

# Real Estate Investing

By: Lee Phillabaum



# Sovereign Property Investments

- ▶ “Primum Non Nocere”
  - ▶ “First, Do No Harm”
- ▶ Mission Statement of SPI
  - ▶ SPI’s purpose is to grow the wealth of its partners through investing in real estate opportunities and seeking reliable returns on Investments.
- ▶ Investing Practices
  - ▶ SPI was formed as a way to give our investment partners the opportunities to invest in income producing properties at a lower capital requirement. This is done by investing in real estate projects with a pool of investment partners to reduce the capital needed for each partner to invest in income producing properties.
  - ▶ Feel free to visit our website at [sovereignspi.com](http://sovereignspi.com)



# Why We Invest

- ▶ Financial Freedom
  - ▶ To make a profit.
  - ▶ To have your money work for you.
  - ▶ To stop trading hours for money and have your money work independent of you.
  - ▶ To have other sources of reliable Income, a diversification of incomes and assets.
- ▶ Improving Community
  - ▶ As an Investor you are in a unique position to improve your communities and leave something better than you found it.
  - ▶ This revitalization can effect whole neighborhoods, and over time towns and communities.
- ▶ The Enjoyment of Finding Investments Deals
  - ▶ There is enjoyment in finding and working out investment opportunities.



# We need to go over some Real Estate Terminology

- ▶ You need to build your base of knowledge of Real Estate Terms and what these terms mean, and how these terms are necessary for investing.



# Real Estate Investment Terminology

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- ▶ **Gross Scheduled Income “GSI”**
  - ▶ GSI is the annual income of a property if all rentable space were, in fact, rented and all rent collected.
- ▶ **Net Operating Income “NOI”**
  - ▶ Net operating income equals all revenue from the property minus all reasonably necessary operating expenses.
- ▶ **Operating Expenses**
  - ▶ An operating expense is an expense a business incurs through its normal business operations.
- ▶ **Vacancy**
  - ▶ Vacancy allowance is a line item on a real estate pro forma that accounts for expected vacancy of the property.
- ▶ **Turnover Expenses**
  - ▶ Whenever a tenant leaves a property, making the property rent ready and finding another qualified tenant will cost money.
- ▶ **Cash Reserves**
  - ▶ Cash reserves are funds that companies set aside for use in emergency situations



# Real Estate Investment Terminology

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- ▶ Comparative Market Analysis “CMA”
  - ▶ A comparative market analysis is an examination of the prices at which similar properties in the same area recently sold.
- ▶ Equity
  - ▶ Equity is the difference between the market value of your home and the amount you owe the lender who holds the mortgage, i.e. Equity is the amount of an asset/company you own.
- ▶ Market Value
  - ▶ Market value is the price an asset would fetch in the marketplace.
- ▶ Break-Even Ratio “BER”
  - ▶ Break-Even Ratio it allows lenders and other investors to assess the rental property for its ability to meet its operating expenses, debt service, and provide a level of profit.
- ▶ Capital Expenditure “Cap X”
  - ▶ Capital expenditures, commonly known as CapEx, are funds used by a company to acquire, upgrade, and maintain physical assets such as property, buildings, an industrial plant, technology, or equipment.
- ▶ Loan-to-Value Ratio “LTV”
  - ▶ Ratio is an assessment of lending risk that financial institutions and other lenders examine before approving a mortgage.



# Real Estate Investment Terminology

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- ▶ After Repair Value “ARV”
  - ▶ ARV estimates the future value of a distressed property after it’s been repaired.
- ▶ Buy, Rehab, Rent, Refinance, and Repeat “BRRRR”
  - ▶ BRRRR is a method and process of which to invest/acquire real estate; Buy, Rehab, Rent, Refinance, and Repeat.
- ▶ **Appreciation**
  - ▶ Is the increase in a home's value over time.
- ▶ Buy and Hold
  - ▶ Buy and hold is a passive investment strategy in which an investor buys stocks (or other types of Investments) and holds them for a long period of time regardless of fluctuations in the market.
- ▶ Fix and Flip
  - ▶ Flipping refers to purchasing an asset with the intent of selling it for a quick profit rather than holding on for long-term appreciation.



