life.

Then you are going to receive a simple, commonsense lifetime investing strategy, which involves Keepers and Flippers. **It is virtually foolproof in Steady Markets** … and will be illustrated with easy to understand examples.

It's essential, however, that you must first learn where your real estate market is in the market cycle that all real estate markets go through. If you buy or invest at the wrong time, you can capsize and sink, like 9 million did before you.

You will learn, like the Kenny Rogers song, The Gambler – "when to hold 'em, when to fold 'em, when to walk away, and when to run." The signposts will be on

a list I created for you, with large print for you to copy and put on your office wall. I don't want you to ever forget them, so don't you dare thumbtack a picture of your favorite movie star or rock star over it. (Next to it is okay. It will hold your attention.)

There are three groups of people who need to know what lies in the pages ahead.

**The first group are already life long real estate investors and want to expand their horizons**. They want a reference book to go to throughout their investing career to check out the current signposts of a Boom, or a Bust, and to take the appropriate actions to multiply their wealth, or to protect themselves. Mortgage lenders fall into this group. They need to know when it's too risky to lend.

**The second group are the Newbies, first time investors**, interested in real estate, who have never invested before. They are concerned because of the recent Boom and Bust and don't want to get trapped. They will now be armed with the best information for a lifetime of real estate investing, to help them make the most profit, and protect them from dangers like a Global Financial Crisis.


**The third group this book is intended for are the nine million homeowners and investors that lost their homes or real estate investments during the Global Financial Crisis**.

It is estimated only a third will lick their wounds, get back in the race, and own another home. The other two-thirds will be locked out of home ownership for a long, long time. I would like to improve those statistics, and I will show you in Appendix III how to own your next home at a greatly reduced cost, with financing that is ***forgiving,*** even with ruined credit.

For those of you in the third group, once you are re-established in a home, you need to start again on the road to Financial Independence. Real estate is the easiest and fastest way to do it, even with little credit and cash. You need to buy investment property again, and you can, even with your checkered credit history and little cash. Uncle Zally will to help you get back on your feet again.

**BUT**!

You must be protected in the future from falling into the same traps that sent you back to square one in the past. That is my goal, and I take it very seriously.

Now, perhaps you are wondering, "Why doesn't Uncle Zally just close his word processor (and also his mouth) and keep this valuable information for himself?"

One simple reason: I want to leave the world a little better place than how I found it. I enjoy it when people read my writing, use it to benefit their lives, and send letters and emails thanking me. All I ask in return is that you name your first million after me, like you would a newborn child. Call it your "**Uncle Zally Million**."

I've also added a little "special sauce," like a Big Mac.

In addition to being a successful real estate investor for 35 years, I have trained more than 5,000 people from all over the world, during the last 20, how to invest in real estate.

In order to do this, I had to hold people's attention for 3 days straight, 8 hours each day, while I was training them. This was not easy to do considering I had college professors who put me to sleep after 15 minutes in one of their lectures.

How did I learn how to hold people's attention? By watching them yawn. When they yawned, and I could see the results of their expensive dental work, I knew I was on the wrong track. The right track was directing all the training toward creating wealth, which I will continue to do in this book.

I also learned to pepper my classes with questions to make people think for themselves, to become independent.

**I will, during the pages that follow, propose questions, then ask you to close this book and think about the answer**.

Please do yourself a favor and don't cheat – think about how you would answer, before I give it to you.

The final tactic I learned on how to hold people's attention was by **being funny**.

I learned about funny from a friend of mine, a professional comedian who did standup comedy for 38 years. We wrote routines and jokes together, and it was some of the best time I ever had while writing.

Because of that, your Uncle Zally morphed. I learned to enjoy making people laugh while imparting wisdom about wealth. I did this on the book tour with Steve, during my funny seminar on negotiating. I was told, point-blank, "If I taught a little less, and make the audience laugh a little more, it got better results."

They were right.

Don't worry, this is not going to turn into a joke book. It's not going to be rip roaring funny, because in order to do so, I would need to exaggerate - exaggeration is a large part of comedy. I want to give you the truth, the "straight skippy," and not bend it or exaggerate just to make you smile. Our goal together is serious … but there's nothing wrong with using comedy once in a while as a refreshing breeze while learning. It will energize your mind so you can absorb information more easily.

Okay, enough of the introductions. It's time to begin. Nephews and nieces, I'm going to take you by the hand and guide you through some new ideas. Few things are as exciting, or as scary, as a new idea.

