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18th, 2007

Rev N You with Real Estate

Wake Up Richer Everyday

Dear Dave,

It's time to face the hard facts. If you haven't committed to yourself that you are going to build your wealth, made a plan to do so and started working on that plan, then you are probably only building your wealth when you are awake and working. Isn't it better to know that when you sit down to watch t.v. or you close your eyes at night you are still making money?

Passive wealth creation, or waking up richer everyday, is one of the reasons we love real estate. We talked a bit about this in our [March issue](#) this year. Of course, there are other reasons why real estate is one of the main ways we've pursued to build our wealth. We've never been as scared of real estate as we have of investing in stocks (we started right around the time that most of our friends and family lost buckets of money in the Nortel stock crash). And we've never found real estate as daunting or as time consuming as creating a business.

This month we're investigating one book's advice on wealth creation and dissecting the option of purchasing investment properties with no money down (100% financed).

*Welcome to the seventeenth edition of our newsletter -
Rev N You with Real Estate.*

Thank You

by Dave
Peniuk &
Julie Broad

Just a quick note to thank all of our readers that responded to the flipper story last month. We received some great emails, including one story we will feature in a future month concerning the hidden fees in buying a pre-built condo unit with the intent of flipping it.

Is there a topic you want us to cover? Or a story you want to hear? Please let us know and we will try and answer your questions.

Automatic Wealth

by Julie
Broad

An Overview of Michael Masterson's "6 Steps to Financial Independence"

Recently, Dave and I attended a 4 day marketing bootcamp in Delray Beach, Florida. We each went with different objectives, but we both came

out incredibly impressed with Michael Masterson, the keynote speaker of the conference. He is best known for his copy writing expertise and affiliation with the American Writers and Artists Institute, but he started with little, held many jobs over the years, and has built his wealth through just about every kind of business imaginable. He's owned businesses for things like pool installations, direct marketing, selling discount jewelry, and has been involved in half a dozen real estate development ventures. This book didn't profoundly change my 5 year plan like *Rich Dad Poor Dad* did, but I did like the mental tune up it gave me. Masterson offers sound advice in the book from someone who has been there and hasn't lost touch with reality despite his profound wealth and success. I thought some of our readers would enjoy a snapshot of his [6 steps to financial independence](#).

The Nuts and Bolts of the 6 Steps:

1. You will make you wealthy...and it won't happen as easily as putting 10% of your income away each month,
2. You have to plan to be wealthy - wishing won't work,
3. You must develop rich habits as the rich are different from ordinary people and it's not just because they have more money,
4. Increase your income radically. He isn't talking about a 3% a year raise here, he is talking about boosting your income by 150% for starters,
5. Get rich automatically - true wealth is built through the creation of equity,
6. Retire early, if you want to.

After you have taken stock of your current financial situation, you must plan to become wealthy. As we have said in several issues, "[What are your goals?](#)". His approach to goal setting asks you to imagine your funeral. What do you want people to say about you? What are the words from your family or close friends? A coworker? A mentor? And someone you didn't know? Based on that, determine your goals in the long term, and then dive in and figure out what the medium and short term looks like. Make them specific and measurable, and write them down.

Plan in hand, it's time to develop wealthy habits. My favourite chapter of the book is "Step 3: Develop Wealthy Habits". Masterson says "Budgeting is like dieting: It's enormously sensible but almost never effective". I have been a budgeter for over 10 years. I have a great understanding of where I spend my money, but I also have a lot of stress about spending money.

Instead of continuing to focus on where I spend my money, as I already have a deep understanding of where my money goes, I'm taking the Masterson approach of doing a personal balance sheet.

Create a spreadsheet that lists all of your assets and all of your debts.

Conservatively estimate the value of all of your valuable assets (stocks, bonds, real estate, art) and how much you owe. Then, each time you check your balance sheet, promise yourself (And take the steps necessary to make it a reality) that next time you check you will be wealthier. Before you make a purchase or a decision to do something new, you will find yourself asking "Will this make me richer or poorer?".

Let me skip ahead in his book now, as this is a newsletter about putting the "Rev N You with Real Estate", not about general wealth accumulation and life goals. *Step 5: Get Richer While you Sleep* is all about investing in stocks, real estate investing and investing in businesses to build your wealth. He gets right to the meat of real estate investing as a means to create wealth by saying "While you are building wealth, you should treat your rental real estate portfolio as an equity play. You will want to use leverage (by taking mortgages) to get the maximum appreciation on your cash...As your equity increases in each property, you should consider taking some of that money out of it and reinvesting it in other properties" pg.185.

