

# **How to Achieve Financial Independence and Live Your Passion Regardless of Age or Income**

10 Paths to Financial Independence Analyzed



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From a *Declaration of Principles* jointly adopted by a Committee of American Bar Association and a Committee of Publishers and Associations.

# Dedication

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Dedicated to those that have the discipline to implement a plan—any plan—towards achieving Financial Independence and Living Their Passion. You are farther along the trail than the other 99% who don't even try.

And dedicated to the professionals that help us all achieve our financial independence to live our passions: the accountants and CPAs, the real estate agents, the lenders, the attorneys, the financial advisors and planners. As complexity increases, we need professionals with highly specialized knowledge and skills to guide us along the way. Thank you, everyone.

To my son James: you are amazing. This should answer your initial questions about achieving financial independence and living your passion. Your father loves you very much.



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## Introduction

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*"Plans fail for lack of counsel,  
but with many advisers they succeed."*

*– Proverbs 15:22*

This book is written *to* my son, James. Over dinner just after he graduated from college, he asked me about how to achieve financial independence (FI) so he could perhaps retire early or, at least, pursue his passion without worrying about money.

But, while the book is written *to* my son, it is written *for* you.

Regardless of your current age, you can use the strategies and analysis in this book and apply them directly to yourself. A plan for a 22-year-old seeking financial independence is often similar to that of a 45-year-old trying to catch up on saving for retirement.

The same is true for income; you may earn more, or you may earn less than my son. You will still be able to modify the plans using the links provided in the book. This will allow you to fit them to your personal needs to achieve your own version of FI and live your unique passion.

### **How This Book Is Structured**

This book uses the Real Estate Financial Planner™ software to model various approaches to achieving FI. I will be explaining to my son how each approach works and what the assumptions are for each one. You will see how long it takes to achieve FI with the assumptions we used.

Then, I'll compare how quickly we achieve FI with each new approach to how quickly we achieved it with previous approaches we considered.

Note: At times I may refer to the Real Estate Financial Planner™ simply as the Planner™ for short.

### **Definitions, Abbreviations, and Acronyms**

Sometimes I like to create new phrases and terms which you will not find definitions for outside of this book. If any of the terms I use in the book are unfamiliar to you there is a Glossary in the back. I included a list of the acronyms and abbreviations I used as well. If at any time you feel a bit lost do not hesitate to take a quick peek at them before jumping back into the path you were reading about.

## My Assumptions Versus Your Assumptions

It is inevitable that the assumptions I select to use for my son will be different than the assumptions you would have preferred I use. I remember reading books on personal finance or investing where the example the author used was interesting to me, but I always wished I could see how the example would have applied to my unique situation.

Historically, books can't give you the ability to change the assumptions used in examples to see how the results would apply to your situation.

This book is different.

Since we used the Real Estate Financial Planner™ software to calculate all the scenarios, it allows us to grant you the ability to change any or all of our assumptions to whatever you would like to use.

Here are a few examples that this book, when combined with the Real Estate Financial Planner™ software, will allow you to modify:

- My son is starting with zero dollars saved, but you have some in savings already. How does that impact the results for you and your ability to achieve FI?
- My son currently rents and owns no properties. What if you already own a home? Or, a home and some rental property? How does that change things?
- We are starting in an environment where interest rates on 30-year fixed rate mortgages for owner occupant loans where you pay a single up-front private mortgage insurance (PMI) payment is 4.375%. If interest rates are higher when you start, how will that affect you? What if interest rates are lower? Does that matter?
- The properties my son can buy are very likely to have break-even to slightly negative cash flow if he bought them with 20% down payment. If you can find properties with better cash flow—or worse cash flow—how will that impact you and your pursuit of FI?
- My son will likely be buying properties for full retail price because he is in a strong seller's real estate market where properties are being bid up above asking price. If you can negotiate better deals, what does that mean for you and your situation?
- My son is saving 30% of his income to invest in his FI. What if you save more? What if you save less?
- We are assuming the stock market and bonds will continue to provide the same returns they have since 1871. What if they are better? What if they are worse?
- We believe property values will keep pace with inflation as they have nationwide for over 100 years according to Case and Shiller. What if property values go down? What if property values stay the same? What if they go up faster than inflation? How will each of those impact your plan?

For each scenario that we run using the Real Estate Financial Planner™ software, we will provide you with a link to copy that scenario into your own Planner™ account. From there, you can modify any of our assumptions and rerun it to see personalized, customized results for you and your journey toward FI.

So, while this book is written *to* my son, you can see it really is written **for you and your unique situation and your unique assumptions about the world**. It truly is a book on how to achieve financial independence and live your passions regardless of age or income since the book (with the help

of the Real Estate Financial Planner™ software) adapts itself to you, your age, your income, and your assumptions about the world around you.

## 10 Paths to Financial Independence Analyzed

The sub-title to this book is: 10 Paths to Financial Independence Analyzed. That's because I will be analyzing 10 different scenarios to get to FI. Each scenario is its own chapter.

There are additional paths one could take. You could combine some aspects of the paths to create new approaches. You may opt to try a path I opted not to cover. That's fine.

Who knows, perhaps there will be a second book analyzing 10 additional paths in the future.

For this book, these are the 10 paths I will be analyzing and explaining:

1. Investing in Stocks and Bonds
2. Saving Different Percentages of Your Income
3. Investing in Stocks and Nomading™
4. Investing in Stocks and Nomading™ With Gift Down Payments or No Down Payment
5. Investing in Stocks, Own Your Own Home, Buy 20% Down Payment Rentals
6. Investing in Stocks, Nomading™ and House Hacking (HH) or Getting A Side-Hustle (SH)
7. Investing in Stocks, Nomading™ with HH/SH and Paying Off Mortgages Monthly with Cash Flow
8. Investing in Stocks, Nomading™ with HH/SH and Paying Off Mortgages in Full
9. Investing in Stocks, Nomading™ with HH/SH and Buying Fewer Properties
10. Investing in Stocks, Nomading™ with HH/SH and Selling Some Properties to Achieve Financial Independence and Live Your Passion (FILYP)

## Encouragement and a Warning

If you are a bibliophile like me, I imagine you have high expectations at this point. Here's both encouragement and a warning.

First, the encouragement: I believe this book will exceed your expectations. You may have seen similar modeling completed by others for chapters one and two on investing in stocks and saving different amounts of money. So have I.

I have been reading and studying real estate investing books and courses for over 20 years. I've been teaching classes to the local real estate investor group I co-founded with my friend Paul in 2003 for over 15 years. I tell you this because you've never seen anything like what I am going to share with you in chapters three and beyond. The closest thing you can find are a couple of sections from the book *Creating Wealth* by Robert Allen. However, the comparison is like watching an old 11-inch black and white television to experiencing an IMAX.

Your high expectations are justified. Now, the warning.

You will see an overwhelming amount of detail about each scenario. I will slow down and take my time to explain every assumption made.

I hate it when an author gives an example—especially one I would consider implementing personally—but fails to adequately explain the inner workings, assumptions, and the details. Details matter. The saying “the devil is in the details” is appropriate here. This is your financial future we are working on after all. Details could mean the difference between eating caviar and cat food in your retirement.

The Real Estate Financial Planner™ software is refreshingly complicated. It is not “enter a few numbers on a web page” and it just spits out equally simplified (and meaningless) results. I think of the Real Estate Financial Planner™ software like a programming language to “code” your investing strategy. Then, the software runs and returns lots of data for you to analyze and reflect on.

The warning then is detail.

I could have written a fluff book that gets you excited and pumped up about these strategies. I chose not to. Although, I do hope you will get some of that.

Instead, I opted to write a detailed analysis and explanation of 10 plans to achieve Financial Independence, Live Your Passion (FILYP). It may seem dry and dull at some points—although I might try to add some silliness to make it more bearable.

Feel free to skip ahead a little on the first reading. You have my permission to do so. You can always come back later and check my math and drill down into the details later, on a second pass.

## **Dream Team**

I chose to include the biblical quote, “Plans fail for lack of counsel, but with many advisers they succeed,” from Proverbs 15:22 at the start of this introduction for a reason.

Even with my experience teaching many of these concepts for over 15 years to local real estate investors in Northern Colorado and the level of detail I warned you about, implementing these plans can be complex and highly nuanced.

**You need counsel.** You need professionals that specialize in their unique fields to assist you. You need a dream team.

Perhaps you are a potential client of mine and you received a copy of this book as a gift from me. Or, maybe you received it as a gift from a professional in your local market. **Ideally, get with the person who gave you this book and start building your dream team.**

One good team member can usually introduce you to other key dream team members. Great lenders and real estate agents typically work together. Accountants, bookkeepers, CPAs, financial planners, and estate planning attorneys—all critically important team members for various parts of implementing your plan—tend to work together.

So, reach out to the person who shared this book with you—they are one of the few that truly understand the strategies we are presenting here—and schedule a time to start working on implementing your own variation of these plans.

## **Biggest Understatement of the Book**

I love charts.

You may not yet know it, but that is the biggest understatement in this entire book.

Throughout this book you will see more charts than you thought it would be possible to produce. You'd be wrong in that assumption. There are even more charts for you to drill down into if you decide to copy the scenario to your own Planner™ account.

I've tried to show only the charts that illustrate a concept, make a point, show an end result, or compare scenarios to one another. And with that, let's get started.





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## Path 1: Investing in Stocks and Bonds

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A very common approach people use to achieve FI is to work at their job and invest part of their income. In this chapter, I'll show you how saving part of your income and investing in stocks and bonds in different ratios will impact how quickly you might expect to achieve FILYP.

Before we get too far into this, let's define what financial independence is.

### Financial Independence

There is a growing movement called Financial Independence/Retire Early (FIRE) and there are some great additional resources available for you to learn more about it. One I would recommend you read for context on how many others think about it is *Your Money or Your Life: 9 Steps to Transforming Your Relationship with Money and Achieving Financial Independence* by Vicki Robin and Joe Dominguez.

However, for the sake of this book, I have both a philosophical definition and a mathematical one.

### Philosophical Definition of Financial Independence

Philosophically, I believe you have both human capital and financial capital. Human capital is your ability to work and generate income. Financial capital is your ability to have money work and generate more money for you.

Most of us start our careers with very high human capital and little or no financial capital.

Financial independence is when your financial capital can produce your target required income to be able to meet your desired standard of living.

### Mathematical Definition of Financial Independence

To define it mathematically—and how we will use it in this book—will take additional explanation.

For this book, the mathematical definition of FI is when your net cash flow from any rental properties after all expenses plus a safe withdrawal rate (SWR) of any non-real estate investments (like stocks or bonds) meets or exceeds your desired standard of living.

It might be best explained with an over-simplified example.

Let's say you have five rental properties that each produce \$200 per month in cash flow after all expenses including:

- Mortgage payment (principal and interest)
- Property taxes
- Landlord insurance policy
- Vacancy allowance
- Maintenance on the properties
- Property management costs
- And any capital expenses like roofs and replacing furnaces, etc.

Five properties with \$200 per month each = \$1,000 per month in net cash flow after all expenses.

$$\text{\$200/month} \times 5 \text{ Properties} = \text{\$1,000/month}$$

Let's also assume that you have \$300,000 invested in stocks and bonds.

Furthermore, let's assume that you believe that it is safe to withdraw 4% of the money you have invested in stocks per year and not run out of money. We call that 4% your safe withdrawal rate (SWR).

If you can safely withdraw 4% of your \$300,000 dollars per year, that means you can withdraw \$12,000 per year or \$1,000 per month.

$$4\%/year \times \text{\$300,000 in stocks and bonds} = \text{\$12,000/year or \$1,000/month}$$

If you add up the \$1,000 per month from your stocks and the \$1,000 per month from your rental property cash flow, you can spend \$2,000 per month total from all your investments each month.

$$\text{\$1,000/month rental cash flow} + \text{\$1,000/month from stocks/bonds} = \text{\$2,000/month}$$

Here's the check to see if you've achieved FI: can you live your passion on \$2,000 per month?

Some people will try to complicate things and ask: what if living my passion still brings in income? Am I FI if the income from living my passion plus the returns from my investments will support me? Probably.

It is more conservative to have your entire standard of living covered by the return from your investments and that is what we will use for all the math in the book. It is even more conservative to have your investments cover twice your desired standard of living, but that's a topic for another book. Regardless, for now, you can adjust these assumptions in the Real Estate Financial Planner™ software to model your actual reality and desires if you'd like.

The income you earn from the work you do will provide you with the resources you need to both support yourself in the short-term and buy back your time. You buy back your time by investing the fruits of your human capital, income, into financial capital.

Here's how I personally think about it. For the sake of this book, I am assuming you are earning \$70,000 per year.

**IMPORTANT NOTE:** Remember, if you are not my son and you have a different income, you can modify this (and all other assumptions) in the Real Estate Financial Planner™ software to accurately represent your actual income.

Back to the story: How much would you need to have invested to be able to generate the \$70,000 or so per year that you are earning from your job? If you assume that your safe withdrawal rate is 4%, you would need to have:

$$\begin{aligned} \text{Amount Invested} \times .04 &= \$70,000 \\ \text{Amount Invested} &= \$70,000 \div .04 = \$1,750,000 \end{aligned}$$

Congratulations... for the hard work you did in college and getting a good job, just out of college you essentially have the equivalent of \$1.75 million dollars in net worth. Another way I would describe this is you (the person) are a \$1.75 million-dollar asset that when put to work daily in a job, earns \$70,000 per year.

Remember though, to achieve financial independence, we want to convert the fruits of your human capital (your income) into financial capital to buy back your time.

If you assume that you need to work 40 hours a week for 50 weeks a year, that means that you work about 2,000 hours per year to generate \$70,000 per year. That's:

$$\begin{aligned} \text{Income Per Hour} &= \$70,000 \div 2,000 \\ \text{Income Per Hour} &= \$35 \end{aligned}$$

If you wanted to buy back an hour of your time per year (at your current earning power/human capital rate), you'd need to have investments in financial capital that generate a return of \$35 per year. How much would you need to have invested at a 4% safe withdrawal rate to earn \$35 per year to buy back an hour of your time?

$$\begin{aligned} \text{Amount Invested} \times .04 &= \$35 \\ \text{Amount Invested} &= \$35 \div .04 = \$875 \end{aligned}$$

What that means is each time you save \$875 in your financial capital account, you buy back an hour of your time per year. I know you are the "undisputed king of computation" (according to your grade school teacher), so I am sure you can see that if you multiply that by 12 you can find out how much you would need to have invested to earn back an hour per month. In your case, you'd need to have \$10,500 invested to buy back one hour per month of your time.

$$\begin{aligned} \text{Amount Invested} \times .04 &= \$35 \times 12 \\ \text{Amount Invested} &= (\$35 \times 12) \div .04 = \$10,500 \end{aligned}$$

Or, multiply your \$35 per hour by 50 to find out what the "cost"/investment is to buy back an hour per week of your time.

$$\begin{aligned} \text{Amount Invested} \times .04 &= \$35 \times 50 \\ \text{Amount Invested} &= (\$35 \times 50) \div .04 = \$43,750 \end{aligned}$$

I will be going into a ton more detail about how to accumulate the money to buy back your time, but I believe it is important to realize the relationship between human capital and financial capital. And, in my opinion, a key concept of financial independence and living your passion is that you are trying to convert human capital (time) to financial capital (money) that produces more passive income (the fruits of your financial capital) so you no longer have to invest your human capital in work you deem undesirable (more on desirability of work later as well).

## Keeping Expenses Low and the Obvious Relationship Between Income and Financial Capital

I will direct your attention to the obvious relationship between your income and financial capital invested. If you need more income to support your expenses, you will need more financial capital to support those expenses.

This raises an important early discussion about your expenses.

You are lucky. You are just out of college and still have the standard of living expectations of a young adult in college. **Beware standard of living creep.** You don't need to live in a house like you grew up in. You don't need to buy a car like your mom or I drive. You don't need to eat a burrito at Qdoba everyday like I do. You don't need to buy every Hearthstone™ card like I do. You don't need to have the fastest high-speed internet in your house like we had when you were growing up; well... maybe that one.

And, that snarky comment about high speed internet... is another point. You get to choose what is important to you and what you are willing to splurge on. I would strongly recommend you pause to consider what you are spending your money on though.

I have a couple rules of thumb that complement the discussion above on human capital and financial capital. I call it my "Qdoba burrito rule" or my "Netflix rule." Same rule, different names. Here's how it works: if you want to eat out and get a burrito at Qdoba once a month or subscribe to a service like Netflix, you will need to have about \$3,000 invested to afford that from investment income with a 4% safe withdrawal rate. I am assuming the burrito or Netflix is about \$10 per month and the same safe withdrawal rate, but here's the math:

$$\begin{aligned} \text{Amount Invested} \times .04 &= \$10/\text{month} \times 12 \text{ months} \\ \text{Amount Invested} &= \$120 \div .04 = \$3,000 \end{aligned}$$

How long will you need to work at \$35 per hour (fruits of your human capital), to save up \$3,000? That's 85.71 hours. Ignoring taxes, you are over two weeks. If you consider income taxes to net \$3,000, you are closer to three weeks of work just to be able to enjoy a Qdoba burrito or Netflix from financial capital and a 4% safe withdrawal rate. Ultimately, it is up to you to decide whether you do want the monthly burrito or Netflix service. As you well know, I would need to have about \$90,000 invested to support my daily Qdoba habit (estimated at \$300 per month) and I may be OK with that while you may not be. If you do decide you want Netflix or a burrito every month, it will extend how long it will take for you to achieve FILYP by about three weeks if you were saving 100% of your income (which you are probably not).

Every additional expense you have means two things that will slow down your ability to achieve FILYP.

***First, it means you need to save more to keep that expense in retirement since you will need more money invested to generate income to continue it. And secondly, it takes dollars away from you that you could be using to buy back your time by investing them.***

That's an important concept. Probably worth highlighting. It raises an interesting way of looking at your income and expenses when thinking about retirement and I'll discuss that next. And, yes, we are getting to discussing investing in stocks and bonds.

## Save 10% per Year

I would like you to imagine for a moment that you have decided to do what many popular personal finance related newspapers, magazines, and blogs suggest and that you save 10% of your income and invest it in stocks. You decide to enjoy the remaining 90% of your income and use that to fund your current lifestyle.

In your case, you are earning about \$70,000 per year (\$5,833.33 per month), so that means you are saving \$7,000 per year and living on the remaining \$63,000. Furthermore, since you are currently enjoying the lifestyle that \$63,000 per year can buy you, I am going to also assume that when you achieve FI, you'd like your investments to provide you the same \$63,000 so you can maintain the same lifestyle and standard of living as you pursue your passion. If we were discussing retirement, there is some data to suggest that your expenses tend to go down slightly once you enter retirement, but there is some question as to whether this is by choice or necessity. I would rather plan for you to sustain your current lifestyle, and if you choose a lower standard of living, that will be up to you to decide in the future.

## State and Federal Income Tax

If you are earning \$70,000 per year to start and saving \$7,000 of it each year, we will need to estimate what dollar amount and ultimately what percent of your income will be consumed in federal and state income tax.

By consulting with your accountant or CPA or by visiting a reliable tax estimating website, we were able to get an idea of what a single person earning about \$70,000 per year with just himself as an exemption will pay in both state and federal income tax. It looks like you are going to be paying about \$14,055 in federal income tax and about \$3,242 in state income tax. That means you are paying a total of \$17,297 in income tax or about 24.71% of your income in income tax. This 24.71% is your effective income tax rate and it is what the Real Estate Financial Planner™ software uses to estimate your taxes when it does the modeling.

Let's walk through the math together. You are earning \$70,000 and paying 24.71% or \$17,297 in state and federal income tax. You have \$52,703 per year left over before your savings. If you decide to save \$7,000 per year, then you need to live on \$45,703 per year. That's about \$3,808.58 per month.

**IMPORTANT NOTE:** This 24.71% is the effective income tax rate I'll use throughout this book on this and other scenarios. In the very likely case you happen to not be a single person earning \$70,000 per year, then you can modify this and a myriad of other assumptions in your own Real Estate Financial Planner™ account to reflect your reality.

## Target Monthly Income in Retirement

For this scenario, we are going to say you want to have your investments (your financial capital) producing income of \$5,250.00 per month. In the Real Estate Financial Planner™ software we call that your *Target Monthly Income in Retirement* and it is your current standard of living considering your current level of income, income taxes, and savings rate.

Remember, the more you save the lower your *Target Monthly Income in Retirement* can be because you've been living at a lower standard of living and will continue that same standard of living in retirement. Some other folks in the FIRE community seem to take this logic to the extreme and practice extreme frugality.

Your mother and I have not opted for quite that level of frugality. Whether you choose that or not is up to you. It will help you get to your FILYP date sooner, so you will want to weigh what is most important to you: a lower standard of living on lower spendable income and sooner financial independence and living your passion, or delayed FI and a higher standard of living. Mom and I choose a middle ground (although I suspect many people looking in would not consider us frugal at all).

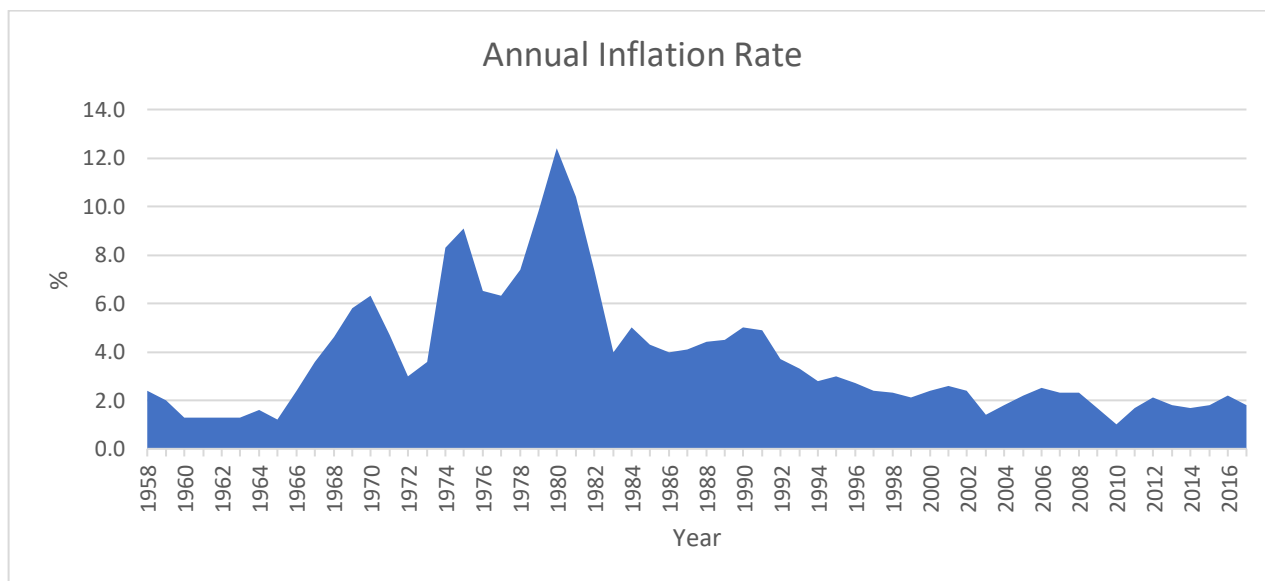
Your brother on the other hand, might have the benefit of self-induced extreme frugality. It will be much easier for him to hit his *Target Monthly Income in Retirement* number and any help he gets from us can have a much bigger impact. While much of what I write here applies equally to your brother (as it does for many of our other readers), I will explain this concept in a lot more detail when I write about his situation in a future book. Back to you for now.

## Inflation

We are moving toward running our first scenario where you are saving 10% of your income (as we discussed above) and achieving FILYP on 90%, but before we do that, we need to have a brief discussion about inflation. Later, I will go to "freaky-town" and show how inflation impacts all the various plans we are considering.

For now, I want to point out that things tend to get more expensive over time. Living on \$3,793.85 per month in 2019 won't be the same as living on \$3,793.85 per month in the year 2040. If we look at the Bureau of Labor Statistics historical data on inflation rates since 1958 through the last full year, 2017, the average historical inflation rate has been 3.7% per year and the median has been 2.7% per year.

Here is a chart showing the yearly inflation rates.



For running this first scenario, I am going to use an inflation rate of 3% per year.

I will assume that you get raises at a rate of 3% per year and that your expenses increase at 3% per year. That also means that the dollar amount that you are saving increases at 3% per year too.

However, because your personal expenses (which is your standard of living) are increasing at 3% per year because the cost of goods and services are going up, on average, at a rate of 3% per year, your standard of living is staying the same. This is true even though it looks like you are living on a much higher dollar amount per month.

Another way of looking at this is if you are earning the same amount of money each year, you are not keeping even. If you are not keeping even, you are losing ground to inflation and lowering your standard of living.

## Safe Withdrawal Rate

I briefly described safe withdrawal rate when I defined financial independence, but there is more to it.

Imagine for a moment that you are 40 years old and have a million dollars in the bank. You want to stop working for money and live your passion from the return on that million dollars. How much money can you spend per year so that you never run out of money? This is what we are talking about when we discuss safe withdrawal rate.

Three professors (Philip L Cooley, Carl M Hubbard, and Daniel T Walz) from Trinity University researched this question and wrote a paper about it<sup>1</sup>. In the paper, they concluded "the lower withdrawal rates of 3% and 4% recommended by some analysts appear to be excessively conservative for portfolios with at least 50% stock, unless the investor wishes to leave a substantial portion of the initial retirement portfolio to his/her heirs." If you start to read about FIRE elsewhere you will see the "4% Rule" referenced. What

<sup>1</sup> <https://afcpe.org/assets/pdf/vol1014.pdf>

they are suggesting (usually citing the same Trinity study) is that you can safely take 4% of your initial retirement portfolio out per year (adjusting it up with inflation each year) and you will be "safe." I do not agree with this and I would strongly advise you NOT to use 4% as a safe withdrawal rate.

While I have not gotten through all the content on his blog<sup>2</sup>, Karsten Jeske has done some serious research into safe withdrawal rates. From what I've read so far, it looks like using 3.25% as a safe withdrawal rate is a much more conservative approach. This is the number I will recommend we use for our modeling of various scenarios. However, the Real Estate Financial Planner™ software will allow you to enter whatever safe withdrawal rate number you believe to be correct. In the future, should you decide you want to rerun these scenarios with 3% or 2.75% or, heaven forbid, 5%... you can easily do that by modifying the safe withdrawal rate variable on the scenarios page.

Since I know you like to do some quick computations, when we were thinking about the 4% rule, you could easily take the amount you needed to earn in retirement and multiply by 25 to quickly discover how much you would need to have invested to generate that amount. So, if you needed \$100,000 per year, you would have needed  $25 \times \$100,000$  or about \$2.5 million at 4% safe withdrawal rate in retirement. With the new, more conservative 3.25%, a rough rule of thumb might now be 30 times. Using the same \$100,000... you'd now need  $\$100,000 \times 30 =$  about \$3 million.

## Stock Market Rate of Return

For the sake of looking at the impact the percentage of your saved income will have on your ability to retire early, we are going to use a very simple, but very common investment strategy: investing in an index fund of stocks. For the stock portion of your mother's and my investments, we personally invest in an index fund. So, this strategy isn't that far-fetched. Of course, meeting with a financial advisor before implementing this would be strongly recommended.

For determining what rate of return to use for the stock market, I am going to use Simba's Backtesting Spreadsheet<sup>3</sup> from the Bogleheads® website. More specifically, I am going to look at the returns for Vanguard Total Stock Market Index Fund Investor Shares (symbol VTSMX). Your mother and I don't use this specific index. Instead, we use one that tracks the Russell 2000, but that's not particularly important at this point in our conversation.

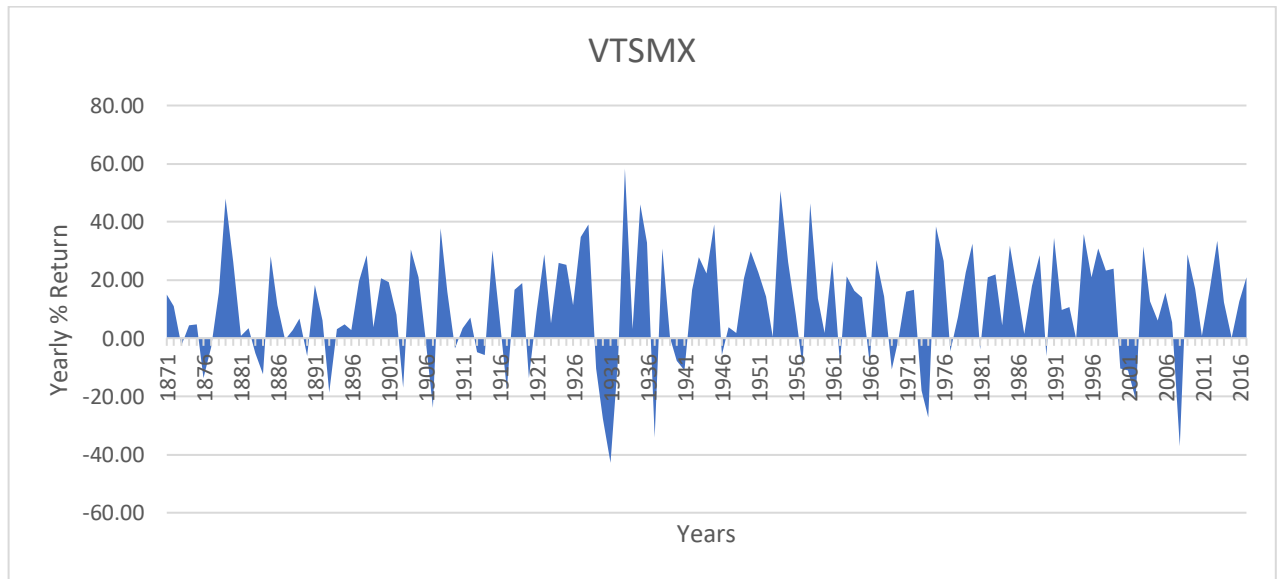
The following is a chart showing what the return was for each year going back to 1871 through 2017 for the equivalent of VTSMX.

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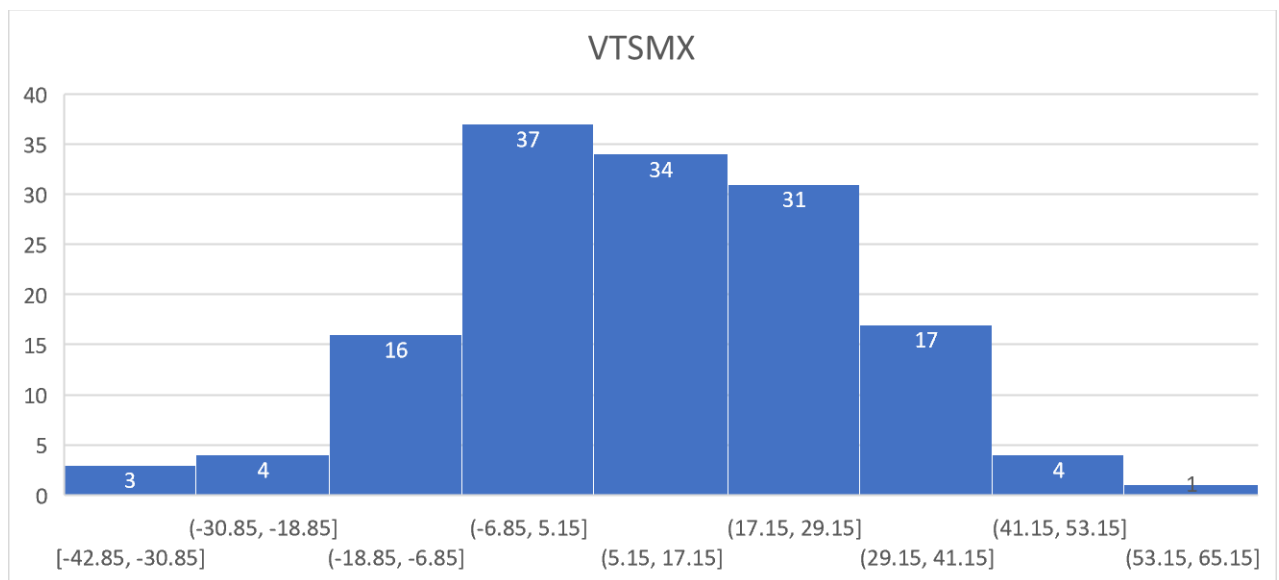
<sup>2</sup> <https://EarlyRetirementNow.com>

<sup>3</sup> [https://www.bogleheads.org/wiki/Simba%27s\\_backtesting\\_spreadsheet](https://www.bogleheads.org/wiki/Simba%27s_backtesting_spreadsheet)





The following histogram shows how frequently certain ranges of annual returns appear for VTSMX.



The average return for VTSMX for that period is 10.57%. The median return for that same period was 11.23%. The compound annual growth rate (CAGR) for that period was 8.97%. For running our scenario, I am going to use the 8.97% CAGR return.

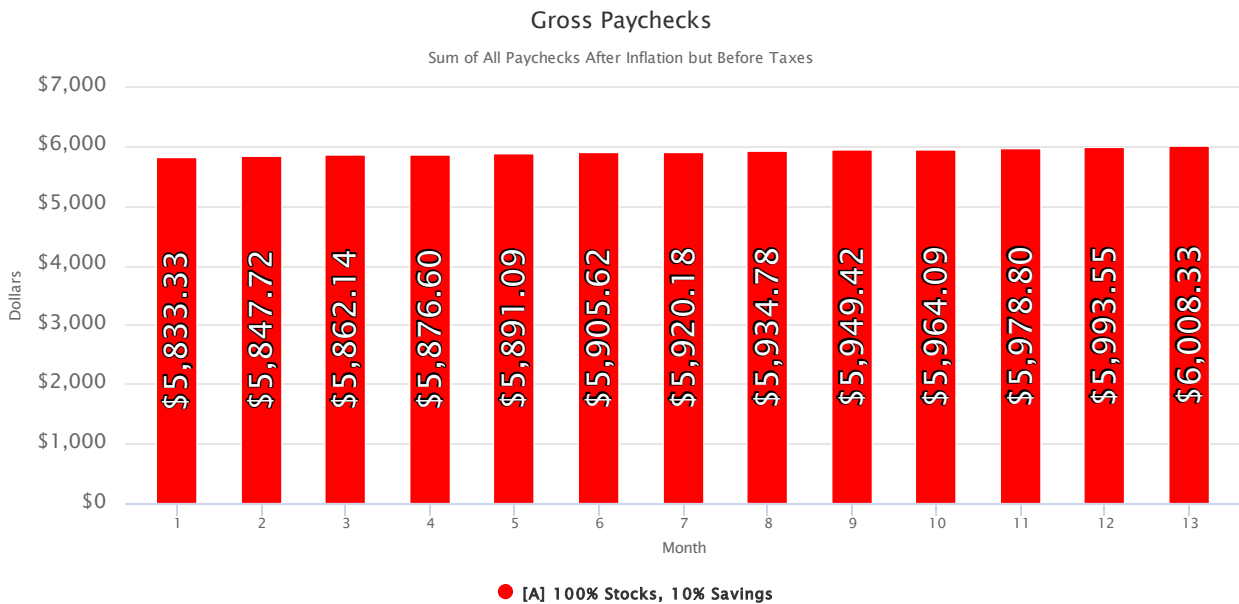
### Setting Up the Model

I am going to do a very basic model of your situation using the Real Estate Financial Planner™ software. For this very first one, I am going to go into a lot more detail than I will later as we compare it to other

scenarios, so please be patient as I explain to you my assumptions and how I set it up. Since we will use a lot of these same settings in future scenarios, we won't have to go over these again. Instead, I'll be able to tell you when something has changed and how it is different.

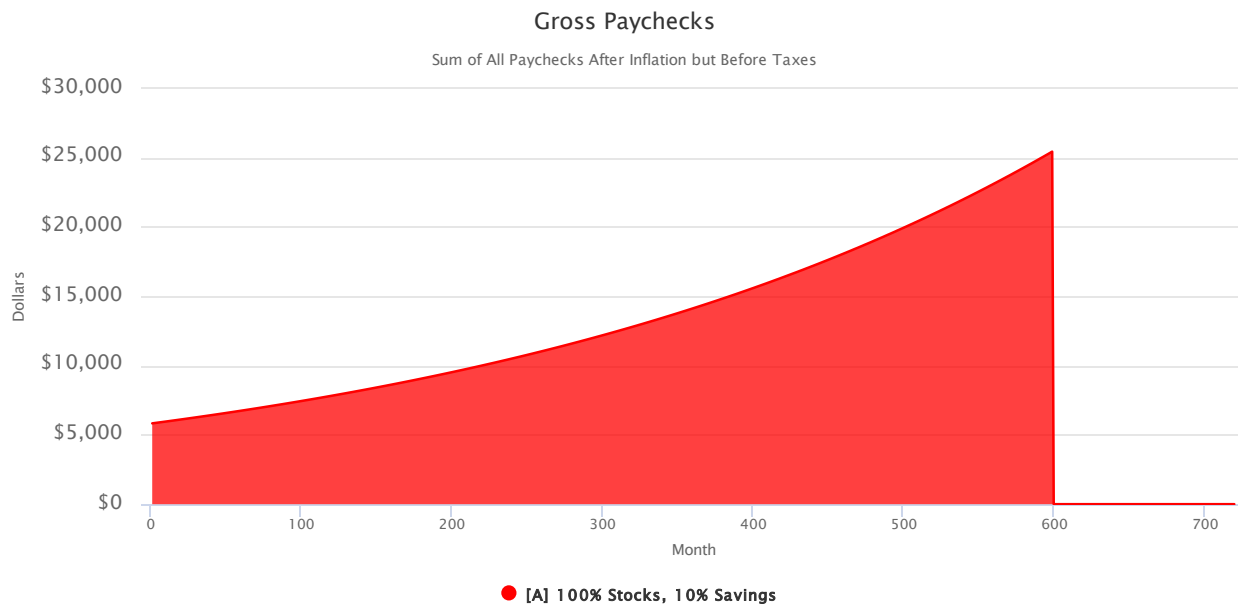
## Gross Paychecks

First, since you are earning \$70,000 per year, that works out to be \$5,833.33 per month gross from your paychecks. We are assuming that your paycheck is increasing by the inflation rate of 3% per year (but calculated monthly). That means that you make \$5,833.33 in the first month but make a little more in the second month. It continues to go up a little bit each month such that in month 13, you are making 3% more than \$5,833.33 which is \$6,008.33. The following chart shows your gross paychecks for the first 13 months.



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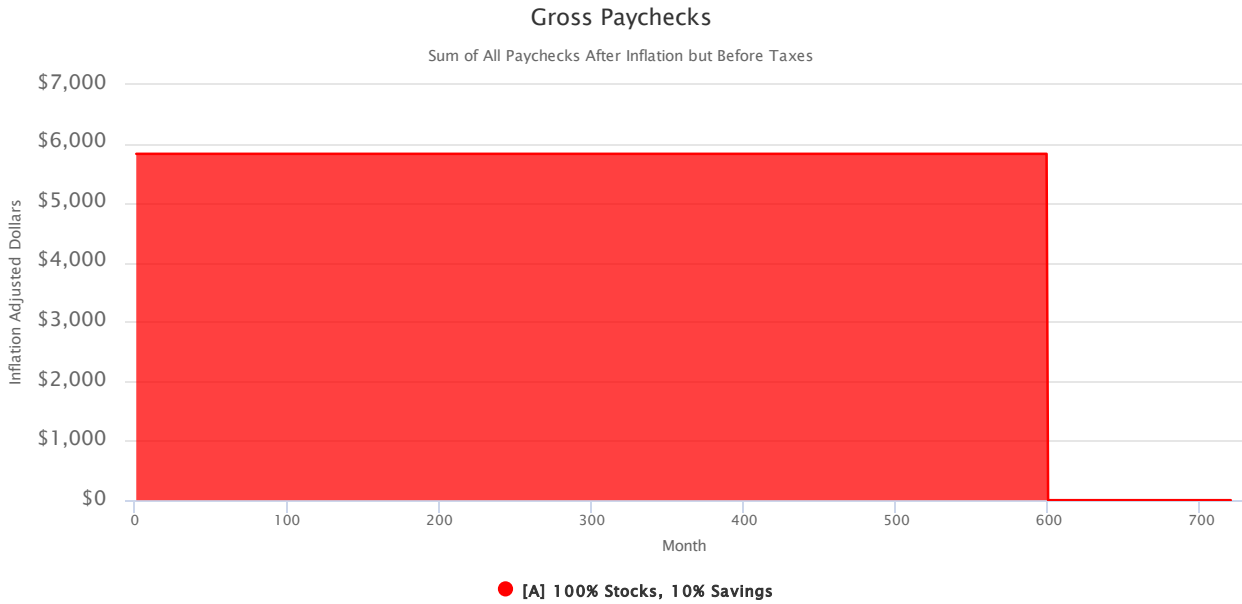
If we look at this over 60 years (that's 720 months), the chart of your gross income looks like this.



A few comments about this chart of your gross income. First, you can see a very steep drop off around month 600. That happens because we set up this scenario to simulate you stopping work and for your income from your paycheck to go to zero once you hit your financial independence goal. Surprise! You end up hitting your goal around month 600. More on that in a bit.

The second thing I want to point out about the chart above is that your income is going up over time from just under \$6,000 per month to just over \$25,000 per month 50 years later (around month 600). Are you really making \$25,000 per month 50 years from now? I will give you a hesitant yes. But that's not the whole story.

If we take that same chart above and we adjust it for inflation, you can see it flat-lines your income to consistently be \$5,833.33 per month. Here's a chart (because I like charts and because I can).

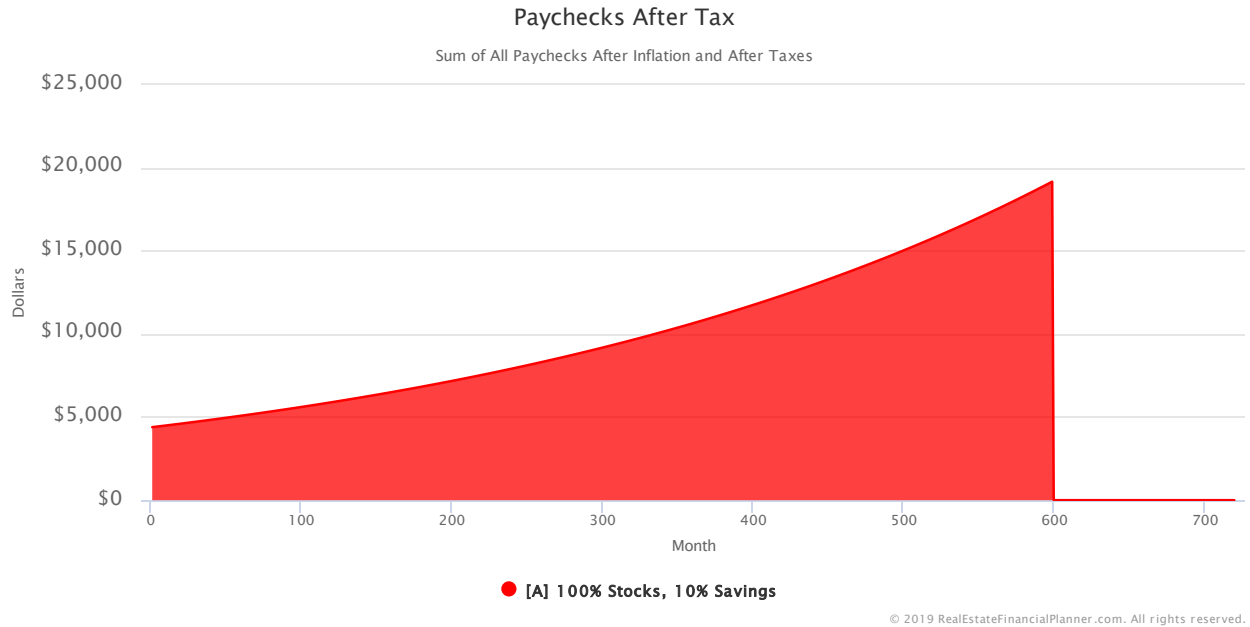


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In other words, your inflation-adjusted gross paycheck before taxes will remain the same \$5,833.33 per month. If ever you feel your income will not keep pace with inflation, you can adjust the income rule to not automatically adjust your income up with inflation in the Real Estate Financial Planner™ software. I personally do not think this is accurate for you. Your income will likely keep pace with inflation.

## Paychecks After Taxes

The following chart shows your \$5,833.33 per month after we subtract out the 24.71% state and federal income tax we discussed earlier.



## Personal Expenses

In this scenario we are assuming that your personal living expenses (your standard of living) is \$3,808.58 per month. Later, we can separate out your personal expenses to include the cost of the house you are living in. For the sake of this simplified scenario, we are assuming you are renting and that it is already included in your personal expenses.



Notice anything interesting about the chart above of your personal expenses that is different than the chart of your paychecks after tax? Maybe something that resembles a cliff? That's right, your personal expenses never go away (until you die). So, while your paycheck from your job goes to zero when you hit FI, expenses have no cliff-like drop off around month 600.