# Net Operating Income “NOI”

- ▶ Net Operating Income “NOI”
  - ▶ Net operating income equals all revenue from the property minus all reasonably necessary operating expenses.
- ▶ How to find Net operating Income “NOI” From Gross Scheduled Income “GSI”
  - ▶ The difference between NOI and GSI is Operating Expenses (OP-GSI) = NOI.
- ▶ Examples of Operating Expense’s for an Investment Property
  - ▶ Vacancy, Turnover Expenses, Property Management, Taxes, Insurance, Repairs/Maintenance, HOA’s fee, Utilities, lawn care/snow removal, and Miscellaneous
- ▶ It’s critical as a Real Estate Investor that you understand how to find and use NOI!





# How to Analysis Real Estate Deals

## ▶ Gross Rent Multiplier “GRM”

- ▶ Gross Rent Multiplier is the ratio of the sale or purchase price of a real estate deal to its annual rental income before deducting operating costs such as utilities, taxes, insurance, etc.
- ▶ **Gross Rent Multiplier** = Purchase Price / Gross Schedule Income

## ▶ Capitalization Rate “Cap Rate”

- ▶ The capitalization rate is used in the world of commercial real estate to indicate the rate of return that is expected to be generated on a real estate investment or to determine the Fair Market value of the property based on Cash Flows.
- ▶ **Capitalization Rate** = Net Operating Income / Purchase Price

## ▶ Cash On Cash Return “COC”

- ▶ Cash-on-cash return is a rate of return often used in real estate transactions that calculates the cash income earned on the cash invested in a property.
- ▶ **Cash On Cash Return** = Net Operating Income / Total Cash Invested

## ▶ Return On Investments “ROI”

- ▶ Return on Investment (ROI) is a performance measure used to evaluate the efficiency of an investment or compare the efficiency of a number of different investments.
- ▶ **ROI** = (Current Value of Investment - Cost of Investment) / Cost of Investment



# Gross Rent Multiplier “GRM”

## ▶ Gross Rent Multiplier “GRM”

▶ Gross Rent Multiplier is the ratio of the sale or purchase price of a real estate deal to its annual rental income before deducting operating costs such as utilities, taxes, insurance, etc.

▶ Gross Rent Multiplier = Purchase Price / Gross Schedule Income

▶ GRM is a quick and easy way to check and see if this deal is realistic

▶ You want to have a GRM lower than 10 but higher than 4

## ▶ Investment Property A has a purchase price of \$70,000

▶ Rental income is \$800 per month ( $\$800 \times 12$ ) = \$9,600 GSI

▶ Purchase price \$70,000 / GSI \$9,600 = GRM 7.3 ratio

## ▶ Investment Property B has a purchase price of \$80,000

▶ Rental income is \$850 per month ( $\$850 \times 12$ ) = \$10,200 GSI

▶ Purchase price \$80,000 / GSI \$10,200 = GRM 7.8 ratio



# Capitalization Rate “Cap Rate”.

## ▶ Capitalization Rate “Cap Rate”

▶ The capitalization rate is used in the world of commercial real estate to indicate the rate of return that is expected to be generated on a real estate investment.

▶ Capitalization Rate = Net Operating Income / Purchase Price

▶ Purchase Price = Net Operating Income / Cap Rate

## ▶ Investment Property A has a purchase price of \$70,000

▶ Rental income is \$800 per month ( $\$800 \times 12$ ) = \$9,600 GSI.

▶ Operating Expenses are \$4,000 / Net Operating Income = \$5,600

▶ NOI \$5,600 / Purchase price & rehab \$70,000 = Cap rate 8% Rate

## ▶ Investment Property B has a purchase price of \$80,000

▶ Rental income is \$850 per month ( $\$850 \times 12$ ) = \$10,200 GSI

▶ Operating Expenses are \$4,200 / Net Operating Income = \$6,000

▶ NOI \$6,000 / Purchase price = Cap rate 7.5% Rate



# Cash On Cash Return “COC”.

- ▶ Cash On Cash Return “COC”
  - ▶ Cash-on-cash return is a rate of return often used in real estate transactions that calculates the cash income earned on the cash invested in a property.
  - ▶ Cash On Cash Return = Net Operating Income / Total Cash Invested
  - ▶ If you Finance the real estate instead of using Cash this will decrease your COC returns.
- ▶ Investment Property A has a purchase price of \$70,000 and a rehab of \$10,000
  - ▶ Rental income is \$800 per month ( $\$800 \times 12$ ) = \$9,600 GSI
  - ▶ Operating Expenses are \$4,000 / Net Operating Income = \$5,600
  - ▶ NOI \$5,600 / Total Cash Invested \$80,000 = COC 7% Return
- ▶ Investment Property B has a purchase price of \$80,000 and a Rehab of \$5,000
  - ▶ Rental income is \$850 per month ( $\$850 \times 12$ ) = \$10,200 GSI
  - ▶ Operating Expenses are \$4,200 / Net Operating Income = \$6,000
  - ▶ NOI \$6,000 / Total Cash Invested \$85,000 = COC 7% Return