Please get comfortable while your Uncle Zally shows you the Signs of Wealth and Signs of Danger while you become Financially Independent in real estate.

These lessons will benefit you, and your loved ones, for the rest of your life.

# Chapter 1

# The Goal – Financial Independence


Financial Independence is a goal most people desire, but few know how to achieve.

First, what is it?

I have discussed this with people from my training sessions. Most answers were basic – Financial Independence meant owning your home free and clear, without a mortgage. In other words, no house payments.

Oh … and also having a new car that was paid for – no car payments.

Oh … and having enough money for bills and a few luxuries, so you didn't run out of money before you ran out of month.

The list continued to grow.

Oh … and savings accounts for your children's college education, and a retirement account that would cover you during your golden years.

The ones that dreamed the biggest defined Financial Independence as:

**Never Working Again**

Money was supposed to come pouring in each month from their investments, whatever they were – real estate, stocks, bonds, hedge funds, the Internet, franchises, business, etc. - and all they had to do was deposit the checks in the bank, then play around and travel 24/7 for the entire month. They would spend it all just in time for the new checks to come in the next month, so they could play around and travel some more.

Is there something wrong with that picture?

You bet there is!

It's the belief that work is bad, a drag, a waste of time, and the best thing to fill your life with is playing around, doing whatever your heart desires, with no restrictions.

Well, your Uncle Zally is going to suggest something radical now:

**Work is good for you**.

**Yes, and even a little struggle is good for you** – it will make you into a better person, an improved person, who feels proud of overcoming challenges.

**Best of all, having a fulfilling career is good for you**.

Studies have shown that working well at a career you enjoy will make you live longer, and feel better about your life.

Here is some more radical information:

Many of the people who never work and have large inheritances, or endless cash flow with no effort, turn to alcohol and drugs to produce the feelings they are missing from using their mind and talents to improve the world and themselves with a challenging career.

So let's establish a definition of Financial Independence, for purposes of this book:

**Financial Independence is creating a comfortable secure life for yourself and your loved ones, while you work at a career that energizes you, challenges you, and keeps you fit and happy.**

The full time career you choose may or may not involve real estate. That's okay. If your career makes you happy and fulfilled, but doesn't provide enough money, then you can use the information in this book to help you earn the extra money you need for your lifestyle. In that case, real estate will be an investment, a part time avocation, not a full time career.

It's more efficient, time wise, to have real estate as both a career and an investment path for Financial Independence, but it's not absolutely essential to your happiness or well being. You can do both.

How do I know?

Because I've trained religious leaders, artists, actors, writers, poets, dancers, singers, musicians, teachers, etc., who loved their careers, wanted to keep them, but needed more money than their careers provided to obtain Financial Independence. I showed them how to achieve their monetary goals investing in real estate, in their spare time, because they knew that real estate was still the easiest way to do it, especially if you start out with little credit and not much money.

How about a cute story about how my own definition of Financial Independence evolved?

When I was a single man in my early 20's, Financial Independence meant not having to wake up and go to "work." It meant turning off the alarm clock, rolling over, going back to sleep, then waking up when I felt like it and going to work. I didn't like the morning song, "I owe, I owe, it's off to work I go!"

I became thrifty, and put all my spare money in the bank. Then I did a calculation:

I took my savings account balance and divided it by my monthly "nut," the absolute least needed for food, shelter, and living expenses. That number represented how many months I didn't have to get up and go to work. When that number hit a year, I felt like a success. I continued to work, but didn't feel pressured that I **had to** work.

Then I got married.

And my wife got pregnant … and got pregnant again … and again.

I'm not blaming her – I had an important role in the process.

Now I had to make more money and get a better job. That meant a boss ordering me around, holding a very important need over my head – my family's well being.

This created a big problem because I am burdened by a severe personality defect:

**I don't like someone ordering me around, telling me what to do, and threatening to fire me if I don't obey.**

Perhaps some of you suffer from this personality defect also?

So Financial Independence evolved into not having a boss ordering me around. I had to create our own business.

But what business?

I liked real estate, and felt passionate about owning property to rent out. I also liked taking run down, beat up properties, and breathing new life into them – improving the world around me.

I started working for myself in my 30's and continued for the rest of my life. While I worked, there remained a fear lurking in the back of my mind as I went from a young man entering the job market, to a family man with responsibilities: There was no safety net – if I failed in our real estate business, I couldn't regroup and work for someone else.