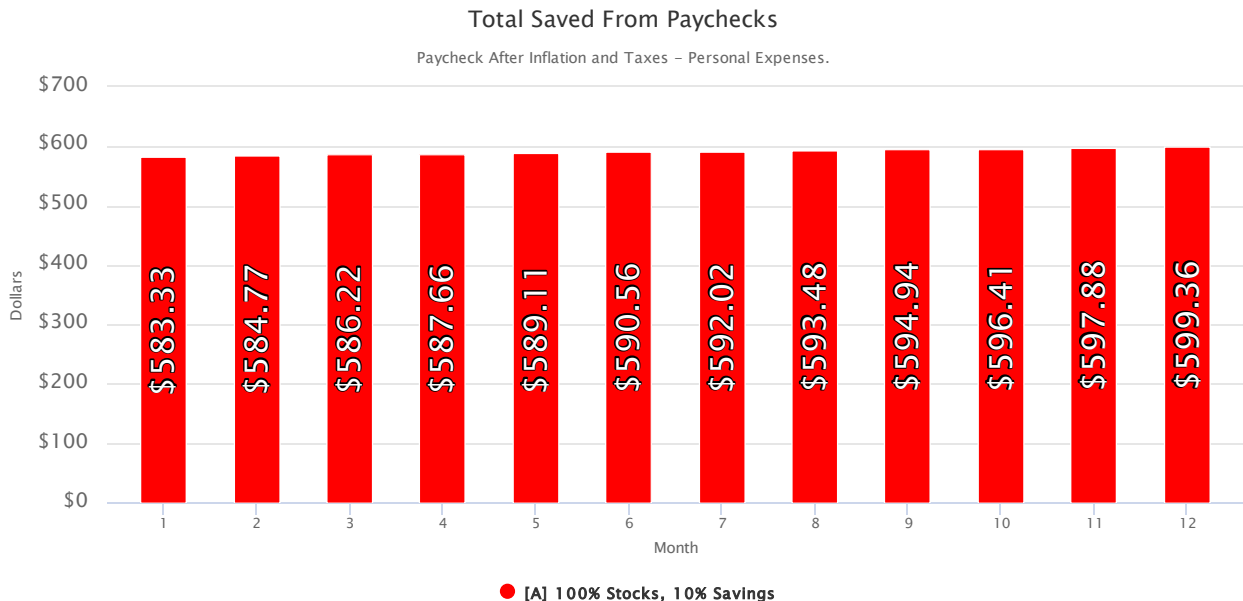
Just like your paychecks, your personal expenses are increasing at a rate of 3% per year.

## Savings

If we take your monthly gross paycheck and subtract your income taxes and personal expenses, what you are left with is the amount you are saving each month. I manipulated your personal expenses for the sake of this scenario such that you are saving 10% of your monthly gross paycheck. So, you are saving 10% of the \$5,833.33 per month that you are earning.

You may have heard of the idea of "pay yourself first." That's what I've done here. I looked at your paycheck and figured out what 10% of your paycheck would be. Before subtracting income taxes on your paycheck, I have you immediately setting aside 10% of the \$5,833.33 each month, or \$583.33, into your VTSMX investment stock market brokerage account. Then, you live on whatever is left over. In a few moments, I will walk you through how changing this savings rate will impact your ability to achieve FI. However, for now... let's continue looking at how we set up this scenario.

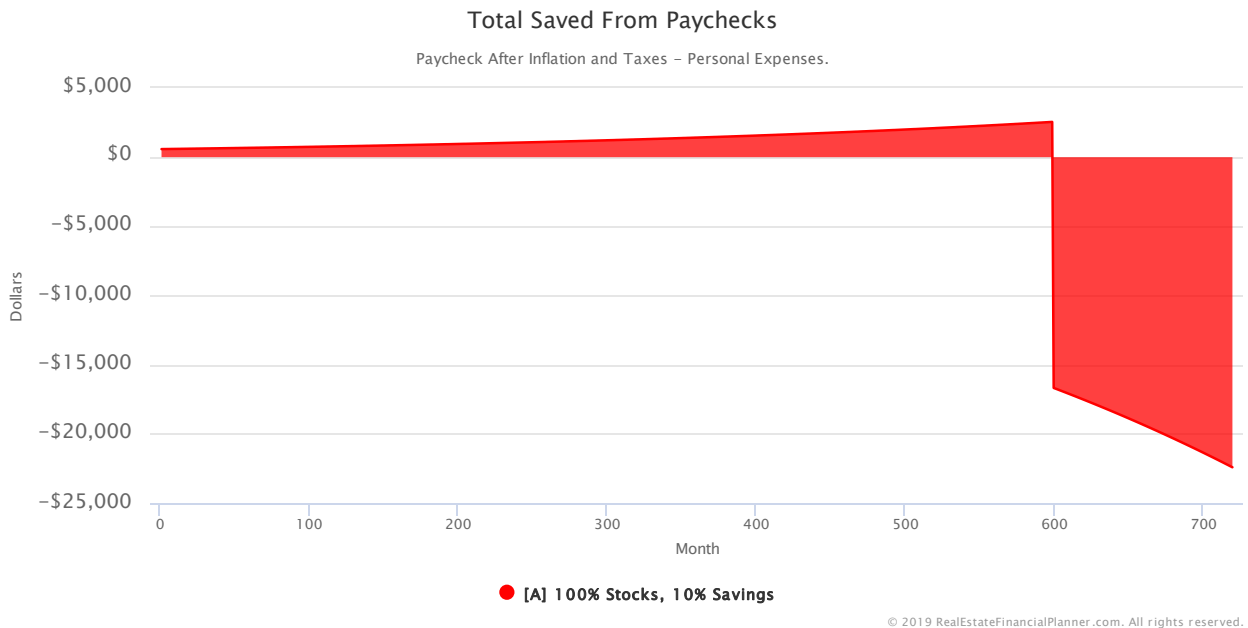
The following is a chart showing how much you are saving and investing in VTSMX for each month for the first 12 months.



As you can see, since your income is going up a tiny bit each month (from inflation) the amount you are saving is also going up a tiny bit each month as well. This is also true of your personal expenses.

If we adjust these numbers back for inflation, it is like you are saving the same \$583.33 per month. I'll spare you a chart showing a flat horizontal line even though I really want to show you this. I do love my charts, as you know.

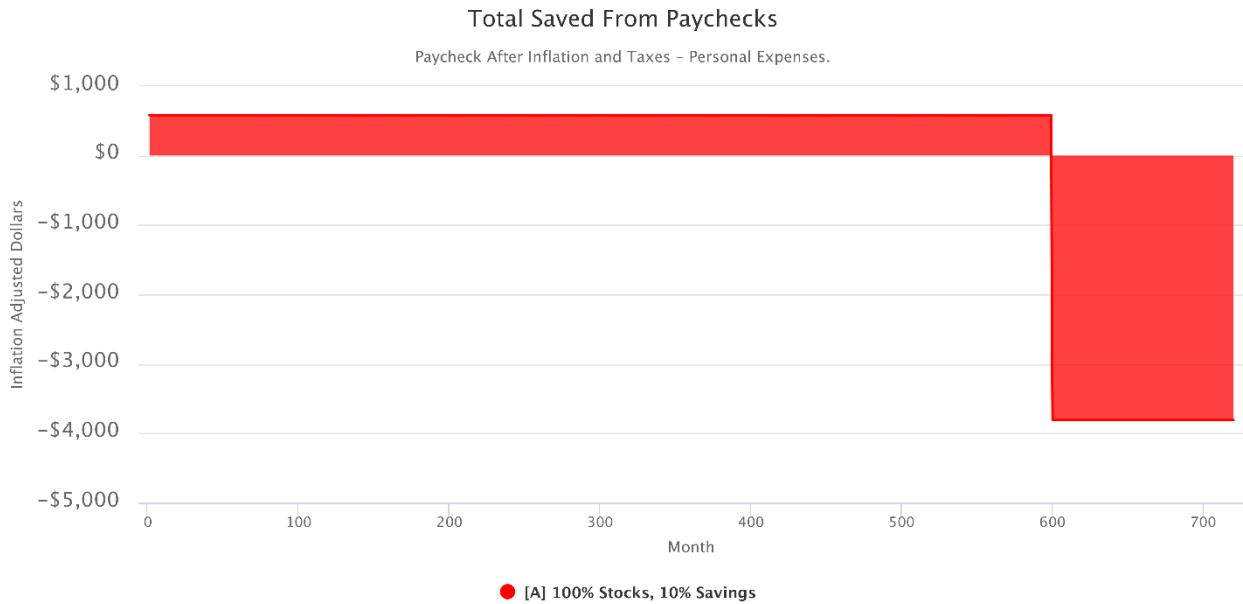
Instead, I am going to zoom out and show you the same chart as above but instead of just showing you the first 12 months, I am going to show you the chart for the full 60 years. Before I do that, it is important to remember what we are showing. It is the difference between your paycheck (after increasing it for inflation and after we subtract out your federal and state income taxes) minus your personal expenses. Got it? OK... here's the chart.



What is going on in the chart above at approximately month 600 again? Well, that's when our paycheck goes to zero, but we still have our full expenses. So, the chart shows you how much you are saving up until approximately month 600 then, how much of a deficit you have for your living expenses.

I find it particularly interesting to see the relative sizes of these two sections. When you've got a paycheck and you are saving, you are saving in the \$2,500 per month range near the very end (not adjusted for inflation), but as soon as your paycheck stops, you need to fund the entire \$16,000 plus for personal expenses from your investments.

If we adjust back for inflation to today's dollars, you can see that you are just saving a fixed \$583.33 per month and that your expenses once your paycheck stops are still just about \$3,800 per month. See, I was able to show you some horizontal lines in a chart after all.



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## VTSMX Account Balances

As you keep saving \$583.33 (and adjusting up with inflation each month) and investing in VTSMX, your account balance for that stock market brokerage account increases. We are assuming that the VTSMX is getting a fixed 8.97% return each year.

**IMPORTANT NOTE:** We've made a big, silly assumption here and I want to call your attention to it. We've assumed that you are getting 8.97% annualized return on your money and that it does not vary. However, we know from the chart above of VTSMX stock market returns how erratic the actual returns for VTSMX are. It is not realistic in the least to think that you are going to get 8.97% every year for the next 60 years. That's just silly.

We could have a year where the value of your holdings in VTSMX drops by 30 to 40%. There were three such years that I showed you above. What happens if you are about to achieve FI and you have a year where the value of your investments drops by 40%?

In other words, let's say you had spent 50 years saving up \$8 million dollars. Then, just as you are about to achieve financial independence, your \$8 million account drops 40% to be worth \$4.8 million. If you were using a 3.25% safe withdrawal rate, you've gone from \$21,666.67 per month on the \$8 million to \$13,000. Those numbers seem high until you realize that you need to adjust them back for inflation and that the \$13,000 is just under \$3,000 in today's dollars. I would say that's a bummer and you would be right to think that's an understatement. I will, however, remind you that the biggest understatement of this book is still: I love charts. Still don't believe me... you will see. There are many more charts coming.

Back to the huge drop in your net worth: The stoics might remind me that while I have control (albeit limited) over what I invest in, I really have no control over how they ultimately perform. The erratic

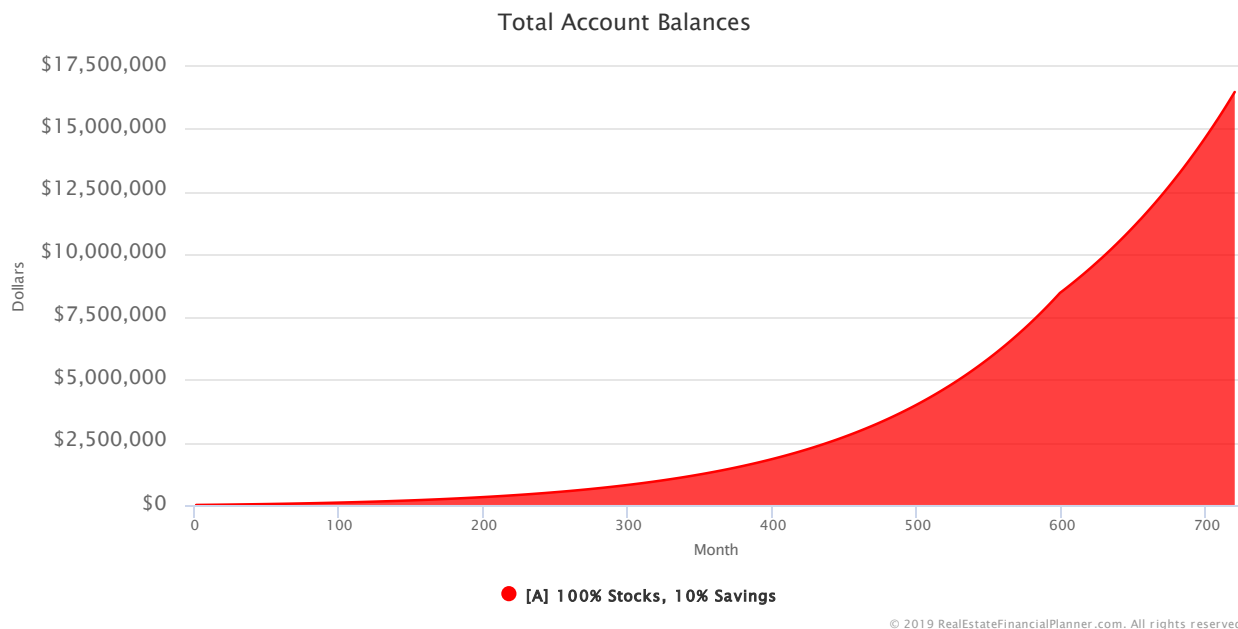


returns that we get from investing in stocks, bonds, and real estate are often referred to as sequence of return risk. You could have some horribly bad return years at the worst possible times.

I can, and probably should, write a sequel to this book to model sequence of return risks using the Real Estate Financial Planner™ (REFP) software. In the meantime, you can do it for yourself by copying this, or other scenarios, to your Planner™ and setting up rules to make the return on your VTSMX account variable each month to simulate the actual historical or projected return instead of a static, unchanging return for the full 60 years.

And of course, you can use rules in the REFP to do similar things for appreciation rate, rent appreciation rate, vacancy, maintenance, and mortgage interest rates to model sequence of return risks for real estate as well. When using rules to make these parameters variable, it might also help to do multiple runs to see the range of possible results or use the advanced Monte Carlo features to have REFP summarize the range for you.

Tangent concluded. Back to our static 8.97% return from stocks. Here is a chart showing how compounding your monthly savings into stocks really pays off.



Yes, I just showed you a chart saying that you have over \$16 million in your stock market account on this plan after 60 years. You will be just over 80 years old at that point. Who knows what life expectancy will be when you are 80 years old. Life expectancy seems to be getting longer every day. Maybe we'll be living to be 200 years old then and we will want to rerun these numbers to extend them.

You need to remember though that \$16 million in 60 years ain't like having \$16 million today. In fact, it's like having \$2.8 million today when you adjust for inflation. And, I'll remind you that you are not living high on the hog... you have the same standard of living you are enjoying today when we adjust for inflation. If you have medical concerns or need to go into some type of care facility you may have to increase the amount you are spending to pay for that. That may exceed your safe withdrawal rate.

## Financial Independence Date

If you remember, the FI date is the date you've achieved financial independence and can live your passion. For the sake of this scenario, it is when your VTSMX account balance is high enough that if we take out 3.25% of it in a given year it can support your gross paycheck minus your savings rate. For a 10% savings rate, you need your assets to produce:

$$\text{Gross Monthly Income} - \text{Savings Each Month} = \text{Target Monthly Income in Retirement}$$

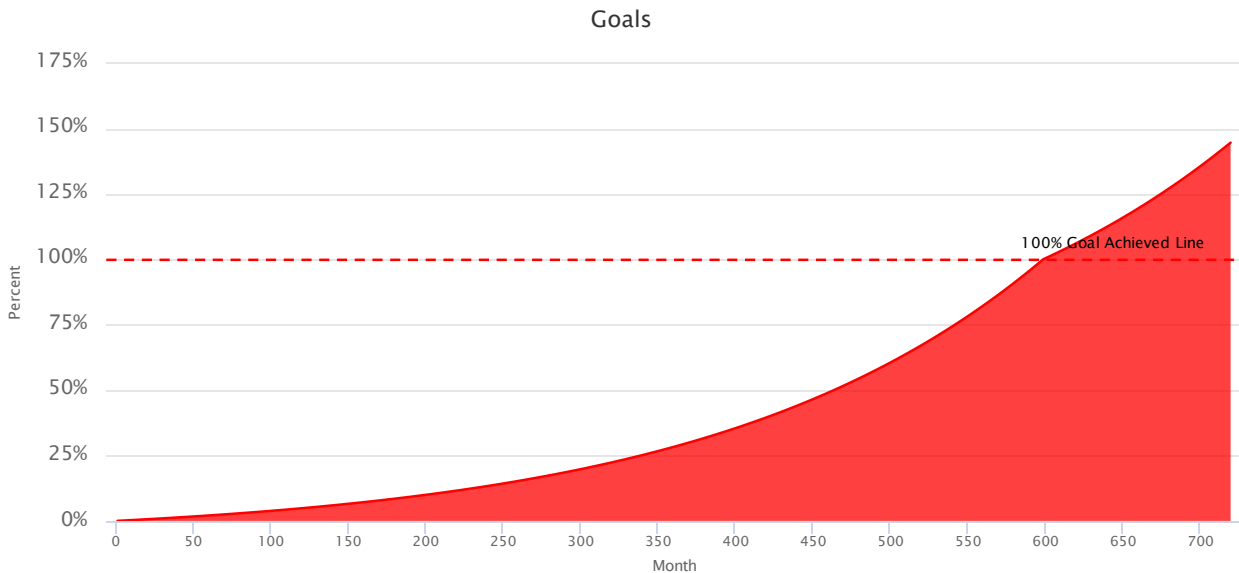
$$\$5,833.33 - \$583.33 = \$5,250$$

But we need to adjust this number up each month for inflation as well. The longer it takes to hit our FI date, the more money we need.

How long does it take in this example? Turns out it takes 599 months, or a month shy of 50 years to be able to achieve financial independence with this plan. You would be 72 years old at that point. Of course, you could probably retire a little earlier when you start collecting Social Security to supplement your shortage at that age. Again, this is assuming you are only saving 10% of your paycheck. I suspect you are willing and able to save more. It further assumes you are investing 100% in VTSMX; however, we will discuss some additional options that might speed it up as well.

Can you see why people, if they are saving 10% of their income, end up having to wait until about 65 or so to retire?

Here is a chart showing what percentage toward achieving your goal of FI you are at, at any given month within the scenario. As we mentioned before, your goal is to have the 3.25% safe withdrawal rate provide you with your target monthly income in retirement.



● Safe Withdrawal Rate and Cash Flow Toward Target Monthly Income in Retirement

## Model It Yourself

If you want to change the assumptions for our scenario to save 10% and invest 100% in stocks, you can copy this scenario to your own Planner™ using this link:

<http://refp.io/710>

Since we are only modeling the stock market, if I were going to evaluate it more realistically using Monte Carlo simulations, I would probably start by using the following:

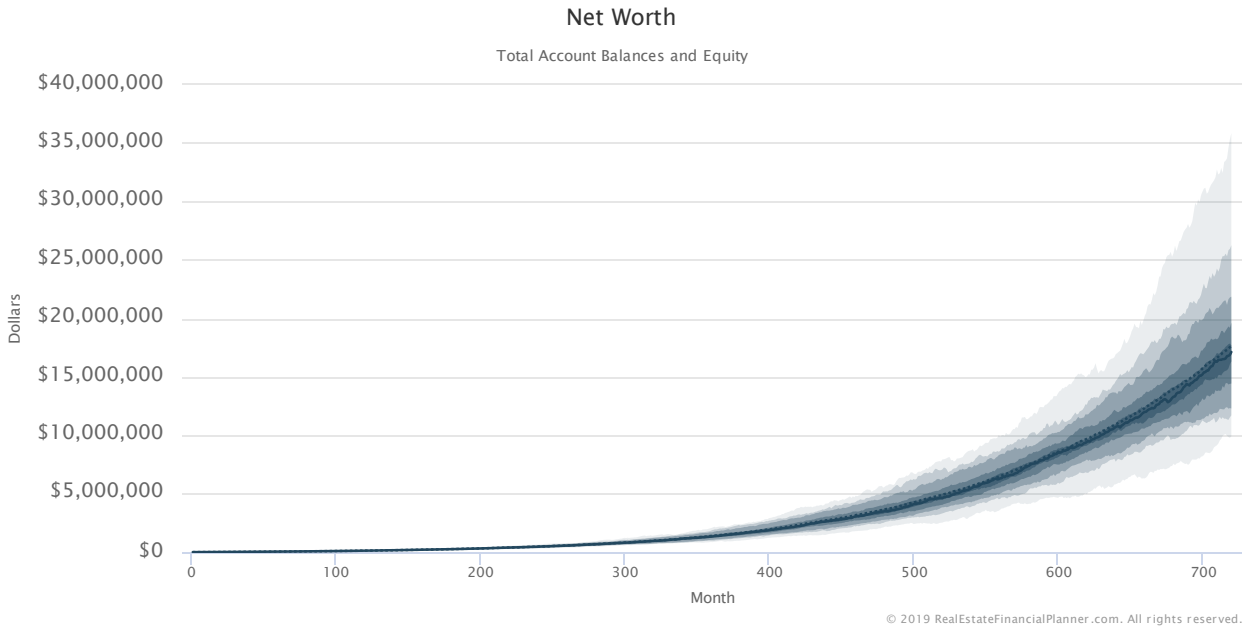
- Yearly Rate of Return for the stock market account
  - Mean 10.57% per year
  - Standard deviation of 18.30
  - Range of -44.33% to 65.47% (3 standard deviations)

## Monte Carlo Sample

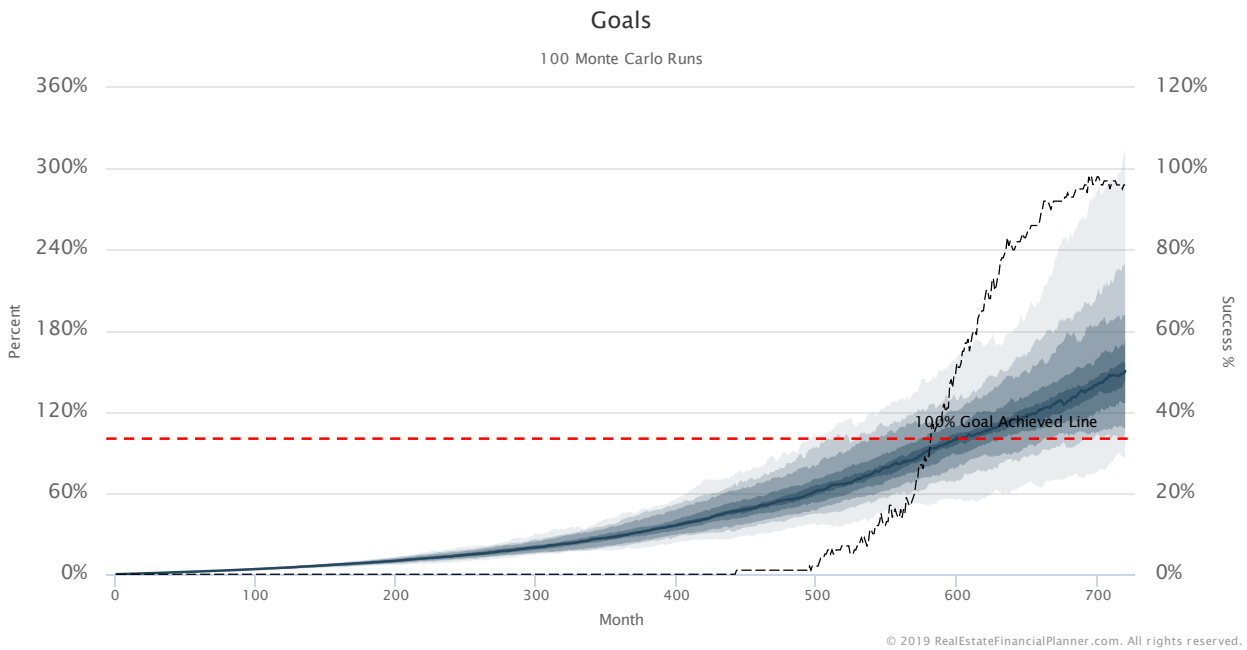
Monte Carlo Simulations (also known as multiple probability simulations) are used to predict the probability of different outcomes for processes involving random variables. In terms of the Real Estate Financial Planner™ using the Monte Carlo feature calculates the results of a scenario over and over, each time using a different set of random values. This produces an expected range of possible outcomes and the likelihood that each will occur and plots it on a chart. Using Monte Carlo Simulations allows for better decision making in the presence of great uncertainty.

While beyond the scope of this book, the following is a preview of what Monte Carlo results look like for *Net Worth* when investing 10% of your income into 100% stocks.

As you can see, it gives you an expected range of results. In this case, it is the expected range of results if we ran it 100 times investing 100% in stocks.



And here is a sample of what the range of results looks like for achieving your goal of FILYP for stocks.

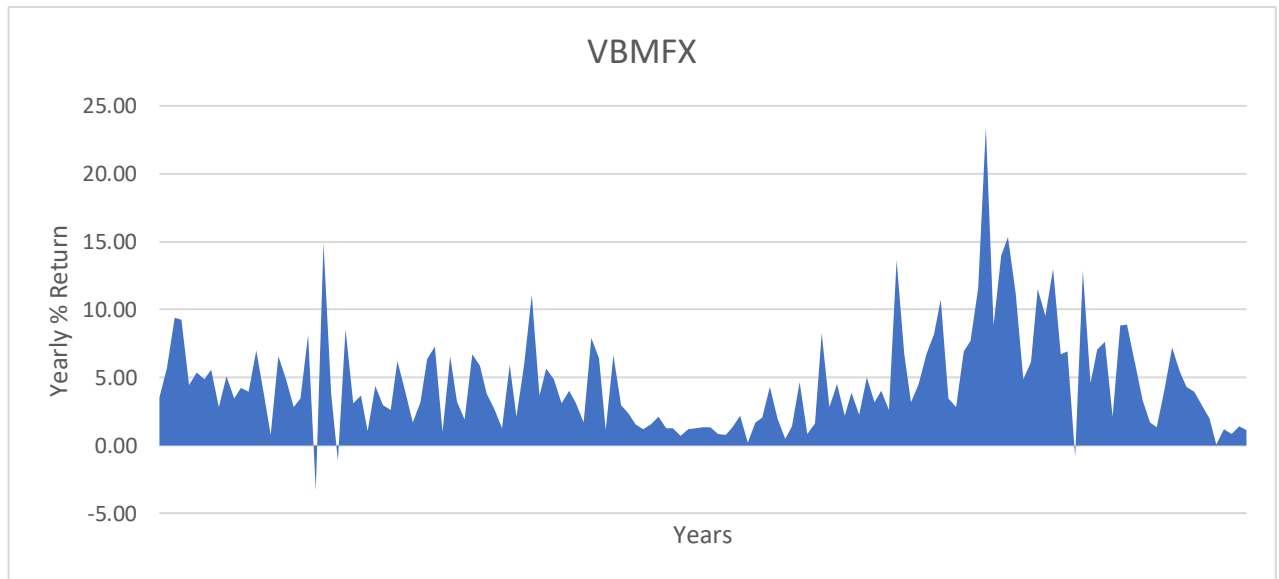


I would strongly advise you to do Monte Carlo runs for your specific situation to see the range of possible outcomes you are likely to experience should a variety of market conditions occur, and to better model sequence of return risks.

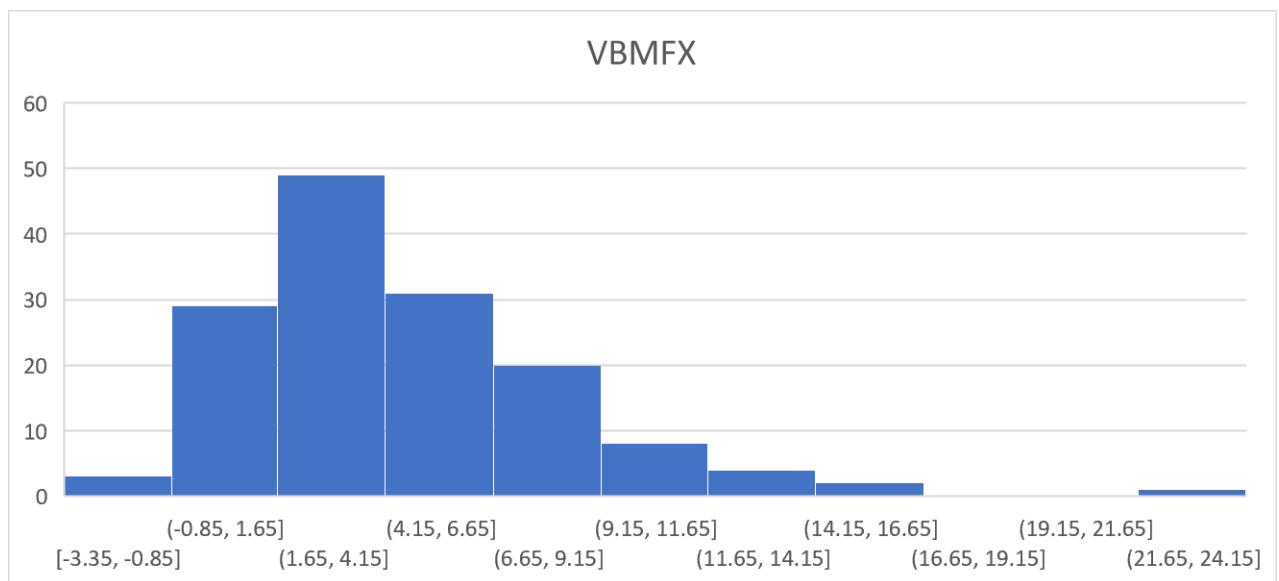
## Switching to 100% Bonds

What if you are concerned about the higher volatility of investing in stocks and would prefer to invest all your 10% savings into bonds?

If we use the Vanguard Total Bond Market Index, VBMFX, from 1871 through 2017, the following chart shows us the historical yearly returns.



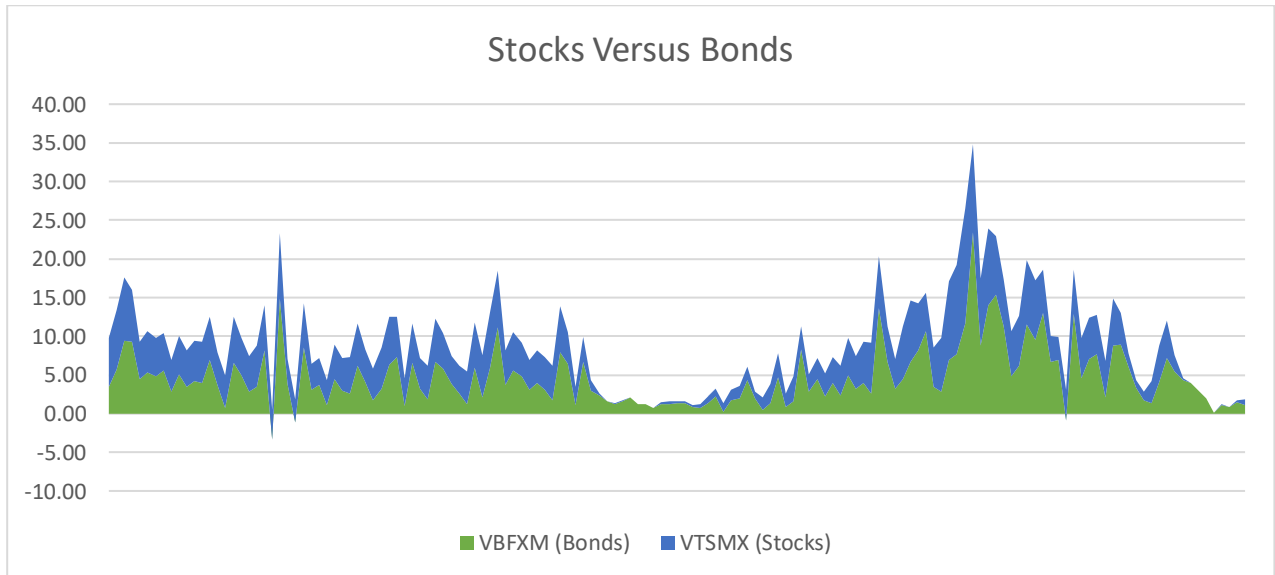
And the following chart is a histogram showing how frequently ranges of yearly returns occurred for bonds.



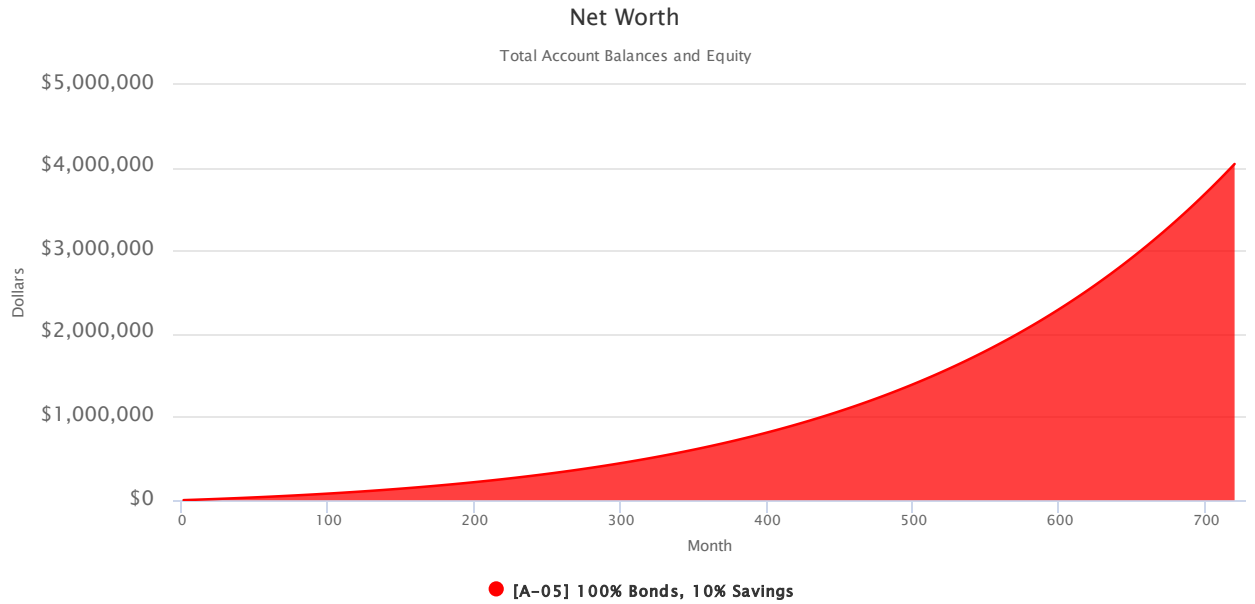
One thing I do want to point out is that bonds are much less likely to have negative yearly returns, but simultaneously they are less likely to have returns as high as we've seen in the stock market.

The compound annual growth rate (CAGR) for the Vanguard Total Bond Market Index has been 4.59% per year. Compare that to the CAGR for the stock market we've been using of 8.97%. Over a long period of time if these historical returns remain similar, we'd expect to see much larger returns from the stock market.

You can see the difference in returns in the chart below where I've plotted both the VTSMX stock market return and the VBFXM bond returns on the same chart.

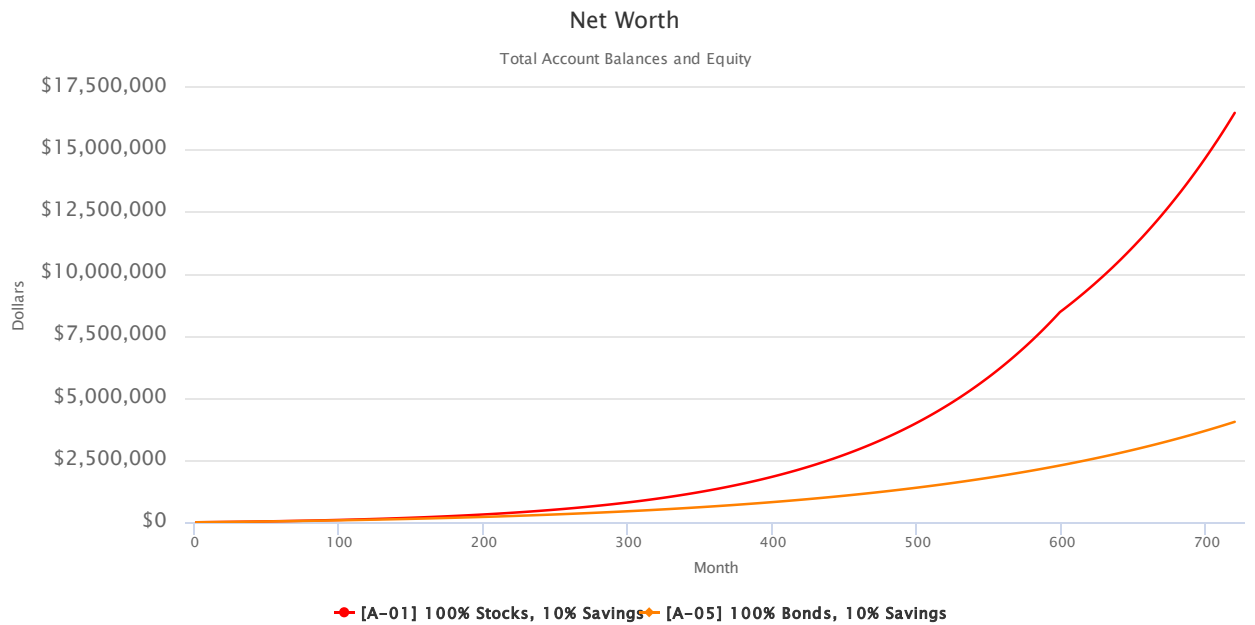


So, how does investing all your money in bonds impact your net worth? Here's a chart showing the net worth over the full 60 years when fully invested in bonds.



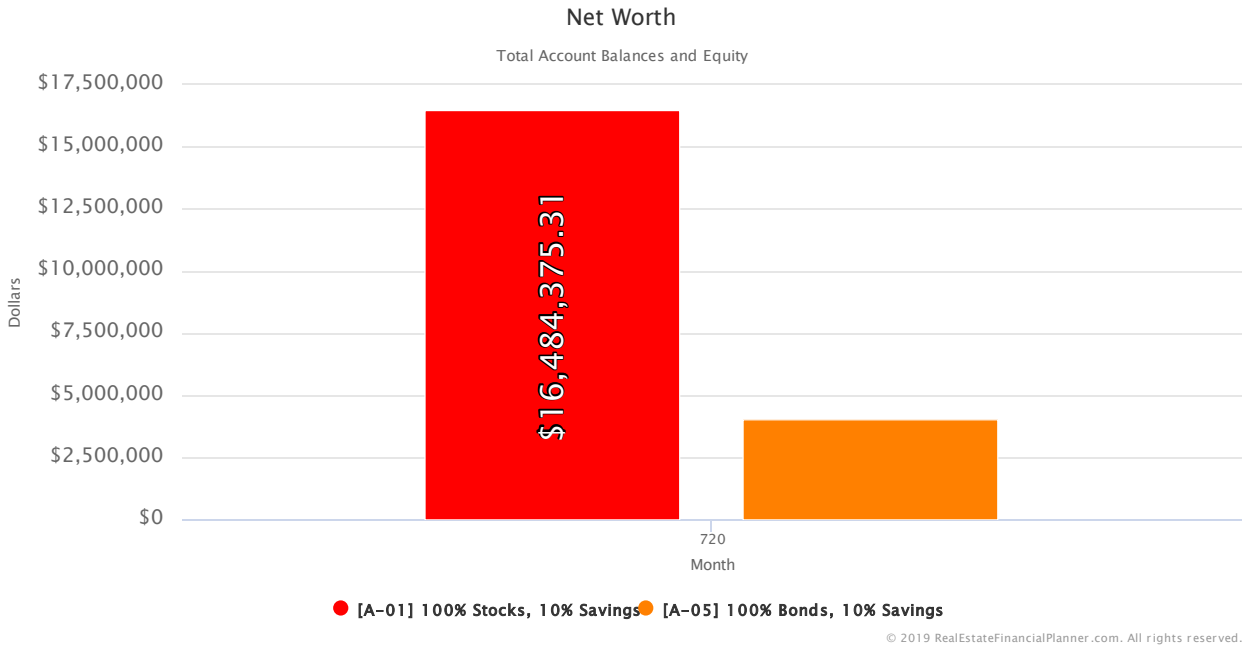
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If we compare this to stocks, you can see the difference in net worth.



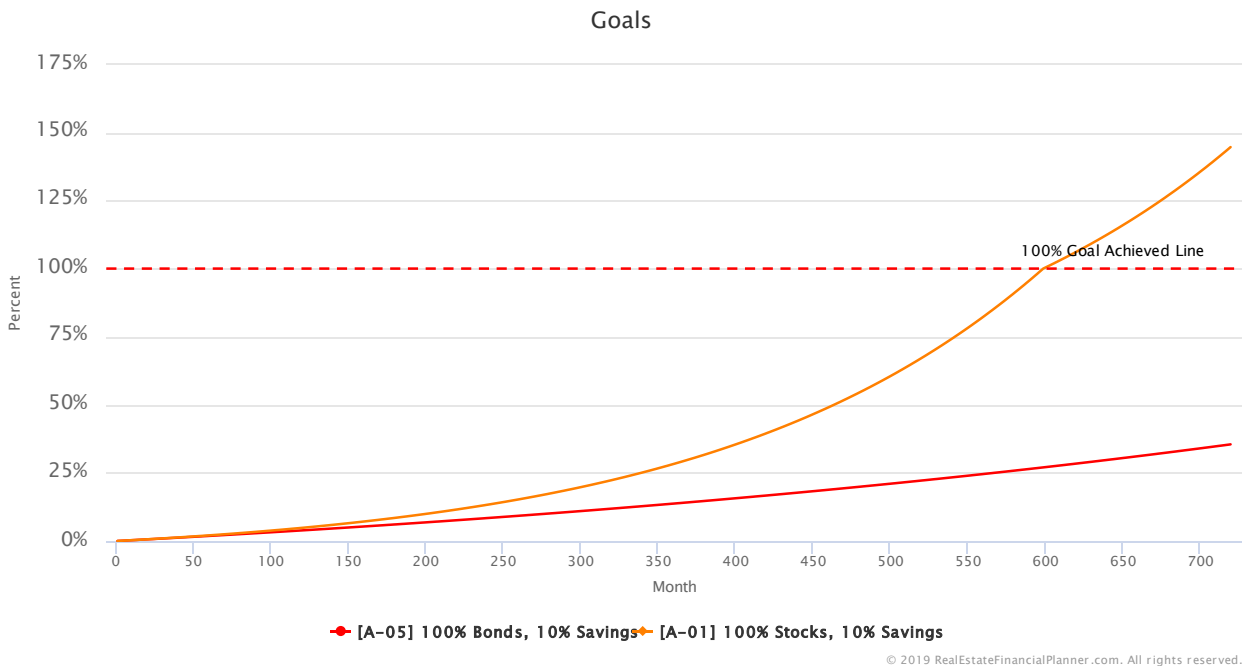
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Yes, investing in stocks gives you over \$16 million in net worth instead of \$4 million with bonds by year 60 as you can see in the chart below.



It begs the question, why bother with bonds? That’s why you should consider copying this to your Planner™ and look at modeling sequence of returns risks using Monte Carlo.

With bonds and only saving 10%, we never quite get to the point where the safe withdrawal rate of 3.25% per year will provide enough income for us to achieve FILYP. This is shown in the chart of our goals below.