This has been our strategy, and it's worked very well, especially since the market has been so strong. It hasn't put cash in our pockets (in fact it often feels like our properties take cash out of our pockets) but our balance sheet is better every time we look at it.

He goes into a lot of detail and examples to convince you to invest in real estate. But his bottom line, and we agree, is "If you haven't already begun investing in real estate, start doing so today. If you are a budding real estate tycoon, resolve to add to your empire this year. You'll find that actively investing in real estate can give you much-better-than-the-stock-market returns, and the comfort of knowing your investments can't disappear" page 219. Couldn't have said it better myself Michael!

I think you'll find some golden nuggets in this book, so I do recommend you pick up a copy for some "get on track motivational" reading. But if you haven't already read [Rich Dad Poor Dad](#), do that first!

100% Financing - a Dream or a Curse?

by Dave
Peniuk

On the surface, 100% Financing of an investment property seems like a fantastic idea. With no money down, it seems you can't go wrong. But, that is not necessarily true.

Recently CMHC (Canadian Mortgage and Housing Corporation), who insures non-conventional mortgages (less than 20% down payment mortgages) in Canada, introduced the [100%](#) financing for investment properties. This same product has been in existence for a couple of years for primary residence purchases but now, if you want to get into real estate

investing (and your credit is great and you can qualify for the 100% financing), you no longer need a stack of cash to jump in! The challenge is obtaining rent that's high enough to cover the mortgage and the 7.25% insurance premium they hit you with! Here's an example:

- \$300,000 purchase price (100% financed)
- 7.25% CMHC insurance fee (\$21,750)
- Total mortgage of \$321,750
- Amortized over 25 years at a 5.99% interest rate =
- \$2,056.67 monthly payment!

So, right off the bat you have *negative equity* of \$21,750. If you wish to sell that property after 5 years, your mortgage balance will be \$289,008. The property will have had to appreciate at least 15% over those years just to get a little bit of money out of it (remember there's sales commissions, legal fees, property purchase taxes, etc. that will also come out of the sale price).

The next challenge is getting the \$3,000 in rent each month that you would need to carry this property. Remember, it's not just about covering the mortgage. You also have:

- Insurance fees (approx. 5% of rent);
- Management fees (approx. 5% of rent);
- Maintenance fees (5% to 10% or more);
- Water, hydro, other utilities (2% to 5% of rent);
- Strata or condo fees, if applicable (10% or more);
- Vacancy coverage (2% to 5%), etc.

From our experience, if you keep your mortgage payment at a maximum of 65% of your rental income, you should be pretty close to having neutral or even positive income. In this example, that means you want to earn approx. \$3,200 in rent to cover everything. Not very likely unless you are running a rooming house and if you've read about my two properties in Niagara Falls, you know how fun and lucrative rooming houses have been for me.

Now, there are two advantages to using the CMHC program:

1. No money down - you don't need lots of cash to begin investing; and
2. Potential for a GREAT return on investment (ROI) if the market is on the upswing;

So, it's not the worst thing to use, but be very aware of what it will "cost" you in terms of potential negative monthly cashflow and negative equity.

Now, what about other forms of 100% financing? Well, there are creative ways of obtaining 100% financing such as Vendor Take Back's (the Seller holds the mortgage on the property); Obtaining a conventional mortgage

(80% loan to value) thru a bank or lender and then obtaining a 2nd mortgage from either the Vendor or a private lender and registering it after you purchase the property (you must still have the 20% down payment upon closing); or using your line of credit for the 20% down payment. So, this is not to say that 100% financing doesn't work or isn't useful, it's just quite costly to do it. Costly because not only your monthly debt (mortgage/line of credit) servicing is higher, but usually a 2nd mortgage or line of credit interest rate is substantially higher than a 1st mortgage rate.

I have done 100% financing once and 98% financing another time, and the only reason I was able to was because both sellers were very motivated to sell. Why were they so motivated? Because their properties were beat up and in bad areas. The rent vs. financing was strong in both cases, so I bought. I wouldn't do it again. As the saying goes, "You get what you pay for".

Rev N You - Next Edition

Remember to look for our Christmas edition where we'll discuss:

- Real estate vs. Stocks - what's the better ROI?; and
- A special announcement!

If you know someone who would enjoy and/or learn from our tales, please pass this along. If you want to continue receiving this, please subscribe below.

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