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# STOCK MARKET VS. REAL ESTATE

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**There’s a reason it’s called legalized gambling...**

Fretting about the stock market has been an endless worry for countless Americans.

**We’d like to offer an alternative.**

## Stock market returns aren't what They appear to be

The average stock market return over the last 15 years was **7.04%** (from 2004 to 2018) and **9.06%** over the last 30 years (from 1989 to 2018).

***If you invested $100,000 in 2004 it would be worth $277,454 in 2018.***

## Volatility

What most investors don't realize is that the same $100,000 weren't actually worth $277,454 fifteen years later - that's because of the volatility of the stock market from year to year. In fact, that same $100,000 was actually worth $225,425 – which is only a **5.6%** return compounded every year. Not nearly as good but still not bad ... until we realize these returns are BEFORE brokerage fees.

## Fees

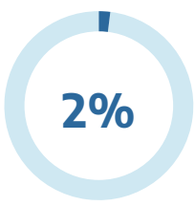
The average expense ratio for actively managed mutual funds is between 0.5% and 1.0% and and can go as high as 2.5%. For passive index funds (ETFs), the typical ratio is approximately 0.2%. Most investors have a blended portfolio of ETFs and mutual funds, so let's assume the averagefee is 1.0% per year. After taking out a 1% fee each year, instead of being worth $225,425, your $100K invested fifteen years ago is now only worth $193,879 – a mere 4.5% compounded return.

## Taxes

If you're filing jointly and making more than $77,201, your long term capital gains rate is 15%. If you sold your entire portfolio, the taxes you'd have to pay would push your average annual return from 4.5% to 4.0%.

# Inflation

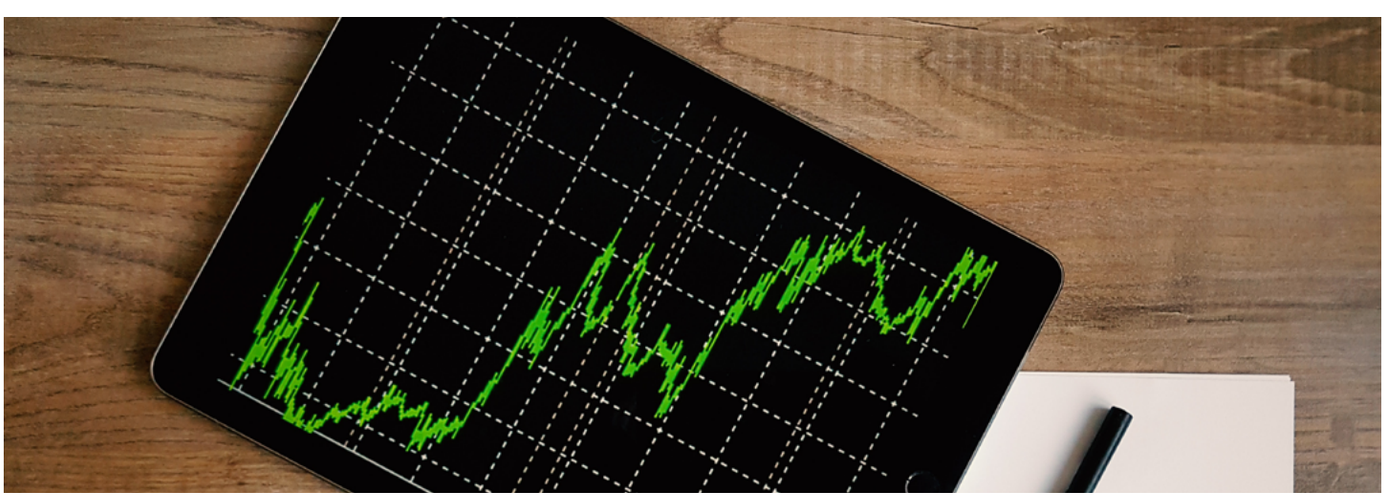
According to the Federal Reserve web site, the annual inflation target is 2%. In fact the Fed has done a good job meeting their stated objective, achieving an actual inflation rate of 1.6% over the past ten years. Of course, inflation silently erodes the buying power of your portfolio. Compounded over fifteen years.




the annual inflation target

**an inflation rate of 1.6% reduces your after tax return from 4.0% to 2.5%.**

All of this means that if you invested $100,000 in 2004, your ACTUAL return, i.e. the kind of return you can actual BUY something with in 2018 dollars AFTER you pay brokerage fees and taxes is a mere 2.5% compounded per year. More specifically, after getting your initial investment back, you have $44,382 in net gains after fifteen years. Here you manage to save and invest $100,000 and patiently keep it invested for a LONG time. And when it's time to sell, you've actually made very little money while paying your broker and the government along the way and in the meantime, your purchasing power went down due to inflation!



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“Real estate cannot be lost or stolen, nor can it be carried away. Purchased with common sense, paid for in full, and managed with reasonable care, it is about the safest investment in the world.”

**- Franklin D. Roosevelt, U.S. president**

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“Ninety percent of all millionaires become so through owning real estate. More money has been made in real estate than in all industrial investments combined. The wise young man or wage earner of today invests his money in real estate.”