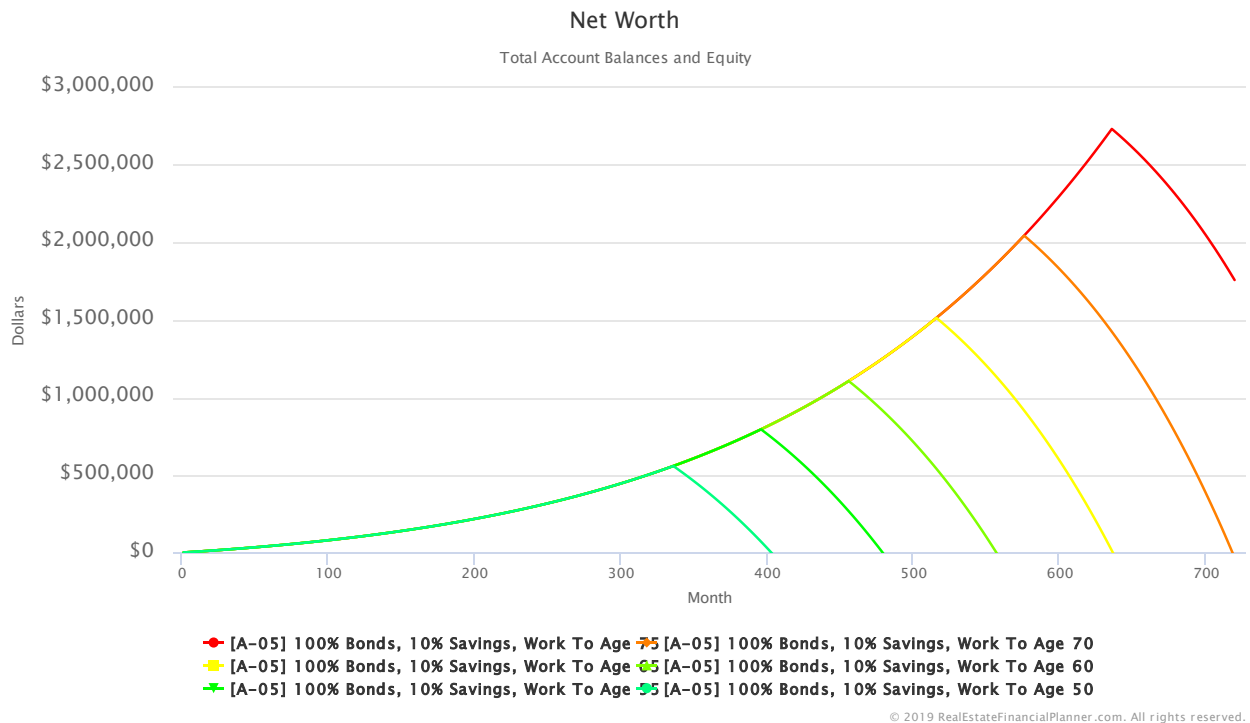




## Retiring on 100% Bonds

Since you never quite hit the point where you are FI investing in bonds, can you ever stop working and have enough money to retire?

You could opt to work until a reasonable age then stop working and deplete your investments. This would be ignoring your safe withdrawal rate. The chart below shows your net worth if you stop working at various ages from 55 to 75.



In all the 100% bond scenarios except where you work until you are 75 years old, if you start withdrawing money to live on before you achieve FI, you run out of money before you turn 82 years old. With the advancements in medicine and the increase in average lifespan, I am not sure I would personally be comfortable with that chance of running out of money.

If you believe you are going to be able to collect social security at some point in the future, when you copy it to your Planner™ feel free to add social security as an additional income and see how much that prolongs your ability to survive before running out of money. I think you will be happy to see how much of a positive impact that extra social security payment has on you being able to achieve FILYP.

Of course, you could also run a similar test of how soon you could stop working investing 100% in stocks as well. I'll leave that open for you to discover on your own.

## Model It Yourself

In the meantime, if you'd like to copy investing 100% in bonds to your Planner™ use the link below:

<http://refp.io/712>

And, if I were seriously considering implementing this plan, I would also do Monte Carlo testing to model sequence of return risk. To model sequence of return risk investing 100% in bonds, I would adjust the following assumptions:

- Yearly Rate of Return for the bond investment account
  - Mean 4.69% per year
  - Standard deviation of 4.76
  - I would probably use a range of -9.576% to 18.962% (3 standard deviations)

## Mixing Stocks and Bonds

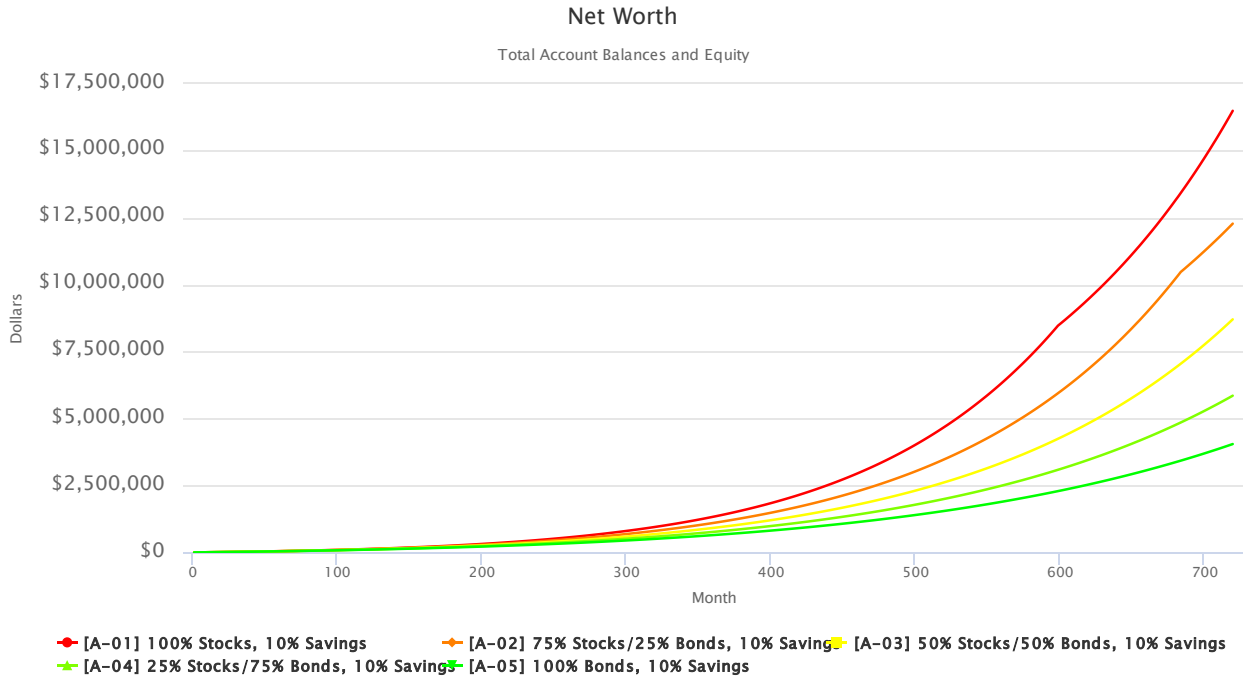
Some financial advisers will suggest that you invest some of your money in stocks and some in bonds. That might allow you to have some of your financial capital invested in higher volatility, but potentially higher return investments like stocks, while still having some of your financial capital invested in lower volatility, but likely lower return investments like bonds.

I have a lot of other models to run for you that include real estate, but I will share with you some summary charts for the following mixes:

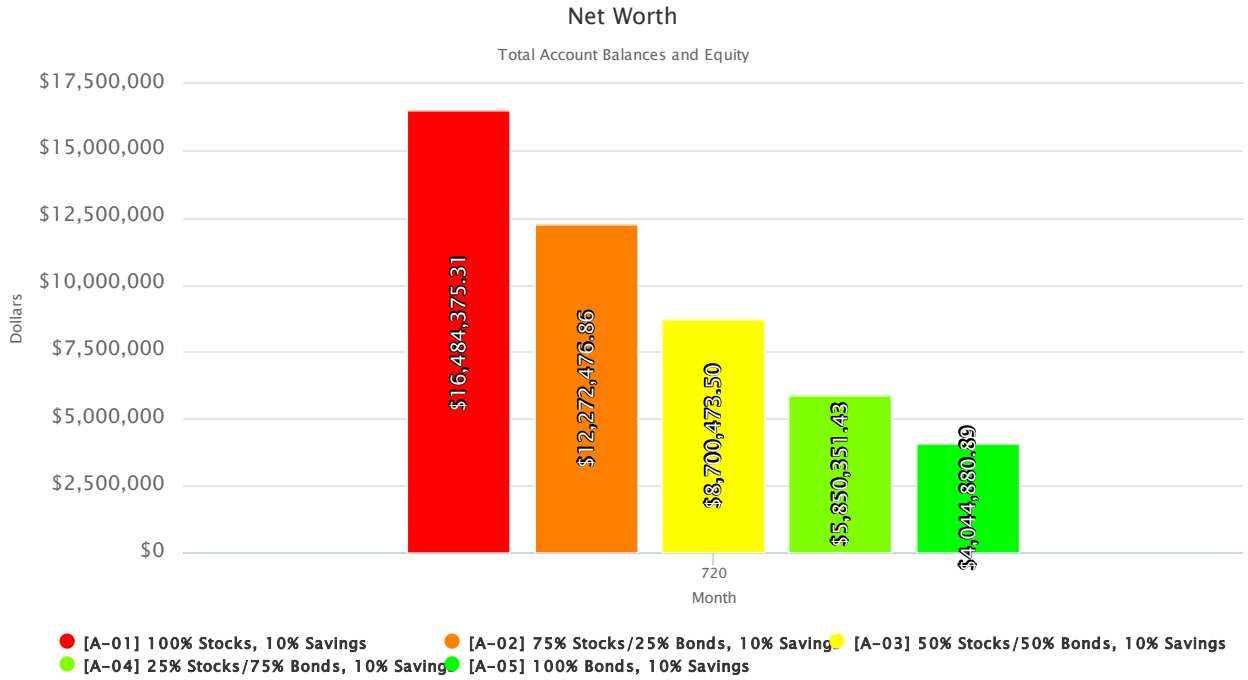
- 100 stocks, no bonds (we covered this first)
- 75% stocks, 25% bonds
- 50% stocks, 50% bonds
- 25% stocks, 75% bonds
- No stocks, 100% bonds (we just covered this)

All the previous assumptions for your personal income, expenses, savings rate, safe withdrawal rate and the returns for both stocks and bonds are preserved for these new scenarios. The only thing that we are changing is that once per month, we are rebalancing how much money we have invested in each, stocks and bonds, based on our desired split.

Let's jump right to looking at the difference in net worth between these five different scenarios.



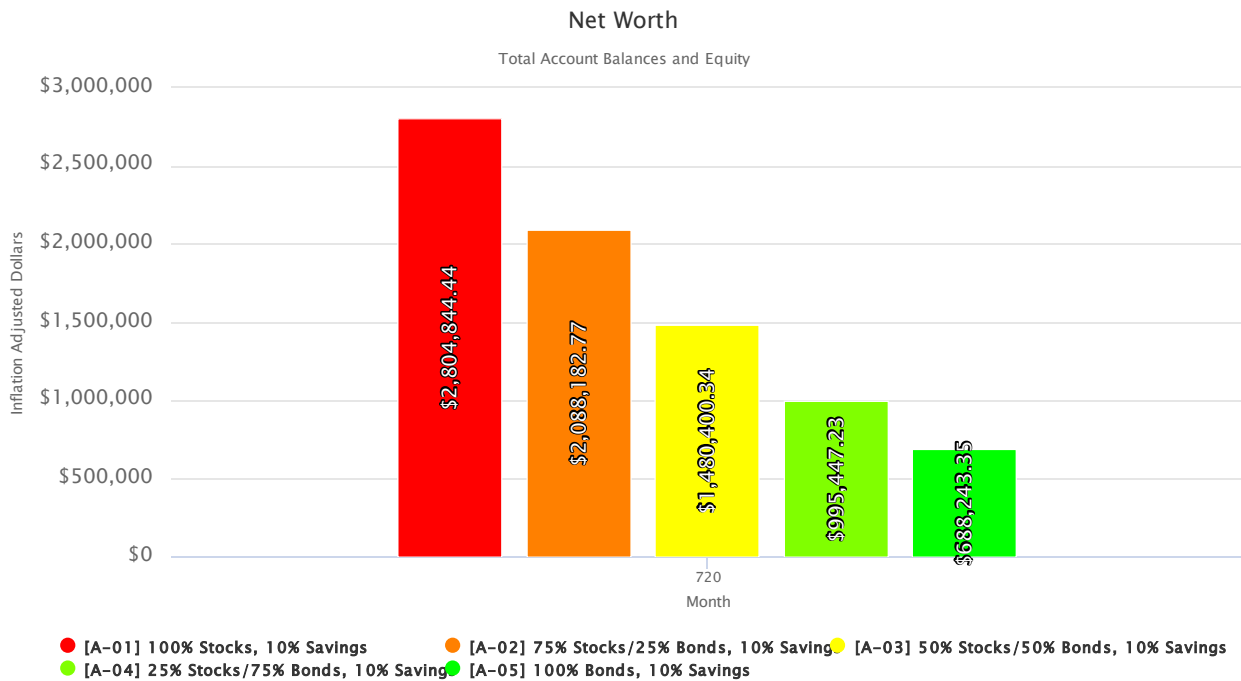
If we zoom in and just look at month 720, you can see the relative values.



As you can see, and as you probably suspected, the 100% stock scenario outperforms all the others. The 75% stock and 25% bond scenario is the next best and so on. The lowest net worth is the 100% bond scenario.

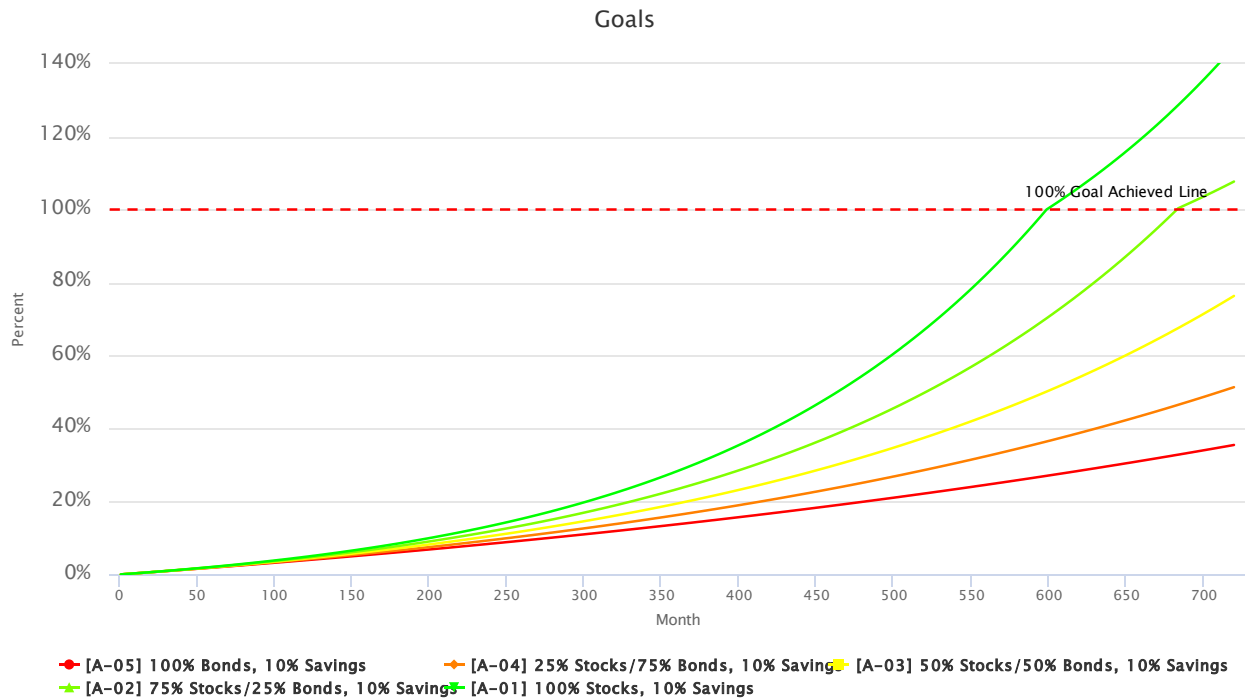
However, if you were to model sequence of return risk by using Monte Carlo, depending on what you use for your assumptions for the stock and bond returns, you might see that bonds remove some volatility.

If you are thinking, I am not sure I really need \$16 million, you should remember that these are inflated dollars 60 years in the future. If we adjust for inflation, they are much lower as shown in the next chart. Starting to feel my comment about loving charts was even more understated than you could have first imagined? Right? Yes, I thought so.



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If you want to live off a—what I believe to be very conservative—safe withdrawal rate of 3.25%, then only the 100% stocks and 75% stock/25% bond mix scenarios even get you to your target monthly income in retirement goal without taking into account social security or some additional income.



So, what should you do about that? That's largely what the rest of this book will strive to answer. Here are some options that we will cover.

- What if you save more than 10% of your income, live on less than 90% of your income?
- What if you include some real estate?
- What if you receive some gift money or can buy properties with no down payment?
- What if you get a side hustle (or roommates) to increase your income?
- What if you pay off mortgages on properties you own faster?
- What if you buy fewer properties?
- And finally, what if you buy more properties than you need to achieve FILYP and sell off the ones you don't need when that would allow you to achieve FILYP?

We will answer all these questions in the upcoming chapters.

## Model It Yourself

In the meantime, if you want to copy any of the stock/bond mix scenarios to your own Planner™ as a starting point to changing the assumptions and testing these strategies for yourself, here are links to be able to copy them.

- 100% Stocks  
<http://refp.io/710>
- 75% Stocks and 25% Bonds  
<http://refp.io/722>
- 50% Stocks and 50% Bonds  
<http://refp.io/721>
- 25% Stocks and 75% Bonds  
<http://refp.io/723>
- 0% Stocks and 100% Bonds  
<http://refp.io/712>

Of course, if you plan to implement any of these, I strongly advise you model this using Monte Carlo simulations varying the returns on the stock and bond investments. I gave you my recommendations for the settings of the stock and bond variability previously; use those or change them to better reflect your perception of reality.

To find and copy any of the other scenarios covered in this book, follow the link below.

- <https://realestatefinancialplanner.com/filyp/>

## **Path 2: Saving Different Percentages of Your Income**

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In the last chapter we assumed you were saving 10% of your \$70,000 per year income. Where we spend or invest our money reflects our priorities. Someone saving a mere 10% of their income may not be really prioritizing their retirement. So, how important is FLYP to you? The percentage of your income that you save and invest will tell us.

Saving more of your paycheck helps you achieve FI faster in two important ways.

First, the more you save and invest the more money you have that can contribute to the income you will get from your safe withdrawal rate and, eventually, cash flow from rentals (when we begin to model that in the next chapters).

But there is a second important way that saving more of your paycheck helps you achieve FI faster. By saving more, you are living on a smaller percentage of your income. That means your target income in retirement can be lower to maintain the same lifestyle.

For a simplified example, imagine you were earning \$10,000 per month. If you were saving \$1,000 per month (10%) and living on \$9,000 per month, you'd only need your investments to generate the \$9,000 per month in income to have the same standard of living once you achieve FI.

However, continuing with the example, if you save 20% of the \$10,000 income, you are living on \$8,000 per month. That lowers your target monthly income in retirement from \$9,000 to \$8,000. So, the amount of income you need to replace with your investments is lower and therefore easier to achieve.

How much of an impact does saving more have on your ability to reach FI so you can live your passion?

### **Saving 10% Versus 20%**

You have already seen the chart for saving 10%, so let's see what happens if you double that and save 20% instead.

Remember, that with the 10% savings rate you have higher personal expenses (standard of living) than when you save 20% of your paycheck. Here's a chart showing you this important concept.

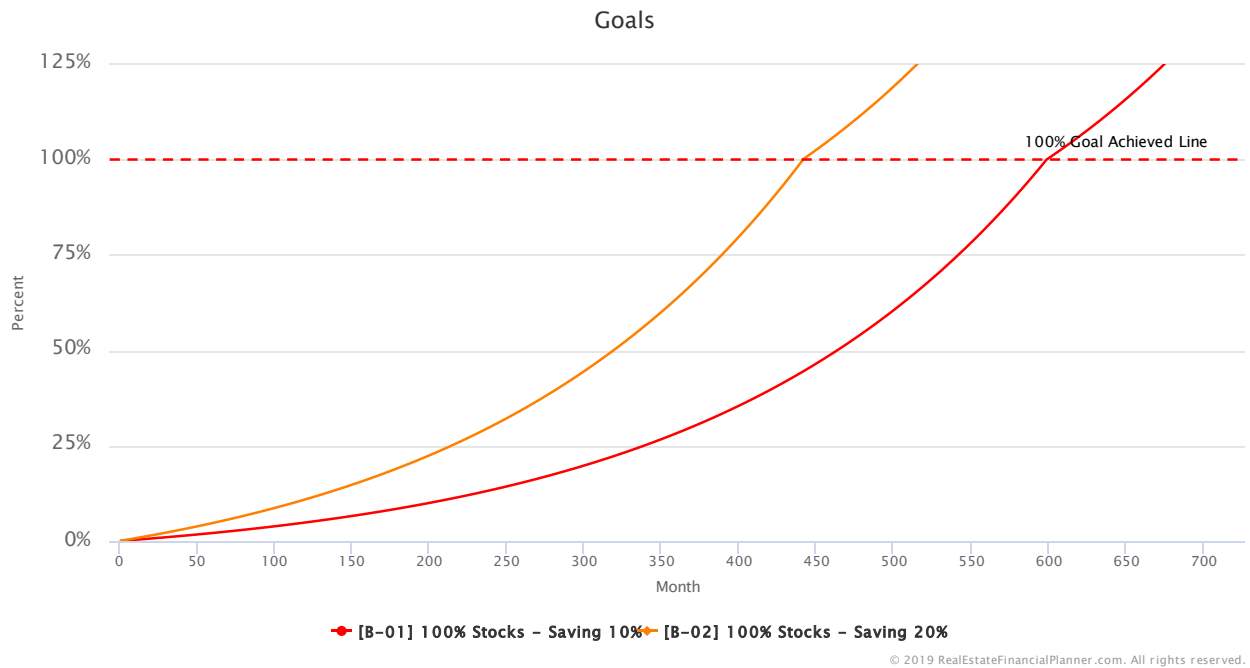


This also means that your *Target Monthly Income in Retirement* (your goal toward FI) is lower when saving 20%. Here's a chart showing the target monthly income for saving both 10% and 20%.





So, how quickly do you achieve your goal of achieving FILYP with a 10% savings rate and a 20% savings rate? The following chart shows that you are able to achieve FI almost 13 years earlier by increasing your savings from 10% to 20%.

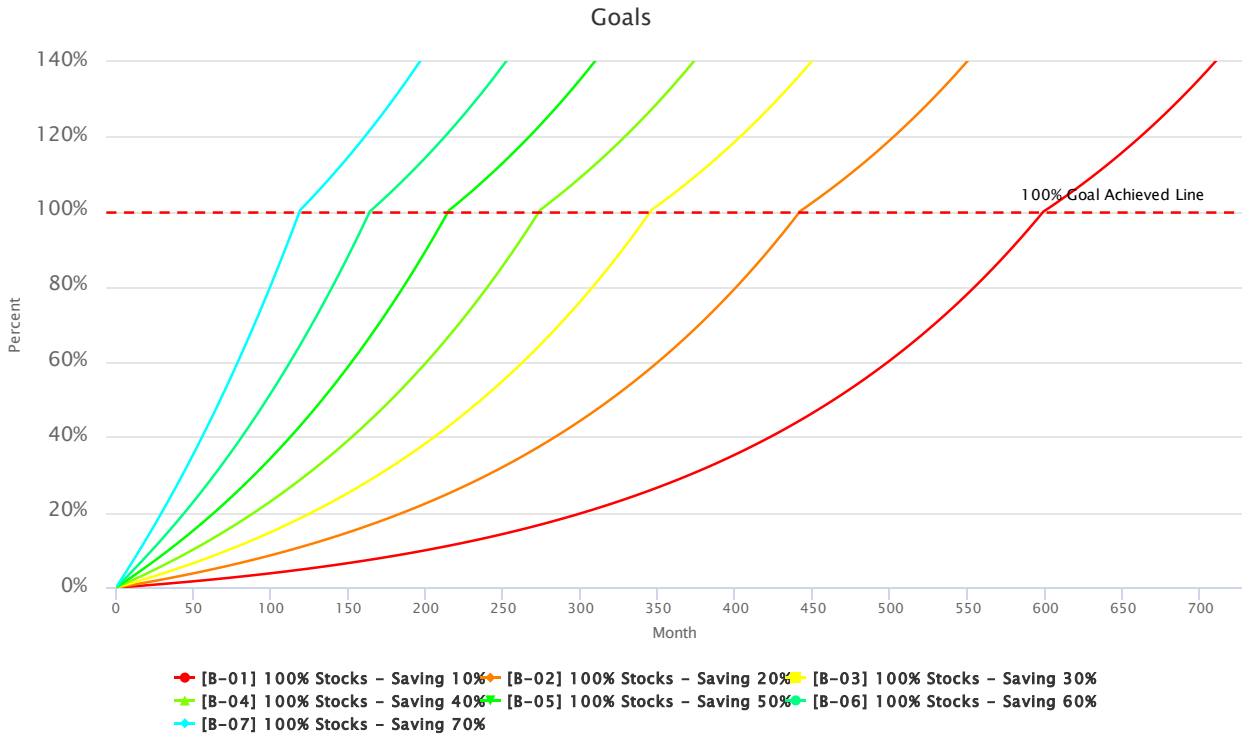


Remember, you can reach FI so much earlier from a combination of saving more and a lower target goal to achieve.

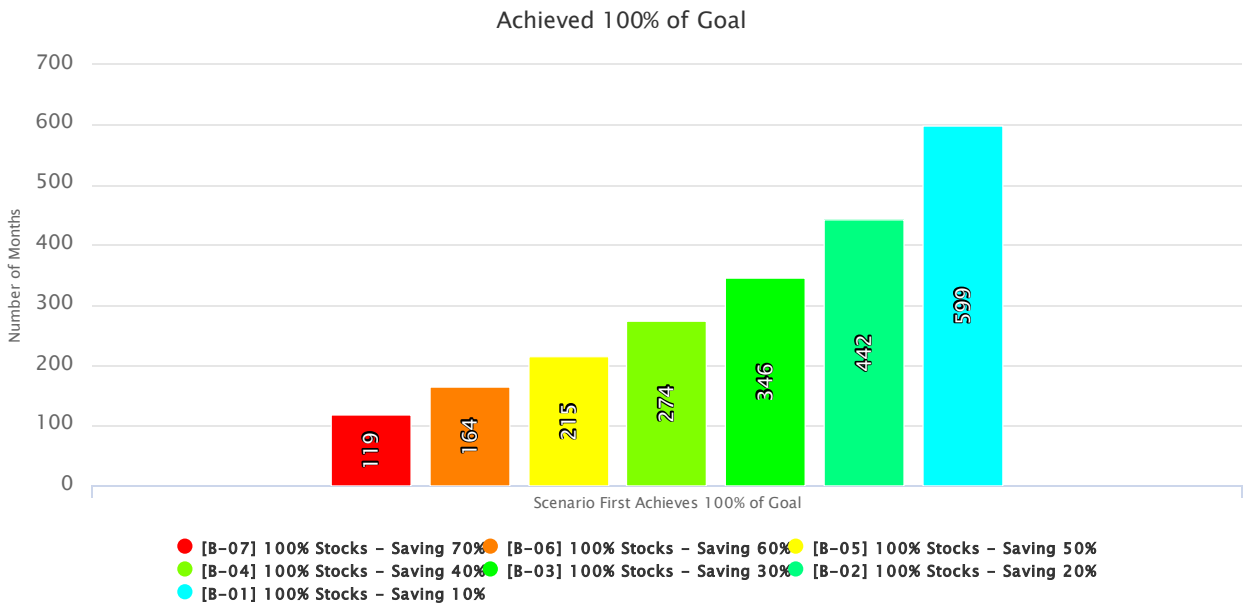
## A Myriad of Savings Rates

So, you could achieve FI in 36 years and 10 months if you save 20% versus 49 years and 11 months if you only saved 10%. That would mean that you could begin to live your passion at age 59 instead of age 72.

How much of a difference does saving more have on your ability to achieve FILYP? Let's look at saving between 10% and 70% all on one goal chart.

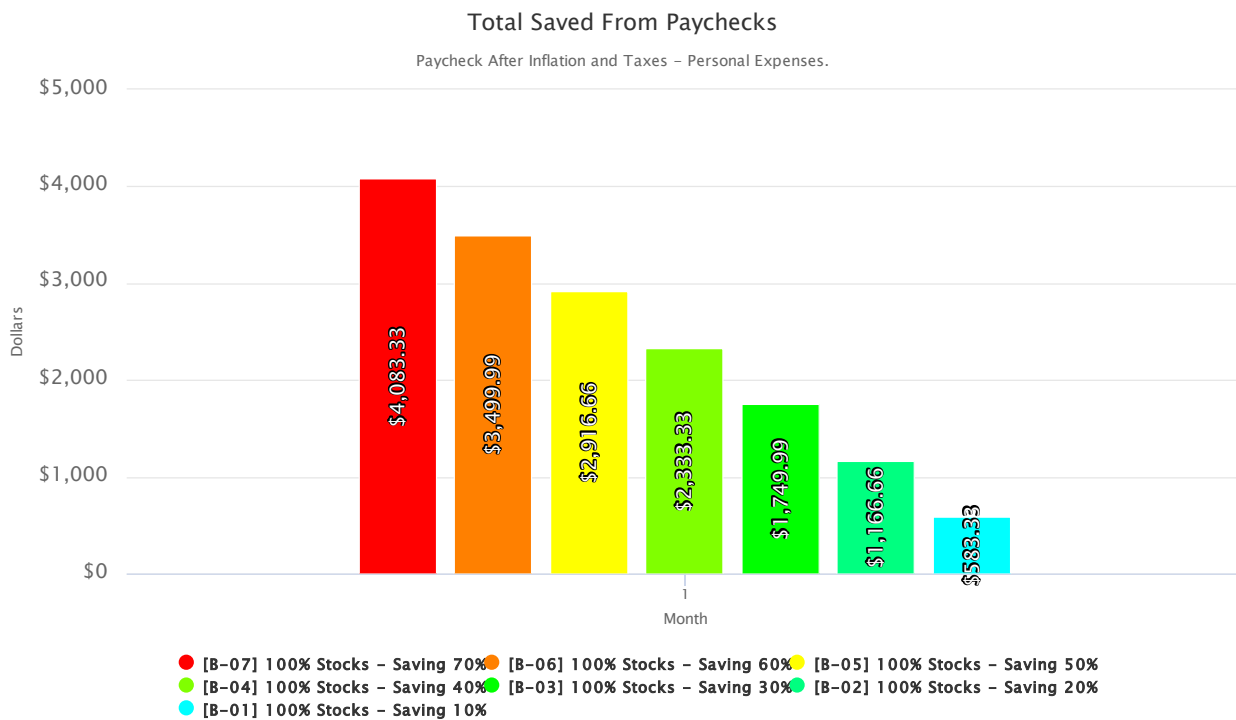


Ready for an obvious observation? The more you save, the faster you can achieve FI. Let's look at the numbers.



So, if you are willing to invest 70% of your income (before taxes), you would be able to achieve FI in a mere 119 months... that's nine years and 11 months.

Time for a reality check though. How much are you living on if you are saving 70% of your income after you pay your federal and state income taxes? Turns out I have a chart for that for each of these scenarios. Here it is.

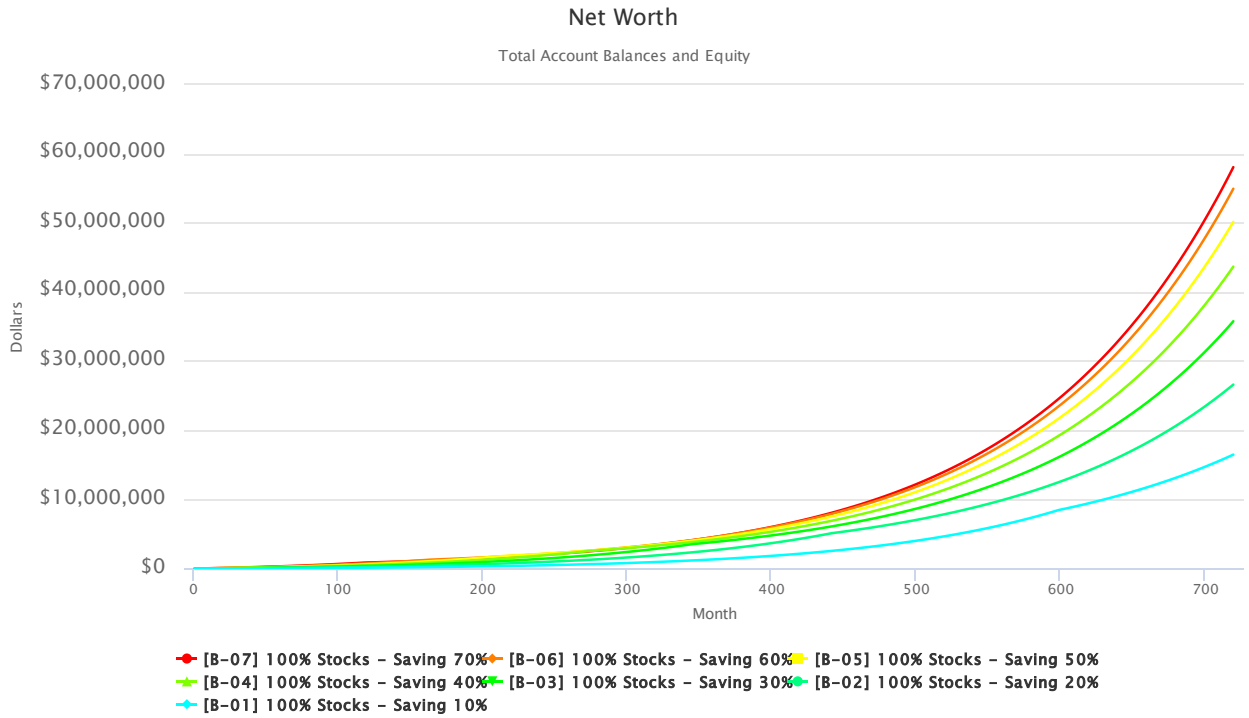


Can you live on \$583.33 per month? Maybe. My guess is that it would be a challenge to pay all your personal expenses including food, shelter, clothing, and entertainment on a mere \$583.33 per month.

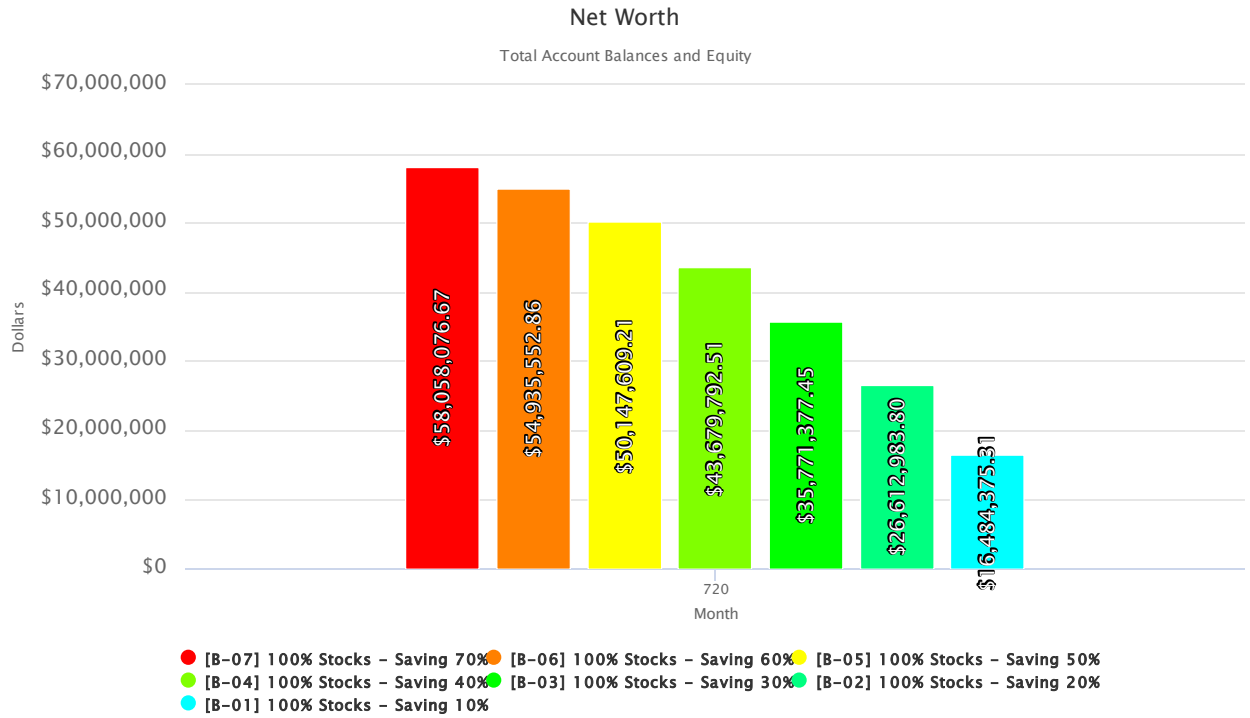
If you tried to save 80% of your income with an effective income tax of 24.71% that would not even be possible as you'd have essentially no money left over.

You may want to argue that some of your savings could be done pre-tax with special retirement accounts. Sure, that could help some and you could model that for yourself using the Planner™.

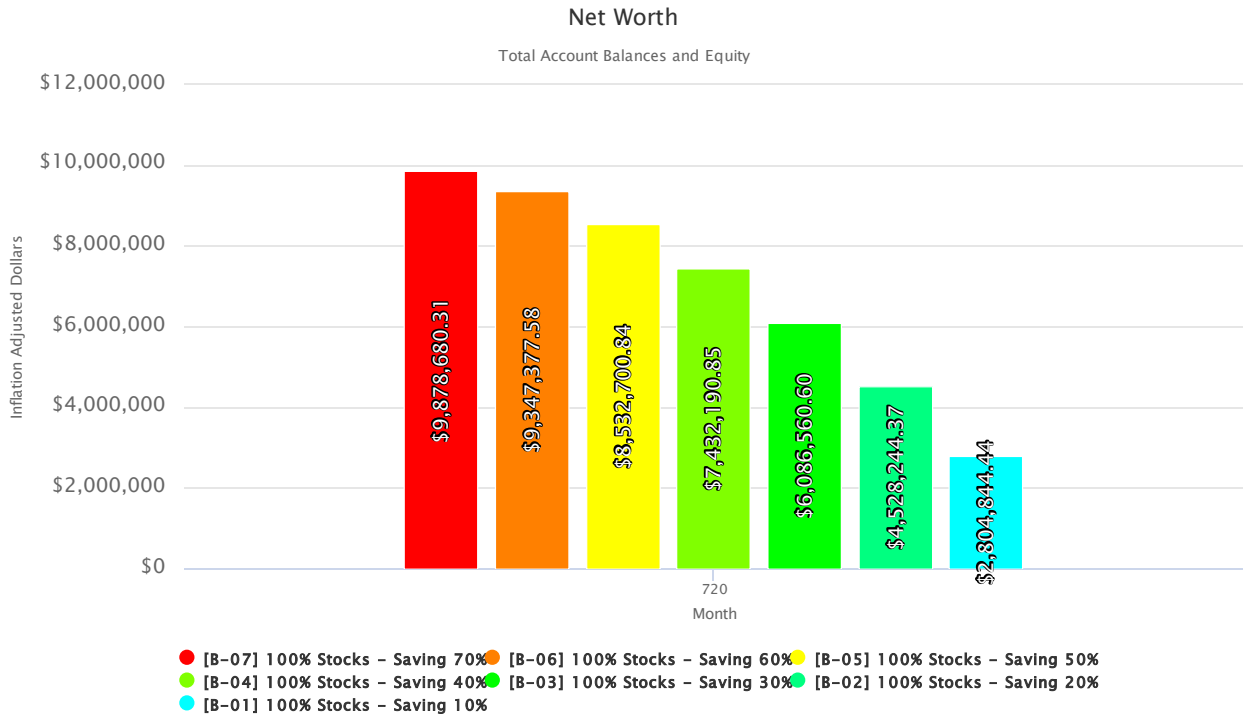
What would your net worth be in each case saving between 10% and 70% of your income?



Zooming in on just month 720, when you'd be 82 years old, you'd have the following in inflated, future dollars for net worth.



If we adjust for inflation back to today's dollars, it looks like you'd have the following for your total net worth.



Not bad. Not bad at all.

## Model It Yourself

In case you want to drill down into some of the other charts or start with any of these to model more sophisticated or different scenarios, here are the links to be able to copy any of these scenarios into your own Planner™.

- 100% Stocks – Saving 10%  
<http://refp.io/606>
- 100% Stocks – Saving 20%  
<http://refp.io/607>
- 100% Stocks – Saving 30%  
<http://refp.io/608>
- 100% Stocks – Saving 40%  
<http://refp.io/609>
- 100% Stocks – Saving 50%  
<http://refp.io/610>
- 100% Stocks – Saving 60%  
<http://refp.io/611>
- 100% Stocks – Saving 70%  
<http://refp.io/612>

There must be a repeat button here because I am going to tell you again that if you do plan to implement this—or a variation of this—scenario, you should model it using Monte Carlo with variability in the stock market return.

To find and copy any of the other scenarios covered in this book, follow the link below.

- <https://realestatefinancialplanner.com/filyp/>

I will point out that while you will be able to change our assumptions at any time using the Real Estate Financial Planner™ software for the future chapters, I did ask you what percentage of your paycheck you plan to save, and you told me about 30%. So, I will use 30% for the rest of the scenarios moving forward.

Next, let's consider adding some real estate for the first time.





## Path 3: Nomad™

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Previously, we assumed you were renting a property to live in and that you did not own any real estate. That means no owner-occupant home and no rentals.

That all changes here.

In this chapter, I will walk you through all the assumptions we made for the properties we will be buying in subsequent chapters. I will go off on many tangents to explain important concepts and assumptions along the way. Then, after walking you through the assumptions—and the tangents—I will show you what buying a home to live in looks like and compare that to just investing in stocks and renting until you reach FI.

But I won't stop there. After I show you what buying a single home to live in looks like, I will then walk you through systematically buying additional properties and keeping the previous ones as rentals using an investing strategy we call Nomad™.

We call it Nomad™ because you are moving from house to house like a Nomad might roam from cave to cave on a woolly mammoth with money bags swinging in the wind. Well, maybe not quite like that, but hopefully you get the idea.

Specifically, the Nomad™ strategy has you buy a home as an owner-occupant and move into the property. You will stay in the property for at least a year, sometimes longer. When you are ready to buy your next home, you will keep the property you were living in and convert it to a rental. You will move into the new home as an owner-occupant again.

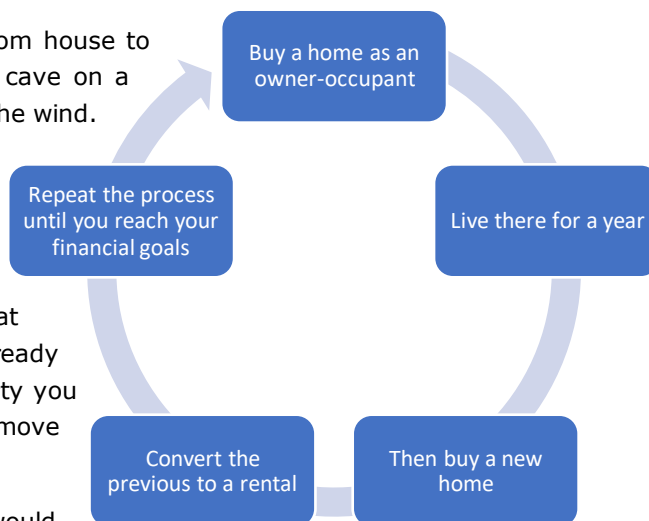
You can repeat this process as often as you would like, provided that you continue to qualify for the loans with your job income and the help of rental income from the houses you have converted to rentals.

You stop buying more properties once you have acquired the number of rentals you desire.

### Why Nomad™

If Nomad™ sounds like a lot of work, it is. If you are wondering why even bother when we can buy rental properties, easily, with 20% down payments, then you are in for a treat. I will tell you why to bother.

First, owner-occupant loans typically have lower interest rates than non-owner-occupant (investor) loans. For example, while preparing to write this book, I asked a local lender here to work up a good faith estimate for several loan scenarios. For an investor (non-owner-occupant) loan with a 20% down



payment, the interest rate would have been 5.125%. At the same time, an owner-occupant loan ranged between 4.375% and 4.875% depending on how we opted to pay for private mortgage insurance (PMI).

## Private Mortgage Insurance

This brings us to our first of many tangents. What is private mortgage insurance? If you put 20% down to purchase a property, the overwhelming majority of lenders feel like they have an adequate buffer in case the property drops in value and you have a healthy amount of your own money invested in the deal to motivate you to take care of the property and make payments on the 80% (or less) they are loaning to you. By putting at least 20% down, the lender does not feel like they need extra protection or insurance in case you default on the loan. If they foreclose on the property, the 20% down creates enough buffer so they get their money back.

However, if you put less than 20% down, most lenders will require you to bring in a third party to insure them against loss should you default on making your payments. So, if you put 5% down to purchase a property the lender may require that you pay a private, third-party to insure the loan. If you don't make your payments and the lender needs to foreclose, this third-party insurer will help reduce any potential loss the lender may experience. We call this insurance *private mortgage insurance* (or PMI). In case it is not clear, this insurance is paid for by you to protect the lender, in case you do not perform, when you put less than 20% down to buy a property.

