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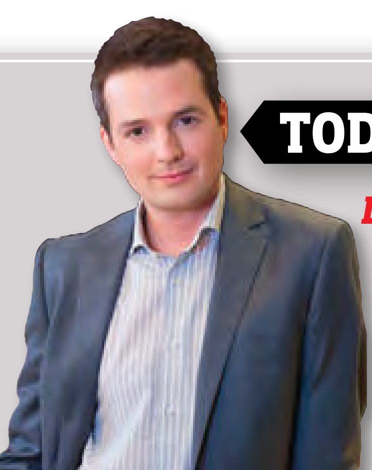

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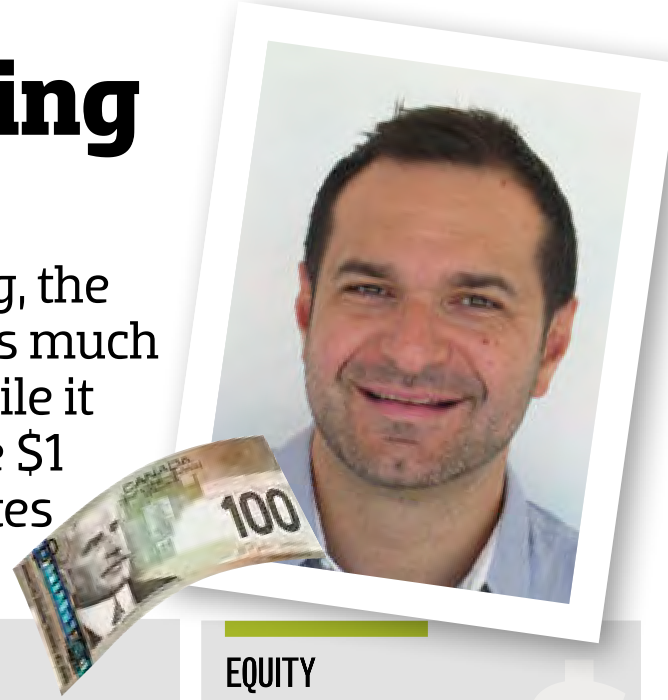
The 50-something investor

With retirement fast approaching, the 50s investor is looking to have as much money acquired as possible. While it may seem like a steep climb, the $1 million plateau is reachable, writes *Paul Kondakos*



As retirement age approaches, having enough money or equity to retire comfortably is an ongoing concern. Our couple, in their 50s, have done relatively well to this point, but are now looking to pad their retirement nest egg even further by attaining at least $1 million in real estate equity within 10 years. While it may seem like a daunting task at first, their retirement goal is achievable if they approach their real estate investing aspirations with a sound strategy in place.

We must first analyze the current financial situation of the couple to identify their assets, liabilities and cash flow to establish how much equity the couple has available to invest in their real estate investing plan.

The couple's largest asset is their principal residence valued at $750,000. With a current mortgage of only $106,646, the house has a substantial amount of equity that can be tapped into through a refinance. As evidenced below, the couple can access $500,000 of equity for their real estate investing plans.

THE INVESTORS
Married couple, 50s, living in Halifax, NS

THE GOAL
Wants to have a $1 million net equity in real estate within 10 years

THE PAYOFF
Security, additional money for retirement

INCOME/SAVINGS
Household income $200,000/year, $0 in RRSPs, $50,000 in savings, $10,000 credit card debt

ASSETS/LIABILITIES/CASH FLOW
Principal Residence: $750,000 Current Value with $106,000 mortgage

Once the principal residence has been re-financed, we must analyze the couple's cash flow to ensure they can support the new mortgage payments, along with their existing living expenses. Both earn respectable salaries for a combined gross income of $200,000. Once taxes, mortgage payments and yearly living expenses are taken into account, the couple is left with annual positive cash flow of approx. $28,400. The first order of business is to pay off their high interest credit card debt of $10,000 which they should be able to accomplish comfortably within the first 12 months using their cash flow.

EQUITY
Principal residence value: $750,000
Existing mortgage: $100,000 (rounded down from $106,646)
New mortgage (Refinance at 80% LTV): $600,000
Total equity available: $500,000

We explore two real estate investing strategies to help our couple achieve their goal of $1m in equity within 10 years – conservative and aggressive.

CASH FLOW

Salary 1: $80,000
Salary 2: $120,000
Gross income: $200,000 (employment income)
Net income: $140,000 (average tax rate is approx. 30%)
Annual mortgage payments ($600,000 @ 4.5% / 10 year term): $39,600
Annual living expenses: $72,000
Cash flow: $28,400

THE RECENT GROWTH RATE FOR MURS IN HALIFAX HAS BEEN IN THE DOUBLE DIGITS

CONSERVATIVE APPROACH

WHERE TO INVEST: HALIFAX, NS

The couple is based in Halifax, N.S., which is fortuitous as Halifax has become a favourable area to invest within Canada. In 2011, Irving Shipbuilding was awarded a $25 billion shipbuilding contract from the federal government which is expected to yield 15,000 jobs annually over the next 30 years.

The $25 billion contract, however, is a double-edged sword. As a result of this contract, real estate investors have already started snapping up properties, causing prices to rise and reducing supply making it more expensive to get into the Halifax market. Nonetheless, the long term prospects of the area outweigh the recent run up in prices making Halifax an ideal place for our couple to invest in.