Why?

Because even if I overcame my personality defect of not being ordered around, I had another problem. What if I depended on someone else for a career and security for my family, and their business failed due to no fault of my own? And what if I was middle aged when it happened, like 40 or 50? I would be phased out of the job market, unemployed, replaced by someone younger and less costly.

Uh oh, back to square one.

Therefore, we didn't want our family depending on anyone but me and my wife for our security. The only way to do that was to have our own business, and ***make sure that business was a fortress, secure from all threats.*** We had to evolve strategies that grew our wealth, but were less risky, so our family was protected through the ups and downs of market cycles.

And guess what? The business that still made the most sense, with the least amount of risk, was real estate.

What about the next generation we were raising? What would become of them?

We did not insist our children go into the business with us. They could have picked other careers, but they chose to stay in the family business – real estate. One of the advantages of that was they stayed around, and now we have our children and their children living close by.

We taught our children how to manage the real estate investing business so when it passes on to them they will be trained to run it, hopefully better than my wife and I did. We didn't worry that the real estate business would become obsolete and antiquated by the Internet, like many businesses are nowadays – even Internet businesses. We believed that people will always need affordable housing to live in, and affordable places for their businesses, like warehouses. In the 35 years we've been in real estate, the only major change is how to communicate with renters and buyers – we use the Internet. Everything else remained the same. Why?

**Shelter is a basic human need, after air, water, and food.**

So for me, with my personality defects, Financial Independence included having our own business, which provided challenging careers for my wife and myself.

And yes, we were blessed to eventually have a home with no mortgage payments, a car with no car payments, college tuition paid for our kids, and a retirement income for our later years.

Now, whatever your own personal definition of Financial Independence is, real estate can probably provide it, whether you make it your main career, or a part time avocation. Please do yourself a favor and think long and hard about Financial Independence.

We own a rental property that serves residents aged 55 and older. I can tell you from firsthand experience, it's heartbreaking watching some of them grow old, struggling to survive solely on their social security checks.

Okay, now that we defined our goal, let's get going on the virtually foolproof ways to multiply your wealth, and protect your ass-ets with real estate.

How many businesses have a foolproof strategy for becoming wealthy and financially independent?

# Highlights of Chapter 1

1- Work is good for you, having a fulfilling career is good for you, and a little struggle is good for you. It will make you into a better person.

2- Financial Independence is creating a comfortable secure life for yourself and your loved ones, while you work at a career that energizes and challenges you, and keeps you fit and happy

3- Real estate will not be made obsolete by the Internet – people will always need affordable housing and affordable places to put their businesses, like warehouses. The Internet only changed the way you communicate with renters and buyers.

4- Shelter is a basic human need, right after air, water, and food.

5- It's no fun getting old and trying to survive solely on social security.

# Chapter 2

## Foolproof Strategies – Keepers and Flippers

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Just for one more chapter, let's put aside the excitement of Booms and Busts. Instead, let's focus our attention on the strategies that lead to Financial Independence.

As you were told before, these strategies are virtually foolproof, as long as you execute them in a Steady Market and perform the due diligence and background research. This is one of the few places in the business world where you have a precise formula for calculating profit before you own a business. Since a Steady Market prevails the majority of the time, these proven strategies will serve you well throughout your investing career.

The first way you achieve Financial Independence with real estate is buying property, and then renting it out each month. We call those **Keepers** because you keep the property. For 35 years, we've been buying residential and commercial real estate, getting good deals, and then letting ***other people*** occupy them.. That's what investors do – we buy real estate, keep it, then let others use it, and charge them rent to do so.

There is a simple formula called the **Cash Flow Formula** that will show you whether you should buy a property or not as a Keeper. First, you add up the rents, then you subtract the expenses. Like any business, there must be a profit at the end of each year for the business to survive.

**The Cash Flow Formula is:**

**Total up Rents**
**then subtract**
**– Insurance**
**– Taxes**
**– Repairs and Maintenance**
**– Mortgage Payment**
**– Management Fee** (it's zero if you do it yourself)
**= Profit**

If the formula gives you **enough profit**, then you buy the property, Keep it, and collect rents.

What is enough profit?

Enough profit is expressed as a percentage – it's the profit you put into your pocket at the end of each year divided by the money you took out of your pocket in the first place to buy the property.