When buyers put less than 20% down, they typically can pay private mortgage insurance in one of three ways:

1. As a single lump-sum, up-front payment at the time they get the loan.
  - a. This requires you to have the cash—in addition to your down payment—to pay this up-front insurance premium.
2. By asking the lender to raise the interest rate so the lender can give you a credit to cover the cost of the one-time, up-front payment.
  - a. While you won't need to come out of pocket for this up-front payment, you end up paying a higher interest rate for however long you keep this loan with this option.
3. Or, by asking the lender to allow you to pay the private mortgage insurance premium monthly.

If you recall, this whole conversation about private mortgage insurance began when I told you that there are a range of mortgage interest rates for an owner-occupant depending on how you choose to address private mortgage insurance.

If you decide to pay the single lump-sum, up-front payment at the time you get the loan, you might pay about 1.5% of the loan amount as your private mortgage insurance premium, but your interest rate would be 4.375%. If you are buying a \$350,000 property with 5% down, you would need \$17,500 for your down payment plus approximately \$5,000 more for your up-front mortgage insurance payment. But your monthly payment would be lower with your lower interest rate. Which also means your cash flow will be better when you convert this property to a rental.

If you opt to ask the lender to give you a credit to cover this fee and you'd accept a higher interest rate, you would not need the extra \$5,000 for the up-front PMI payment but your interest rate would have

been 4.875%. That means your monthly payments would be higher. It also means when you convert it to a rental, your cash flow will be slightly worse as well.

The third option was to ask the lender if you can pay your PMI monthly. This does not require any additional up-front payments and your interest rate, in this case, was between the 4.375% and 4.875% at 4.5%. But you are paying over \$100 per month in private mortgage insurance payments.

So, what should you do with PMI? I wish I could tell you definitively to always pick a certain option when dealing with PMI, but the real answer is to talk to your mortgage broker. Let them know what your plans are for the property and ask them to walk you through all three options. Remember, you can model all three scenarios in the Planner™ to see which works out best for you.

In general, if you plan to keep the property forever, I would probably lean toward the lump-sum, up-front PMI payment to get the lowest interest rate as this will likely have the biggest impact over the full 30 years. That is what we will use for this book. It requires a little extra time for you to save to have enough to buy the property but gives you a little lower monthly payment and ultimately a little bit better cash flow when you convert your owner-occupant property to a rental after living there for a year. You know... like what a good Nomad™ does.

Which brings us out of our tangent on private mortgage insurance and back to why you should bother doing Nomad™. I just told you one reason is that you get better interest rates as an owner occupant—even when you factor in the cost of PMI.

Another reason to put up with the hassle of having to move into a property and live there for at least a year before making it a rental is you can opt to use low down payment loan options offered to owner-occupants. At the time of this writing, there are 15% down payment non-owner-occupant loans available for investors. However, since you are putting less than 20% down, you have PMI on those as well and, from what I've seen, the interest rates are quite a bit higher than the much more common 20% down payment loans (without PMI) that non-owner-occupant investors can get.

If you are moving into the property though, you can easily get 5% down payment mortgages with better interest rates than the 20% down payment loans that investors can get. You could buy four properties, over four years, for about the same total down payment you'd need to buy a single 20% down property.

So, down payment size is yet another reason for bothering with Nomad™.

How about a third reason? If you are buying non-owner-occupant properties, you will very likely cap out your ability to get 30-year fixed-rate financing once you have 10 mortgages (owner occupant and investor combined). To get more than 10 loans to buy a non-owner-occupant property, you will likely need to seek out a portfolio lender who is not selling your loan on the secondary mortgage market. Also, these portfolio loans are very likely to be variable rate loans.

Buying owner-occupant properties does not have this same limitation. Provided you qualify, with the current lending rules, you can always get another owner-occupant property. That means that while we will be stopping with you buying 11 properties for this book, that is not a lender-imposed limit. You could keep buying as many Nomad™ properties as you want; go ahead and test that by copying one of the scenarios we will cover into your own Planner™ and increasing the number of Nomad™ properties you buy.

Are those three reasons compelling enough? If you are not sure, that's good because in this chapter I will walk you through doing Nomad™ properties where you move in, live there for at least a year, and buy another owner-occupant property as you convert the previous property to a rental. But, in a couple chapters, I will show you what putting 20% down looks like. Maybe by putting more down, the cash flow will be better and can help us achieve FILYP faster. See what I did there? I tried to encourage you to keep reading.

## Buying Your First Property

To model this scenario, we are keeping all the previous assumptions the same and assuming you are saving 30% of your income. Here's a quick review of some of the key assumptions:

- Earning \$70,000 per year
- 24.71% effective tax rate (federal and state combined)
- Saving 30% of your income
- Investing 100% in the stock market
- Stock market earns fixed 8.97% per year
- \$4,083.33 is target income to achieve FI (your standard of living)

If you don't like those assumptions you can, of course, modify them by copying the scenario to your Planner™ and making them reflect your reality.

For the first scenario, we are going to assume you buy one property as an owner-occupant, live in it, and never buy another property. We are assuming this is a typical family home near where you work.

Let's walk through our assumptions for the property.

### Purchase Price

We are assuming you are buying a property for \$350,000 and that the property is worth \$350,000. If you can buy the property for a discount or, heaven forbid, you are in a real estate market like mine and you need to pay above asking price to get an offer accepted, you can modify the purchase price and/or value and rerun the scenario to see how that impacts your plan.

Since you are paying full price for the property, it is in move-in ready condition and does not require any money from you up-front. If you were buying a property that needed money up-front to get it ready to live in or rent, we call that *Rent Ready Costs* in the Real Estate Financial Planner™ software.

### Financing

We are assuming that you are doing an owner-occupant loan with 5% down. Since you are putting less than 20% down, you will have private mortgage insurance.

We are assuming that you have opted to pay the one-time, up-front, lump-sum private mortgage insurance to get the lowest interest rate. That means you will need to come up with about 2.5% for closing costs (which includes the up-front private mortgage insurance payment).

With the up-front private mortgage insurance payment, you can lock in an interest rate of 4.375% fixed for 30 years.

## No Depreciation

Since we plan to buy the property and live in it, we do not get the tax benefits of being able to depreciate the property. I will talk about this more when we have our first rental, but out of an abundance of clarity, I wanted to tell you explicitly that when you are not renting the property, you do not get to depreciate the property.

Side note: Talk to your accountant or CPA about this, but if you have roommates, it is likely you *will* be able to depreciate part of your property while living in it. Roommates can significantly reduce your cost of housing. You don't have roommates in this scenario; that's a later chapter... another gentle plug for you to keep reading. I'm getting good at this.

## Accounts

To simplify modeling, we have been using the stock market account as a catch all account. It is where we deposit our paychecks. It is where we subtract all our personal expenses from. It is also where we will save our money for down payment and closing costs until we have enough to buy the property.

It might not be the most prudent thing in the world to keep money you have ear-marked to spend in the next six months to a year in the stock market account which could see a decline in value. Discuss this in more detail with your accountant, CPA, or financial advisor and maybe model it for yourself with your Planner™ to see and truly understand the potential risks and the impact it can have on your plan.

## Appreciation Rates

Property values and rents tend to go up over time. In fact, my interpretation of Case-Shiller<sup>4</sup> data suggests to me that property values (and rents) tend to keep pace or slightly outperform inflation over a long period of time.

For that reason, we tend to model property price appreciation and rent appreciation at about the same rate as we set inflation to. In this case, that would be 3% per year for each: inflation rate, appreciation rate, and rent appreciation rate.

If you feel this does not reflect your reality, the good news is that you can change the assumption at any time using the Planner™.

What does a 3% appreciation rate mean to us? It means that while we are saying the property is worth \$350,000, it is really only worth \$350,000 in month one. Each month the property value (and rent) goes up a little bit (at a rate of 3% per year). So, if we buy a property a year into the scenario, the property we are buying will not be worth \$350,000, it will be worth \$350,000 plus 3% and we will be buying it for

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<sup>4</sup> [https://en.wikipedia.org/wiki/Case-Shiller\\_index](https://en.wikipedia.org/wiki/Case-Shiller_index)

the \$350,000 plus 3%, its then current value. I'll show you charts of this when we start buying more than one property.

## Monthly Rent

In this first scenario, you will be living in the property and not renting it out. For that reason, rent doesn't matter here. However, we will be using this same property as a template for all the properties we buy, and we will be renting those out. When we rent them out, we have assumed that the rent we could get for this property (worth \$350,000 in month one) is \$2,000 per month in month one.

Over time, rent will bump up a little each month (although we model it such that it only changes once a year when the lease renews). In month 13, rent would be 3% more than \$2,000. I'll show you this when we go over the charts for rents when you buy a rental property.

## Vacancy Rate

Again, we are not renting out the property for this first scenario, but when we do start renting out properties in subsequent scenarios, we will need to factor in a vacancy rate. A vacancy rate models what percent of the time the property is not occupied by a tenant and is therefore not collecting rent.

Some real estate investors will be tempted to use higher numbers here to model a property being vacant for a month between tenants to account for turning over the property, doing repairs, and finding the next tenant. A 7.69% vacancy rate means the property is vacant for 1 month every 13 months. Presumably for people who use this, they rent the property for 12 months, then start marketing to find their next tenant and get the property rented by the first of the next month. The cycle repeats. That is 1 month vacant every 13 months. Brace yourself for harsh language... this is the sign of a negligent landlord.

You should have in your lease that the tenant must notify you no later than 60 days prior to the expiration of their lease whether they are renewing or not. Then, you, as the landlord should be marketing to find your tenant in the 60 days prior to the current lease expiring. Do the maintenance on your property while the tenant is in the property; you should be maintaining your properties anyway, so why are you waiting for a new tenant? If you do need to replace carpet or other flooring and paint, schedule that to happen the day your tenant moves out in the afternoon or the next day. It should be able to be completed in a day or two at most (not a month).

Start looking for your next tenant at least 60 days prior to your lease expiration. That way you can start with an optimistic rent and drop your rent slightly every few days if you are not getting a reasonable number of calls and interest. It is better to drop your rent slightly and get a qualified tenant than to have your property sitting vacant. Note I said *qualified*. Never bend your written rental criteria to rent to an unqualified tenant to avoid vacancy. Better to get slightly lower rent than to have to deal with damage and more likely evictions for letting an unqualified tenant rent. You should have it rented by the time the current tenant is out of the property and the new tenant should be moving in immediately.

If you are being a good steward of your assets by being proactive with your property management, I feel comfortable using 3% for vacancy, so that's what we have used for modeling this for you. When we start modeling rentals, you will see us account for a 3% vacancy rate on income from the property each month.

## **Property Taxes and Property Insurance**

We model property taxes and property insurance as a percentage of the current value of the property. As property values go up, your property taxes go up as well. Similarly, as property values go up, it becomes more expensive to insure that property so property insurance increases as well.

Over time, as your property value goes up from appreciation, the dollar amount that you are spending on property taxes and property insurance automatically go up.

For property taxes, we are assuming that you are paying 1% of the value of the property each year on property taxes (paid monthly). On a \$350,000 property that means you are paying about \$3,500 per year in property taxes. Ask your real estate agent, lender and/or your accountant and CPA for more information on what they are seeing for the properties you are considering buying. In some real estate markets, 1% seems ridiculously high and in others it may seem equally ridiculously low. In Fort Collins, where I live, property taxes on about 60% of all properties sold in 2018 had property taxes ranging between 0.46% and .6% of their selling price.

For property insurance, we are assuming you are paying 0.4% of the value of the property for property insurance. On a \$350,000 property that means you would be paying \$1,400 per year. This can vary quite a bit depending on which level of deductible you select, your credit score, how close the property is to the nearest fire hydrant and fire department, the construction of the property, and a myriad of other factors.

If you want to have lower property insurance, you could opt to self-insure a little more by having a higher deductible. That way if something goes wrong, you are going to pay for more of the smaller items you might have otherwise made a claim for and if something big happens you are likely going to pay the deductible before the insurance company must pay out. It is important to talk to a good insurance agent and have these discussions with them. You should decide where you feel comfortable with your level of risk exposure and coverage.

Personally, your mother and I prefer a higher deductible as we have enough in savings to be able to handle all the smaller claims and pay the deductible amount in the event of a larger claim. That might not be your situation if you are tight on savings early on.

## **Homeowner's Association**

We are assuming that the properties you are buying are not in a Homeowner's Association (HOA). If they are you can change what the HOA fee is and what rate the HOA cost increases each year when you copy it to your Planner™.

## Maintenance

All properties will require maintenance over time. Carpet and other flooring will need to be replaced. Occasionally you will need to call a plumber, electrician, heating/cooling tech, or handyman in to do work on your property.

For rental properties, we set aside a percentage of the rent that you are collecting for maintenance on your property. We are using 10% of the gross rent collected for maintenance. In the short-term it might be higher or lower than this amount, but over a long period of time, for a well-maintained home in this price range, that's a reasonable assumption. If you are buying new construction properties, you might be able to use a slightly lower number for the first few years, especially if there is a home warranty from the builder for the first year. If you are dealing with properties older than 20 years, it may be higher. If you are dealing with lower priced homes, it will undoubtedly be a higher percentage. Why? The cost of some materials and labor are largely fixed whether it is a \$350,000 home or a \$60,000 home. In other words, entry-level grade carpet is likely to still be \$3 per square foot whether you are installing it in a \$60,000 home or a \$350,000 home. So, the cost for carpet as a material and the labor to install carpet is the same regardless of the price of the home. But, when you consider that cost as a percentage of rent, the cost as a percentage is much higher when your rent is lower.

If you want to model capital expenses on your rentals separately, you can do that with the Real Estate Financial Planner™ software. For the sake of simplification, we are assuming you are not doing significant capital improvements and the small capital expenses (CapEx) you have are included in the maintenance percentage already.

## Property Management

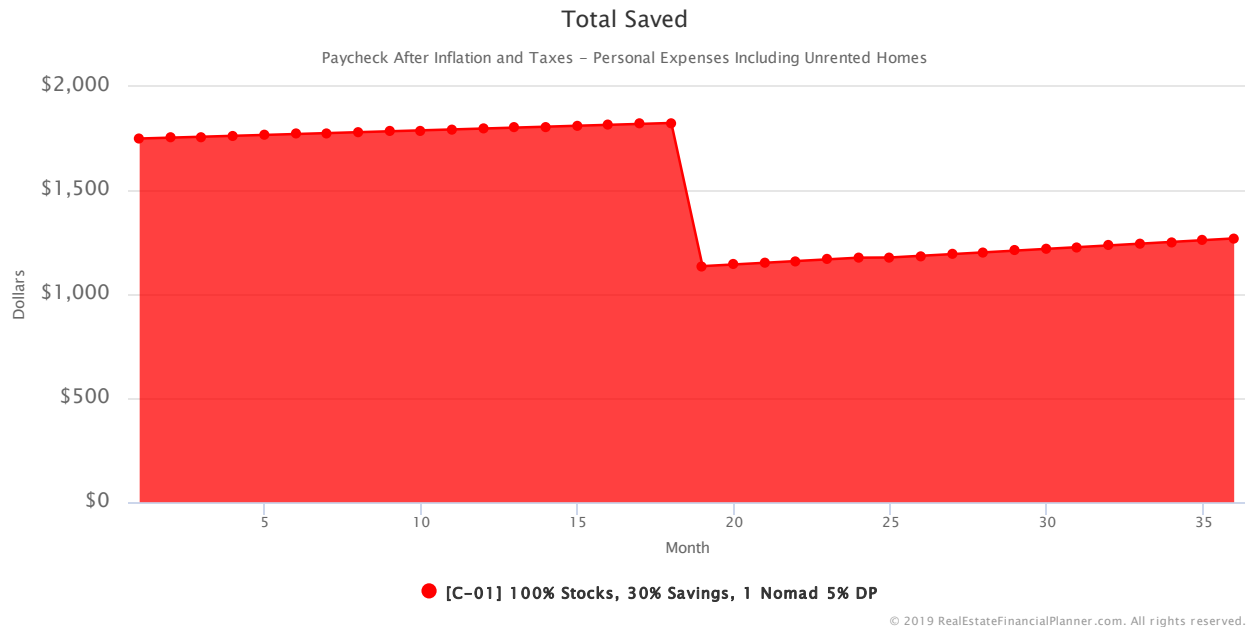
With this first scenario, you are not renting the property at all, since you are using it as your residence. But, when you do start to rent properties in subsequent scenarios, we will assume that you will be doing your own property management. At some point in the future, when cash flow from the properties and/or your ability to earn from your job warrants it, you may consider hiring a property manager. For now, and for the sake of these models, we have assumed you are managing them yourself.

## Saving to Buy Your First Property

Let me tell you a story... the story of your life (in this scenario). You work your job earning \$70,000 per year. You are saving 30% of your income while you are renting and investing that 30% in the stock market.

At first, you are saving about \$1,750 per month (that's 30%) and it takes you 18 months to be able to save enough to have enough money for the 5% down payment on your property plus the 2.5% in closing costs (which includes your one-time up-front private mortgage insurance premium). The following chart shows the total amount you are saving each month.



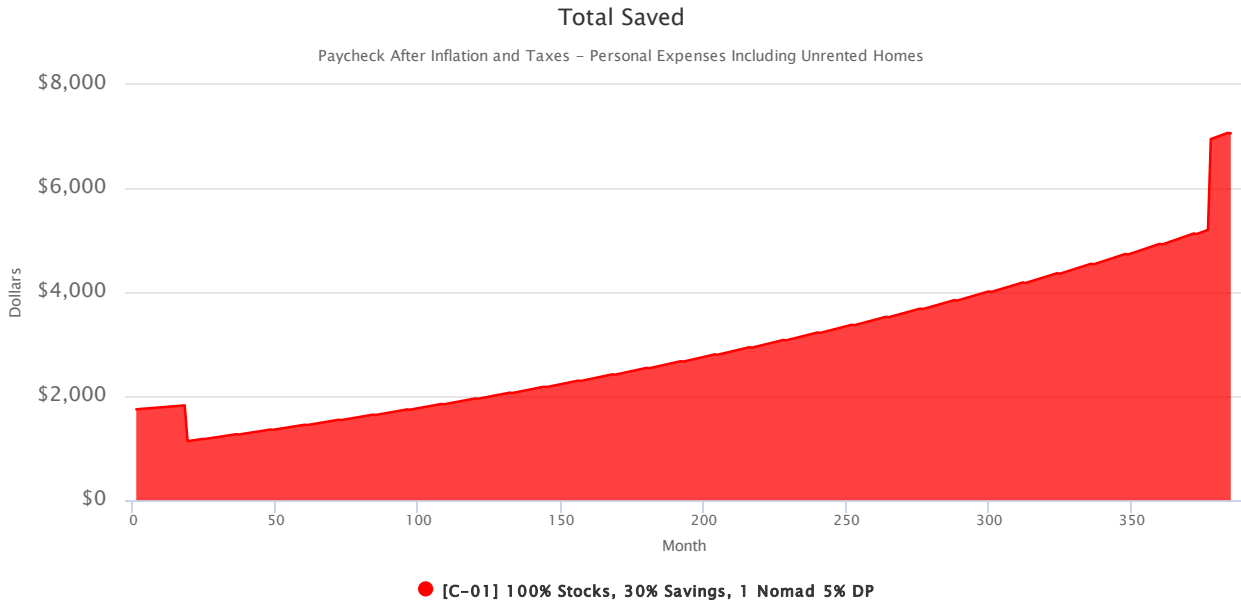


Month 19 is the drop off in the chart above. That's the month when you stop renting and buy your first (and only) home for this scenario. Why is there a drop off in the amount you are saving each month?

It is because the home costs more to live in than the \$1,400 per month in rent we assumed you were spending. When you bought the property, you stopped renting and started being a homeowner, which cost you more. This means you are saving less than the 30% you thought you were. Now, you are contributing part of that 30% toward your housing costs.

This might be a subtle point, but one that is important for you to realize, especially as we start acquiring more properties.

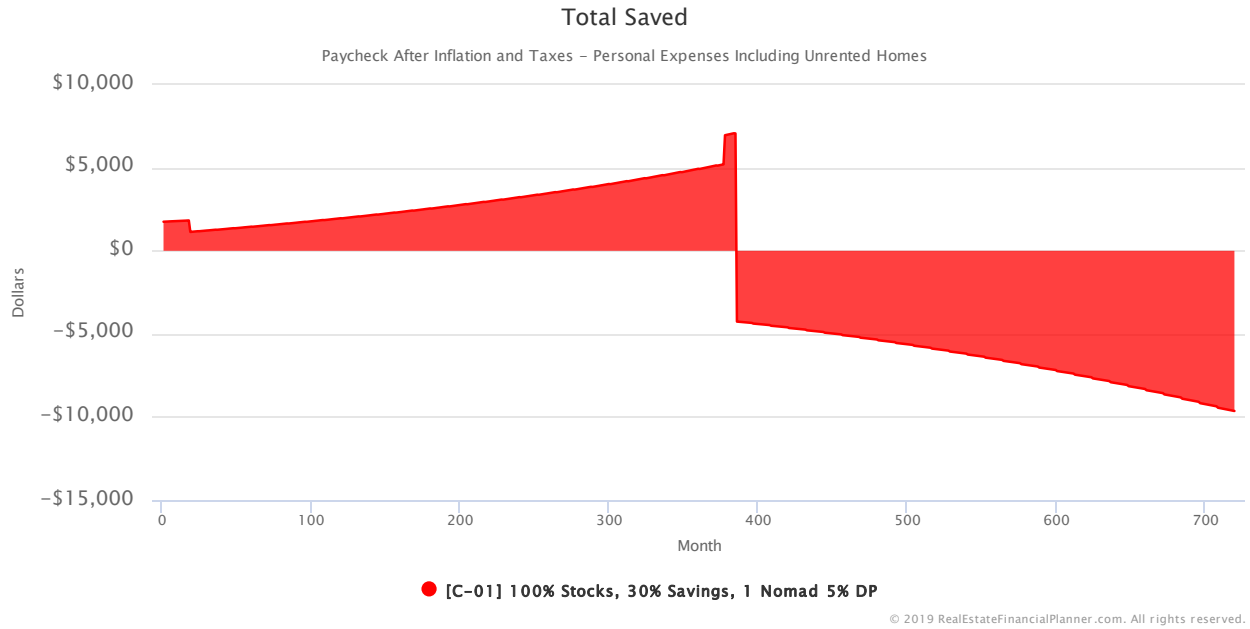
Next, let's look at what happens to your savings over a much longer time horizon... 385 months.



Early on you are saving 30% of your income, then you buy a house and the amount you are saving goes down. It increases with inflation over time until something interesting happens in month 378, exactly 360 months from when you bought your home. Do you know what happened?

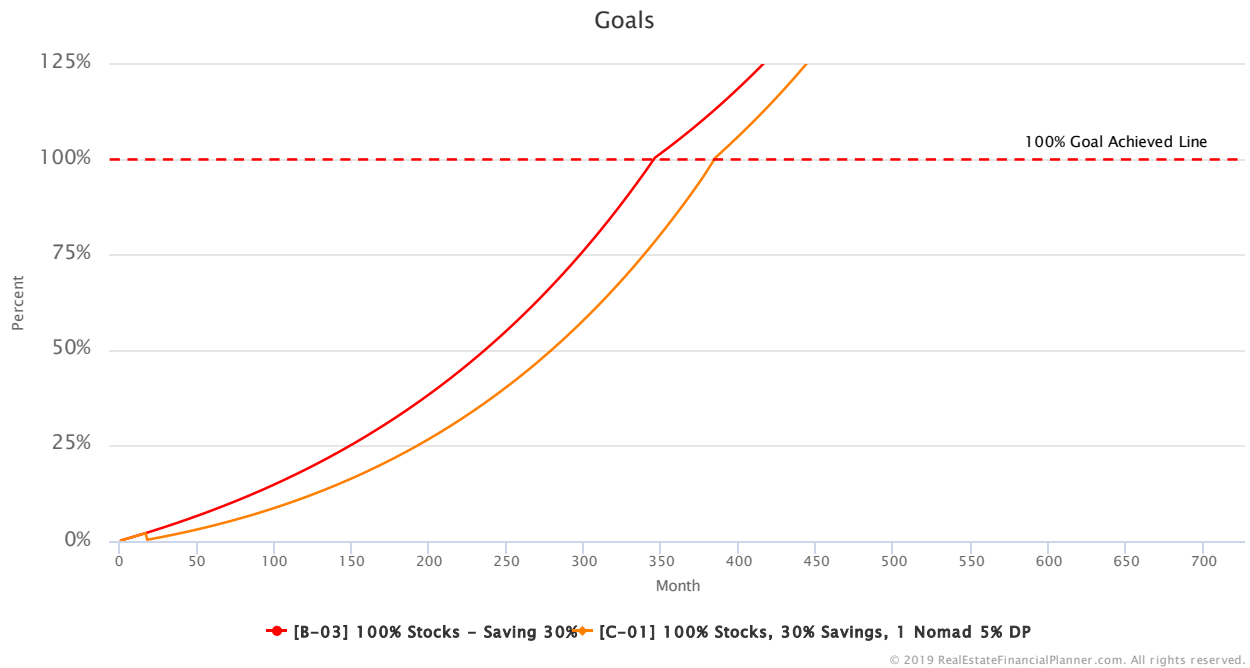
Yes, you got it... you paid off your mortgage on the property, and now you can save even more without a mortgage payment. Turns out you are even able to save more than you could if you were just saving 30% and renting like we modeled in the previous scenario.

Shortly after you pay off your property, you have successfully saved enough in your stock market account such that your safe withdrawal rate of the amount you have invested will allow you to achieve FILYP. At that point, the REFP software is set up to have you stop working for a paycheck and so your savings per month goes negative (you are pulling money out of savings). As your expenses continue to increase the amount it goes negative each month continues to grow. See the chart below.



I want to make one more point related to this very chart, but it requires that I reveal the punch-line related to how quickly you can achieve FI LYP with this scenario compared to the previous scenario where we just rented and saved 30% in stocks. So, here we go... which scenario do you think gets you to FI first?

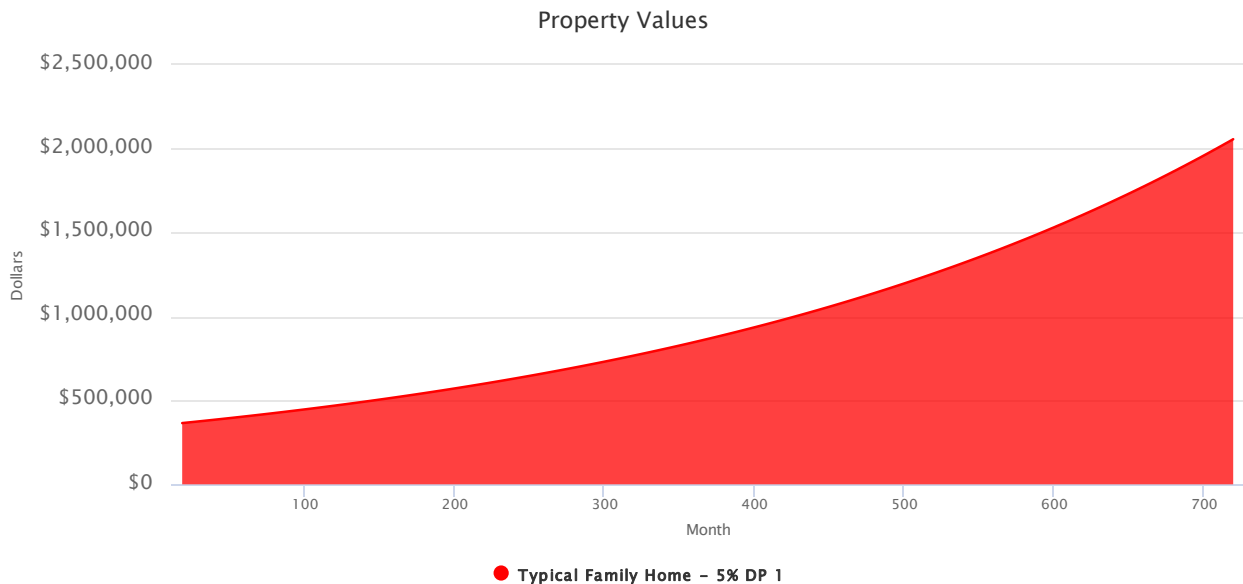
Turns out, renting and investing everything in stocks gets you to FI first as shown in the chart comparing the two goals below.



Renting and investing in stocks has you reaching FI in 28 years and 10 months (at about age 51 for you) and buying just one home to live in means you are able to reach FI about three years later (at about age 54 for you).

But that's not the whole story. What about your standard of living?

When you are renting, your personal expenses—all your personal expenses—are subject to inflation. That includes your rent. Rent tends to go up over time from inflation. However, when you live in your own home, part of your expense for shelter is no longer impacted by inflation. Property taxes still go up with inflation—remember, they are calculated as a percentage of the property value and the property is going up in value. You can see that in the chart below showing the value of your property over time.

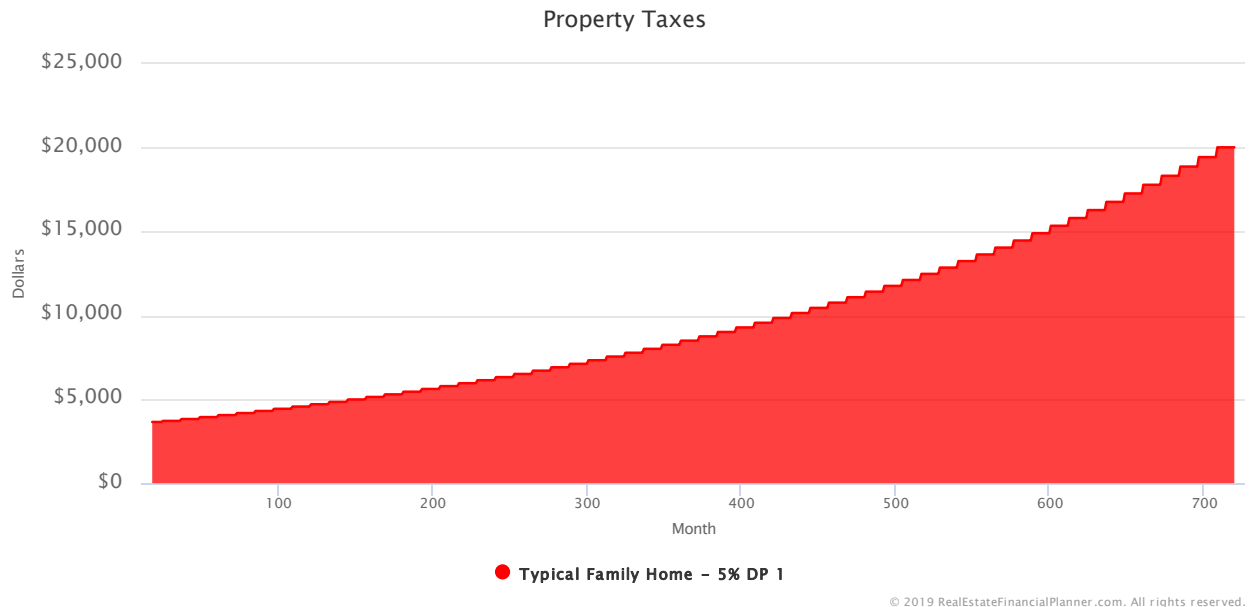


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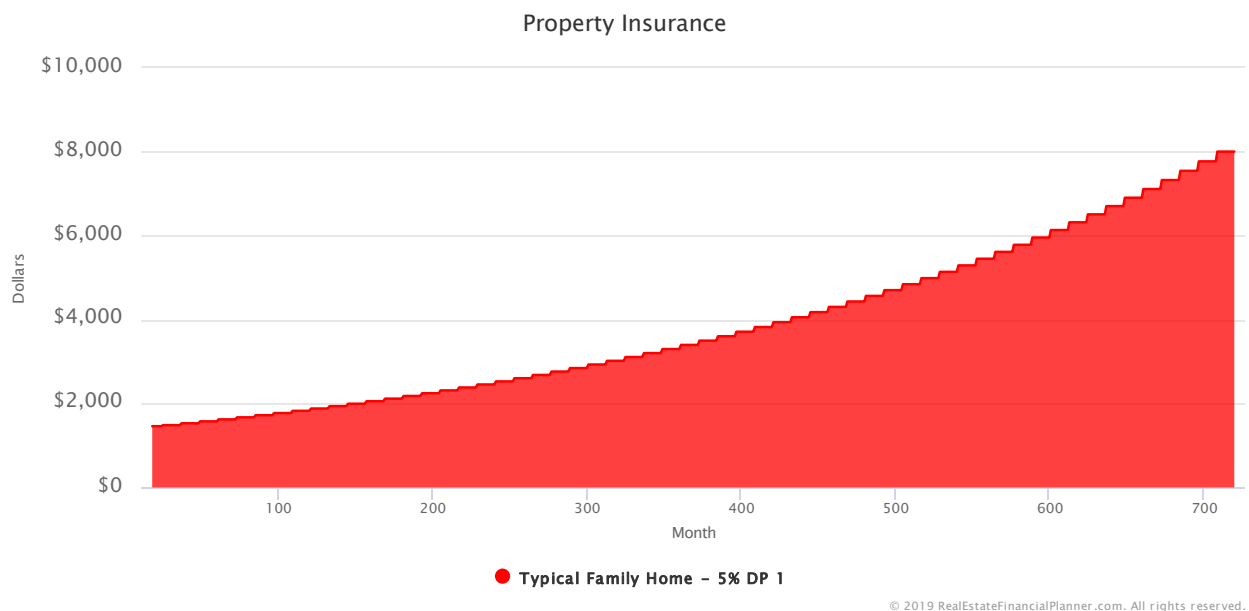
So, by year 60, the property is worth over \$2 million dollars. If we adjust back for inflation, it is still worth the same \$350,000. Remember, we assume housing prices just keep pace with inflation. This means that even though the house is worth over \$2 million in inflated dollars, it really is like having a \$350,000 property in today's dollars.

Looping back to our discussion about standard of living. I was talking about how the cost of your shelter is partially inflation proof. We determined that your property taxes are not inflation proof since those are based on the rising value of the property itself.

I show this in the property taxes chart below. Each January the property is re-assessed, and the property taxes go up based on how much the property appreciated.



So, if property taxes are not sheltered from inflation, how about property insurance? Nope, that's essentially the same story as our property taxes. We've assumed they are a percentage of the increasing property value as well. So, that chart looks very similar to the property taxes. This is the chart of property insurance below. It's hard to tell the difference between property insurance and property taxes from the shape of the chart, right?

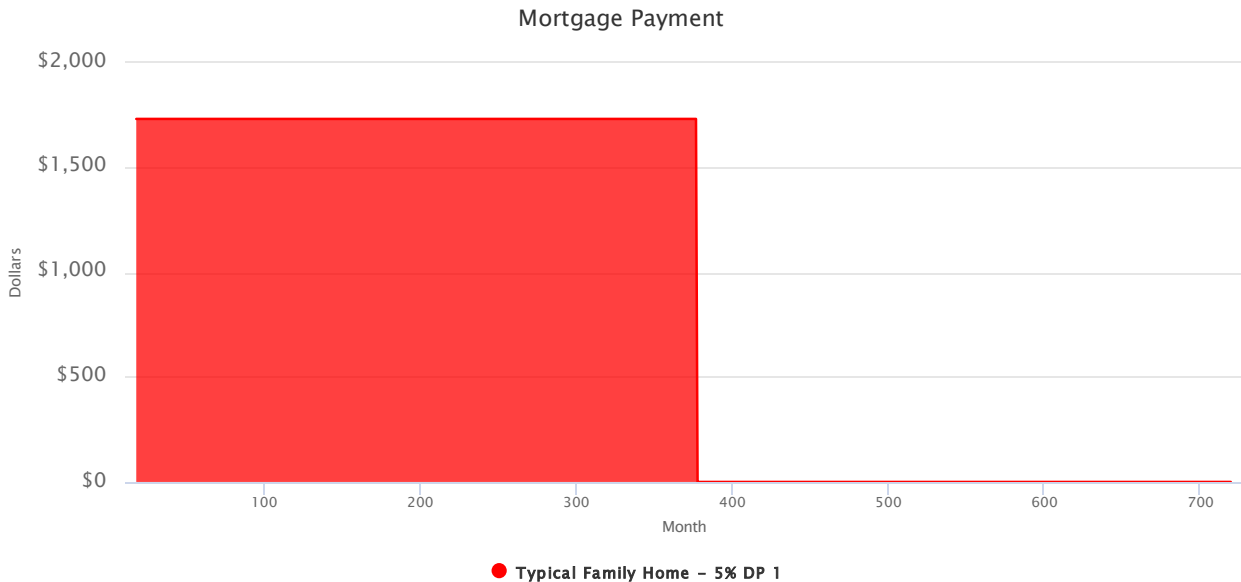


If it is not property taxes and not property insurance, then what is sheltered from inflation? I'll give you a hint... it rhymes with lorgage rayment (which is just a made-up compound word). That's right: Your mortgage payment.

Once you lock in financing for your property with a fixed monthly payment for principal and interest, that payment remains fixed for the entire duration of the loan. That means it stays fixed, protected from inflation for 360 months. You are protected from inflation for the entire duration of payments.

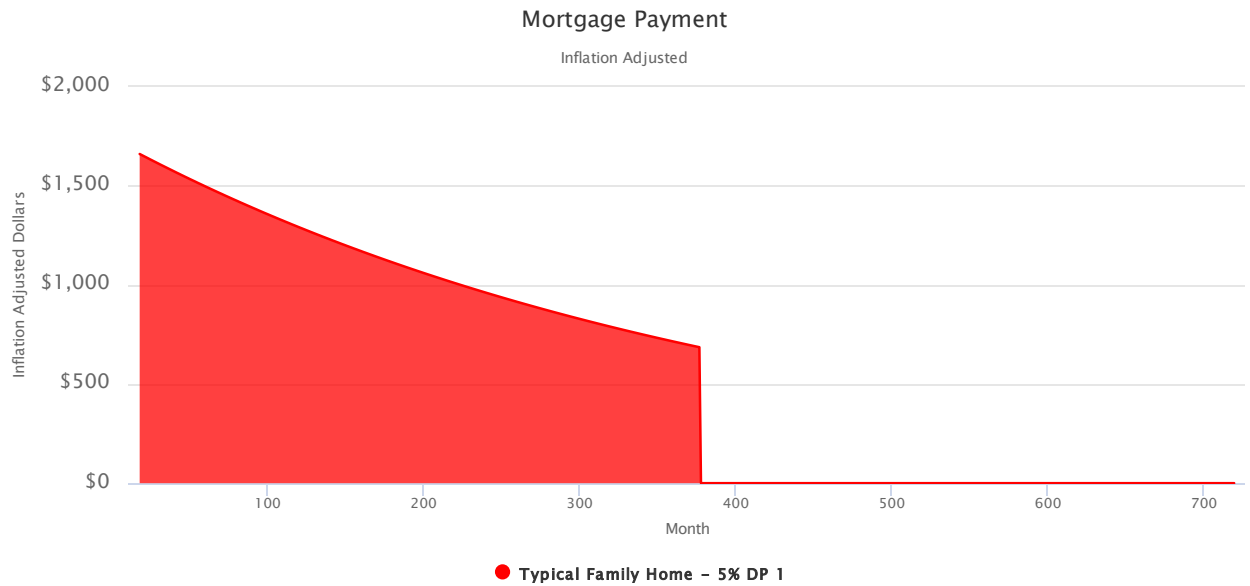
But what happens after the 360 months? The payment goes away completely. You get a huge reduction in your living expenses after the mortgage is paid off.

Let's look at the mortgage payment in a chart.



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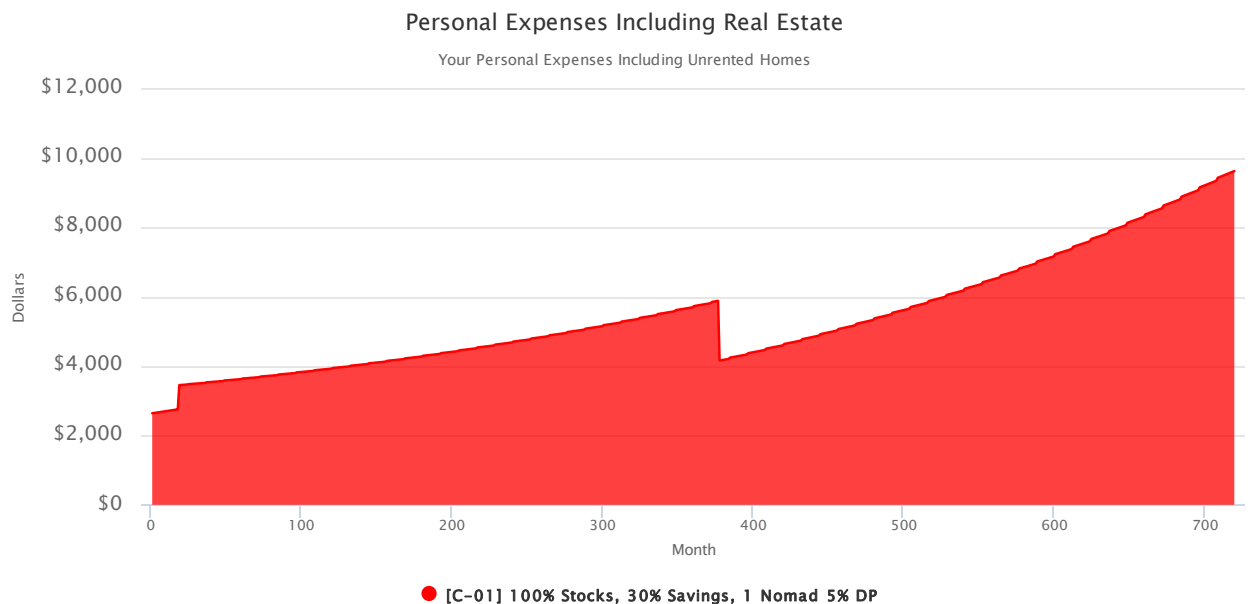
You will notice that this chart shows the same payment of \$1,731.12 per month from the first payment in month 18 through the last payment in month 377. It does not increase with inflation. In fact, if we adjust this very chart for inflation, we can see something unusual happen in the chart: The monthly payment appears to go down.



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That’s because the fixed mortgage payment in the current year of \$1,731.12 feels like a lot less money 30 years in the future when you are making the last payment. It “feels” more like a payment of \$685 today if we adjust for inflation.

But, I told you that your housing cost was more expensive than your rent was. I did. This is a chart showing your personal expenses including the cost of the home you are living in.



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You can see what I’ve already told you. You had some expenses early on which included renting a place for yourself to live. When you bought your property to live in, your living expenses went up. They stayed

elevated for 360 months while you had that mortgage. We will talk about how part of that payment was paying down your loan and building up equity in a few moments, but hold that thought for now. Back to describing the chart above... when you finally make your last mortgage payment, your living expenses decrease significantly and just continue to keep pace with inflation from there on.

I want to share two things about this chart with you. First, what it looks like if we adjust for inflation and second, how it compares to the previous scenario when we were renting and did not buy a house.

Let's start by adjusting the chart showing your expenses for inflation.



Ohhhh... isn't that interesting? When we adjust for inflation, we can see a very different story. Our expenses were essentially just keeping pace with inflation early on until we bought the property and moved in. But we volunteered to have a higher payment when we bought the property to live in. However, you can see that eventually, about 17 years (month 224) into owning the home, the "true" inflation adjusted cost of your expenses starts to drop below what it would have been if you had just kept renting and maintained your current lifestyle. From that point on, you can (1) save more money or (2) enjoy a slightly higher (and improving) standard of living and maintain the same savings rate. Then, once the mortgage is paid off, you see a huge drop in your personal expenses that gives you an even larger boost to your savings, or standard of living, or a little bit of both if you choose.

I promised you a second chart. On this one I am going to add the scenario where you rented instead of bought a home and saved 30% and invested in stocks. I'll even leave the inflation adjustment on for dramatic effect.





Do you see the difference? This is a classic example of a little pain up front for significant benefit later. You voluntarily accepted a higher shelter expense (mortgage payment, property taxes, and property insurance) instead of lower rent early on so you could enjoy significantly lower expenses later. Your expenses in the model where you rented just kept pace with inflation (flat line) where buying a house ultimately yielded expenses of about \$1,000 per month lower (in inflation adjusted dollars). When you are living on just over \$4,000 per month as your target monthly income for FI, savings of \$1,000 per month is significant. Think about how much of a difference an extra \$1,000 per month would mean to you right now. It is the same feeling.

I hinted earlier that there was more to the mortgage payment than just an easy comparison to rent. With rent, you pay your landlord, get to use the property for the time you paid for, and have no long-term residual benefit from it. With a mortgage payment on a 30-year amortizing loan, that's not true.

First, as I mentioned above, the payment each month on your 30-year loan remains the same every month for 360 months. It does not change.