# Return On Investments “ROI”.

## ▶ Return On Investments “ROI”

▶ Return on Investment (ROI) is a performance measure used to evaluate the efficiency of an investment or compare the efficiency of a number of different investments.

▶  $ROI = ((\text{Current Value of Investment} + \text{NOI}) - \text{Cost of Investment}) / \text{Cost of Investment}$

▶ Return on Investment will increase the more you finance the deal.

## ▶ Investment Property A has a purchase price of \$70,000 and a rehab of \$10,000

▶ Rental income is \$800 per month ( $\$800 \times 12$ ) = \$9,600 GSI; with an ARV of \$85,000

▶ Operating Expenses are \$4,000 / Net Operating Income = \$5,600

▶  $((\text{Current value of Investment } \$85,000 + \text{NOI } \$5,600) - \text{Cost of Investment } \$80,000) / \text{Cost of Investment } \$80,000 = \underline{13.25\% \text{ return}}$

## ▶ Investment Property B has a purchase price of \$80,000 and a Rehab of \$5,000

▶ Rental income is \$850 per month ( $\$850 \times 12$ ) = \$10,200 GSI; with an ARV of \$90,000

▶ Operating Expenses are \$4,200 / Net Operating Income = \$6,000

▶  $((\text{Current value of Investment } \$90,000 + \text{NOI } \$6,000) - \text{Cost of Investment } \$85,000) / \text{Cost of Investments } \$85,000 = \underline{12.95\% \text{ return}}$



# Sample Investment Property Analysis.

## ▶ Sample Investment Property Information

- ▶ Asking Price is \$50,000 and Rehab cost will be \$10,000; with an ARV of \$65,000 after rehab.
- ▶ Rents are \$650 per month with a Gross Schedule Income of \$7,800.
- ▶ Operating Expenses are \$3,000 making Net Operating Income is \$4,800.

## ▶ Gross Rent Multiplier “GRM”

- ▶ **Gross Rent Multiplier** = Purchase Price / Gross Schedule Income
- ▶ Answer: 6.41 ratio

## ▶ Capitalization Rate “Cap Rate”

- ▶ **Capitalization Rate** = Net Operating Income / Purchase Price
- ▶ Answer: 9.6% Rate

## ▶ Cash On Cash Return “COC”

- ▶ **Cash On Cash Return** = Net Operating Income / Total Cash Invested
- ▶ Answer: 8% Return

## ▶ Return On Investments “ROI”

- ▶ **ROI** = ((Current Value of Investment + NOI) - Cost of Investment) / Cost of Investment
- ▶ Answer: 16% return



# Different Strategies for Investing in Real Estate

## ▶ BRRRR

- ▶ Buy and hold is a passive investment strategy in which an investor buys stocks (or other types of Investments) and holds them for a long period of time regardless of fluctuations in the market.

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- ▶ Buy and hold is a passive investment strategy in which an investor buys stocks (or other types of Investments) and holds them for a long period of time regardless of fluctuations in the market.

## ▶ Cash Flow Approach of Buying Real Estate

- ▶ A method of investing, with buying assets for the projected Cash Flows.

## ▶ Appreciation Approach of Buying Real Estate

- ▶ A method of investing, with buying assets for the projected appreciation of the market value of said asset.

## ▶ Fix and Flip

- ▶ Flipping refers to purchasing an asset with the intent of selling it for a quick profit rather than holding on for long-term appreciation.



# Different Strategies for Buying Real Estate

- ▶ Buy with Cash
- ▶ Traditional Financing
- ▶ Hard Money Lenders
- ▶ Private Money Lenders
- ▶ Private Equity Partners
- ▶ Home Equity Line of Credit “HELOC”
- ▶ Self Directed Individual Retirement Accounts “IRA”





Thank you for your Time.

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