As an example, let's use one of our own duplexes pictured on the left. We have owned this one since 1986, that's right, over 30 years. We paid $50,000 cash for it. We did not have a mortgage on it at the time.

The **Cash Flow Formula** when we purchased it was:

| | |
|---|---|
| **Total up Rents =** | **$590/month (2 apartments at $295/month each)** |
| **then subtract** | |
| **– Insurance** | **$50/month** |
| **– Taxes** | **$70/month** |
| **– Repairs and Maintenance** | **$50/month** |
| **– Mortgage Payment (0 – we paid cash)** | **0** |
| **– Management Fee** (0 - we did it) | 0 |
| **= Profit** | **$420/month (approx $5,000/ year)** |

Since we spent $50,000 of our hard earned bucks to buy the property, and the property threw off $5,000 per year in profit (before income tax), then we earned $5,000 over $50,000 each year, $5,000/$50,000 or 10% on our money.

After 30 years, $5,000/year times 30 years, means it returned $150,000 in rents, or 3 times what we paid … and it's still cranking out rents as we speak. (It's actually netting more than $8,000/year now, which is 16%)

When we first started out, a ten percent return was out goal, and it's a common goal for many investors. Why?

The only reason I can figure out is … it's 2 digits, not 1. It feels like a lot. ☺

Okay, now, with a Keeper, you own the property. You earn 10% each year while you watch and wait for your property to appreciate in value, from both **increased demand** and **inflation**. This will increase your profits over time.

The **increased demand** comes from more people needing what you have – an affordable home or an affordable place to put their business. For more than 300 years, the trend in the USA has been an increasing population - there have always been more people. The trend around the world is the same – an ever increasing world population. More people means greater demand, and price appreciation.

Why **inflation** exists is not so easy to decipher. Inflation appears when some basic costs go up, like gas or food, and then everyone else increases their prices to maintain their lifestyle when they have to pay more for those basic costs. This triggers the basic costs to once again go up, which causes everyone else to increase their costs again, and a spiral upward is created … without much sense. But sense or no sense (or nonsense) inflation is a fact of life, and has been for 100's of years.

Keep in mind, the income the Keeper produces will also go up with increased demand and inflation.

Now, in order to become Financially Independent, your lifetime goal is to buy more and more Keeper real estate until the cash flow profits, the yearly net income, are enough that you don't have to work for anyone else.

Now I can see some of you Newbies shaking your heads. "Wait a minute," you say. "Keepers mean I have to manage the properties I own. I don't want to be a landlord!"

What about managing the property you own?

Owning real estate means you have two responsibilities:

1- Managing the people you rent to
2- Managing the properties they rent from you

Depending on your time and expertise working with people, and making repairs, you might want to take on both responsibilities yourself, or hire a management company to do it for you. If you do it yourself, and you're good at it, you will earn greater profits. If you hire it out, you will earn less profit because professional

managers have to be paid. Usually they get 10% of the rents they collect for you, and add on 10% of the repairs they arrange for you to their bill.

So if you don't want to be a landlord, it's no biggy. Just factor in the management fees when you calculate your monthly profits.

**That is your first basic strategy- Keepers**

There are also **Flippers** – properties bought at a low cost, to be fixed up, and then sold for a quick profit at a higher price.

How do you a get a low cost, or a good deal?

There are many ways to get a good deal, but to simplify, you should look for a distressed property, or a distressed seller, or both. Even then, you will probably have to make a lot of offers to get one "good deal."

**Remember this – if you're not making offers, you're not making money**.

A distressed property suffers from deferred maintenance – it looks and functions badly. Most buyers don't want that, because it means spending time and money to get it into good condition. The scarcity of buyers for distressed property creates a good deal for you.

A distressed seller is someone who needs to sell, because they need the money, and they need it NOW. Cash talks and everything else walks to these people. Combining a distressed property with a distressed owner, that is where the best deals are.

In our investing career, we specialized in foreclosures and tax deeds. They involved both distressed property and distressed sellers, and there were plenty of good deals – but we had to work to find them, and once we found them, we had to work to make them profitable.

During the Bust, good deals just came to us – we didn't have to work hard to find them. Brokers brought us their listings where their sellers needed to sell, and would give us a great price. Why did they bring them to us?