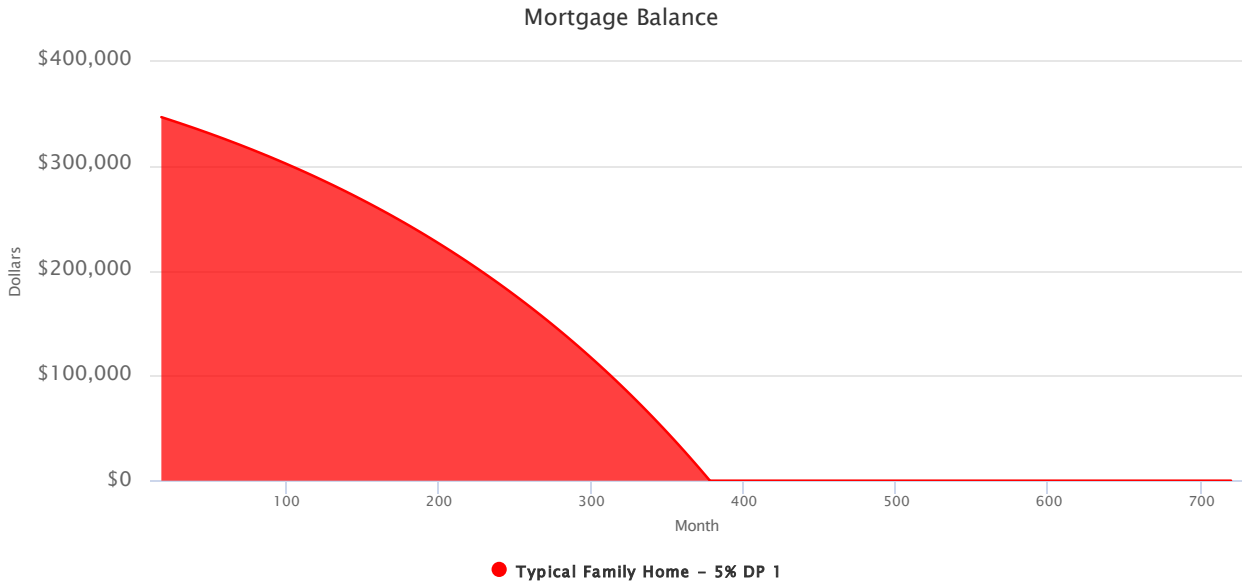
Part of that payment goes to the lender as "rent" for borrowing the money to buy the house. That's the interest part of the payment. Talk to your accountant or CPA about possible tax benefits of the interest you pay on properties, but that's not really the part I want to share with you.

The rest of your fixed monthly payment goes to paying down how much you owe on the loan itself. And this is where the magic happens.

Here's an over-simplified example of what happens each month behind the scenes at your mortgage company. They look at how much you owe. They take your mortgage interest rate, divide by 12 to get the monthly rate and multiply that by the amount that you owe. This is the amount of interest you paid for the previous month from the fixed mortgage payment you sent. Then, with the remaining amount of

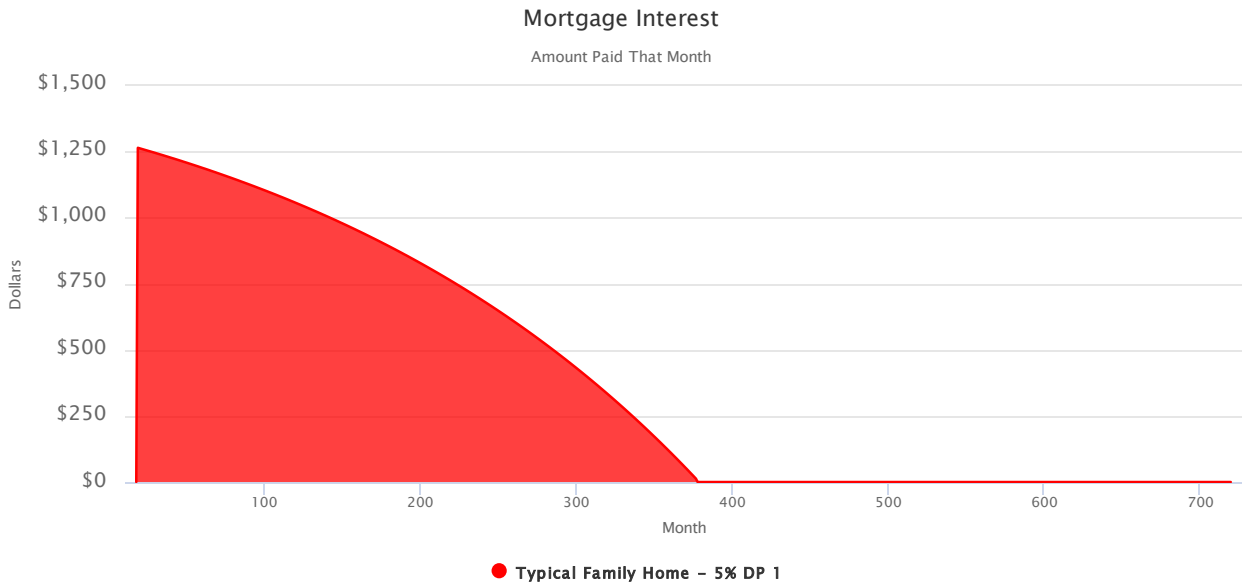
the payment they assume that was how much you paid them back. It reduces the amount you owe from the previous month.

Each month that you make a regular mortgage payment on a 30-year fully amortizing loan, you owe less than the month before. Here’s a chart showing how the balance of your loan decreases over time.



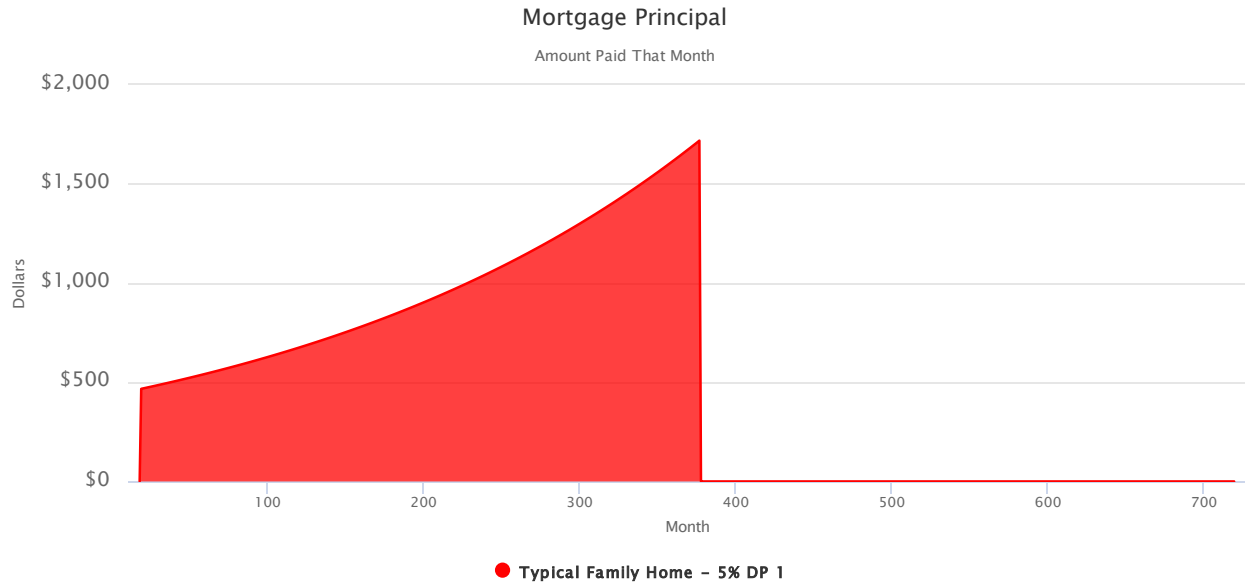
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Similar in shape, here’s a chart showing how much interest you paid each month. Notice, each month you are paying progressively less in interest to your lender even though your payment amount is the same every month for 360 months.



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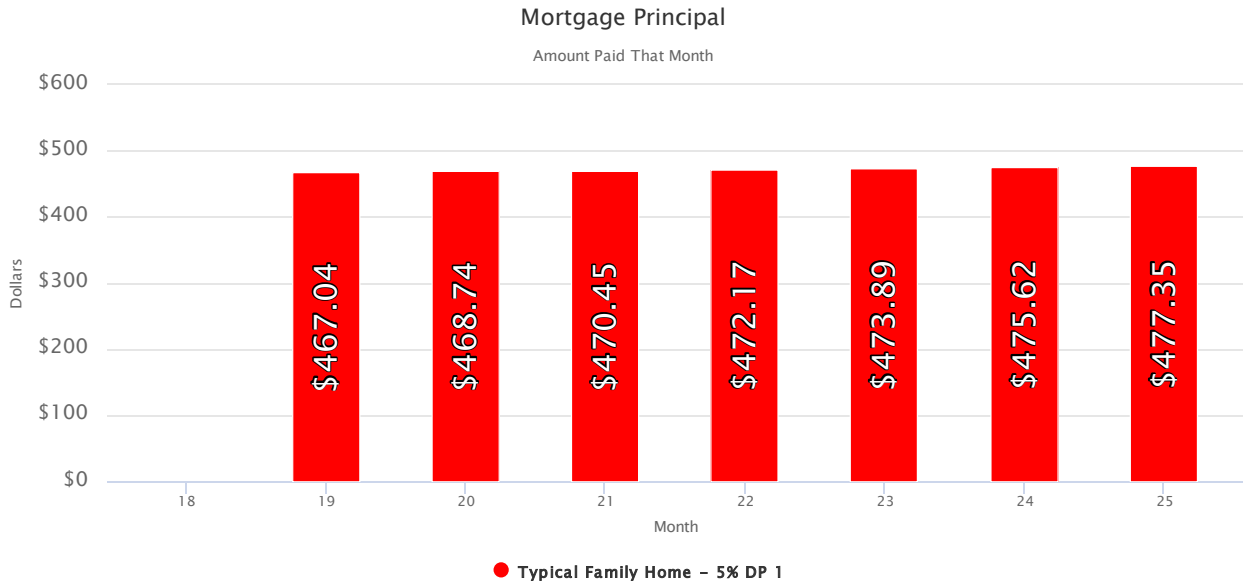
This chart complements the chart for interest paid. It shows the amount of principal you paid down each month on the loan. The amount you are paying off is going up each month.



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This is directly contributing to the equity you have in the property. Equity in property you own directly contributes to your net worth.

In month 19 your personal expenses increased from about \$2,754 per month when you were renting to \$3,455 when you bought your property. That’s an increase of about \$700 per month. Remember, I mentioned that was reducing how much you were “saving” and therefore how much you were investing in the stock market. But, part of that \$700 increase was money that was being “saved” in a different way. It was being “saved” as equity in your property. How much? Here’s a chart showing the first six months of mortgage principal paid.



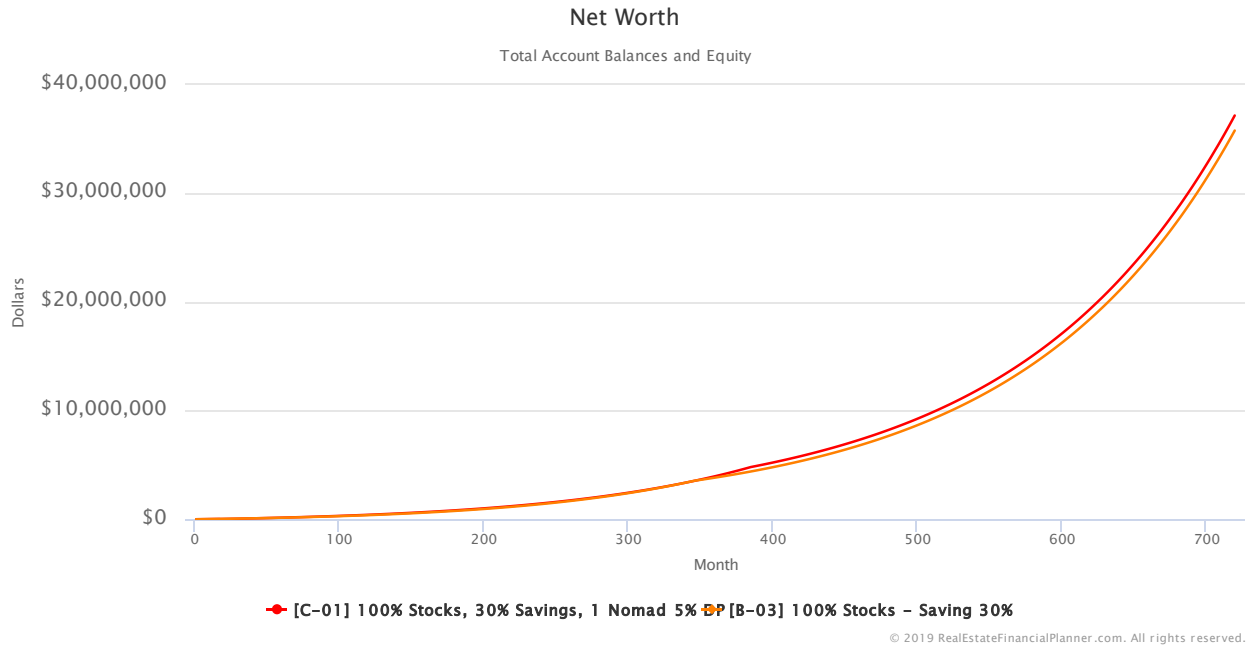
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In the first month, your personal expenses increased by \$700 (and that reduced the amount you were putting into the stock market), but really \$467 of that \$700 was being “saved” as equity in your property now.

You truly increased your living costs by the difference between \$700 and \$467, or about \$233 per month, in the first month you own the property. I emphasize the *first month you own the property* because the amount you “save” from principal paydown increases each month. By month 130 or so, you are paying down over \$700 per month on the loan, more than making up for the increase in housing cost.

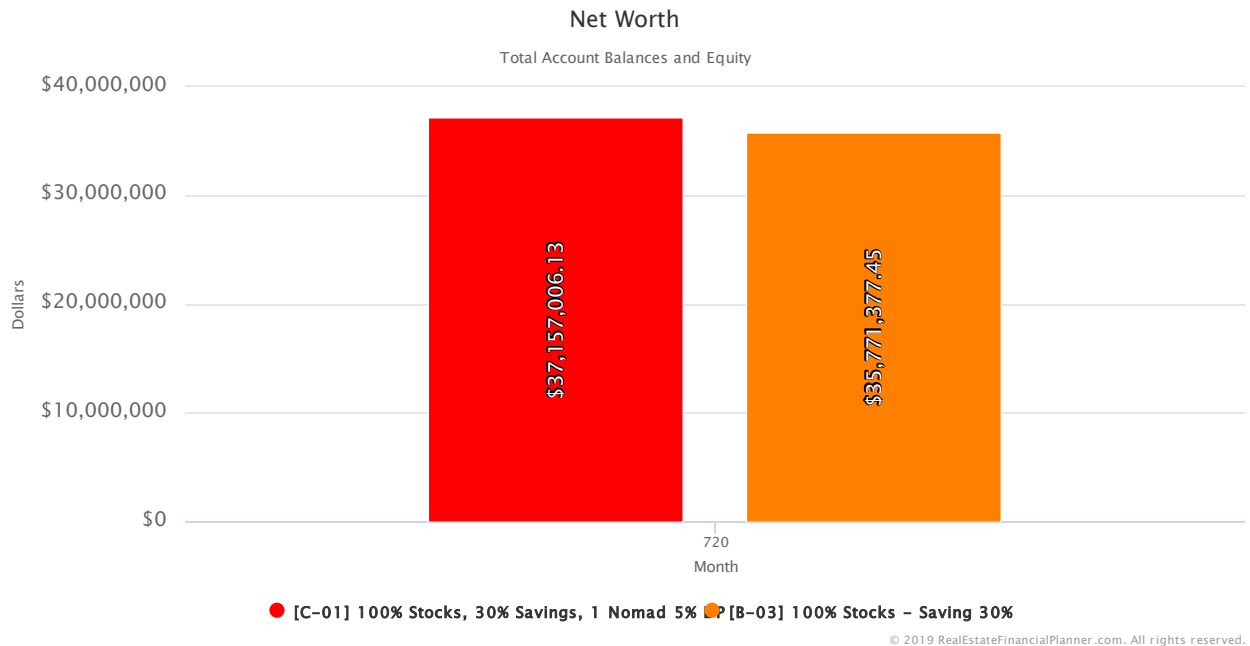
Previously, when we were looking at the scenario of you renting without buying a home to live in, you could look at your stock market account balance and that was your net worth. Now, as a homeowner and business owner (invested in the stock market and owning shares of companies), we would want to look at both your stock market account balance and the equity in your property to determine net worth.

Here’s a chart comparing the net worth in both scenarios.

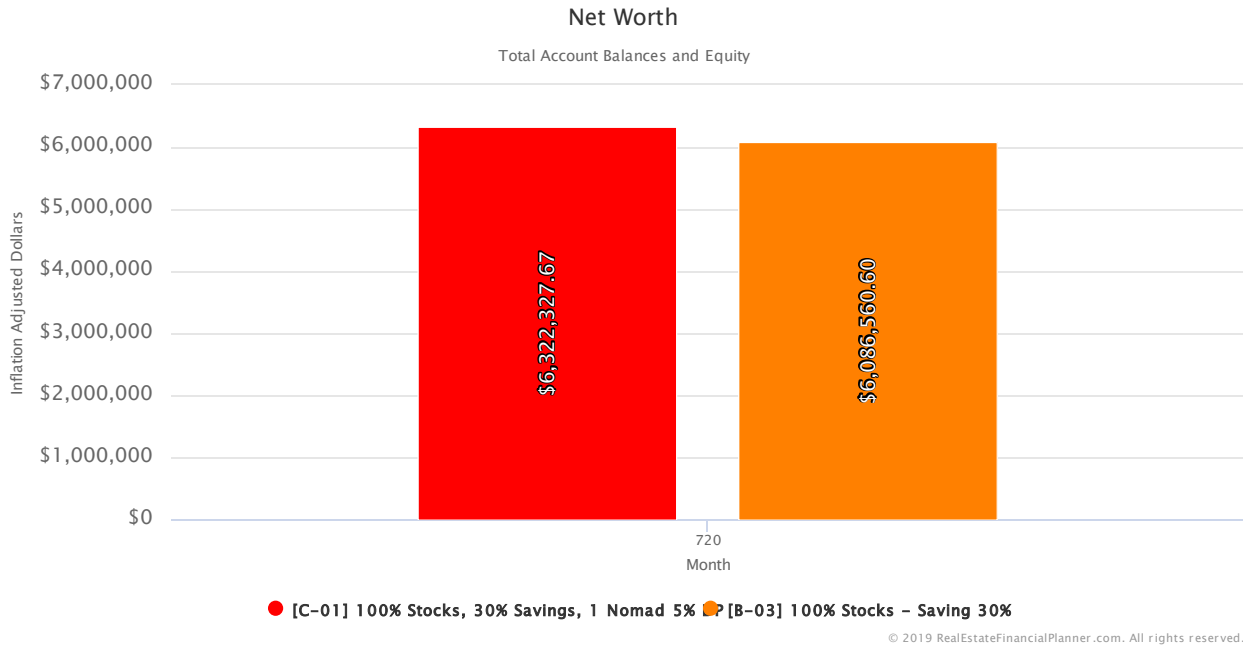


They look relatively close at first glance. Between the markers for months 300 and 400 you can see a tiny bit of separation between the two where buying a home starts to gain some ground over renting in terms of net worth.

If we look to month 720, when you are 82 years old, this is what your net worth would be based on the assumptions we made for the two scenarios.



That's a difference of about \$2.5 million in raw non-inflation-adjusted dollars. If we adjust for inflation, we are about \$250,000 in today's dollars apart.



Remember, renting and investing in stocks did help you achieve FILYP about three years earlier than buying a home. But, also remember, that you are able to live at a significantly better standard of living by buying a home and eventually eliminating a big chunk of your housing expenses.

What happens if you buy more than one property? Perhaps you buy a property just like you did here in this scenario, but then save up for a second property. When you can finally afford that second property, you convert the first property to your first rental. How would that compare? Can you achieve FILYP earlier? Will it bring you a higher standard of living once you get there?

These are questions I will answer next. But, first, here's the link to be able to copy this scenario to your Planner™ should you choose to change the assumptions or dig in deeper to analyze it.

## Model It Yourself

If you want to copy the scenario where you are saving 30% of your income, investing in stocks and buying one home to live in with 5% down payment to your own Real Estate Financial Planner™ account, use the link below:

- 100% Stocks, 30% Savings, 1 Nomad  
<http://refp.io/613>

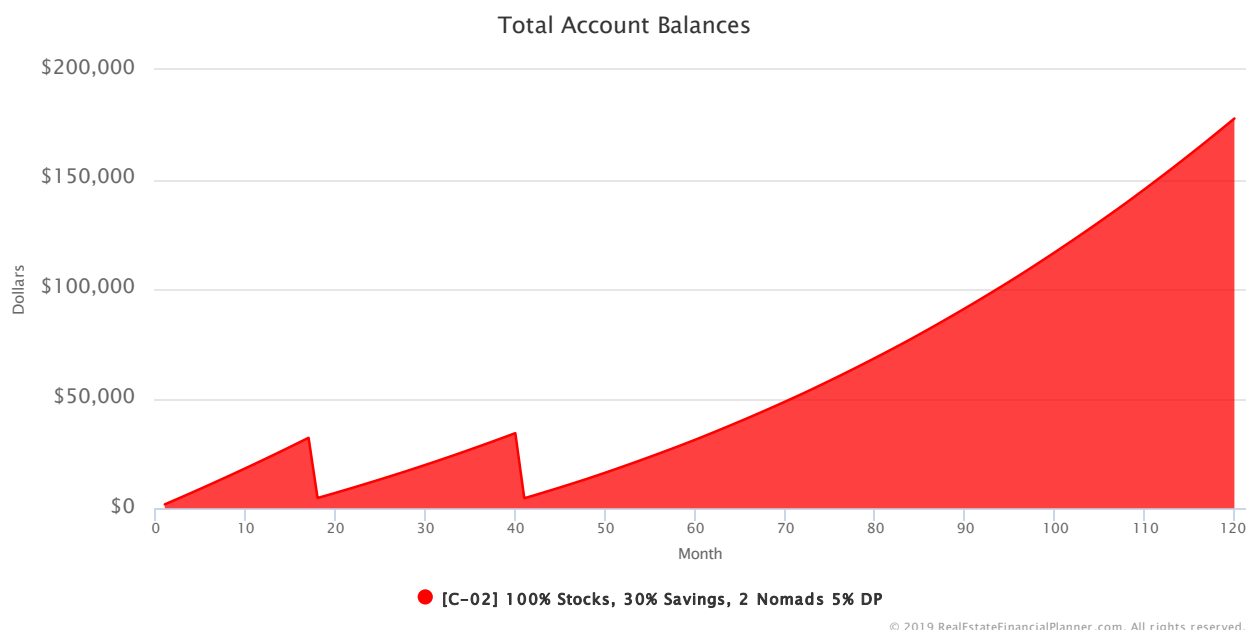
Of course, you can change any or all of the assumptions we made to more closely model your reality. And, if you plan to implement this strategy, I would strongly advise you to do a full Monte Carlo study of this strategy. I will share with you what variables I would use when running Monte Carlo on real estate in the next section when I provide you the link to copy the two Nomad™ plan to your Planner™.

## Your Second Nomad™ Property

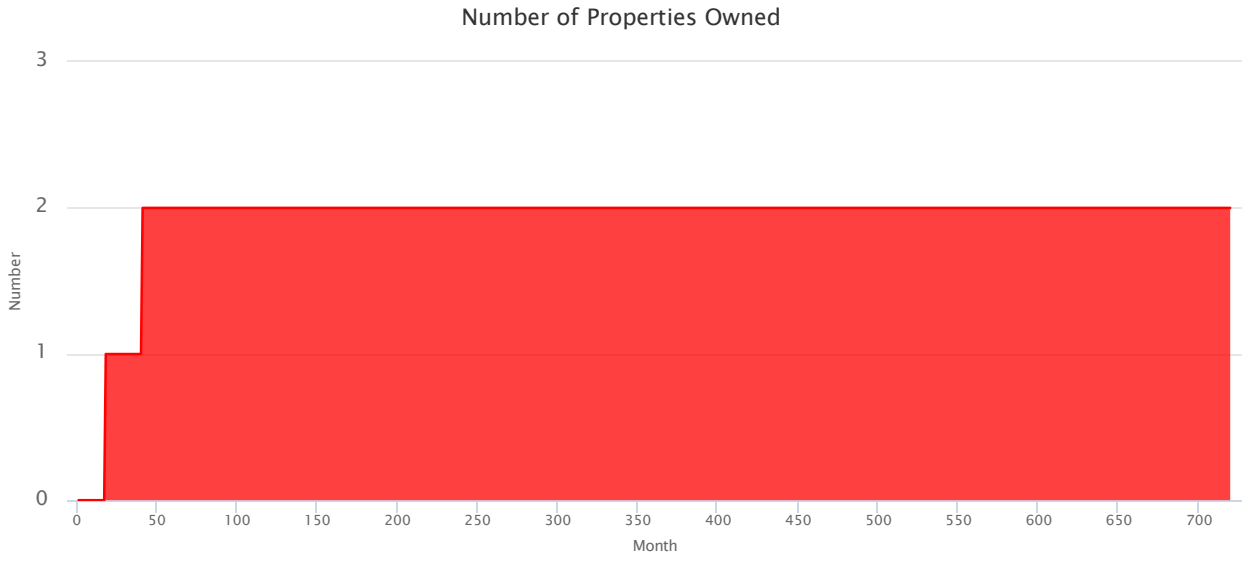
In this scenario you start by renting while you save up for your first home purchase. Then, you will stop renting, move into the first home and live there while you save up for your second home purchase.

Once you have saved up enough for the down payment, closing costs and about \$5,000 in additional cash reserves, you buy your second property and move into that one. You would then convert your first property to a rental.

The following is a chart showing your total account balance as you save up for your first down payment, then buy your first house. That is around month 18. Then you save up for your second down payment and buy your second house. That is month 41. From then on, you are just investing in the stock market and not buying any additional properties.



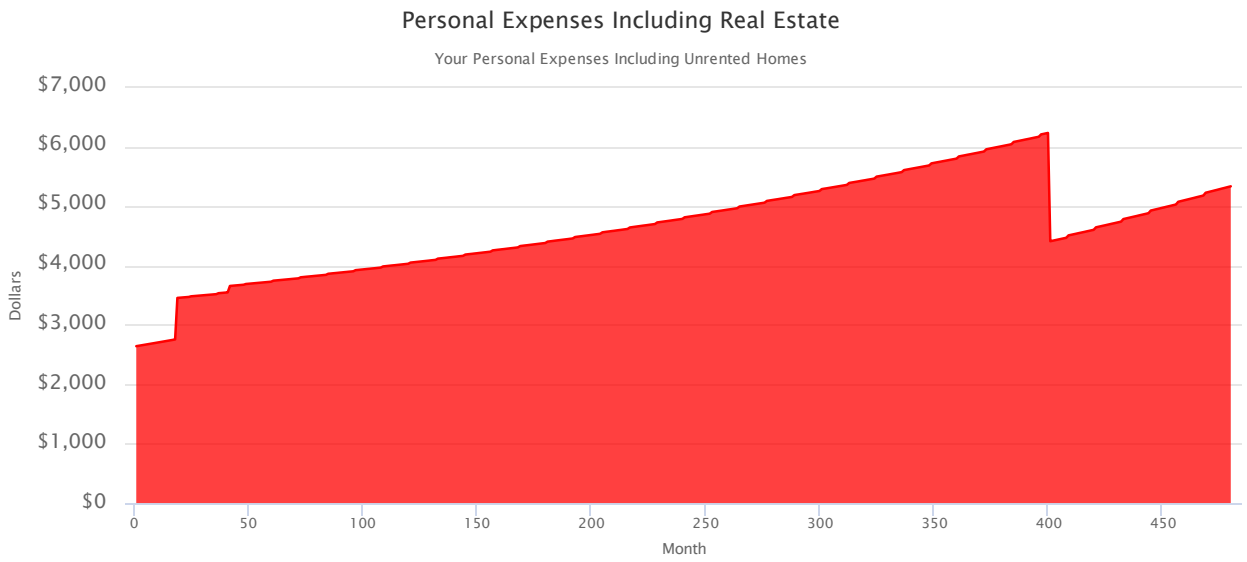
This next chart shows that you bought your first home in month 18, the next in month 41, and then you keep the two houses for 720 months, or 60 years. At that point you will be 82 years old.



● [C-02] 100% Stocks, 30% Savings, 2 Nomads 5% DP

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If you recall our discussion on buying a single property, I shared with you a chart showing your personal expenses including the cost of the home you were living in. Buying this second house does slightly bump up your expenses as well. Why? Because the second house you are buying is slightly more expensive than when you bought the first property. Here's a chart showing your personal expenses for the first 40 years only.



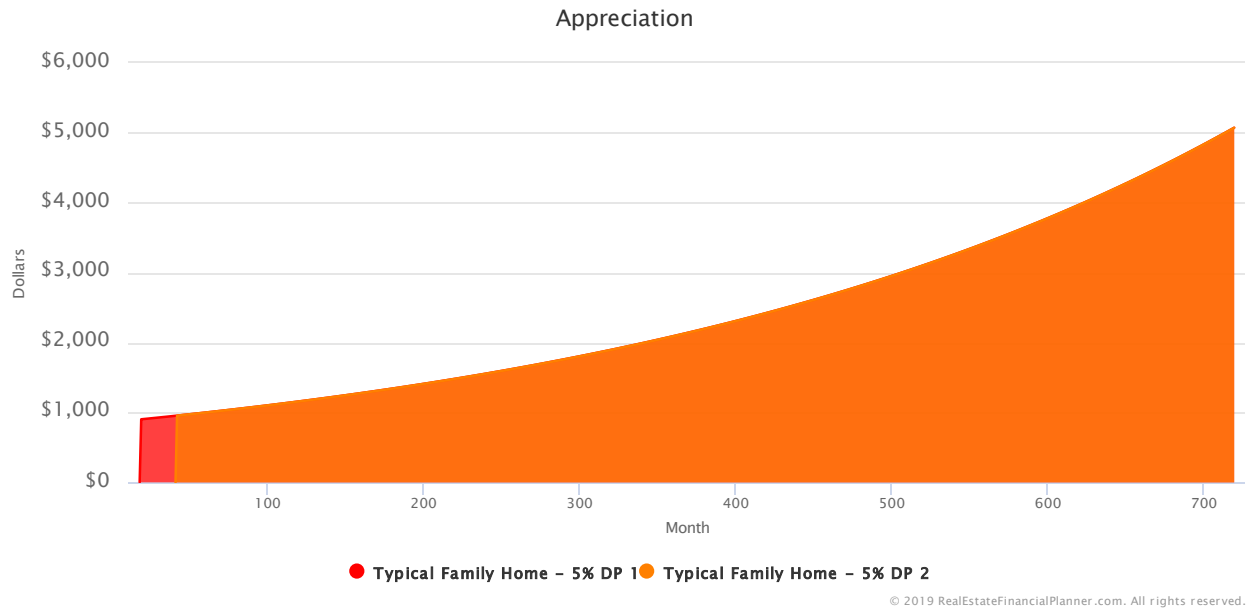
● [C-02] 100% Stocks, 30% Savings, 2 Nomads 5% DP

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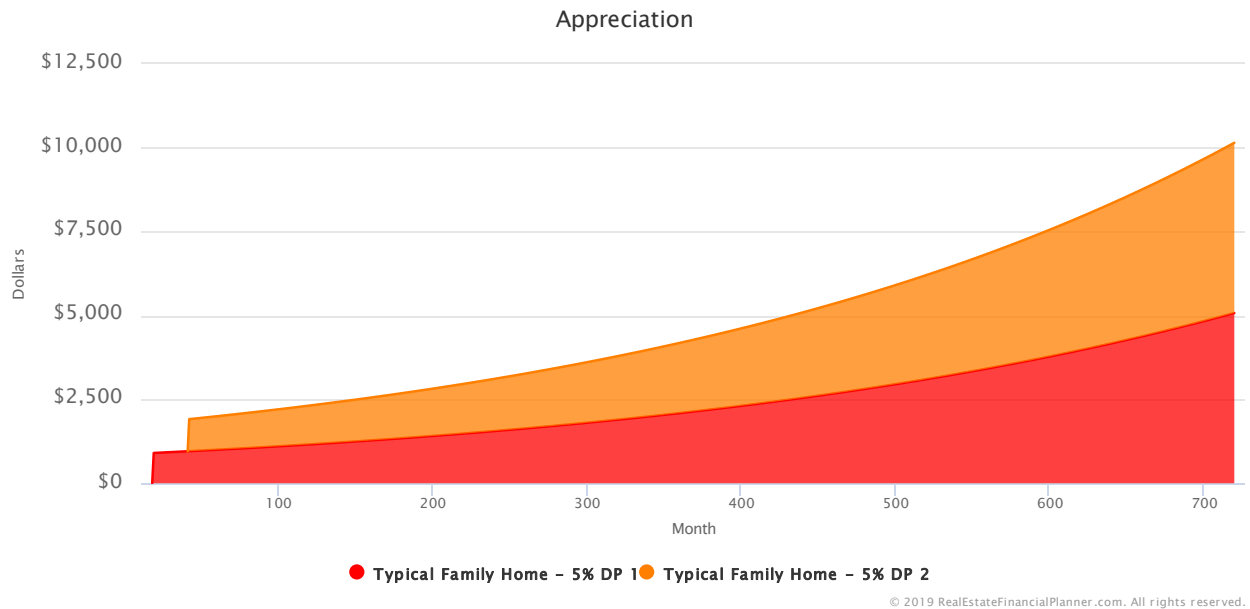
You can see the small bump in the chart above from the extra expense of buying the second property in month 42.



You have two properties now, which means two properties that are going up in value each month (mostly from inflation if you recall our previous assumptions). That means you are getting appreciation on both. The properties are both appreciating at the same 3% per year each. Here's a chart showing appreciation on each property.



If we stack the appreciation on top of each other, you can see the total appreciation from both properties graphically.

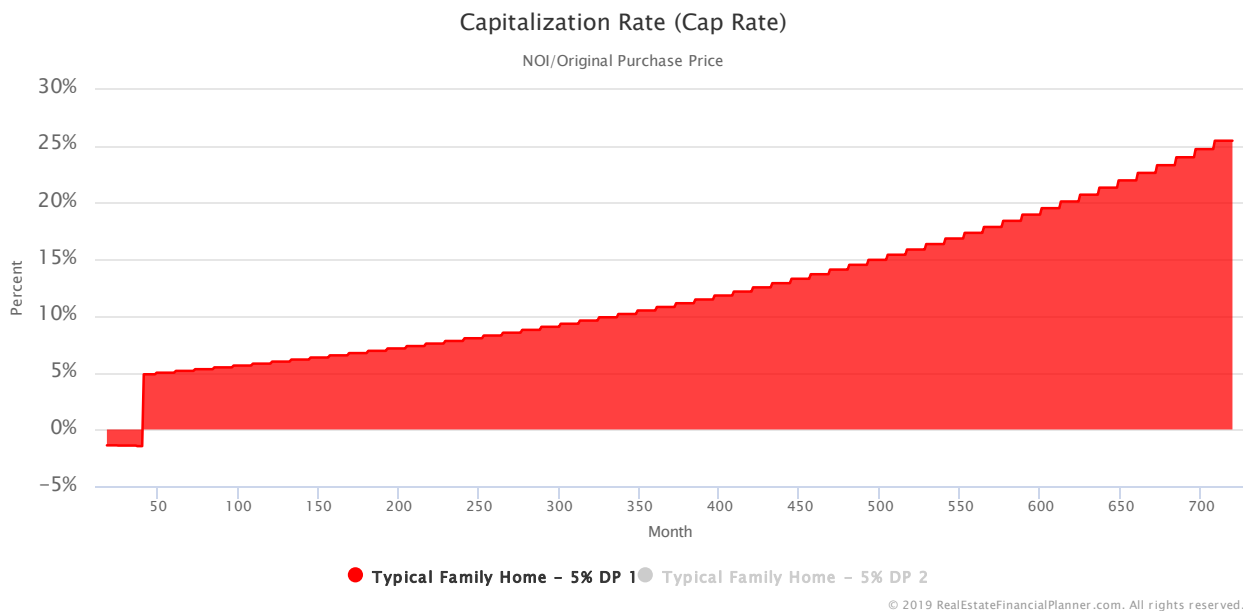


Remember though, you converted that first property from a home you were living in to a rental. That means you have a tenant now with rental income.

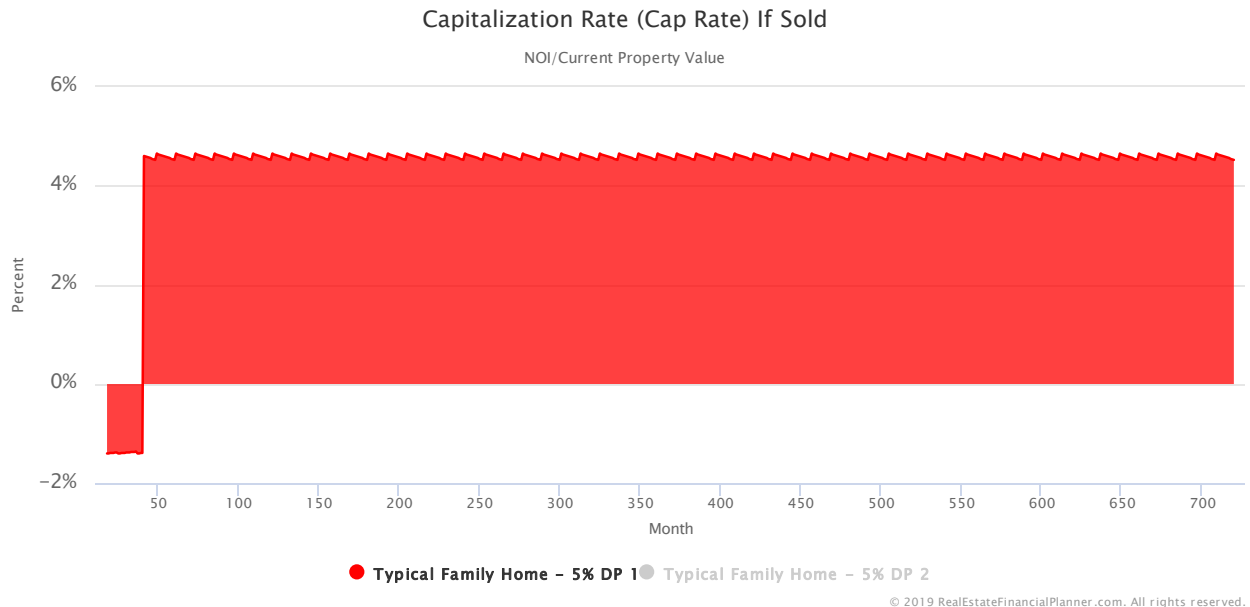
You may hear people talking about Capitalization Rate (or more colloquially Cap Rate). Cap Rate is the ratio of income from your property minus all the expenses—except your debt payments—divided by the purchase price of the property. All the income from your property minus all your expenses is called the Net Operating Income (NOI). Cap Rate, then, is actually:

$$\text{Cap Rate} = \text{Net Operating Income} \div \text{Purchase Price}$$

If we plot Cap Rate over time for the first property, you can see that the cap rate was negative when we lived in the property and did not have any income on it. Then, when we rented it, cap rate jumped up and increased over time as rents rose.

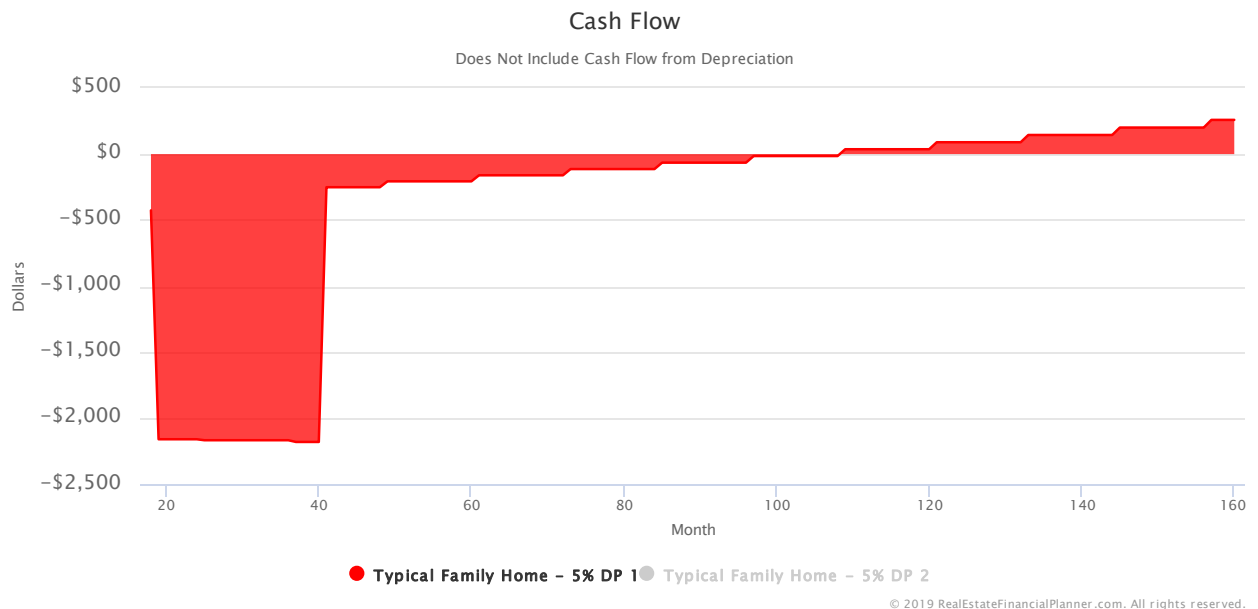


If we adjust the formula for Cap Rate and use the then current value of the property instead of the original purchase price, you can see that Cap Rate appears to stay about the same. The yearly saw pattern is from the property value going up each month from appreciation while rent is fixed for the year from yearlong leases. Once the lease renews at the higher amount, the Cap Rate rises. Then it declines again as property values increase until the lease renews again.



## Cash Flow

Once you start to rent the first property you bought, you start to receive income on that property. Your cash flow on the property goes from very negative (when you were living in the property with no income), to significantly less negative over time.



As rents increase over time with each lease renewal, your cash flow gets slightly better until, in month 109, your cash flow on this particular property finally goes from slightly negative to slightly positive.

A couple points about this.

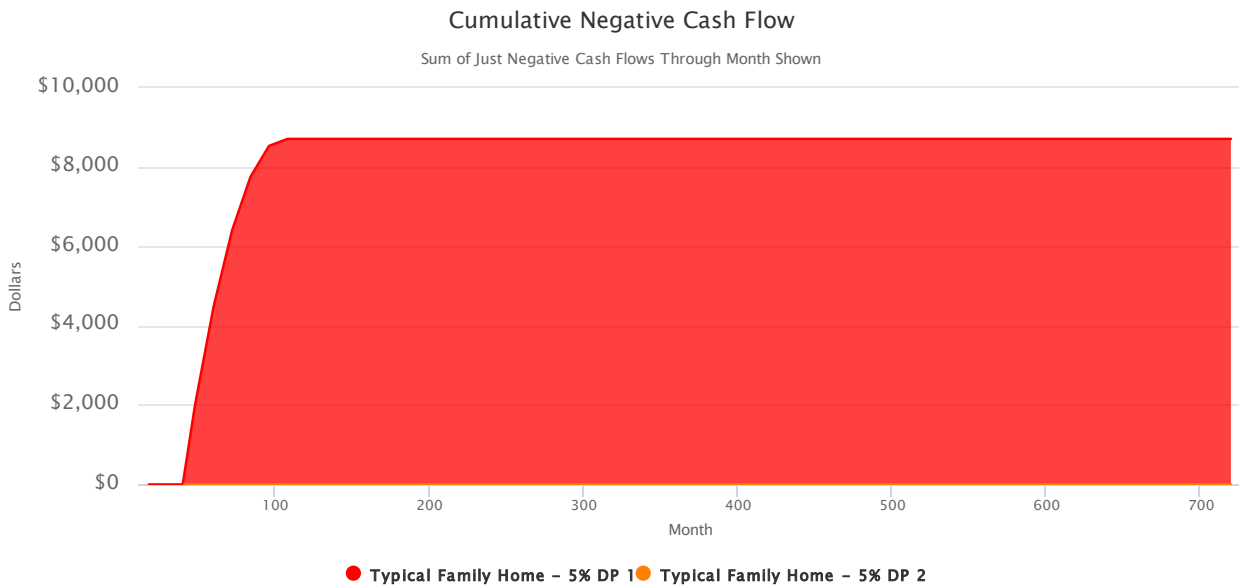
First, I want to remind you that you put a mere 5% down on this property when you bought it. If you had put 20% down, cash flow would be significantly better, but you would have put a lot more down.