WHAT TO BUY: SMALLER MULTI-RESIDENTIAL PROPERTY

As part of the conservative approach, it is recommended that the couple invest in a small multi-unit residential (MUR) property as it is considered as one of the safest asset classes.

MURs contribute to investor wealth in three ways: cash flow, mortgage pay down and appreciation.

The couple needs to do some legwork here and find a property with the following parameters:

- Size: 3 to 6 units
- Price: $500,000
- Cap rate: 6 per cent and more
- Financing: 4-5 per cent

TIMELINE: BUY FOUR PROPERTIES WITHIN THREE YEARS

In keeping with the conservative nature of this strategy, the timeline for the property acquisitions is spread out over three years. The goal is to have the couple buy their first property and become acclimatized with owning and running a MUR for one year before making their next purchase. After three years, the goal is to have four properties.

Year 0 – Buy first property
Year 1 – Buy second property
Year 2 – Buy third property
Year 3 – Buy forth property

The four properties are to be purchased with a 25 per cent down payment ($125,000 per property) which will come from the $500,000 in equity made available through the re-finance of the principal home.

The recent growth rate for MURs in Halifax has been in the double digits since the announcement of the shipbuilding contract. However, that type of growth is neither unrealistic nor sustainable in the long term. As such, a much more conservative growth estimate for Halifax MURs of 3 per cent will be used to calculate appreciation.

If our couple adopts this strategy and able to execute it, in 10 years they will have surpassed their goal of achieving $1 million in real estate equity.

Real estate investors have already started snapping up properties, causing prices to rise and reducing supply making it more expensive to get into the Halifax market.

THE NUMBERS: $1 MILLION+ IN EQUITY ACHIEVED OVER 10 YEARS

Initial equity invested: $500,000

- Equity realized through 3 per cent yearly appreciation on investment properties: $500,000
- Equity realized through investment property mortgage pay down: $350,000
- Equity realized through principal residence mortgage pay down: $150,000
- Total equity realized in 10 years: $1.5 million

AGGRESSIVE APPROACH

For those with a higher risk tolerance, the following aggressive strategy takes key components from the more conservative strategy and augments parts of it to make it a higher risk, yet higher returns. The two key areas where the conservative and aggressive strategies diverge are use of leverage, geographic location, and size of property.

WHERE TO INVEST: HALIFAX AND THE UNITED STATES

In addition to investing in Halifax, the U.S. offers an exceptional investment opportunity, as the housing market and economy are in recovery mode. The growth rate for many U.S. cities is now in the double digits, and this trend looks to keep up for the foreseeable future. Areas where our couple should consider investing include Scottsdale, Phoenix, Houston, Dallas, and San Francisco, among others.

WHAT TO INVEST IN: MULTI-UNIT RESIDENTIAL PROPERTY

Just like the conservative approach, it is recommended that the couple invest in a multi-unit residential property.

WHAT TO BUY: MID-SIZE MUR IN HALIFAX – 12 TO 24 UNITS – INVEST $300,000

The mid-size MUR typically offers better cap rates and stronger cash flow than smaller ones. This allows the investor to hire a superintendent and property manager to manage the property should they choose not to manage it themselves.

The couple needs to do some legwork here and find a property with the following parameters:

- Size: 12 to 24 units

The growth rate for many U.S. cities is now in the double digits, and this trend looks to keep up for the foreseeable future

- Price: $2 million
- First mortgage: 75 per cent LTV
- Second mortgage (Vendor Take Back (VTB)): 10%
- Cap rate: 6.5 per cent or more
- Financing: 4-5 per cent

For the aggressive investor increased leverage via a Vendor Take Back (VTB) can be used to create wealth even faster. In this case, the couple needs to find a property with the above parameters where the seller will entertain holding a VTB. This brings up the LTV of the property to 85 per cent, thus increasing the buyers' leverage. The buyers would then only need to come up with $300,000 (not including closing costs) as a down payment on a $2 million property. After five years, the buyers would refinance the property to pay out the VTB.

WHAT TO BUY: SMALL MUR – 3 UNITS TO 6 UNITS IN THE U.S. – INVEST $200,000

Investing in the U.S. has become a little easier for Canadians, as the credit markets continue to loosen up with the housing market recovery.

The couple needs to do some legwork here and find a property with the following parameters:

- Size: 3 to 6 units
- Price: $800,000
- Cap Rate: 7 per cent or more
- Financing: 5 per cent

The recent growth rate for MURs in certain parts of the U.S. has been in the double digits since as the housing market recovery has started to take place. However, similar to the Canadian model, that type of growth is neither unrealistic nor sustainable in the long term. As such, a much more conservative growth estimate for the U.S. of 4 per cent will be used to calculate appreciation.

THE NUMBERS: $2,000,000+ IN EQUITY ACHIEVED OVER 10 YEARS

Initial equity invested: $500,000

- Equity realized through 3 per cent yearly appreciation on Halifax property: $600,000
- Equity realized through 4 per cent yearly appreciation on U.S. property: $250,000
- Equity realized through Halifax investment property mortgage pay down: $400,000
- Equity realized through U.S. investment property mortgage pay down: $150,000
- Equity realized through principal residence mortgage pay down: $150,000

Total equity realized in 10 years = $2.05 million

Using a more aggressive strategy, our couple is able to realize even greater wealth over a relatively short period of time. If our couple adopts this strategy and is able to execute it, in 10 years they will have far surpassed their goal of achieving $1 million in real estate equity, which will make their retirement years much more comfortable and enjoyable. ■