Because we had a reputation of "getting the job done." When the seller met our terms and price, we didn't "fumpher around" (a Yiddish expression that sounds the

way it means, like most Yiddish expressions) – we bought the property and made the closing process easy – usually by paying cash without the drama of Lenders and their lending process.

If you want good deals to come to you, and the best deals in our whole career were deals that found us, you have to develop a reputation of "getting the job done, and not fumphering around." You write an offer, and then you close.

Now contrary to what many believe, even when you get a "good deal," the seller will thank you – because you supplied something they needed – cash and a closing without drama. You gave them peace of mind.

You should also understand: **the end result of Flipping distressed property is adding value to it, and then getting paid for the increase in the value when you sell it.** You will have to spend money, and time, to increase the value, and that increase in value is more than you put into it.

The **Flipping Formula** is also simple. You take the price you will sell the property for, in its fixed up condition, then subtract the price you pay for it, the closing costs when you bought and sold it, the costs to improve it (fix up costs), the costs to hold onto it (like maintenance and interest payments on the loan you used to purchase the property) and out pops your profit.

The **Flipping Formula** is**:**

**Selling price** (in Fixed Up Condition)
**-Price you pay**
**-Closing costs when you buy and sell**
**-Fix up expenses**
**-Holding costs**
**= Profit**

Let me show you how we applied this to a foreclosure we purchased on the courthouse steps. It is pictured on the left - **3 mobile homes on 1 ½ acres on Breeze Dr in North Ft Myers.** We paid only $29,000 because nobody else bid on the property.

Here is how we applied The **Flipping Formula:**

| | |
|---|---|
| **Selling price** (in Fixed Up Condition) | $85,000 |
| **-Price you pay** | **29,000** |
| **-Closing costs when you buy and sell** | **8,000** |
| **-Fix up expenses** | **22,000** |
| **-Holding costs (8,000 + 13,000 in RENTS)** | **+5,000** |
| **= Profit** | **$31,000** |

This was unusual in that we earned $13,000 in rents while we were fixing up 2 of the 3 mobile homes, which offset some of our closing costs. The $31,000 profit at closing was a welcome treat.

You can also work backwards with **Flippers**. This is what the pros do, like investors, builders and developers. You pick a property that needs improvement, and then figure what it will sell for in its improved condition. Then you subtract the profit you want to make, the closing costs when you buy and sell, the costs of fixing it up, the holding costs, and out pops what you must pay for it.

The beauty of this is that your greedy emotion, that is produced by a low price, is removed from the process – you decide what your profit is going to be, and you don't move off the cost that will provide it.

The **Pro Flipping Formula** is**:**

**Selling price** (in Fixed Up Condition)
**-Profit you want**
**-Closing costs when buy and sell**
**-Fix up expenses**
**-Holding costs**
**= Cost you must pay or less to make a profit**

Flippers are distinguished from Keepers in that your intention is to make money quickly, by trading through and **not** keeping the property. You will then take some of those flipping profits and reinvest them into more long term investments, more Keepers, increasing your income and net worth. You should also take some of your flipping profits and increase your inventory of Flippers, so you can make even more flipping profits.

Many investors start out with Keeping and Flipping single family homes, like the one shown.

Why houses?

Because that is what most people live in, and what they are familiar with. Houses are also the easiest real estate investment to buy, finance, rent, and manage. They can usually return 5 – 10 % of the cash you have invested in them with rents, or Flip easily because there are many buyers interested in them.

Eventually, home investors branch out into multi-family housing, like a duplex or a triplex, to increase their rental returns. You saw one of our own duplexes when we discussed Keepers before.

The next evolution for many investors is investing in commercial property. Why?

Because if you set up commercial property correctly, the tenants are responsible for all repairs, except the roofs, and many commercial tenants stay long term – 3 to 5 years or more. Since turnovers are the most expensive and time consuming part of managing property, the less tenants moving in and out, the better.

When we speak of commercial property, we are usually referring to:

1- Apartment buildings
2- Retail Stores and shopping centers
3- Warehouses
4- Offices
5- Mobile Home and RV Parks
6- Hotels and Motels
7- Self Storage facilities

There are more types of commercial properties, but the seven above are the most common.