In almost every case if we invest a large enough down payment (even up to 100% of the purchase price), eventually we will have positive cash flow. In many cases, if you put up 20% to 25% as a down payment, you will have positive cash flow. In many real estate markets, people can put 20% down and have strong positive cash flow. In other real estate markets, it may be incredibly difficult to get positive cash flow even with 50% down. Regardless, if you put enough down, you can usually achieve positive cash flow.

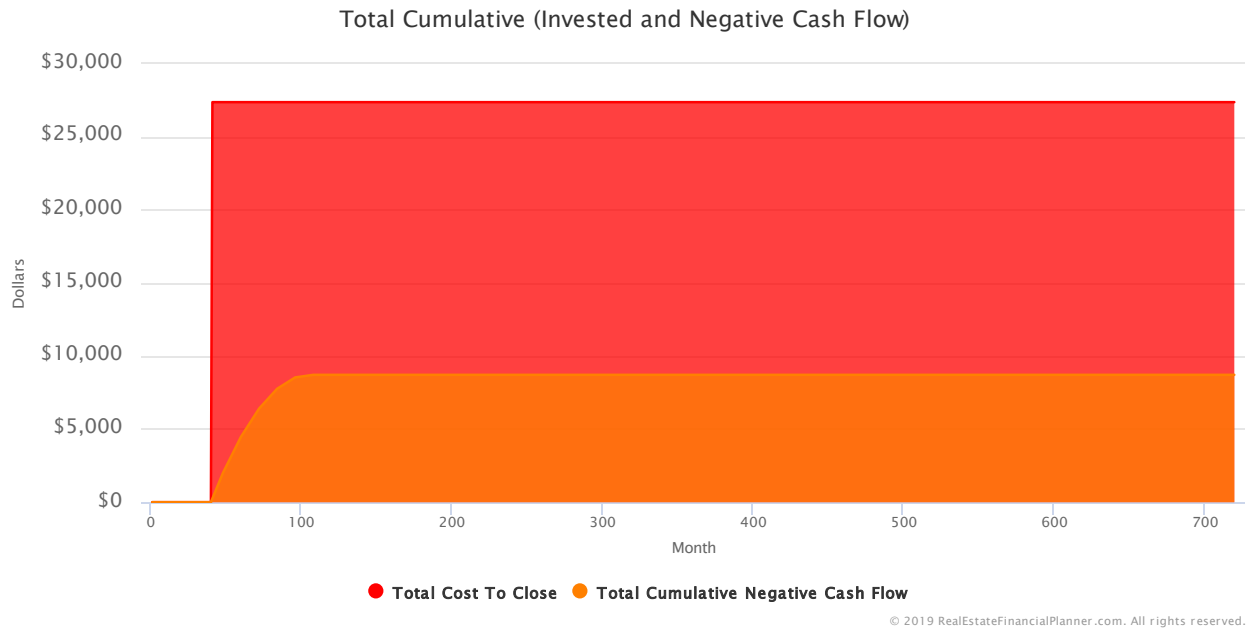
If you put less down than is required to have positive cash flow, you could almost think of the negative cash flow you have as a deferred down payment over time. In other words, the monthly negative cash flow payment you make could be thought of as the down payment you didn't put down to get positive cash flow to begin with.

So, if we do think of negative cash flow as a deferred or financed down payment, how does paying negative cash flow as a deferred down payment compare to putting up the full down payment up front? Let's look at that with this scenario.

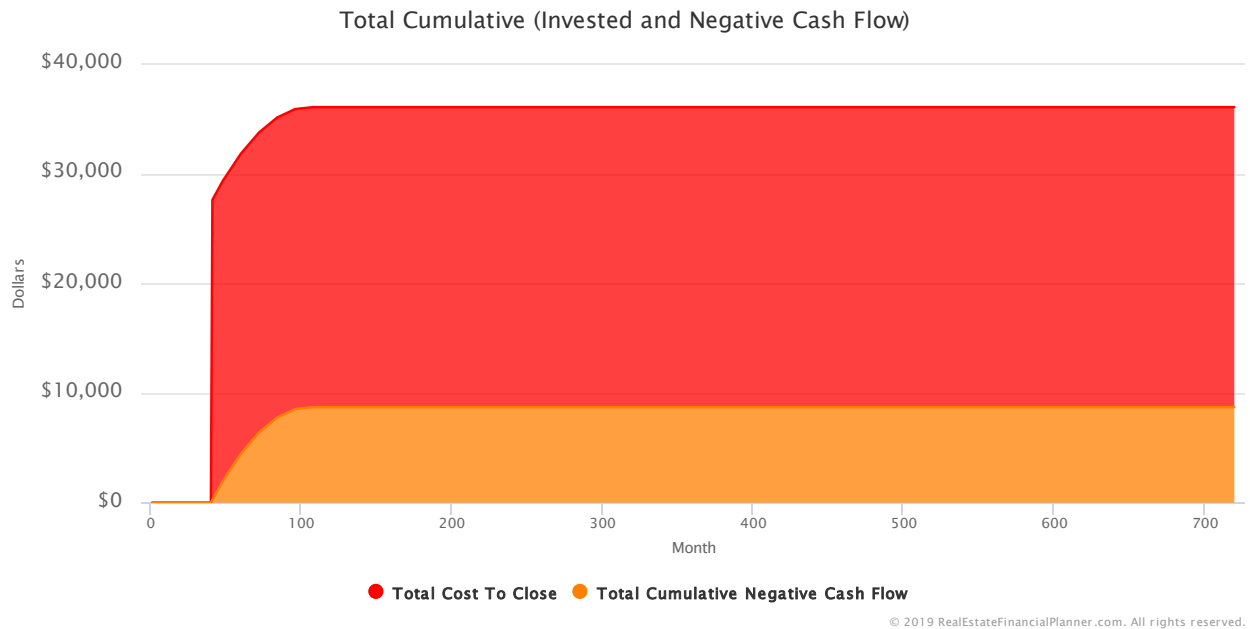
In this case, if we add up all the negative cash flow from the property, how much is it in total? We call this *Cumulative Negative Cash Flow* and here's a chart showing the cumulative negative cash flow on the property for the time we had it as a rental.



This cumulative negative cash flow is just part of what you had to invest to get this property. You also need to look at how much you used as a down payment. Remember, you opted to buy this property with a 5% down payment. Here's a chart showing the relative sizes of your down payment and the cumulative negative cash flow.



If we stack them, we can see the sum of both on the same chart. Here’s a chart showing the total amount you invested in this property including down payment and negative cash flow.



It looks like, even with all the negative cash flow plus the down payment, you have invested about \$36,000 to acquire this property. How much would it have been if you had put 20% down to start with? Assuming you would have had positive cash flow from the beginning, there would be no deferred down payment in the form of negative cash flow, so it really is just the 20% down payment.

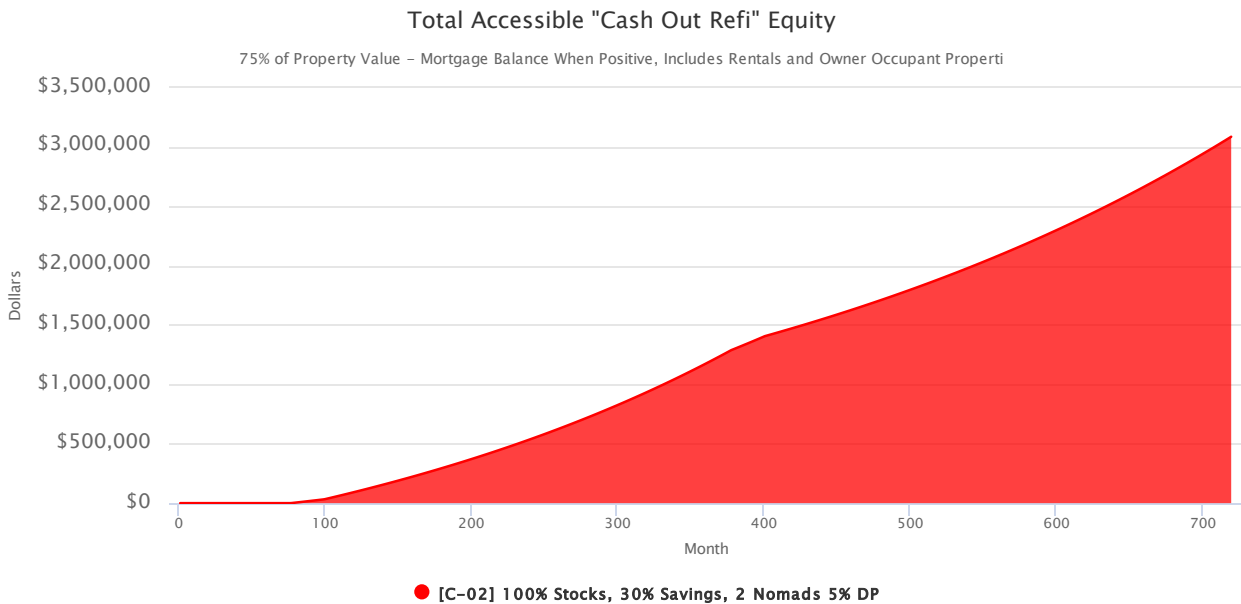
A 20% down payment on a \$365,000 purchase price would be about \$73,000.

This is a personal question for each investor, but I will ask you: would you rather invest \$36,000—which includes the down payment, closing costs and negative cash flow on the property until it becomes positive—or \$73,000 plus a few thousand dollars in additional closing costs to acquire a property with at least break-even cash flow to start?

Personally, if I only had \$80,000, I would rather put up the approximately \$28,000 in down payment and deal with slightly negative cash flow (which isn't even negative as you will see in a moment) with cash reserves of \$52,000. If I bought the 20% down property, I would have a much riskier (in my opinion) \$4,000 or so in cash reserves and a lot more equity. Equity is not easy to access. Many folks would refer to this as being illiquid; it is more difficult to access if you need it quickly. Cash reserves, on the other hand, are very easy to access. I would rather be liquid than have more equity.

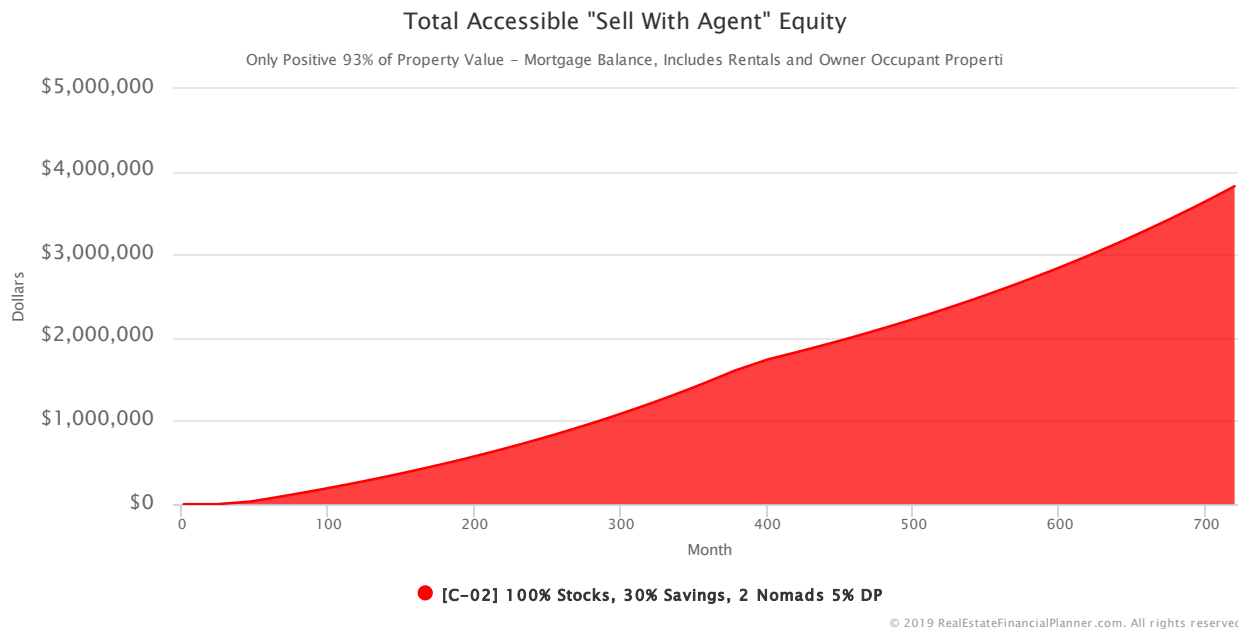
If you run into a cash flow crunch, you cannot easily tap that 20% of equity. You'd need to either sell or refinance. If you sell the property, you pay the transaction costs of a sale including your share of closing costs and the full real estate commissions for both buyer and seller as is customary in all real estate markets I am aware of. If you refinance, you can usually only access 75% of the equity in rental properties unless you can find a lender willing to loan higher than that.

Your total "accessible" cash out refi equity where you can refinance up to 75% of the property value is shown in the chart below.



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Your total "accessible" equity via selling with a real estate agent (referred to as Sell With Agent Equity), where you can net 93% of your sale price minus your mortgage balance, is shown below. Why 93%? We are assuming a 6% sales cost and 1% as your share of closing costs.



In an ideal world, you would always buy properties with positive cash flow to start with. In reality, sometimes we live and work in real estate markets where buying properties with positive cash flow is extremely difficult to do with even 20% down payments. And, if it is difficult with 20% down payments, it is even harder with just 5% down payments.

## Depreciation

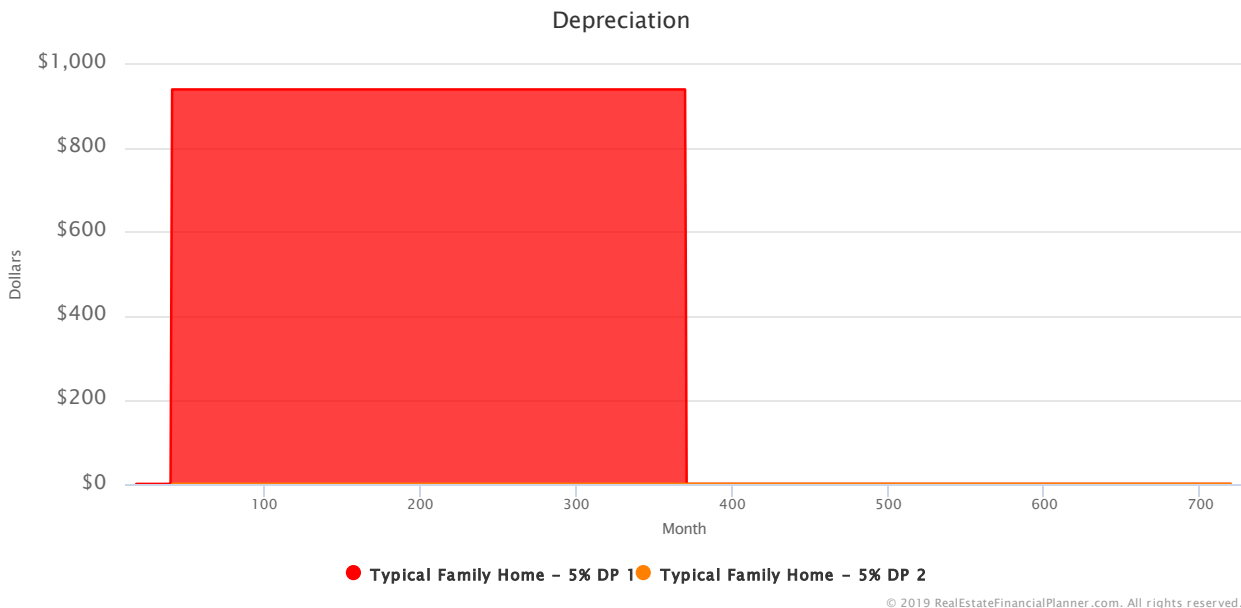
Second, since you are now renting the property, you also have the benefit of depreciation. Depreciation can look like cash flow since it is money you get back on your tax return in the form of not having to pay taxes on some of your income. It is money back in your pocket that you would not otherwise have.

Let's look at how depreciation works and what the depreciation benefit would be on this property.

When you start renting a property, current tax law allows you to depreciate the value of the building (specifically excluding the value of the land). If you are buying residential properties, you can depreciate the value of the building over 27.5 years. If you were buying commercial buildings—which you are not—you would be able to depreciate the building over 39 years instead.

So, if you assume the value of the land to be 15% of the original purchase price, you can then depreciate the remaining 85% of the purchase price over 27.5 years. I would strongly recommend you connect with your accountant or CPA to find out what percentage of the purchase price they will be using for the value of the land and, consequently, what percentage remains for the value of the building. It will give you a rough idea of what you should use in the Real Estate Financial Planner™ when modeling your plan.

Back to calculating depreciation. So, if you take 85% of your purchase price and divide by 27.5 you can determine how much per year you are able to depreciate. The following chart shows the depreciation you can get per year for the time you are able to depreciate the property (27.5 years).



As you can see in the chart above, you are able to depreciate about \$940 per month or \$11,280 per year. Does that mean you are able to get an extra \$940 per month in cash flow? Unfortunately, no. How does depreciation work then?

Seek clarification from your accountant or CPA, but here's a layman's explanation. Depreciation allows you to reduce the \$70,000 per year that you are earning. This reduces the amount of tax that you need to pay. In this example, you are earning the \$70,000 per year from your job plus the rent you are receiving from the property. Let's assume, to simplify the math, that rent is about \$2,000 per month (it's not) and that you are earning about \$70,000 from your job and \$14,000 per year from rent. Your total earnings are now \$84,000 per year and you'd be paying federal and state income taxes on that minus any deductible expenses you might have like interest payments on your loan, etc.

However, with depreciation, you get to reduce the amount of income you are earning by the \$11,280 per year in depreciation benefit you have received from owning this rental property. So, instead of paying taxes on \$84,000 per year, you are paying taxes on \$72,720.

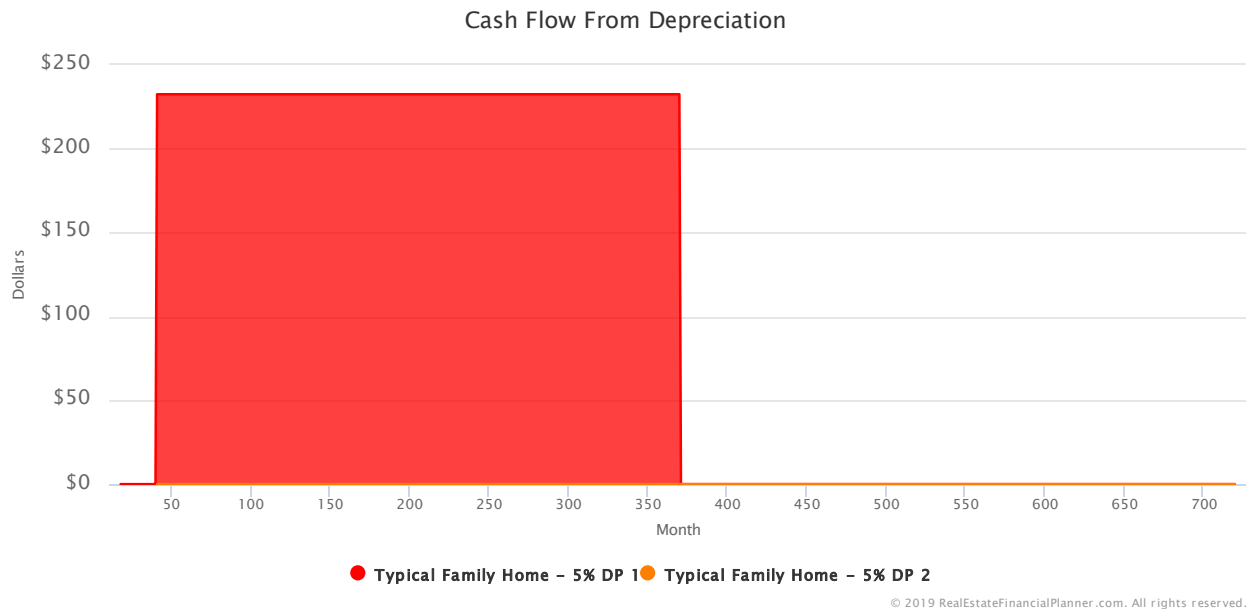
What does this mean in terms of extra money in your pocket? You can choose to pay less in taxes at the end of the year or to get a little bit more in each paycheck from your job by adjusting your exemptions. To figure out the actual cash-in-your-pocket benefit from that \$940 per month in depreciation, it really is your highest tax bracket times the \$940 since you are reducing your income in the top tax bracket.

This means if you are filing as a single person, your top tax bracket appears to be about 25%, so you really get to keep about 25% of the \$940 per month from depreciation or about \$235 per month. I call this *cash flow from depreciation*, which is your tax rate times your gross depreciation. When modeling



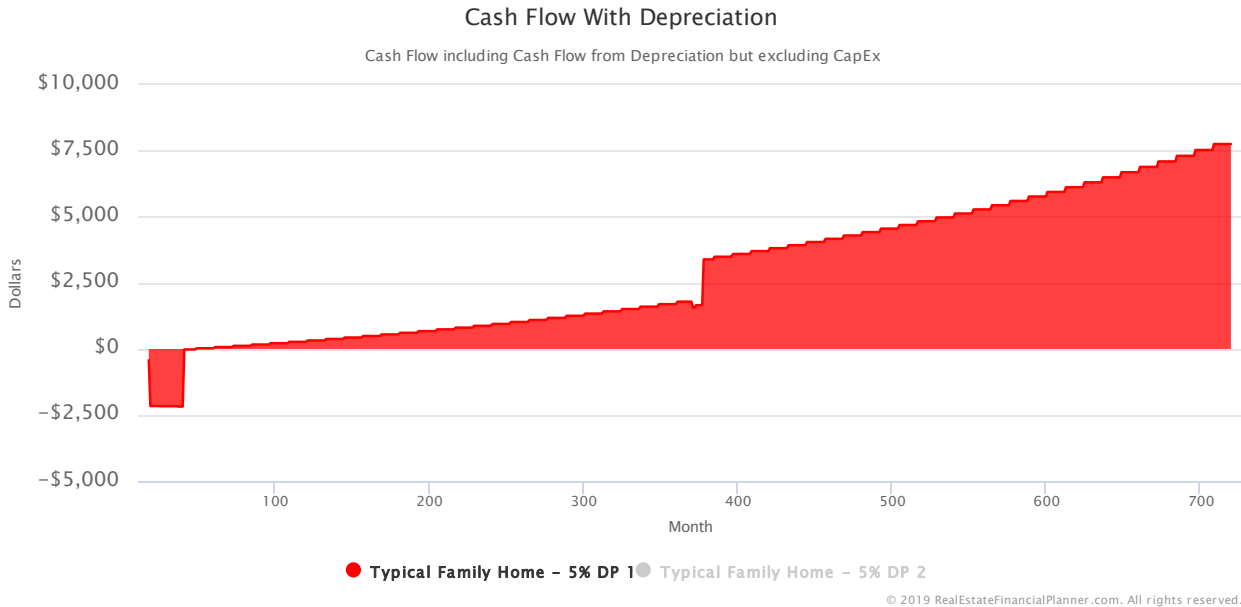
this in the Real Estate Financial Planner™ software, instead of using your top tax bracket, we use your *Effective Tax Rate*. This makes the calculation more conservative since it gives you slightly lower cash flow than you are likely to receive on your filed taxes.

If we take your gross depreciation from the chart above and multiply it by your *Effective Tax Rate*, you can see the results in the chart below which shows your cash flow depreciation per month.



And in case it was not clear from my description above, you only get the benefit of depreciation over the first 27.5 years of renting the property. Based on current tax code, it goes away after that and you no longer get any depreciation benefit.

So, what if we take the cash flow chart I showed you previously and add to it the cash flow you are receiving from your depreciation benefit? We can see a more accurate picture of your cash flow when considering both cash flow and cash flow from depreciation. Here's a chart showing your cash flow with cash flow from depreciation.

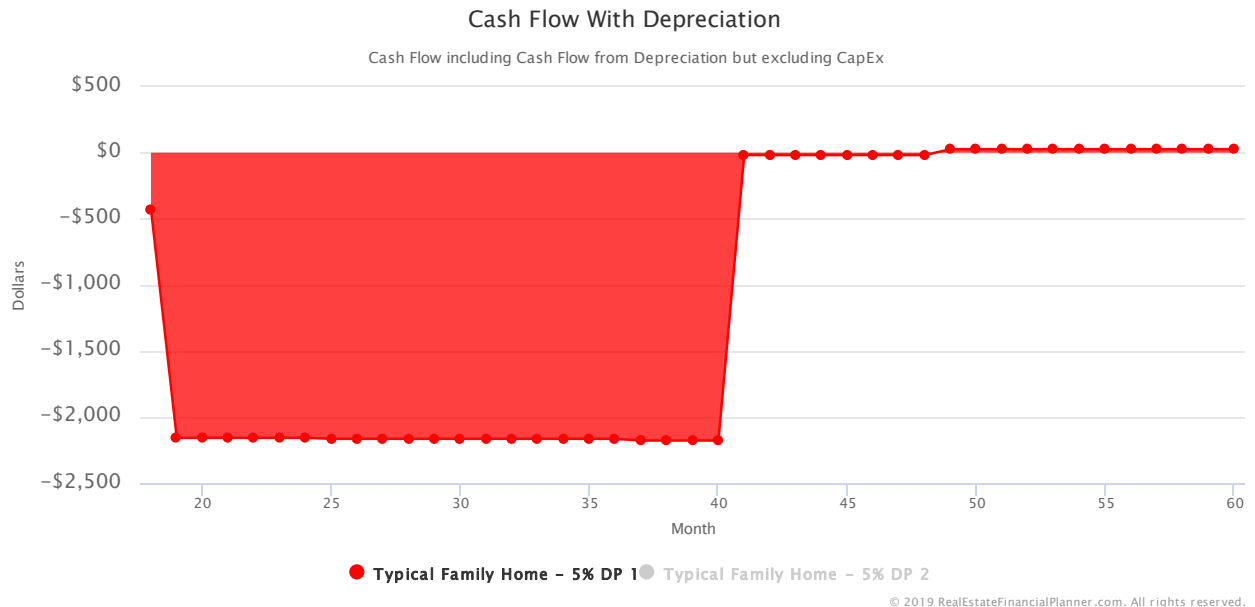


There are two new important things to note about this chart.

First, zooming out to look at the full 60 years, and only looking at your first property, you can see that cash flow significantly improves around month 378. What happened there? That is when you paid off the mortgage on the first property. Since you no longer have a mortgage payment, cash flow improves dramatically at that point. You still have the expenses of property taxes, property insurance, vacancy, and maintenance on the property but no more principal and interest mortgage payment.

Secondly, you can see when cash flow from depreciation goes away. Notice how there is a slight decline just before the big up-tick in cash flow from paying off the loan? That is from hitting the 27.5-year point of having the property as a rental, which is the length of time you can claim depreciation benefits for residential rentals.

With your permission, I would like to zoom in and look at the first five years of the chart above.



If you recall, when you were just looking at cash flow, I described the original chart as going from significantly negative when you were living in the property and had no income on it to going slightly negative until month 109. Now that you are including cash flow from depreciation, that is not true. Instead, you are at negative \$18 per month for less than a year before cash flow, including cash flow from depreciation, goes positive.

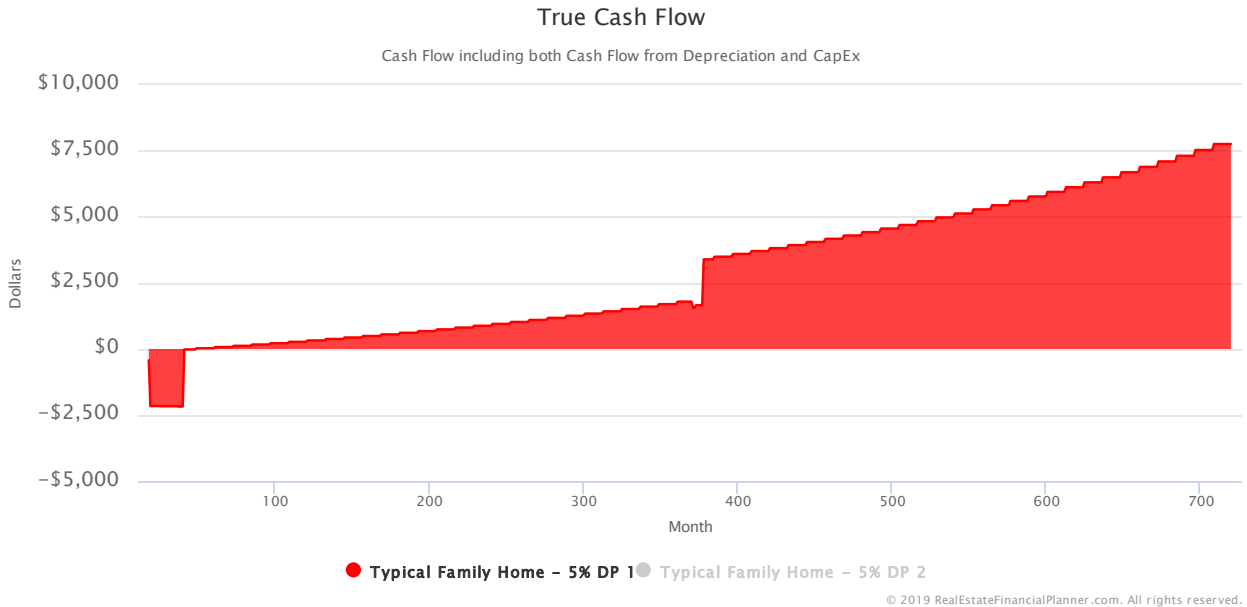
### True Cash Flow™

I got tired of saying cash flow and cash flow from depreciation, so I created a new term that describes cash flow including cash flow from depreciation and, if you are modeling capital expenses, Cap Ex. I call this True Cash Flow™.

$$\text{True Cash Flow}^{\text{TM}} = \text{Cash Flow} + \text{Cash Flow from Depreciation} - \text{Cap Ex}$$

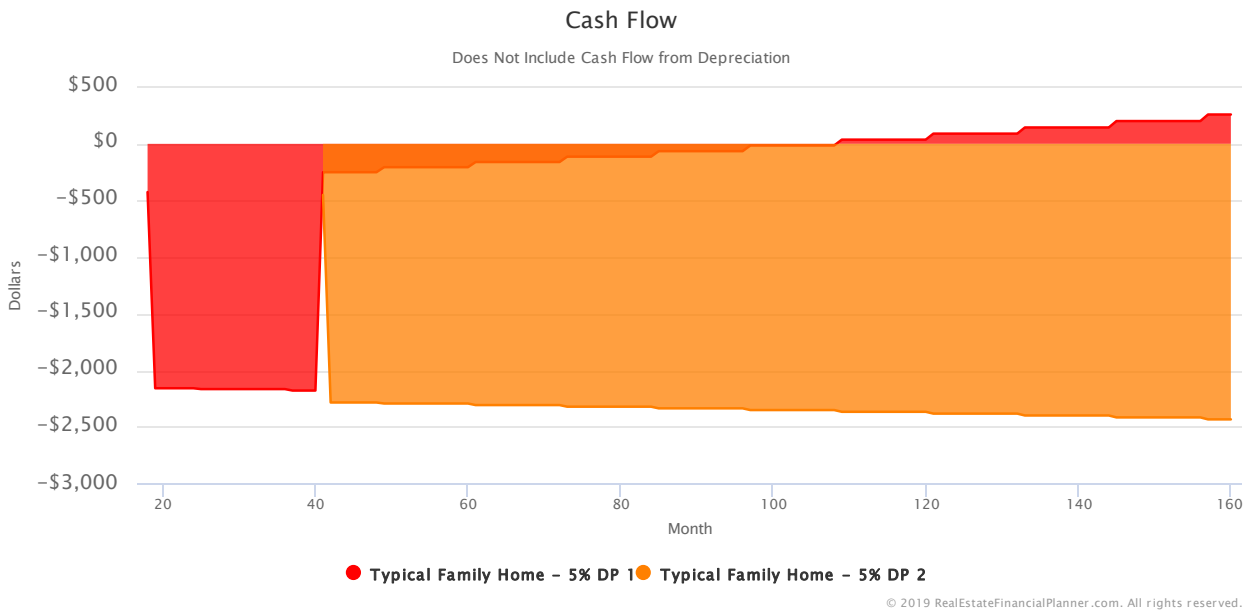
In our model, you have already included Cap Ex with maintenance on the property, so your cash flow number already takes Cap Ex into account.

The following is a chart of True Cash Flow™.



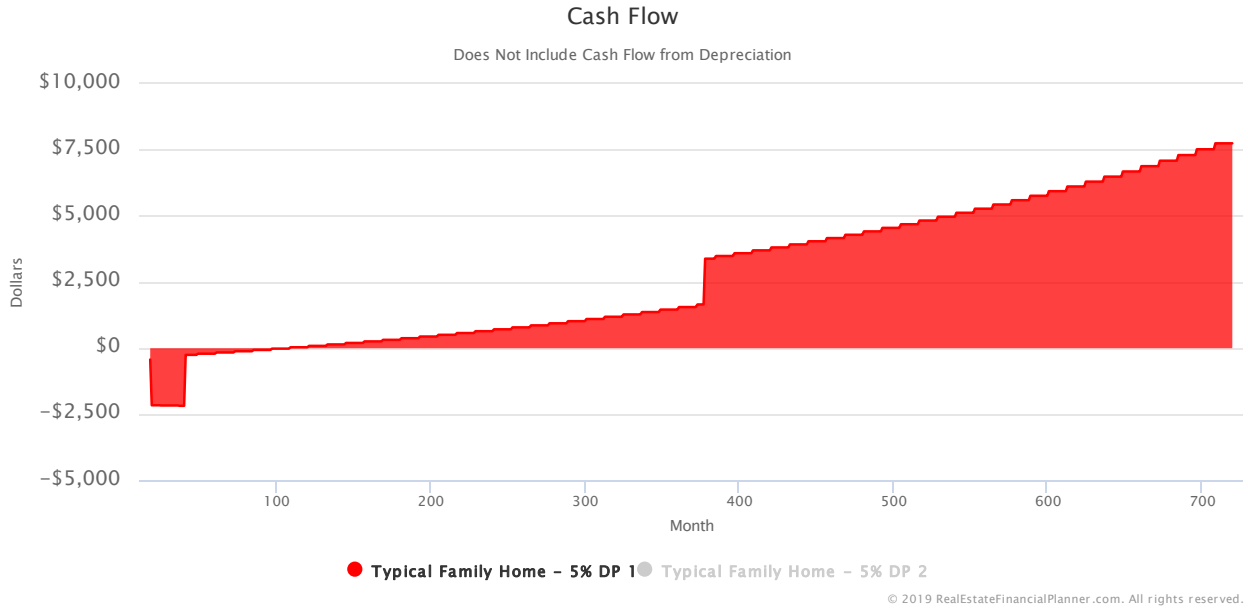
So, cash flow really isn't as bad on this property as we originally suggested in the first chart of plain vanilla cash flow.

Before I finish with cash flow for now, I do want to show you the cash flow for both the property you are renting and the significantly negative cash flow of the property you are living in on the same chart so you can see visually how they relate.

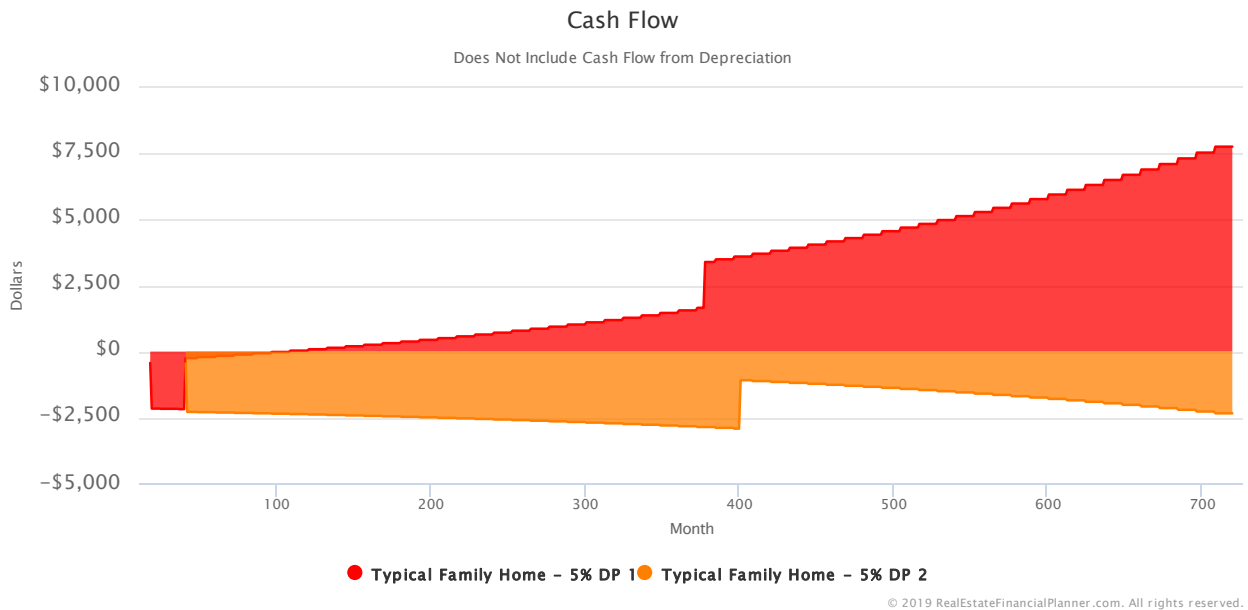


As you can see in the chart above, when you are living in the first property your cash flow is negative for all the expenses on that property. You have no rent on that. But, when you buy the second property and

begin renting the first property, that negative cash flow switches from the first property to your second property. Cash flow on the first property goes to slightly negative as we've already been discussing.

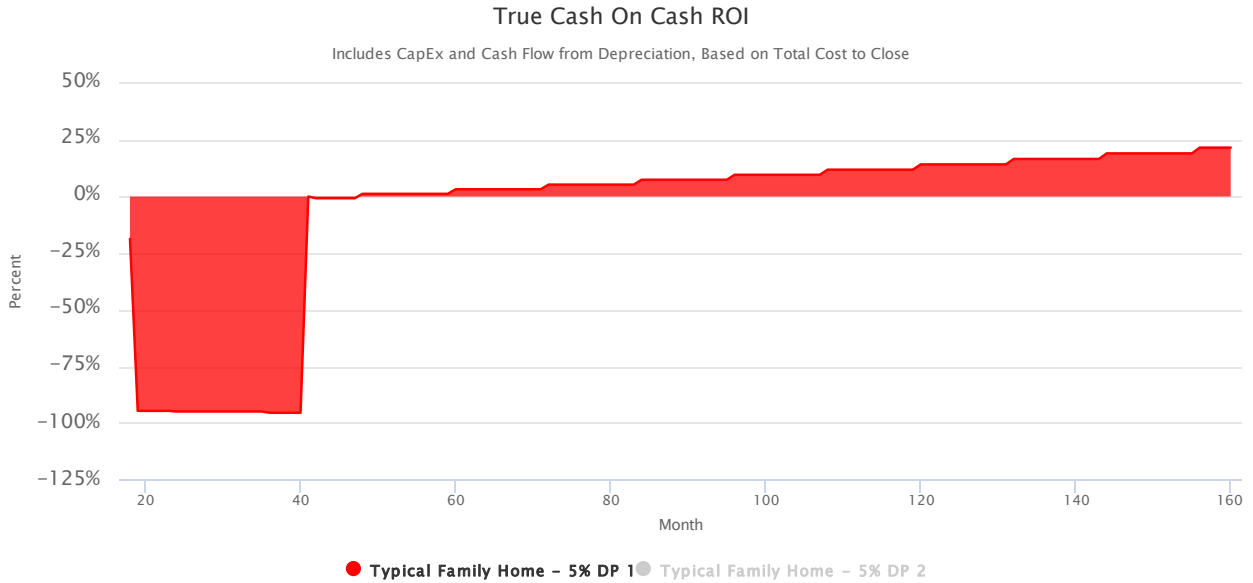


We can see a similar impact from paying off the mortgage on the second property—the one you are living in when we pay off that mortgage as well a few years later. Although the mortgage payoff shows up as less negative cash flow instead of improved positive cash flow.



### True Cash on Cash Return on Investment™

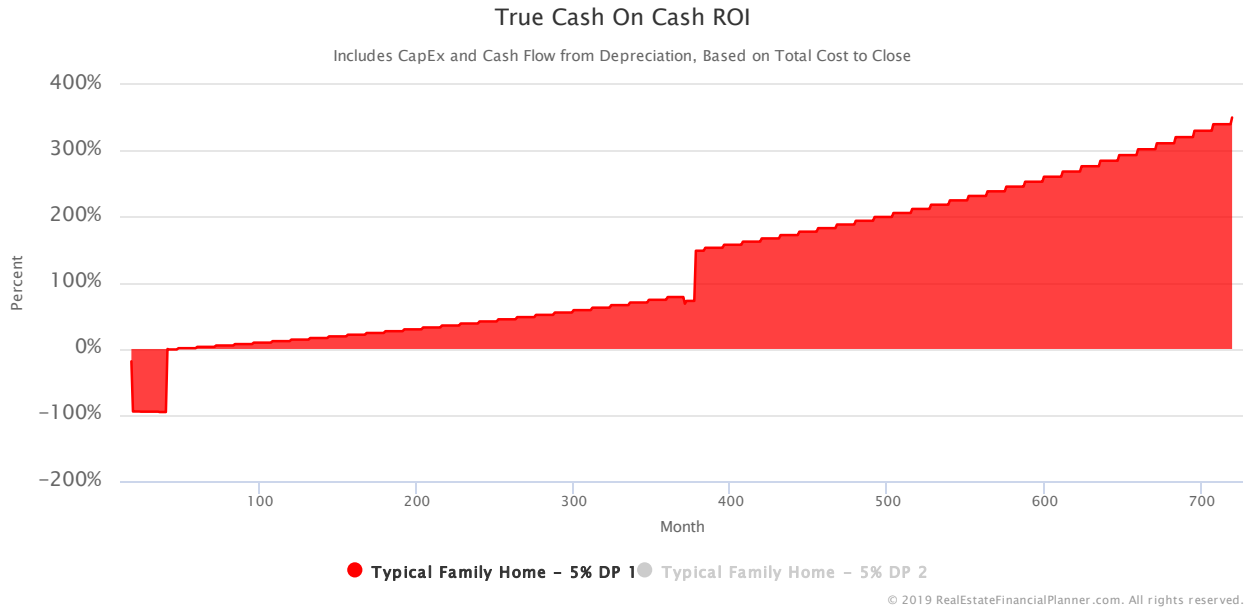
What kind of return on investment are you seeing from True Cash Flow™ on your property when you divide by the total cost to close on the property when you bought it?



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At the beginning, when you are living in the property, your *True Cash on Cash Return on Investment™* starts off very negative. You have no income coming in for the property while you live in it.

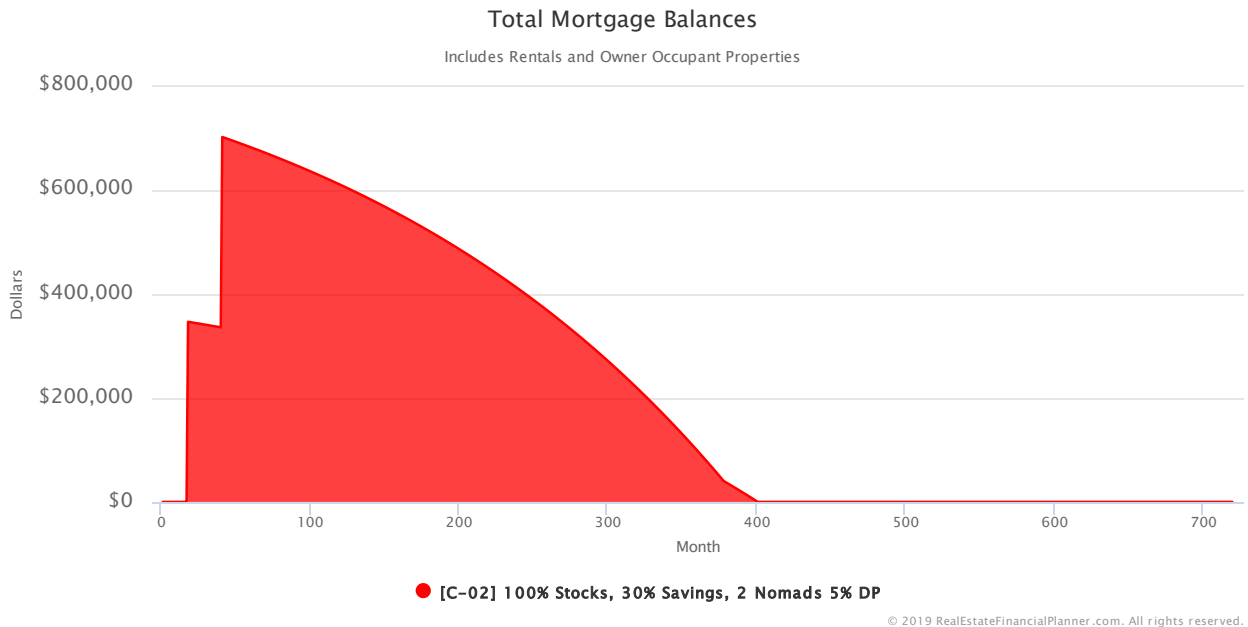
However, once you start renting it, your *True Cash on Cash Return on Investment™* increases from slightly negative, to a very significant return over time. In the chart showing the full 60-year period below, you can see the increase when you pay off your mortgage and the dip when you lose the depreciation benefit as well.