**- Andrew Carnegie, billionaire industrialist**

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“Don’t wait to buy real estate. Buy real estate and wait.”

**- Will Rogers, actorreal estate and wait.”**

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“Landlords grow rich in their sleep without working, risking or economizing.”

**- John Stuart Mill, political economist**

# Invest in real estate through a Multi-family syndication

A multifamily syndication is a group of people who pool their resources to purchase an apartment building which would otherwise be difficult or impossible to achieve on their own. This typically involves the **"general partners"** who organize the syndication, including finding the property, securing financing and managing the property, etc.

The group of people who are providing the cash investment are often referred to as **"passive investors"** or **"limited partners"**. In return for their investment, the limited partners receive an equity share in the syndication along with cash flow distributions and profits.

## 5 Advantages of investing in multi-family real estate

- Below Average Risk
- Above Average Returns
- Passive Income
- Extraordinary Tax Benefits
- Inflation Hedge

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## Below average risk

Perhaps the greatest advantage of investing in apartment buildings lies in its extremely low risk profile. For decades, the multifamily market has proven much less volatile than residential real estate and the stock market.

When the housing bubble popped in 2008, the delinquency rates on Freddie Mac single-family loans soared, hitting 4% in 2010.

**By contrast, delinquency on multifamily loans peaked at 0.4%.**

## Above average returns

As we've seen, the average stock market return over the last 15 years was 7.04% but after fees, inflation, and taxes that return becomes a paltry 2.5%.

**On the other hand, multifamily syndications routinely return average annual returns of 10% and above.**

That's compounded (i.e. without volatility) and after fees, inflation, and yes, even taxes.

## Passive income

Unlike stocks and bonds, multifamily syndications generate cashflow for its investors from the income generated by the property. This cashflow afforded by multifamily investing generates the kind of passive income that leads to financial freedom.

The brilliant part is that the multifamily asset itself is appreciating in value over time and can usually be sold for a significant profit. The combination of passive income and appreciation lends itself to true passive income.

## Tax benefits

Real estate has advantages over nearly every other investment, from stocks and bonds to business investments to precious metals. The IRS allows multifamily investors to write off 3.6% of the value of the building each year as an expense through something called "depreciation".

This is only a "phantom" expense, meaning it doesn't actually cost you anything but it does reduce your taxable income. The reason for this is simple: the U.S. government wants people to invest in real estate; it's actually a tax incentive, and it's required by law.

**To illustrate depreciation, let's look at this example:**

Let's say you invest $100K in a multifamily syndication and make a 10% cash-on-cash return (or $10,000) in a particular year. It appears that you should be paying taxes on your $10,000 gain, but that's without the magic of depreciation:

# Tax benefits
## (Continued)

The main thing to note here is that the $10,000 you put into your pocket is entirely tax free. Instead of showing a taxable income, your tax return shows a taxable loss.
You can even "carry forward" your "loss" to future years or you can use it to offset gains from other passive income – further reducing (or even eliminating) taxes in the future, too.

Depreciation is a benefit of ALL real estate investments, but multifamily gives you an additional tax bonus – called bonus depreciation. This allows us to deduct the entire value of the investment from our taxable income in the first year.

# Inflation hedge

Multifamily investments are a fantastic hedge against inflation. If you recall, the Federal Reserves inflation target is 2% each year, which means everything goes up in costs, including rents.

As income goes up, so does the value of the property. It's true that rents are going up by 2% but so are expenses! And that keeps the net income of the property the same and with that the value of the property, right?
No ... take a look at the following table that shows both the rents and expenses going up 2% each year, look at what happens to the Net Operating Income:

| Purchase | Purchase | Year 1 | Year 2 | Year 3 | Year 4 | Year 5 |
|---|---|---|---|---|---|---|
| Inflation rate | | 2% | 2% | 2% | 2% | 2% |
| Income | **$10,000** | $10,200 | $10,404 | $10,612 | $10,824 | $11,104 |
| - Expenses | **$7,677** | $7,820 | $7,976 | $8,136 | $8,298 | $8,465 |
| = Net operating income (NOI) | $2,334 | $2,380 | $2,428 | $2,476 | $2,526 | $2,576 |

The Net Operating Income (NOI) is going up! The higher the NOI, the higher the value of the property.  In fact that 2% inflation rate results in a 10% average annual return on the cash invested in a typical real estate.

It's like magic: the more inflation goes up, the more the apartment building appreciates – the perfect hedge against inflation.

# The problem with buying single family homes

Most passive investors who are considering investing in real estate think first of investing in single family houses.  One option is to buy one or more single family rentals (SFR) and become a landlord. The challenge is that it's not very passive. Since you're the landlord, you're responsible for finding the tenant, taking calls when something breaks, making repairs, finding a new tenant etc.

The real problem with SFRs is that they're very market-sensitive. Look at what happened during the great recession of 2008: SFRs suddenly had higher vacancies as tenants fled into cheaper apartments and property values plummeted, resulting in a massive loss of capital. As we've already seen, multifamily properties are much more recession-proof, allowing us to ride out a downturn in the market if necessary.

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