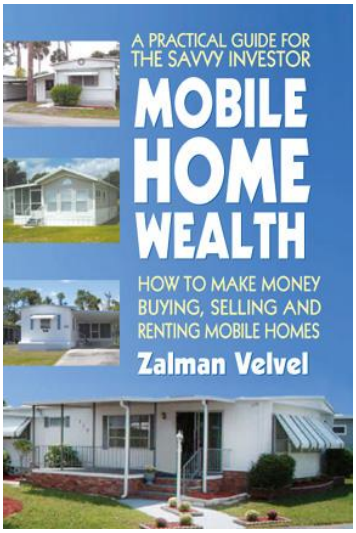
The commercial property we are going to highlight here is one we purchased in 2001 for $200,000. It's a warehouse that contains 22,500 square feet. It was one big space, which would have been difficult to rent.

When we purchased it, we bought it with no money down of our own. We obtained financing for the whole purchase price. (How we did that we will discuss later.)

We then spent $50,000 out of our own pocket to fix it up, by dividing it into 3 smaller spaces that would be easier to rent out. We also did roof repairs and cosmetic improvements.

When we were finished adding value, it returned $1,000 each month in positive cash flow, or $12,000 per year. If you have a calculator handy, you will see we earned 24% on the $50,000 we originally invested.

$12,000 profit each year / $50,000 invested = 24% return yearly




Commercial property requires some new concepts and techniques versus houses and duplexes, but commercial property is not so complicated you can't make even more money investing in it.

There is not enough space in this book to discuss these two basic strategies, Flippers and Keepers, in greater detail. If you want to learn more, I would suggest reading the book, **Mobile Home Wealth**.

Even though the book uses mobile homes as examples of investing, you can replace mobile homes with any other type of real estate, and the strategies remain the same.

## Common Mistakes Investors Make on Both Strategies

I described both strategies as being virtually foolproof, but I would be remiss if I didn't tell you some of the mistakes I have seen investors make along the way. I purposely put them at the end of this chapter because I have learned if I emphasize mistakes, then people believe too strongly in the mistakes, become needlessly

afraid, and ignore the important strategy. If you do this also, you would miss out on an important leg in your journey to Financial Independence.

**On Keepers, the mistakes were:**

1- Underestimating monthly expenses
2- Underestimating repairs and long term capital improvements needed to upgrade the property in the future
3- Overestimating rents and underestimating vacancies

**On Flippers, the mistakes were:**

1- Overestimating the fixed up value of the property
2- Underestimating the cost of repairs and improvements
3- Underestimating the time needed to sell the property

I found the best way to overcome these mistakes was to learn about appraising, and the cost of doing repairs, and then being conservative in all estimates. Networking with other investors and asking questions of the ones you respect will also go a long way toward helping you avoid the above mistakes.

We had the attitude that mistakes were inescapable because sometimes there is no one to ask for help, and no book to look up answers in. You can only try your best.

That's okay. **Mistakes are common on the path to wisdom**.

Just don't repeat the same ones over and over. ☺

**Why is it important to use BOTH of these strategies?**

If you want long-term Financial Independence, you need KEEPERS. They will continue to create cash flow, on a monthly basis, for a lifetime, and it will be ever increasing in response to inflation and demand from an increasing population.

You will also want FLIPPERS to create fast cash, for more down payments on more Keepers. That additional cash will also act as a safety net for the months your KEEPERS don't cash flow so well because of unexpected repairs and expenses. There are always unexpected repairs, like replacing a roof, trees falling on buildings, cracking foundations, repairing parking lots, termites, flood damage, etc.

If you only do Flippers, and I know many investors who choose to do that, it's like a job. "When you ain't a Flippin', you ain't a earnin' money."

Keepers make you money from rents 24 hours a day. "Even when you are a sleepin', you are still a earnin'."

Doing both KEEPERS and FLIPPERS creates a good balance between the expected and the unexpected, as well as increasing your portfolio of Keepers and your inventory of Flippers.

Now that we discussed the two main strategies in a Steady Market to achieve Financial Independence using real estate, let's see what happened in the Boom, The Ride Up, from 1999 to 2005, and then the Ride Down, 2006 to 2012.

The ride is going to be thrilling, so let's strap on our seat belts.

It was the best roller coaster we were ever on.

# Highlights of Chapter 2

1. The way you achieve Financial Independence with real estate is buying property, and then renting it out each month. We call those **Keepers** because you keep the property.

2. The **Cash Flow Formula** shows you whether you should buy a property or not as a Keeper. First, you add up the rents, then you subtract the expenses, and like any business, there must be a profit at the end of each year. Most investors try to get at least 10% yearly income returns.