True Cash flow™, which includes both Cash Flow and the Cash Flow from Depreciation, are not the only returns. There are others like Debt Paydown as well.

## Debt Paydown

In this scenario, you have two properties. That means you have two loans that are being paid down.



The chart above shows the amount you owe on your mortgages combined. At the very beginning, you have no mortgages. Then, you add the first property and your total mortgage balance increases to about \$346,000. You live in that house for over a year and buy another property and get a new mortgage. Your total mortgage balance—between the two properties—increases to be just over \$700,000.

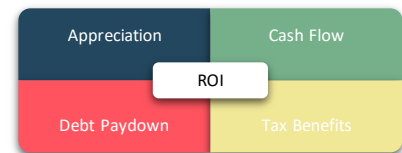
But over time, you (and indirectly your tenants) pay off the mortgages. At approximately month 400, you no longer owe any money on either mortgage. They are paid off and “free and clear” of any encumbrances (in this case... that’s a fancy word for liens from mortgages or deeds of trust depending on what is customary in your state).

Next, let’s look at the four areas of return you get from rental properties.

### Return on Investment Quadrant™

For rental properties, there are four areas of return. I call it the Return on Investment Quadrant™.

The Return on Investment Quadrant™ consists of appreciation, cash flow, debt pay down, and tax benefits. In the center of the four areas of return is the sum of each of the other four. This is labeled as ROI for Return on Investment.



### *Speculative and Uncertain*

The top half of the quadrant is made up of appreciation and cash flow. These are the two speculative areas of return for the quadrant. They rely on the market performing in order for you to get your return.

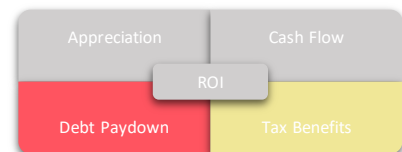
If the market does not go up in value, you don’t get appreciation. In fact, if property values go down in a year, your return from appreciation can be negative for that year.

If you had break-even cash flow and rents did not increase that year, you did not get any return from cash flow. If you have positive cash flow, you will have a positive return from cash flow. If you have negative cash flow for a given year, you can have a negative return from cash flow for that year.

Over time, the amount of return you get from appreciation and cash flow tends to increase.

### *More Fixed and More Certain*

The bottom half of the quadrant is more fixed and more certain than the speculative top half. They rely on your agreement with your lender not changing for debt paydown (your note with the lender) and the US tax code to remain the same for the tax benefits. These are much more likely to remain constant and are, therefore, less speculative in nature.



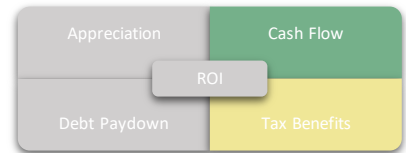


Over time, with the very common 30-year amortizing loan, the amount you pay down in debt each year tends to increase.

Your tax benefits should remain fixed for the depreciation period and then go away once you have depreciated the entire property. For residential properties, depreciation will last for 27.5 years under the current tax code.

### Cash Now

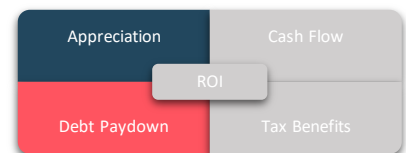
The right side of the quadrant is the “cash now” side as it consists of the two areas of return you are likely to see immediately in the form of cash flow and cash flow from depreciation.



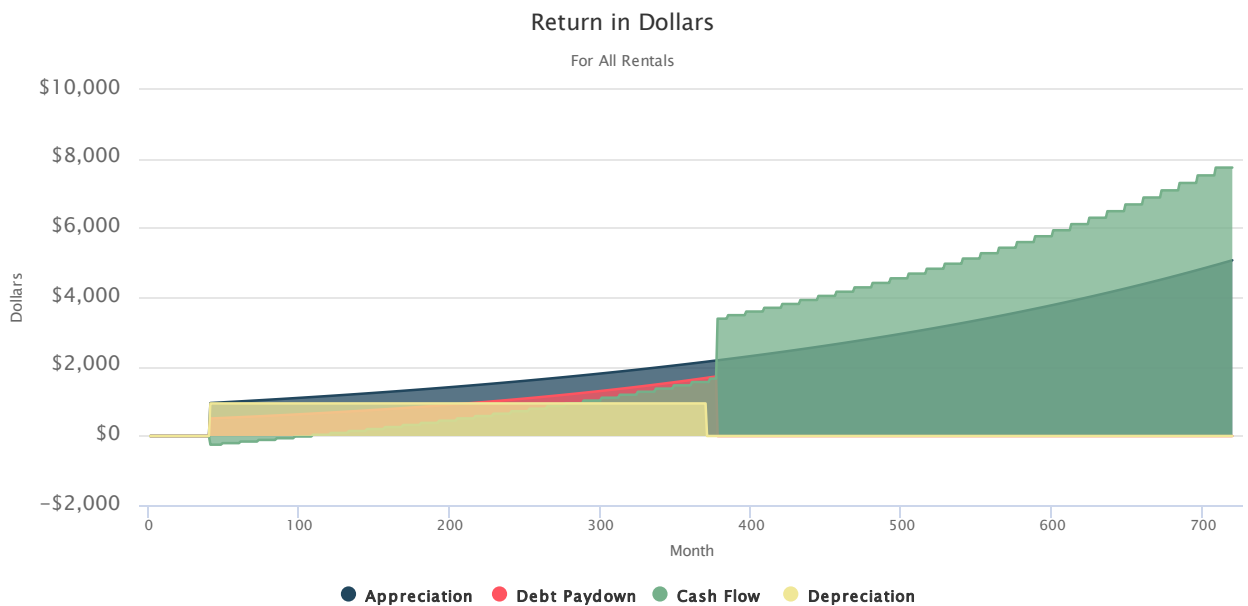
Cash flow and cash flow from depreciation combined is what we call *True Cash Flow™*.

### Cash Later

The left side of the quadrant is the “cash later” side as it consists of the two areas of return you are likely to realize later. Equity from your property going up in value and your loan being paid down over a long period of time.



Want to see how this rental property for this scenario stacks up with each of the four areas of return? Here’s a chart showing each of the four areas of return broken out over the full 720 months.



A couple of things I want to share with you about this.

First, this is all in pre-tax dollars. At first blush that seems like a trivial thing for me to say, but it is not.

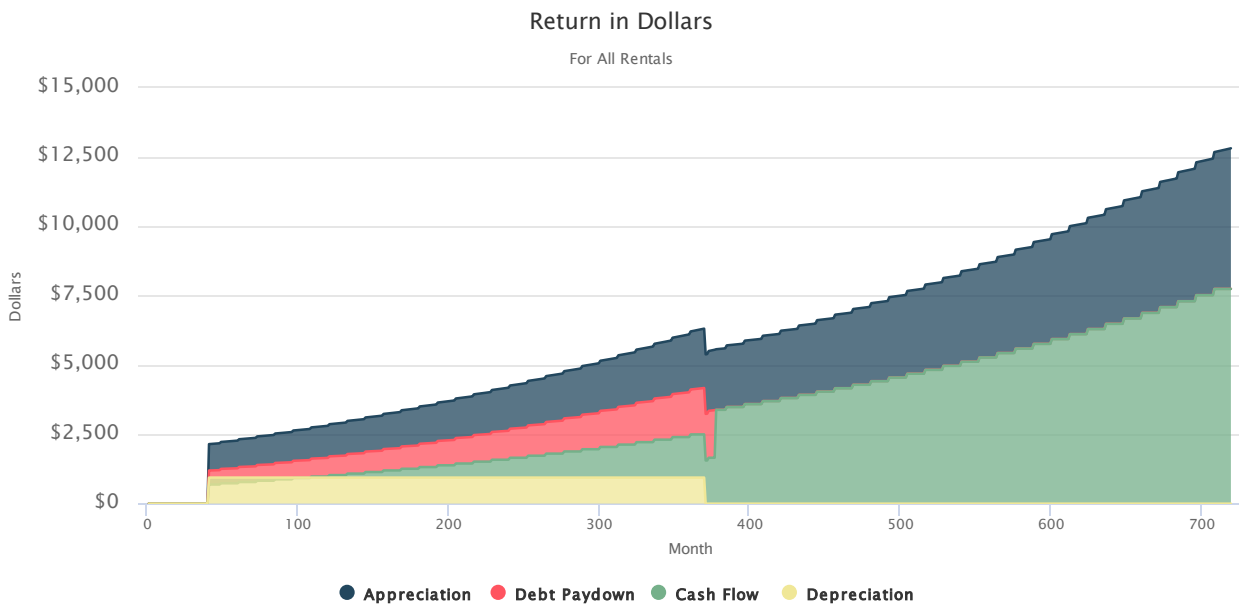
Appreciation is the raw dollars the property went up in value that month based on your assumed appreciation rate. It is easy to see how that is pre-tax. You are not paying taxes on appreciation until you sell the property, unless you consider the increased property taxes you are paying as a tax on a higher property value. But even then, the number shown is still pre-tax.

Debt Pay Down is pre-tax. You are paying down the loan and not being taxed on that. You are paying your normal income tax on the rent you received that is then applied to pay down the loan, but that's not shown here.

Cash Flow is pre-tax. Cash Flow is the profit you have after all your expenses on the property. The number shown is before you pay taxes, hence pre-tax.

Here's the twist though. Depreciation is the gross depreciation benefit you get from depreciating the cost of the building (not the land) on the property. It is the amount you can reduce your income by before you pay taxes. Out of an abundance of clarity, it is not your cash flow from depreciation (which would be post-tax, not pre-tax). This is the one that confuses folks that see this chart. They believe because I am showing the gross depreciation that they are seeing that dollar amount somehow; they are not. This is the gross, pre-tax depreciation benefit or the amount of money you can reduce your income by before paying taxes. Another chart I could show you would be for me to mix pre-tax and post-tax returns and show you appreciation, debt pay down and cash flow pre-tax but depreciation post-tax. I have opted not to mix those here... yet.

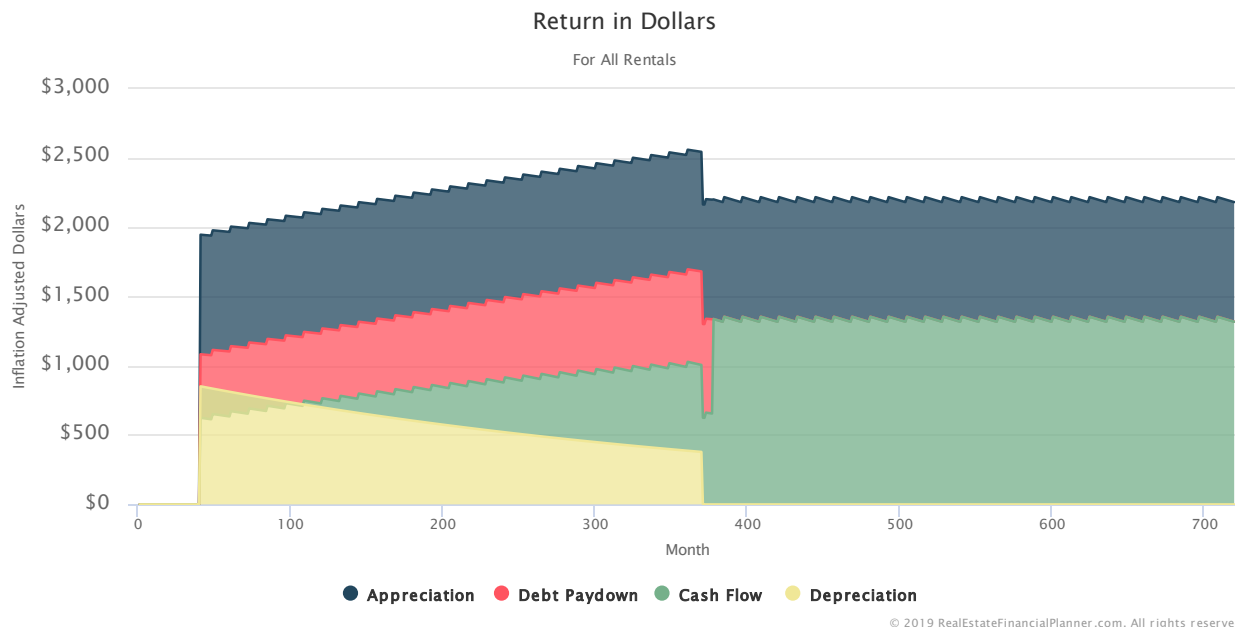
If you want to see the overall return on investment or the sum of each of these returns for any given month, we can take this same chart and stack the four returns. That chart looks like this.



This chart shows the sum of all the benefits you are getting from owning this rental property.

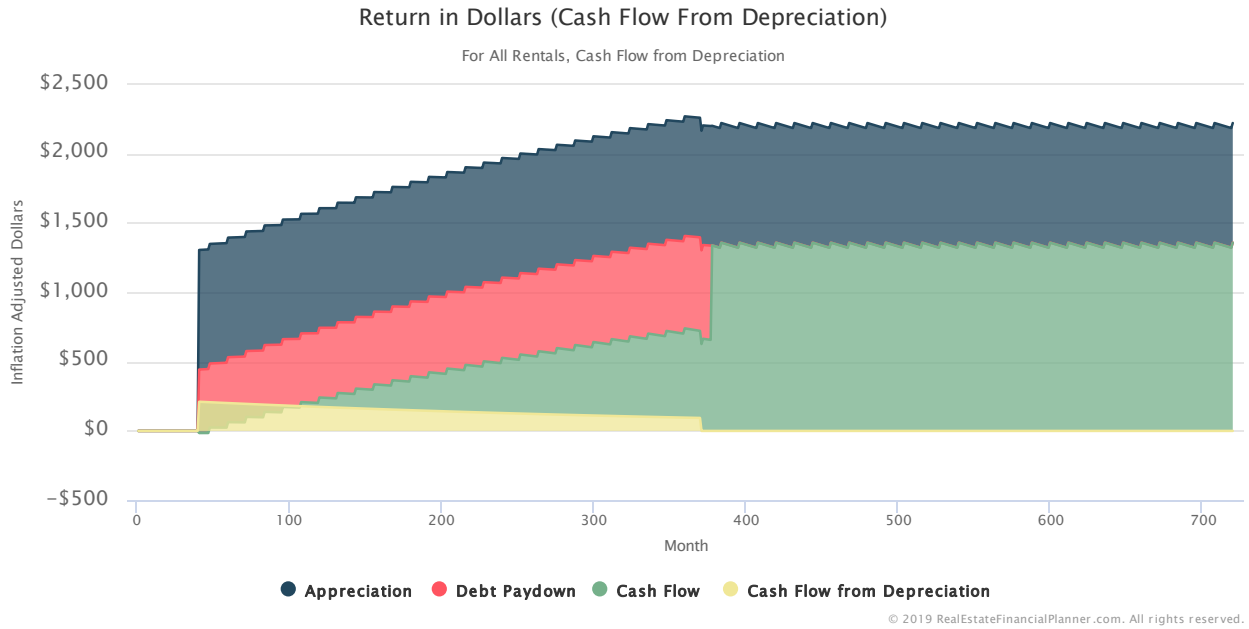
You will notice that the depreciation benefit only lasts for 27.5 years and that the debt pay down only lasts until we pay off the loan in month 360 of having the loan. Appreciation and cash flow continue until the end of the chart. Remember the cash now and cash later sides of the *Return on Investment Quadrant™*?

What if we want to see how these returns look adjusting back to today's dollars for inflation? That would be this stacked chart.



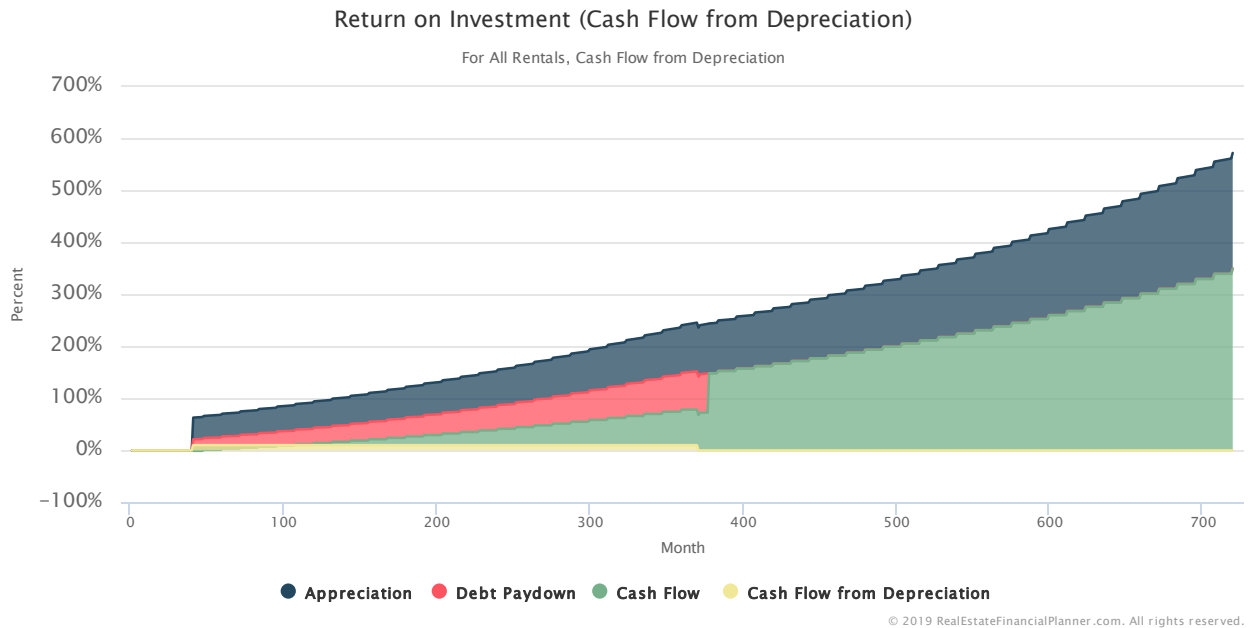
As you can see in this inflation-adjusted chart of your total returns you are realizing about \$2,000 per month, every month, for owning this one rental property. That's like saving \$2,000 per month on an initial investment of about \$27,000.

I mentioned before that this is the pre-tax version of this chart. And, it is a little bit deceptive to think about the gross depreciation benefit in pre-tax terms. Instead, here's the same chart except, in this one I am taking the gross depreciation benefit and multiplying that by your effective income tax rate to convert gross depreciation to cash flow from depreciation. That's the post-tax version of the depreciation benefit. The other three returns of appreciation, debt paydown, and cash flow remain pre-tax benefits.



It still looks like you are getting a good return for an initial investment of about \$27,000.

In previous chapters we talked about the return you were getting in the stock market in terms of a percentage. It was 8.97% per year. What if we wanted to look at the overall return you are receiving on this rental property as a percentage of the return on your initial investment? That would be the following chart.

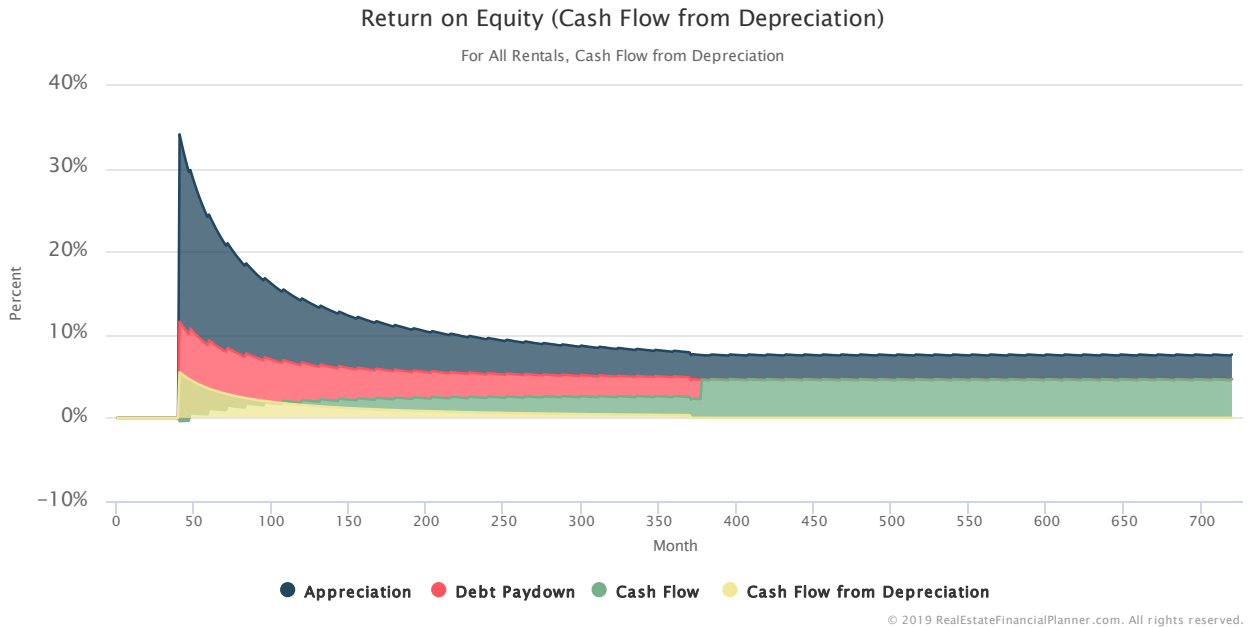


This chart shows that the return you are getting on the initial amount of money you invested is increasing over time. In the beginning—even with negative cash flow—your overall return on owning this rental property with the assumptions I explained earlier are over 60% per year.

However, this is not exactly an apples-to-apples comparison to stocks for the entire chart. The stock market rate of return is a return on the total amount you have invested in the stock market and not the return on just the initial amount you invested in the stock market. To do a fairer comparison, we should look at the return you are getting on the equity you have in property. We can calculate the return on equity (ROE) if we take the return you earned that month (but annualized to make it a yearly return) divided by the equity you have in your property that month.

$$\text{ROE} = (\text{Cash Flow} + \text{Appreciation} + \text{Debt Pay Down} + \text{Tax Benefits}) \div \text{Equity}$$

This is a better comparison because if you sold the property, you’d have that equity (minus any transaction costs of the sale) to invest in the stock market or elsewhere. Seeing the return you get divided by the equity therefore becomes a better, more fair, comparison to the stock market return we’ve been using. The following is the chart showing ROE over time.



In the chart above, when your equity is at its lowest, the return divided by the equity is highest. The return is well over 30% per year.

However, as the property value increases and you pay off the mortgage, your equity increases while your return does not change nearly as quickly. This means that your return on equity drops quickly.

The return on equity though remains higher than the 8.97% return that we’ve assumed you are getting in the stock market until approximately 23 years into the scenario or about 20 years of owning the property. At that point the return on equity for the property drops below the return we are assuming for the stock market.

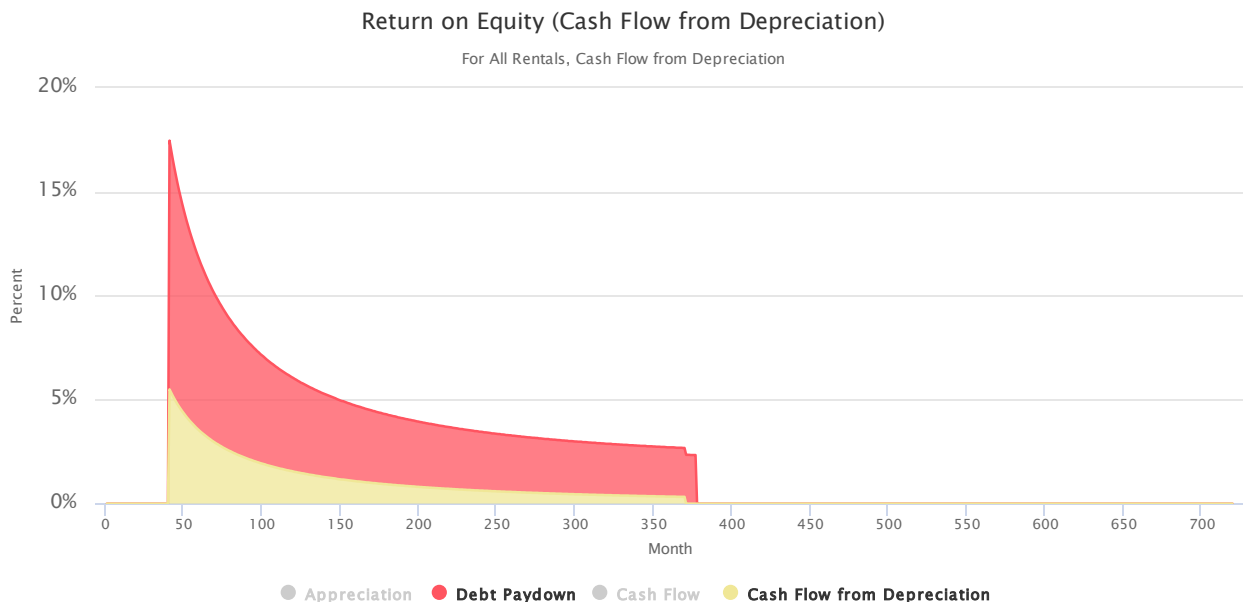
I touched on this briefly with the *Return on Investment Quadrant™* and when explaining the stock market rate of return, but I will say it again here: the return from the stock market is volatile. You saw the range of returns you can get in any year. It varies a lot.

Parts of the return you get on real estate can vary widely as well. Appreciation can be all over the place. Property values can go up or down. It's probably not nearly as variable as the stock market, but you can still have up years and down years.

Cash flow can also be variable. You might have a big expense on the property and have significant negative cash flow for a year. Or, you might get a handy tenant that moves in and just takes care of all the maintenance on your property for 10 years. It is still variable.

However, two returns on your real estate are not variable with the market at all. These are cash flow from depreciation and debt paydown. They smooth out the ride and act as a buoy of sorts to hold up the overall return. You can count of them being there, regardless of what the market is doing. I am tempted to say these two returns are guaranteed, but they are not really guaranteed by a third-party. They are as close to being guaranteed as you can get without them being guaranteed. If you make your mortgage payment and the tax code stays the same, you get those returns.

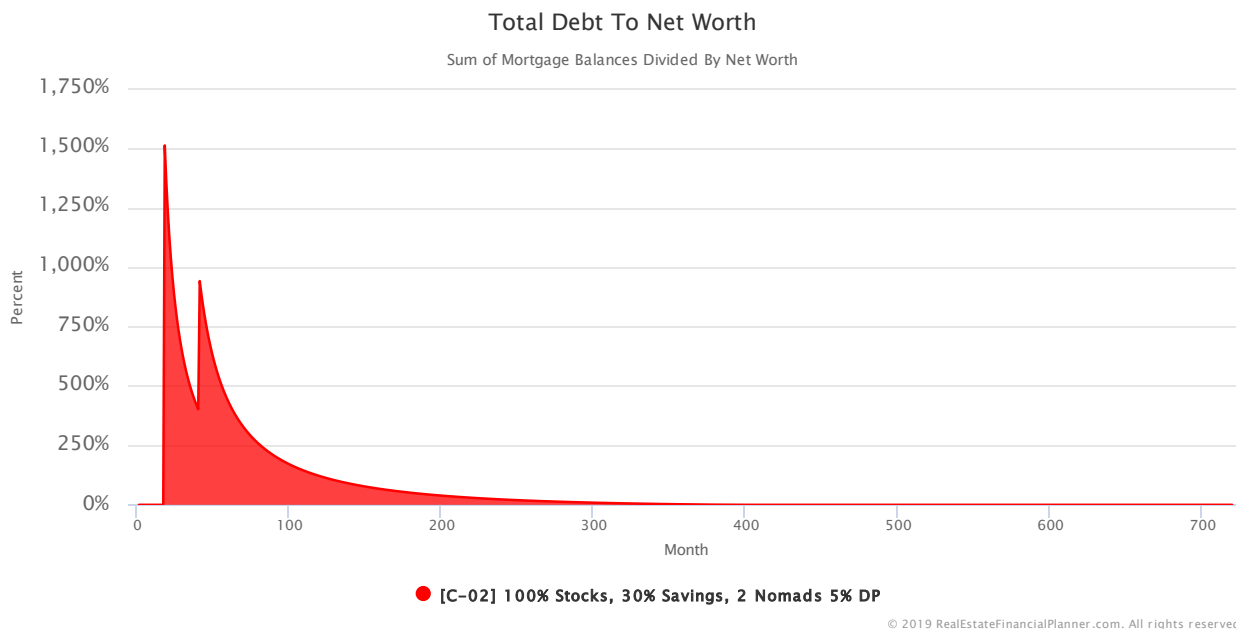
Here's the return on equity for just the two market independent returns of debt paydown and cash flow from depreciation.



These two returns that you can count on, make up over half of your overall return—about 15% return on your equity—early on. Over time, they decline and eventually go away.

If it has not occurred to you yet, it will at some point: if the return on equity goes down over time, why don't we sell the property or refinance the property to constantly boost returns? You could do this. A couple of considerations though.

First, it will keep your debt to net worth ratio higher and remember, this is one way we are measuring risk. Free and clear properties with no mortgage debt on them have much safer, lower debt to net worth profiles from a risk perspective. One of the things I like about our Nomad™ plan is that it has you becoming more conservative over time as you pay off properties the closer you get to financial independence. Here is a chart showing you the debt to net worth chart for this scenario.



Another consideration if you are going to sell or refinance properties are the costs. How much of your equity will you lose in transaction costs if you sell? How much might you lose to refinance costs? It may still make sense to do this in certain situations, but it is something to consider and beyond the scope of this book.

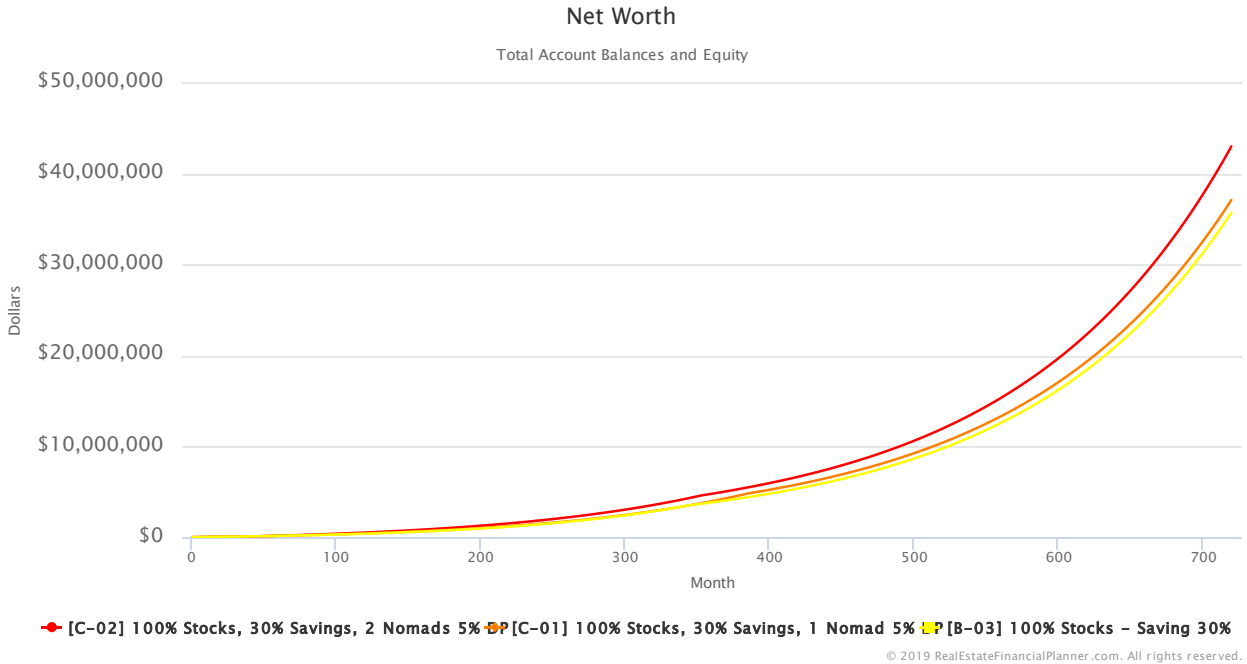
Another consideration in favor of selling is trading into new or newer properties with less maintenance. Over time, maintenance on properties can creep up. Roofs, furnaces, and AC units need to be replaced, kitchens and bathrooms updated, and sewer lines replaced among other things. What if instead, you always bought new or newer properties that are early on in their maintenance lifecycles and sold before you needed to pay for expensive capital improvements? I have clients who buy a new construction property, with the plan of selling the property in 10 years, then using the proceeds to buy two more new construction properties. This keeps the capital expenses low and the return on equity high.

You could use a similar model and set criteria to sell properties once the return on equity dropped below a certain threshold... maybe 15%, 12%, 10%... It is a personal choice.

## Net Worth

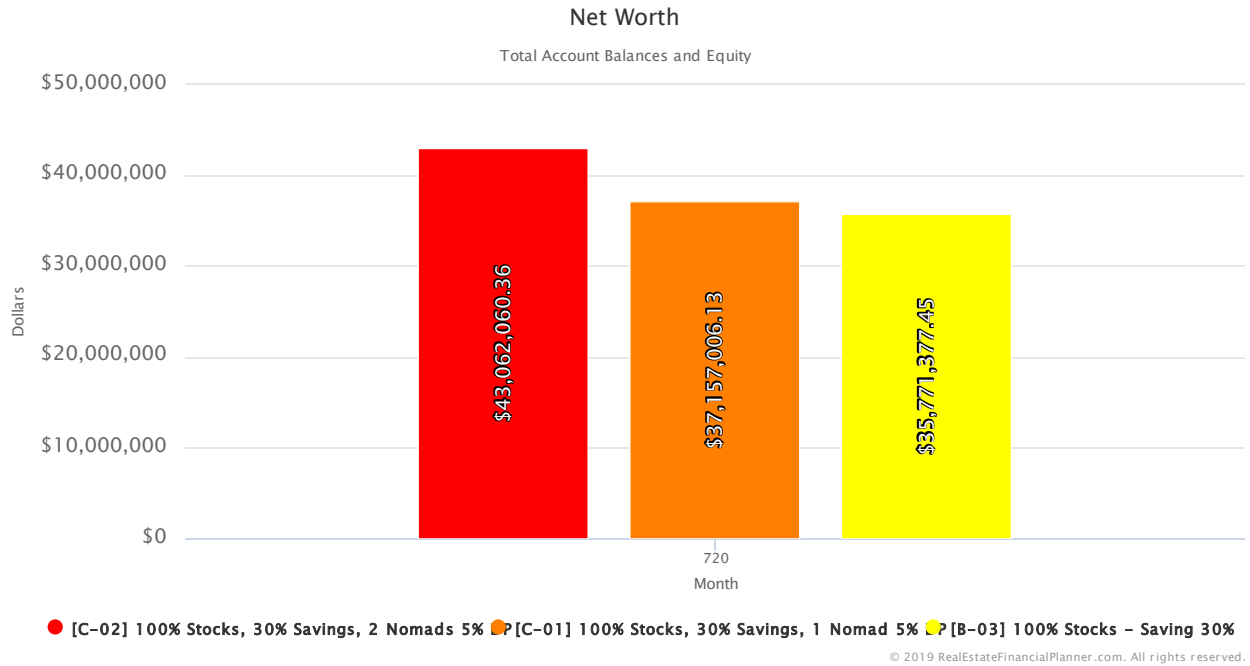
How does your net worth with this scenario compare to your net worth if we just bought one property like we did in the previous scenario we looked at? How does it compare to just investing in stocks and not buying any properties?

Here's a chart showing the net worth comparison of all three.

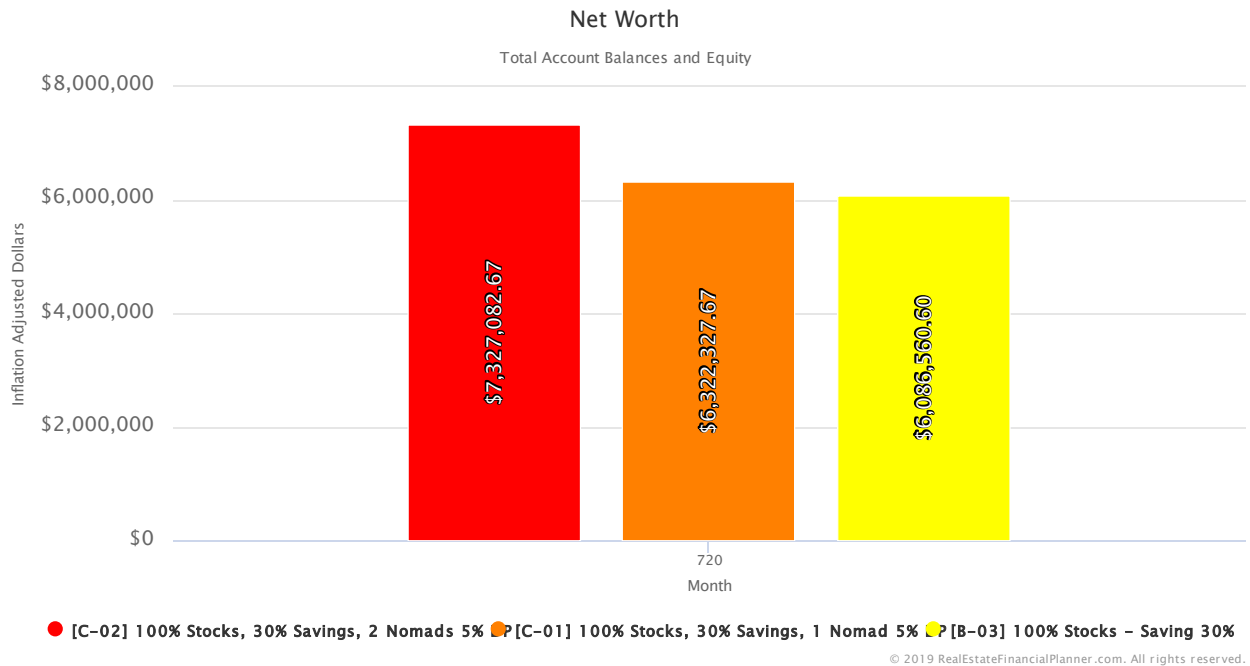


And here's the summary for month 720 when you are 82 years old.



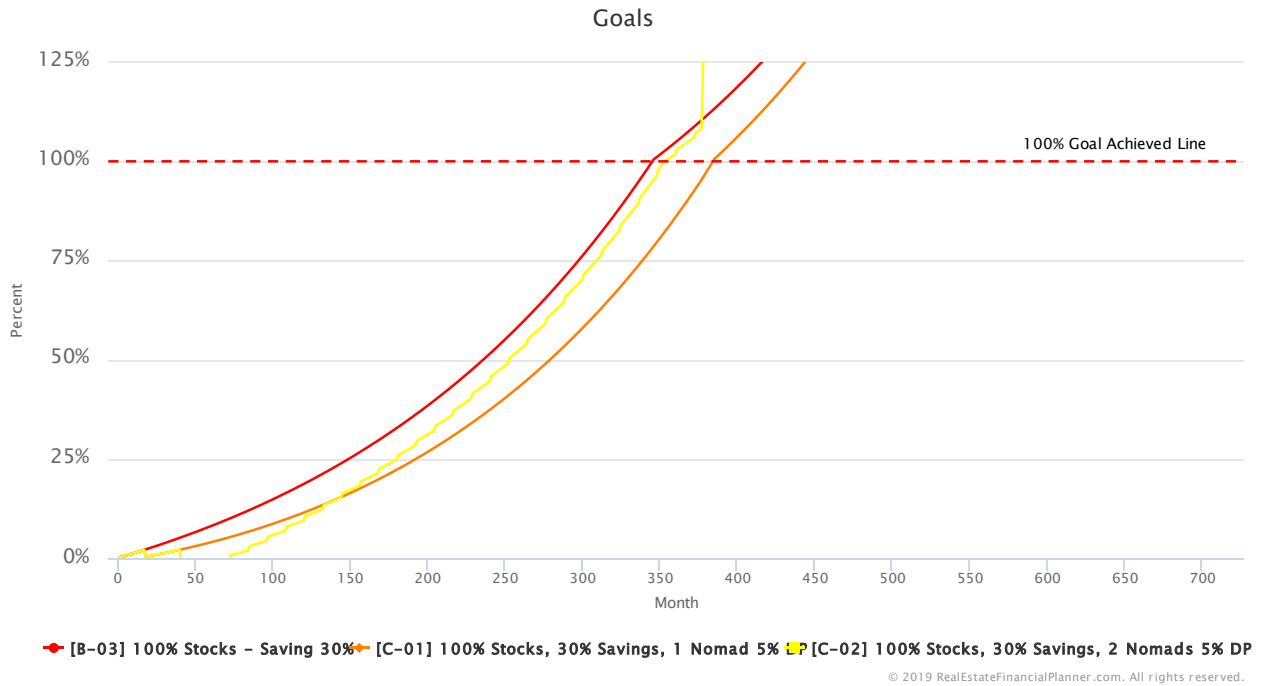


It shows that buying the two properties results in a higher net worth. Almost \$7 million more than stocks alone. Again, this is inflated dollars. What are we talking about in today's dollars?

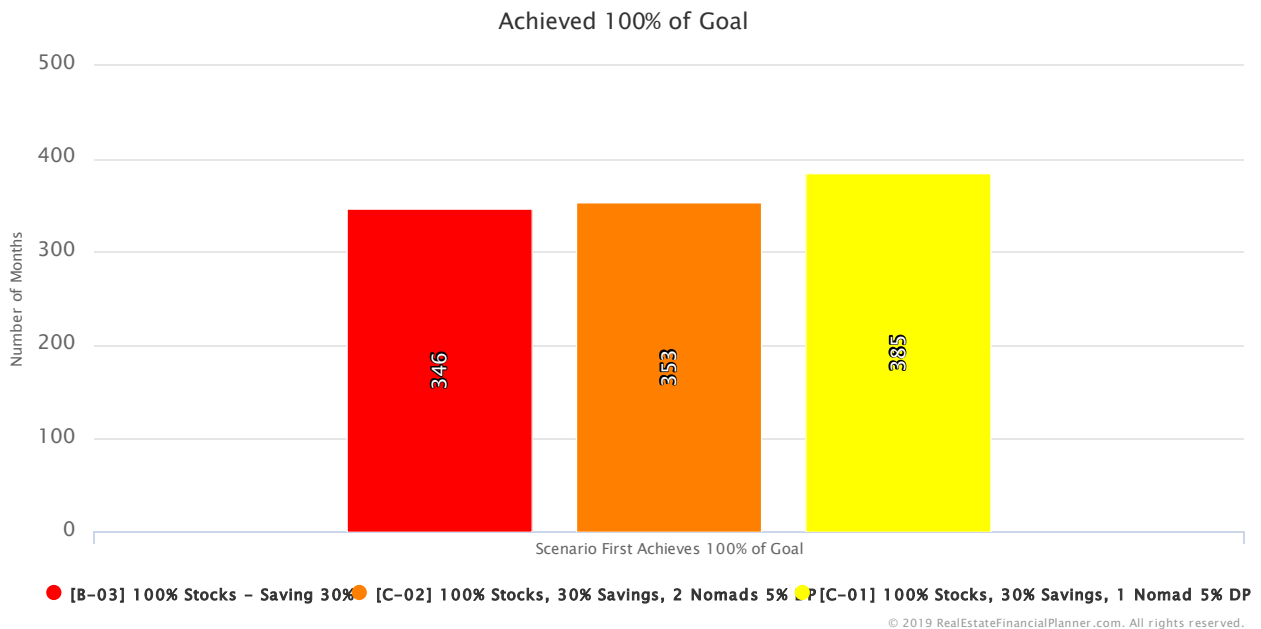


It looks like you are about \$1.3 million dollars better off to Nomad™ twice, than to just invest in stocks, and about a million dollars better off to Nomad™ twice, than to just buy a single home to live in. That is interesting.