3. **Keepers** appreciate in value from both increased demand and inflation. Thus you increase your profits over time.

4. **Flippers** are properties purchased at a low cost, fixing them up, and selling for a quick profit at a higher price. **Flipping is adding value to a property, and then getting paid for the increase in the value when you sell it.**

5. There are many ways to get a good deal, but to simplify, you should look for a distressed property, or a distressed seller, or both. You will probably have to make a lot of offers, but **"If you're not making offers, you're not making money."**

6. If you want good deals to come to you, and the best deals in our whole career were deals that found us, you have to develop a reputation of getting the "job done, and not fumphering around." You write a contract, and then you close.

7. You should take some of your flipping profits and reinvest them into more Keepers, increasing your income and net worth. You should also take some flipping profits and increase your inventory of Flippers, so you can make even more flipping profits.

8. Many investors start out with single family homes, because that is what most people live in, and what they are familiar with. Houses are also the easiest real estate investment to buy, finance, rent, and manage. They can usually return 5 – 10 % of the cash you have invested with rents.

9. Eventually, home investors branch out into multi-family housing, like a duplex or a triplex, to increase their rental returns.

10. The next evolution for many investors is to branch out into commercial property because tenants are responsible for all repairs, except the roofs, and many commercial tenants stay long term – from 3 to 5 years or more. Since turnovers are the most expensive and time consuming part of managing property, the less you have tenants moving in and out, the better.

11. Owning real state means you have two responsibilities, managing the people you rent to, and managing the properties they rent from you

12. If you don't want to be a landlord, then just factor in the management fees when you calculate your monthly profits

13. If you want long-term Financial Independence, you need KEEPERS. They will continue to create cash flow, on a monthly basis, for a lifetime, and it will be ever increasing in response to inflation and demand from an increasing population

14. You want FLIPPERS to create fast cash, for more down payments on more Keepers, and also as a safety net for the months your KEEPERS don't cash flow so well because of unexpected repairs and expenses.

15. Doing both KEEPERS and FLIPPERS creates a good balance between the expected and the unexpected, as well as increasing your portfolio of Keepers and your inventory of Flippers

# Chapter 3

# Where are You in the Market Cycle?

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Okay, you learned a virtually foolproof method of creating wealth for yourself with real estate, so you can become financially independent. Now you are going to learn where the system is not foolproof, and why I used the term "virtually."

I am referring to times during market Bubbles, where prices Boom, and then go Bust.

Logic dictates when you buy a Keeper or a Flipper in a Booming market, when prices are rising rapidly, you are going to create a lot of wealth for yourself – as long as you sell before the bubble bursts.

Logic will also tell you when you buy a Keeper or a Flipper in a market that is going Bust, where prices are dropping rapidly, you are going to create lots of losses for yourself. (On the other side of the coin, if you buy at the bottom of the Bust, when prices are low, you are going to grow wealthier when prices rise again.)

You still have the same two basic strategies, but when they are executed at the either the right time, or the wrong time, you can get entirely different results.

**So before you buy anything, a Keeper or a Flipper, you need to establish where you are in the real estate market cycle in your area of investment. How do you know what part of the market cycle you are in?**

You should go back as far as you can in time and plot on a graph, what the median price of a house was in the area you are looking to invest in, over time. Where will you find that information? Using The Case-Shiller Index. Judging by the shape of the graph, the cycle will make itself known to you, and you will see where you are now in the market cycle.

Why plot the price of houses? Because residential housing is the forerunner to almost all other types of real estate. Remember, "Roof tops come before parking lots." You could do this for commercial property, but the statistics are more difficult to find, whereas housing prices are more common.

Now before we discuss the market cycles, you may be wondering:

> **Why do markets go up and down anyway? Why don't they just stay the same, so you can execute Keepers and Flippers, and grow financially independent without the stress of market gyrations?**

The answer is – markets go up and down in response to change – change that is happening now, or change that people anticipate in the near future.

The average market experiences change like the good old sine curve:


We humans are an emotional species, and when we encounter change, we have two simple reactions to it – greed or fear. When we are greedy, the market goes up, and when we are fearful, it goes down.

Under normal Steady Market conditions, the housing market just bounces up and down a little in response to greed or fear. Then it restores itself to the Steady Market. According to 2013 Nobel Laureate in economics, Robert J. Shiller, the real estate market was a Steady Market for almost 50 years, from 1890 until 1940 (except for vacant land surrounding new construction, which was subject to intense speculation.)

However, when we are exceptionally greedy, it leads to a Boom. When we are exceptionally fearful, it leads to a Bust. Those are the times where you can gain the most … or be hurt the most.

The times that the real estate market went through Boom and Bust cycles were during and after WWII when G.I.'s returned from the war, 1942 until 1960. There was a 1970's Boom in California, and a 1980's Boom on the East and West costs. These were all dwarfed by the recent Nationwide bubble from 1999 until 2012.

You will learn from the pages that follow that fear is the more powerful emotion. When exceptional fear prevails in a market, it will usually go down faster than it will go up when greed prevails. It is an old market axiom that "markets go up in steps, like an escalator, and then crash down like an elevator" (where you get the shaft ☺.)

It would be nice to sell  at the top of the sine curve, at the 90 degree mark, and then buy at the bottom of the sine curve, at the 270 degree mark, like so:


What is the problem with that?

The problem is, no bell sounds when a market is at a top, or a bottom. You have to use judgment and intuition, which comes from experience. But what if you have little or no experience in real estate? What can you do when you are a Newbie, and unfamiliar with Booms and Busts?

**Close the book and think about it.**

The answer is right at your fingertips – you're holding it now. I wrote this book to help you learn from the experiences we had during the Boom and Bust, our successes AND mistakes.

That's what a good Uncle does.

Now, when a market changes in response to greed or fear, you must ask yourself a very important question:

**<u>Is  this change fundamental (permanent), or temporary?</u>**

Most change is temporary, but because we are human beings, fear or greed tricks us sometimes into believing it is permanent.

I have been through 3 Booms and Busts: 1980 to 1990 in New York, 1981 to 1991 in Ft Myers, Cape Coral Florida, and again in 1999 to 2012 in Ft Myers/ Cape Coral. Each time, when the market reached a Boom, a top, the market psychology was at its most positive. People believed it was going to be blue skies forever and the market would never ever go down again.

Then when the market reversed itself and started to trend down, people tried to sell at the previous high Boom prices, and couldn't. They asked themselves, **"What were we thinking, that we allowed it to go up so much without doing anything? Why didn't we sell when it was so freaking high?"**

Conversely, when the market was in a Bust scenario, a bottom, the market psychology was as its most negative, all doom and gloom. You woke up each day to news reports that made you want to go hide in a corner.

Then when the market finally proceeded upward, people tried to buy at the previous Bust prices, but couldn't. They asked themselves the same question as when the market boomed, only in reverse: **"What were we thinking, that we allowed it to go down so much without doing anything? Why didn't we grab everything we could buy with both hands when it was so freaking cheap?"**

The best strategy to use in both cases was coined by Warren Buffett, one of the greatest investors that ever lived. He said:

**"When most people are greedy, we become fearful. And when most people are fearful, we become greedy."**

I have found that many real estate market pros, people with a lifetime of experience, don't expect to sell at the very top of the market, or buy at the very bottom. Instead, they sell after the market reached the top, and then started to trend down, revealing the true high of the Boom. They did the same thing after a Bust. They bought after the market reached a bottom, and then trended upward, revealing the true low of the Bust.

They are referred to as Momentum Invertors.

When pros sell, it's represented on the graph that follows by the 120 degree mark. When they buy, it's at the 300 degree mark.


So what should your strategy be when you sense your real estate market is at a top? Conversely, what should your strategy be when you sense your real estate market is at a bottom**?** And what should you do in between?

I'm going to give you specific strategies of what we did when we were right, and what we should have done when we made a mistake.

Okay, make sure your seat belt is fastened before you turn the page. We are going to up shift, and step on the gas.

The next sound you will hear is your heart pounding.

# Highlights of Chapter 3

1. Markets go up and down in response to change, change that is taking place now, and change that people expect in the future.

2. Human beings are an emotional species – when we encounter change we have 2 simple reactions, greed or fear.

3. Greed makes the market go up, fear makes it go down.

4. Fear is the more powerful emotion.

5. Pros don't try to guess when the tippy top or absolute bottom is, but wait until the top or bottom are revealed, and then act.

6. When a change is happening, you have to ask yourself if the change is fundamental (permanent) or temporary.

7. Most change is temporary, but fear or greed tricks us into believing it will be permanent.

8. "When most people are greedy, you should become fearful. And when most people are fearful, you should become greedy" … Warren Buffett