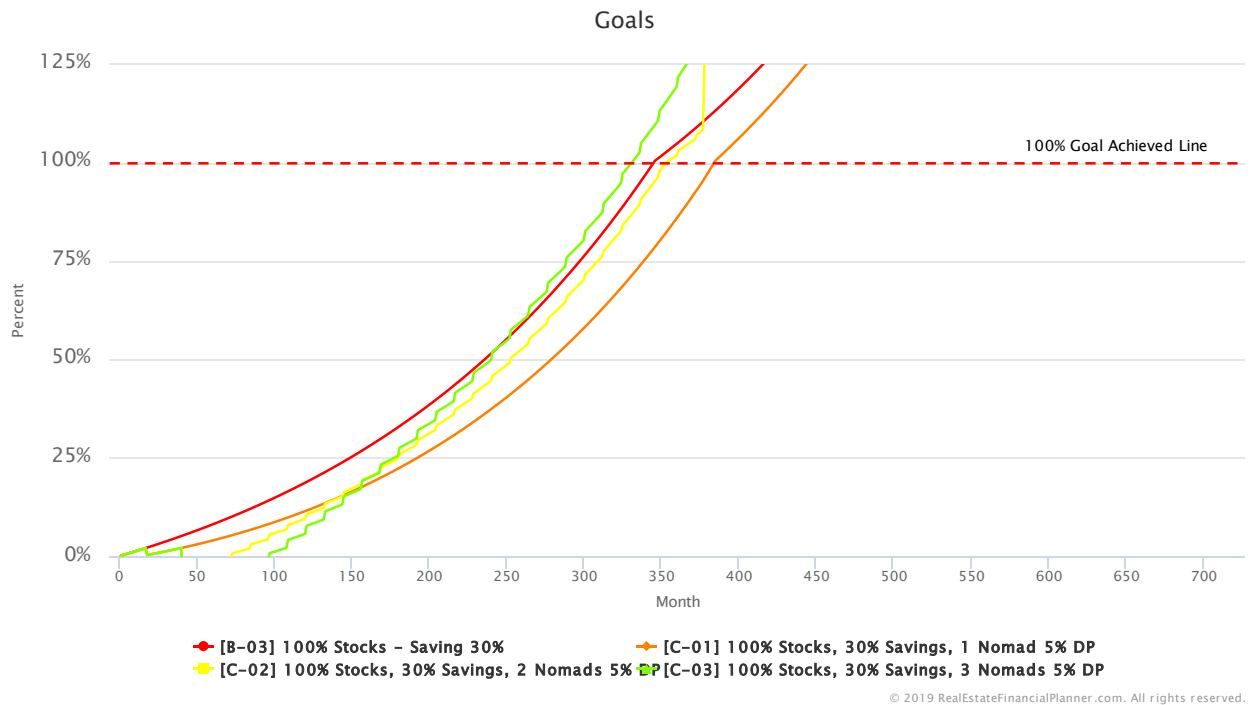
But how does it impact your ability to achieve FILYP? Raw net worth is not the same as having enough cash flow from your safe withdrawal rate on your stock market account, and any cash flow on rentals (which we now have), to cover your target monthly income to achieve FI.



It turns out that investing in stocks is still the fastest way to get to FILYP. Although, adding a single rental property by doing Nomad™ twice gains you about 32 months over just Nomading™ once.

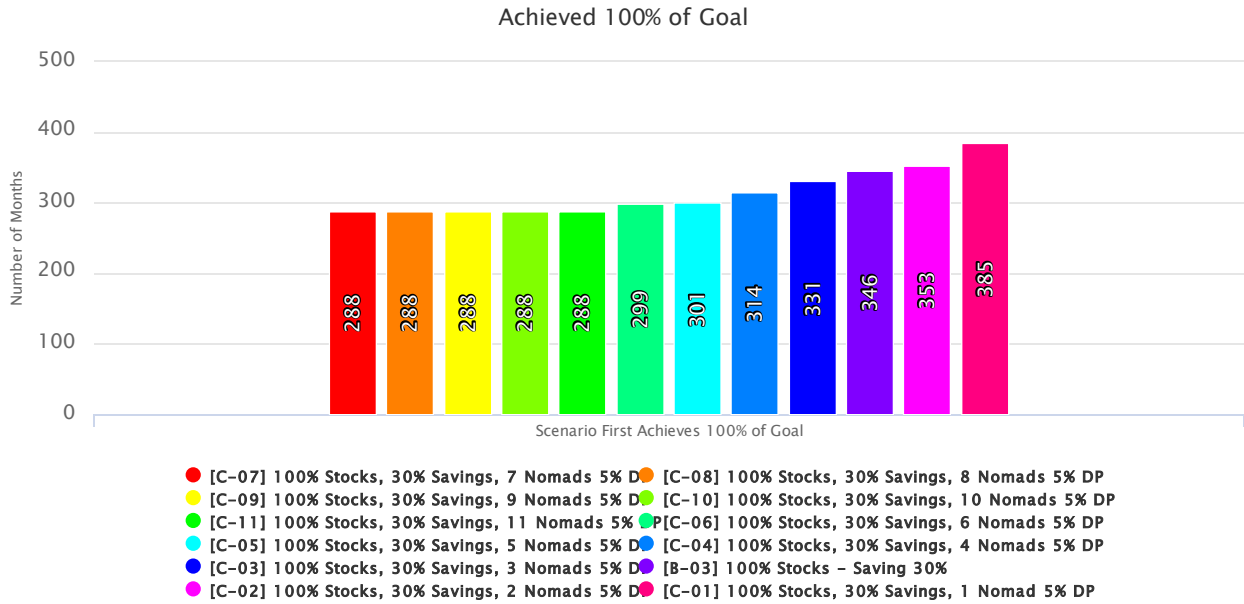


Let's look at doing Nomad™ additional times. What if you Nomad™ three times total and end up converting the first two properties you buy into rentals and live in the third? What happens to your ability to achieve FILYP then?



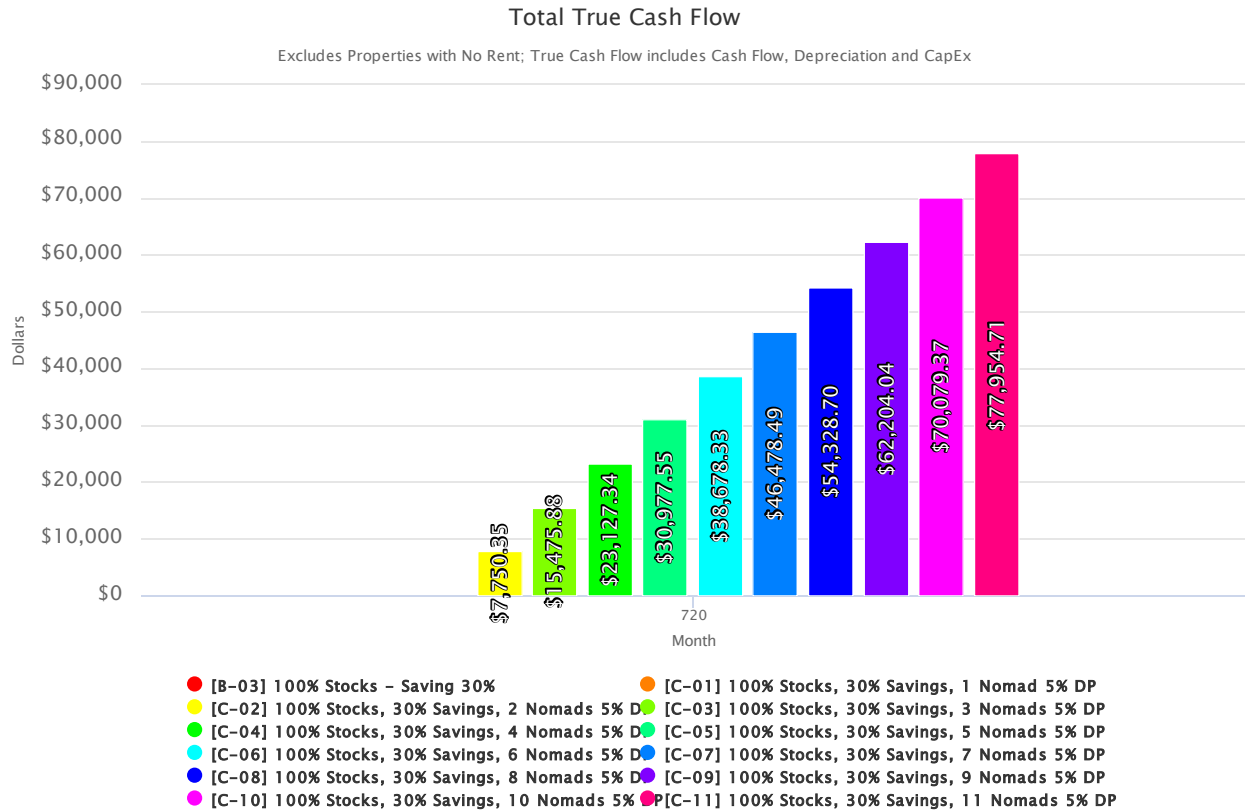
That's different. Turns out that beats out just investing in the stock market for speed to FILYP. You achieve FI in 27 years and seven months, when you are just under 50 years old.

Does adding more speed it up even more? The following chart shows you how many months it takes for Nomad™ variations from not buying any properties (renting yourself), to buying just a home for you to live in, and all the way through buying 11 properties as a Nomad™ with one to live in and 10 as rentals.



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So, it appears as though you can achieve FILYP faster up until your 7<sup>th</sup> Nomad™. Whether you do 7, 8, 9, 10, or 11 Nomads™ makes no difference in speed to achieve FI. However, it will impact your lifestyle later as the cash flow from 10 rentals is significantly better than the cash flow on 6 rentals. The following is a chart of True Cash Flow™ for each of these scenarios in month 720.

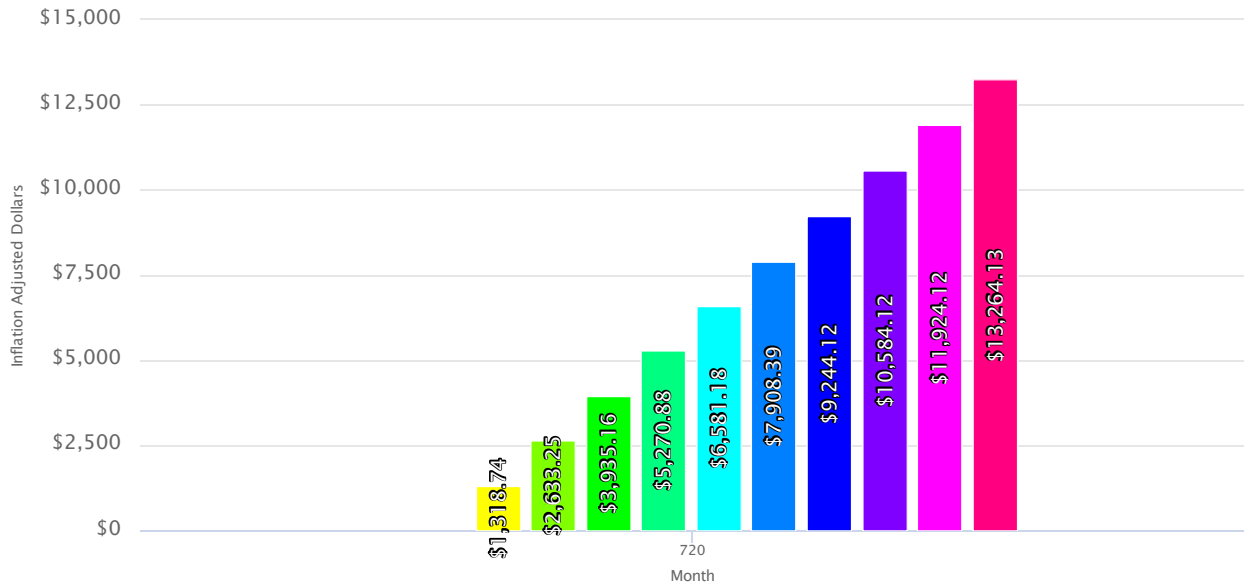


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If we adjust for inflation, it is like living on this amount per month in today’s dollars.

### Total True Cash Flow

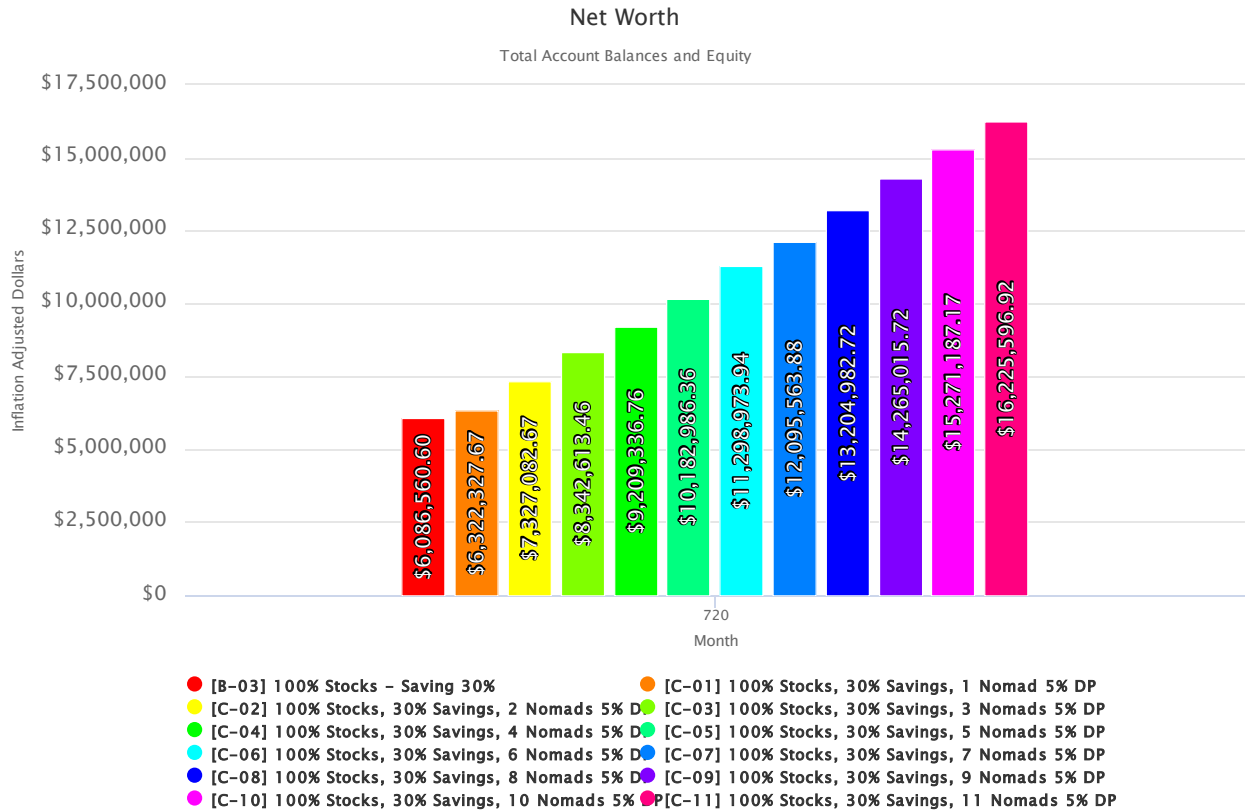
Excludes Properties with No Rent; True Cash Flow includes Cash Flow, Depreciation and CapEx



- [B-03] 100% Stocks - Saving 30%
- [C-01] 100% Stocks, 30% Savings, 1 Nomad 5% DP
- [C-02] 100% Stocks, 30% Savings, 2 Nomads 5% DP
- [C-03] 100% Stocks, 30% Savings, 3 Nomads 5% DP
- [C-04] 100% Stocks, 30% Savings, 4 Nomads 5% DP
- [C-05] 100% Stocks, 30% Savings, 5 Nomads 5% DP
- [C-06] 100% Stocks, 30% Savings, 6 Nomads 5% DP
- [C-07] 100% Stocks, 30% Savings, 7 Nomads 5% DP
- [C-08] 100% Stocks, 30% Savings, 8 Nomads 5% DP
- [C-09] 100% Stocks, 30% Savings, 9 Nomads 5% DP
- [C-10] 100% Stocks, 30% Savings, 10 Nomads 5% DP
- [C-11] 100% Stocks, 30% Savings, 11 Nomads 5% DP

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Realize this is not including the money you have in your stock market accounts or equity in your properties either. If you look at your total net worth for each, you can see the difference that buying extra properties makes in today's inflation adjusted dollars.



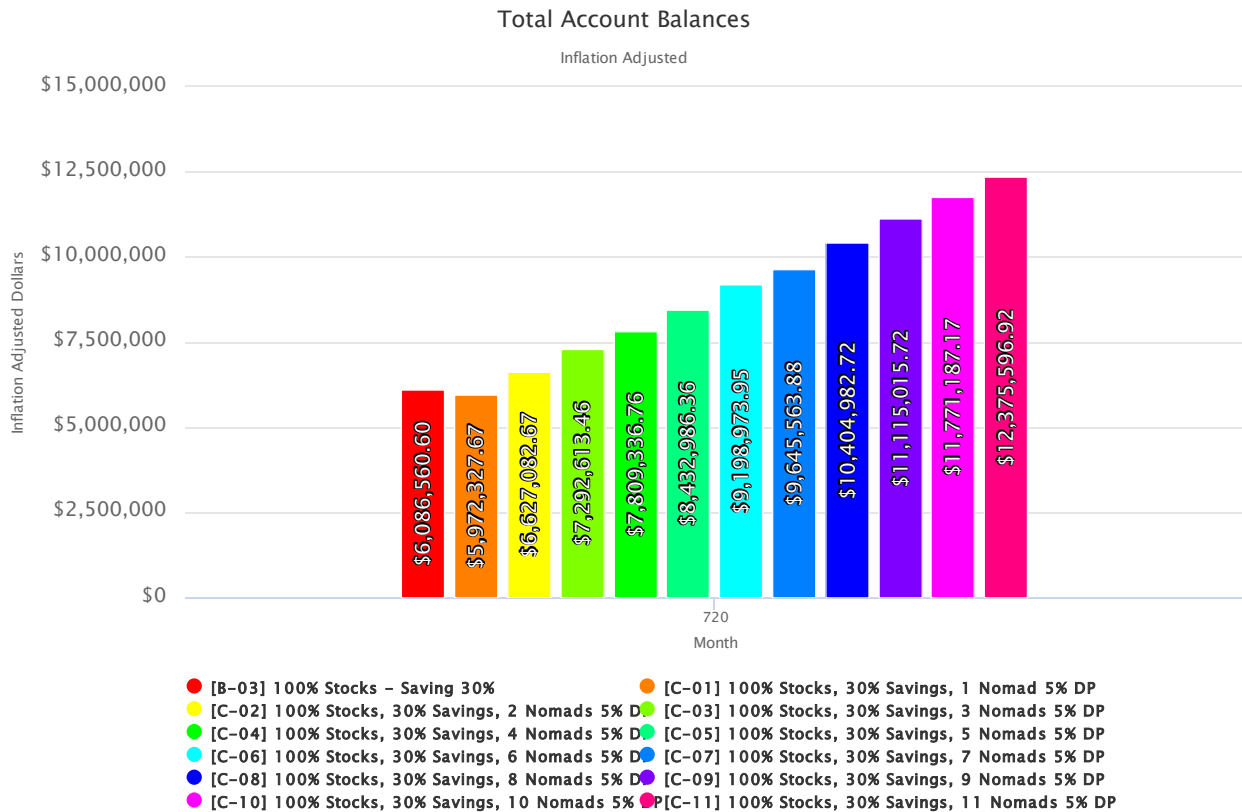
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Some of that net worth is equity in properties. How much of it is in your stock market account balance in today’s inflation adjusted dollars?

This stock market balance also contributes to your standard of living since you can withdraw your safe withdrawal rate from those accounts each year as well. In general, it seems the more properties you have, the more money you have “in the bank.”

We will look at ways we might use this in later scenarios when we take some of that money and pay down mortgages on properties to improve cash flow faster.

For now, here’s the chart showing stock market account balances for a variety of scenarios we’ve covered so far.



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Two points about this.

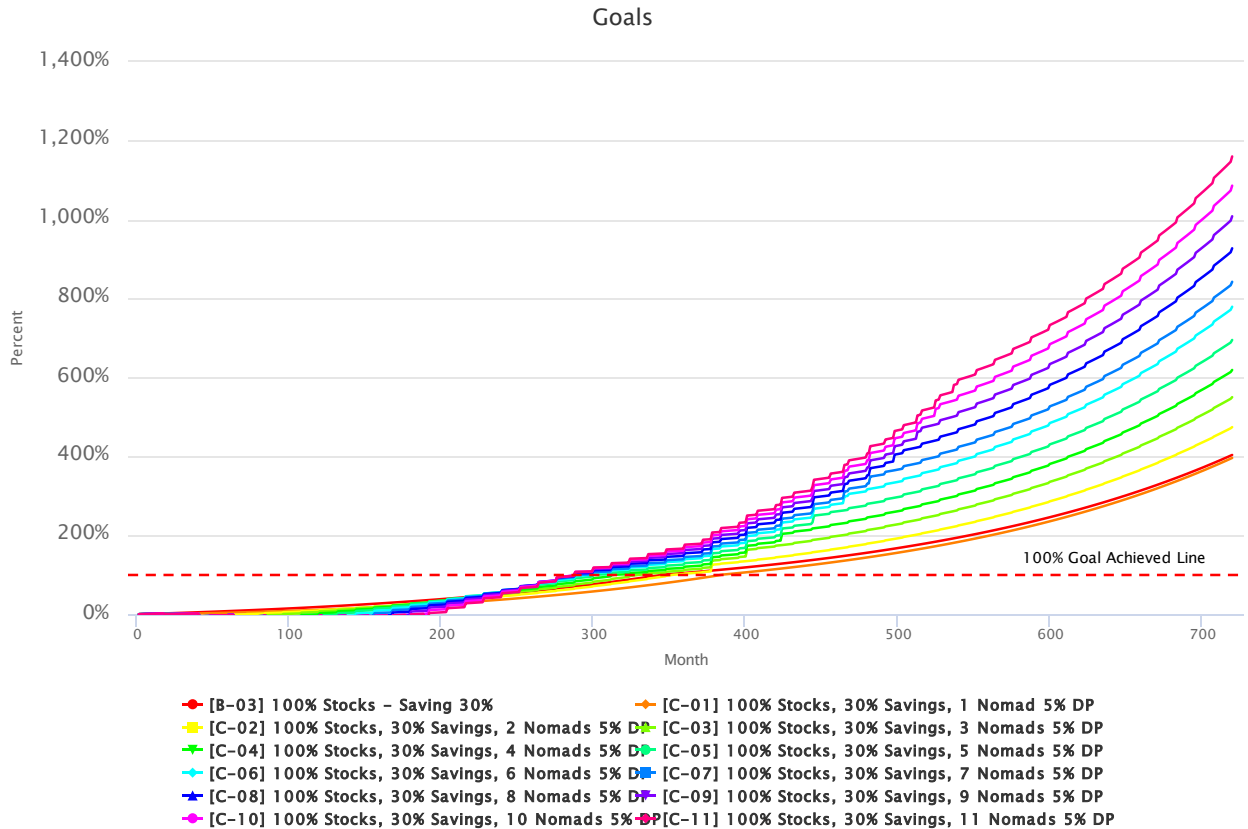
First, you will notice that you end up with more in your stock market accounts even when you are buying more rentals. Why? It is because your properties are generating cash flow which adds money to your stock market account while you are still working and, additionally, reduces the draw you need to take from stocks when you stop working.

Second, while certain plans will get you to financial independence faster, staying the course and continuing with the Nomad™ path does make a big difference in terms of standard of living and net worth later. This might be best illustrated in the chart below showing what percentage of the minimum target income in retirement each scenario is achieving. When you are over the horizontal red goal line, that means you’ve met your minimum to be financially independent.

The higher the percent, the higher your standard of living can be. So, 200% means you are earning two times your safe withdrawal rate and cash flow you set as your target income in retirement. This is double the standard of living you are currently enjoying. It’s like living on twice what you are living on now. If you are at 1,000%, it means you have 10 times the income you are living on now. And, yes, this is still your safe withdrawal rate, and yes, it is adjusted for inflation already.

See the chart below.





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## Model It Yourself

If you want to copy the basic Nomad™ scenarios where you are saving 30% of your income, investing in stocks and buying Nomad™ properties (to live in then rent out as you buy new owner-occupant properties) with 5% down payment to your own Real Estate Financial Planner™ account, use the links below:

- 100% Stocks, 30% Savings, 1 Nomads  
<http://refp.io/613>
- 100% Stocks, 30% Savings, 2 Nomads  
<http://refp.io/614>
- 100% Stocks, 30% Savings, 3 Nomads  
<http://refp.io/615>
- 100% Stocks, 30% Savings, 4 Nomads  
<http://refp.io/616>
- 100% Stocks, 30% Savings, 5 Nomads  
<http://refp.io/617>
- 100% Stocks, 30% Savings, 6 Nomads  
<http://refp.io/618>
- 100% Stocks, 30% Savings, 7 Nomads  
<http://refp.io/619>

- 100% Stocks, 30% Savings, 8 Nomads  
<http://refp.io/620>
- 100% Stocks, 30% Savings, 9 Nomads  
<http://refp.io/621>
- 100% Stocks, 30% Savings, 10 Nomads  
<http://refp.io/622>
- 100% Stocks, 30% Savings, 11 Nomads  
<http://refp.io/623>

Of course, you can change any or all of the assumptions we made to more closely model your reality. And, if you plan to implement this strategy, I would strongly advise you to do a full Monte Carlo study of it. I will share with you what variables I would use when running Monte Carlo on real estate in the next section when I provide you the link to copy the two Nomad plan to your Planner™.

When doing your Monte Carlo analysis, I would recommend you model the following additional variables:

- Stock Market Return
- Mortgage Interest Rate
- Appreciation Rate
- Rent Appreciation Rate
- Vacancy Rate
- Property Taxes
- Property Insurance
- Maintenance

This will help you to see how this scenario would perform if:

- Stock market goes up or down
- Mortgage rates go up or down while you are buying your property
- Property values go up or down (either before you buy or after)
- Rents go up or down (either before you buy or after)
- You enter a period of high or low vacancy
- Property taxes or property insurance in your area go up or down significantly
- Property has high maintenance costs

To find and copy any of the other scenarios covered in this book, follow the link below.

- <https://realestatefinancialplanner.com/filyp/>

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## Path 4: No Down Payment and Gift Money

---

What if you had generous parents who were willing to gift you the 5% down payment for you to do Nomad™? Or, what if you were willing to put in the effort to learn how to buy properties creatively using strategies like owner financing, subject to, or lease-options?

This is what we will be covering next.

I assume that you are buying a property for 5% below the current fair market value with no down payment. This simulates you buying a property and the 5% down payment magically showing up for you at closing from me and your mother. You will still need to come up with closing costs on your own.

All other assumptions are the same.

How much of an advantage does having parents that are willing to help you with down payments give you?

### Buying Just an Owner-Occupant Property

Let us start with you buying just an owner-occupant property and not buying any additional properties. I will compare this to the previous chapter where we discussed you paying the 5% down payment yourself to see how they differ.

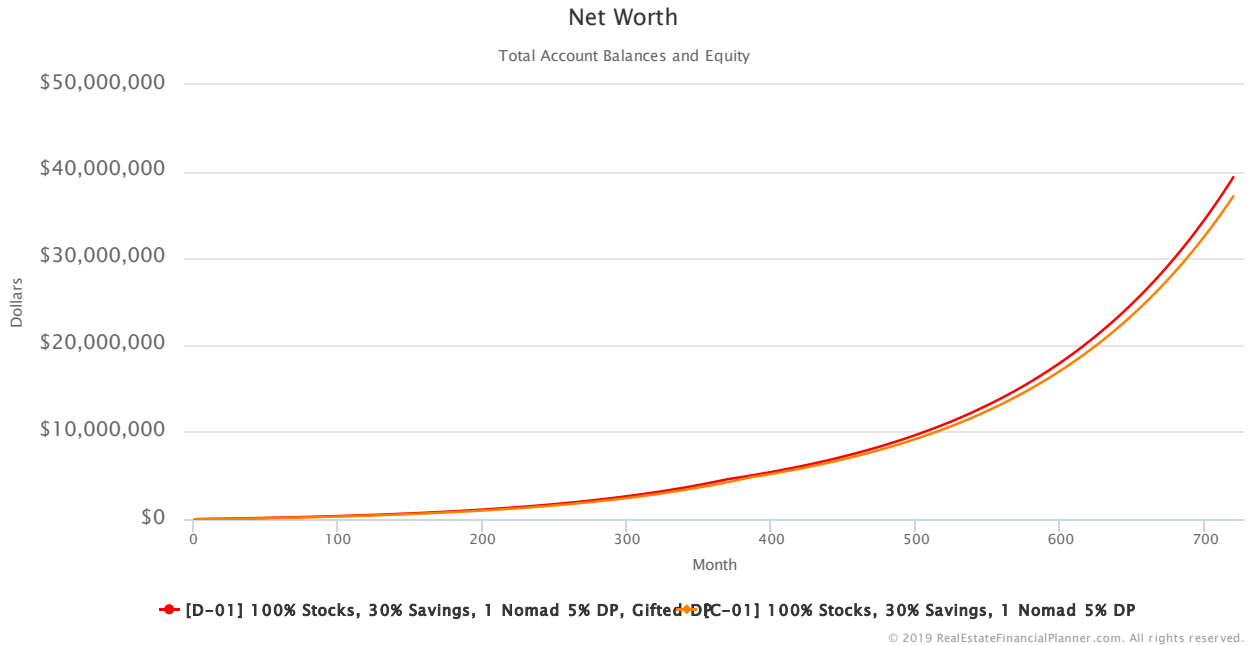
First, how much faster can you buy a property, starting with \$0 saved, but still saving 10% of your income, if you don't have to save up the 5% down payment?

As it turns out, you can buy your first owner-occupant property in month 3 instead of month 18 if you are gifted the down payment or are able to buy the property creatively with no down payment. This means your housing expenses go up faster, so you end up investing less each month in the stock market. But, at the same time, you will pay off the house faster so you will be able to start saving more, sooner, after the house is paid off. Which is more important?

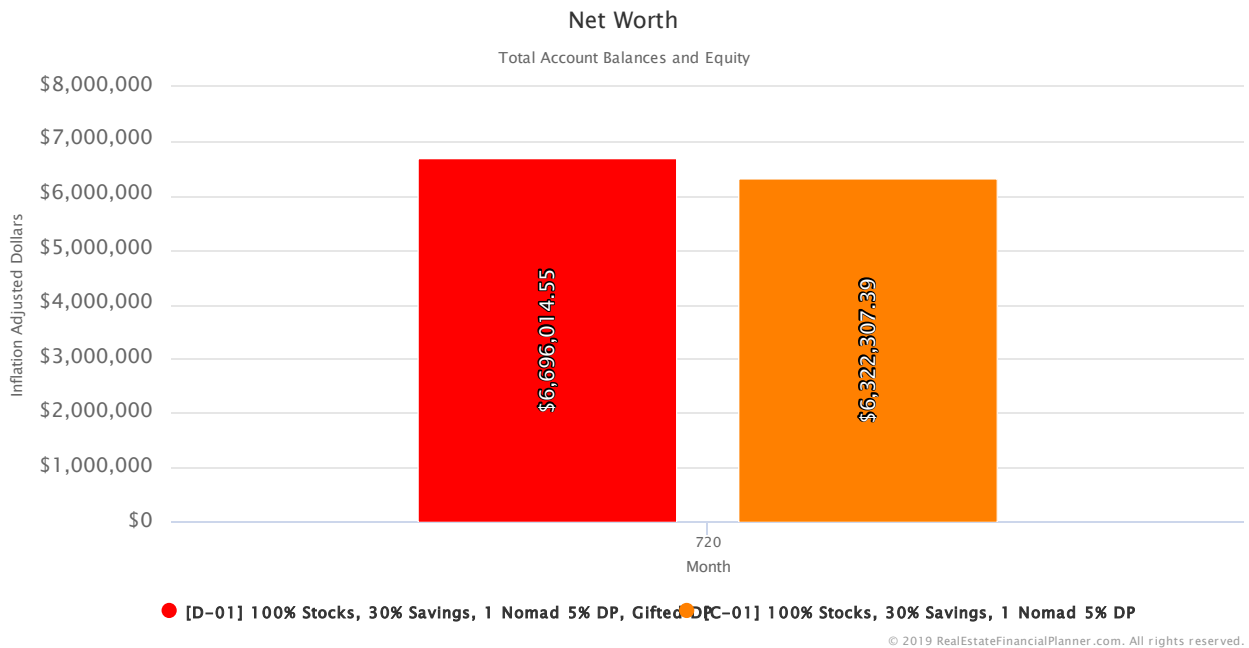
Also, since you are buying the house a year and half earlier it has not appreciated at 3% per year for 18 months. Therefore, it is almost 5% less expensive than the same house you'd buy 18 months later. That means your monthly payment is slightly lower as well, which allows you to save slightly more each month while you are living in the property.

### Net Worth

By being able to purchase your property a little bit earlier, you end up with a higher net worth. The following chart shows your overall net worth which, remember, consists of your stock market account balance and the equity you have in the property you are living in. The chart is showing inflated, future dollars.



If we zoom in on the last month and adjust for inflation back to today's dollars, the difference is a mere \$370,000 over 60 years or so in your favor for you receiving a gift of about \$18,000 today. You would have been better off investing that \$18,000 in the stock market if you could get 8.97% per year. That \$18,000 would have been worth about \$530,000 in inflation adjusted dollars over 60 years in that case.



### Goal of Financial Independence

But, what about how quickly you can achieve financial independence? Does receiving gift money mean you can achieve FILYP earlier? The answer is yes. You reach your target monthly income in retirement from your investments in month 370 instead of month 385 which is a full 15 months faster with this strategy.

### Nomad™ Twice

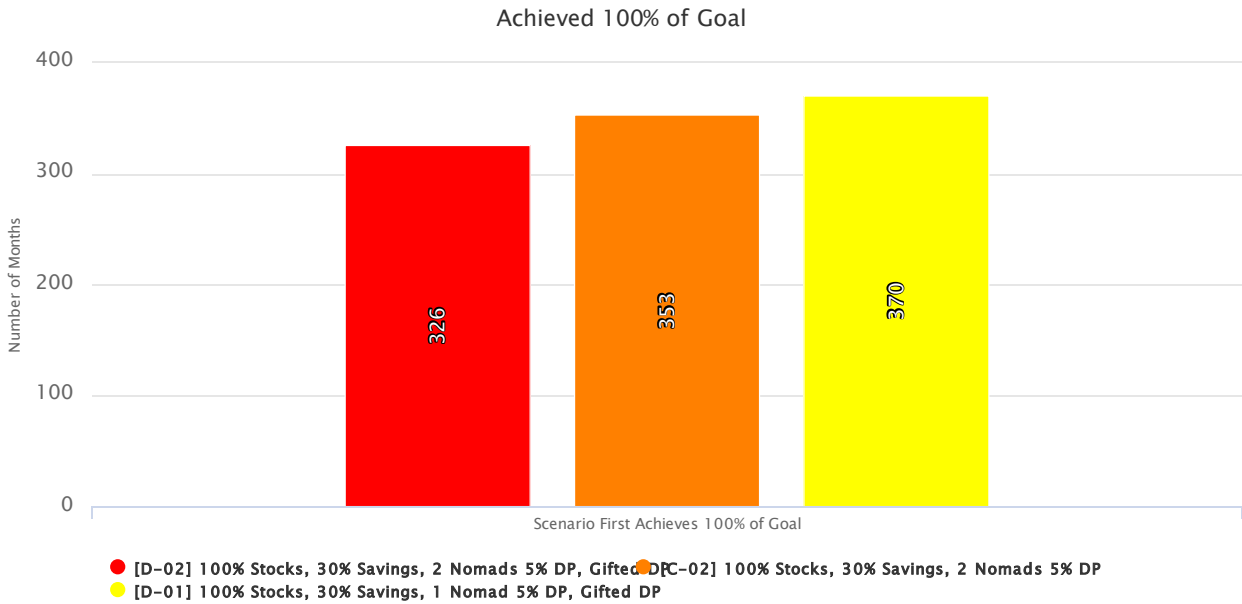
What if you still buy the first owner-occupant property, but instead of living there forever you decide to live there for the one year minimum required by the lender? At the one-year point, you ask us to gift you another down payment and you pay closing costs to buy a second owner-occupant property. You keep the first property as a rental. Rent from that first property will contribute toward your target monthly income in retirement.

In other words, you Nomad™ twice to acquire one rental and one owner-occupant property.

First, let’s look at how much more quickly you are buying this property than in the previous chapter when you had to save up for your down payment. In the last chapter it took you 23 months from when you bought your first property in month 18 to buy your second property in month 41. With a gifted down payment, you are just waiting the mandatory year required by your lender to buy your second property. So, you are able to buy your second property in month 15. That means you get to two properties by month 15 versus month 41.

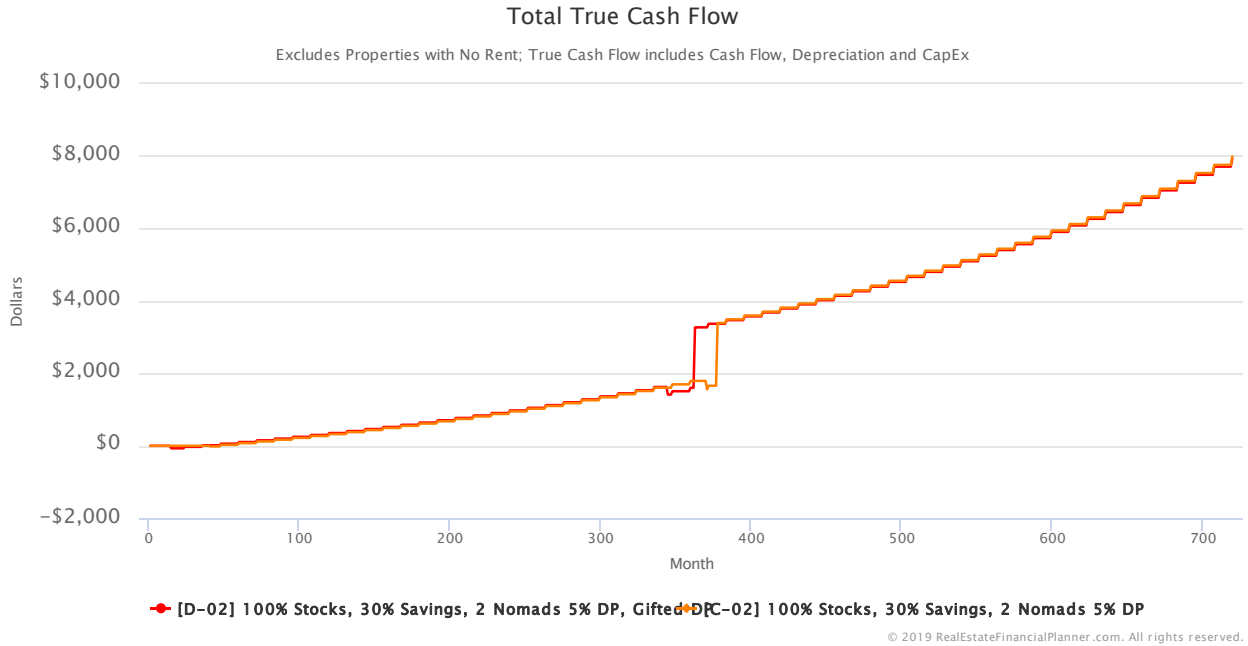


As a result, your first property will start cash flowing earlier, which will help you save more and faster in the stock market. The cash flow itself will also contribute toward your target monthly income in retirement which will help you achieve financial independence faster. How much faster?

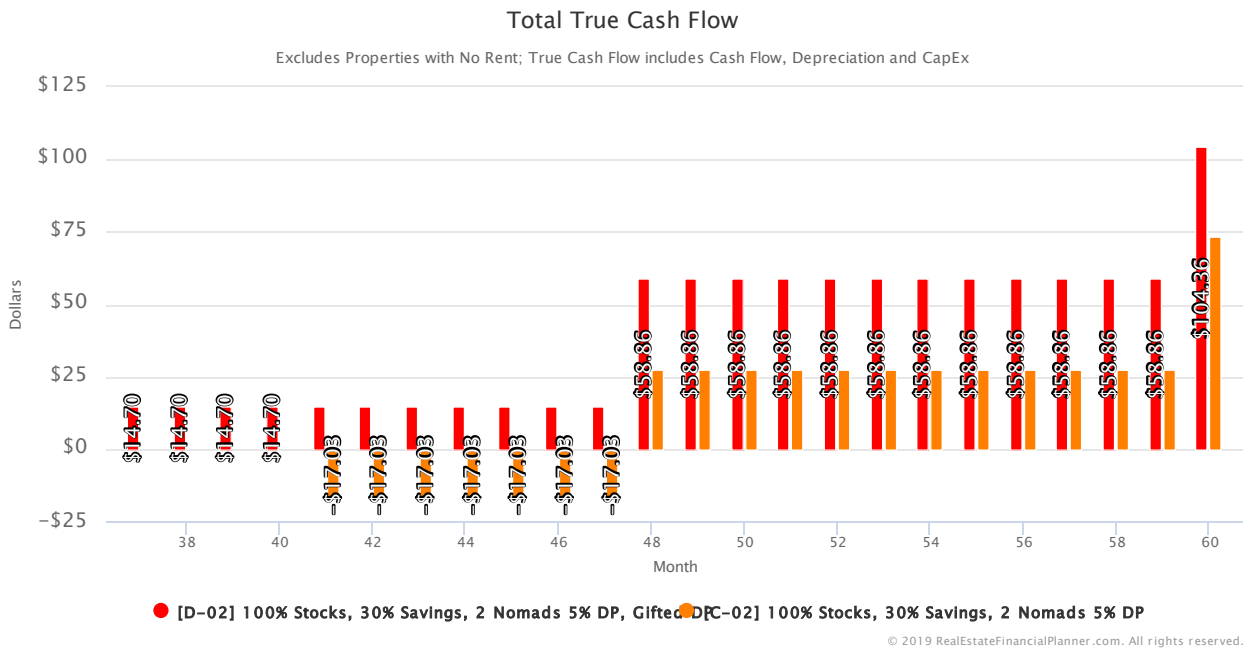


It turns out that you achieve financial independence in month 326 versus month 353 without a gifted down payment. Doing Nomad™ twice with gift money is also 44 months faster than just doing Nomad™ once.

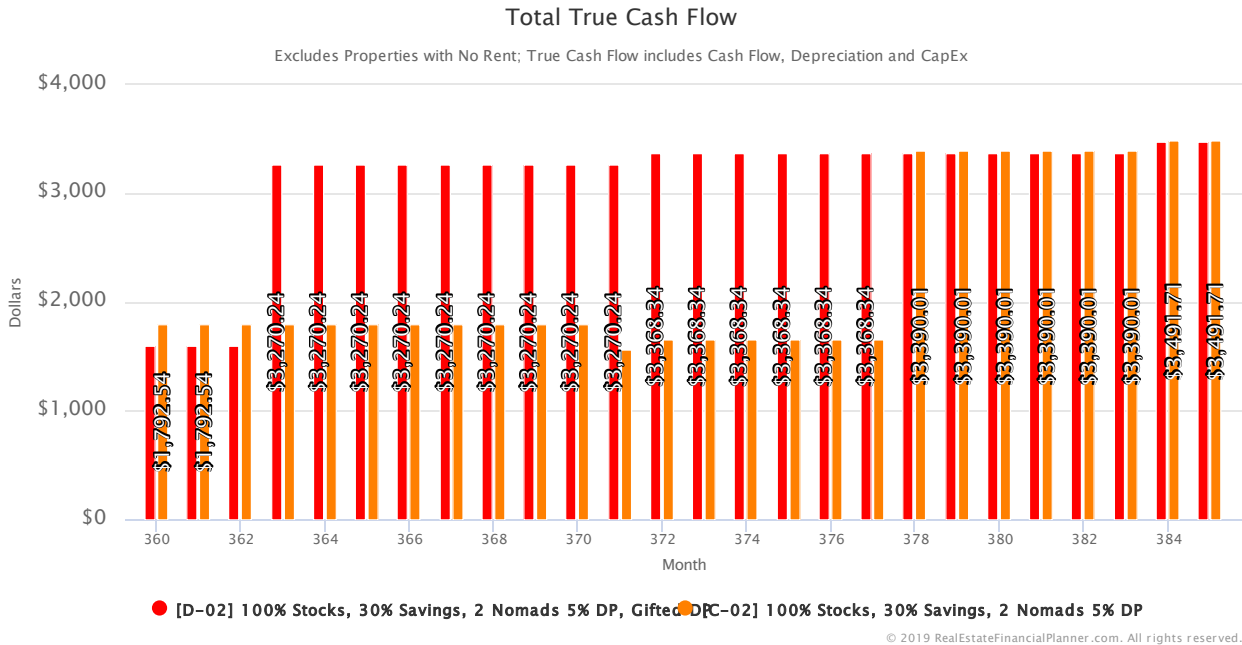
I want to point out where cash flow ultimately ends up after you pay off the rental properties.



The chart above compares receiving gift down payments versus not receiving gift down payments. In both cases, once the property is paid off, cash flow is nearly identical. Receiving the gift down payment will allow you to buy the property sooner and will give you a very small cash flow benefit. This is shown in the chart below when you initially buy your second property.



However, by the time you pay off the properties, the difference is still very small.

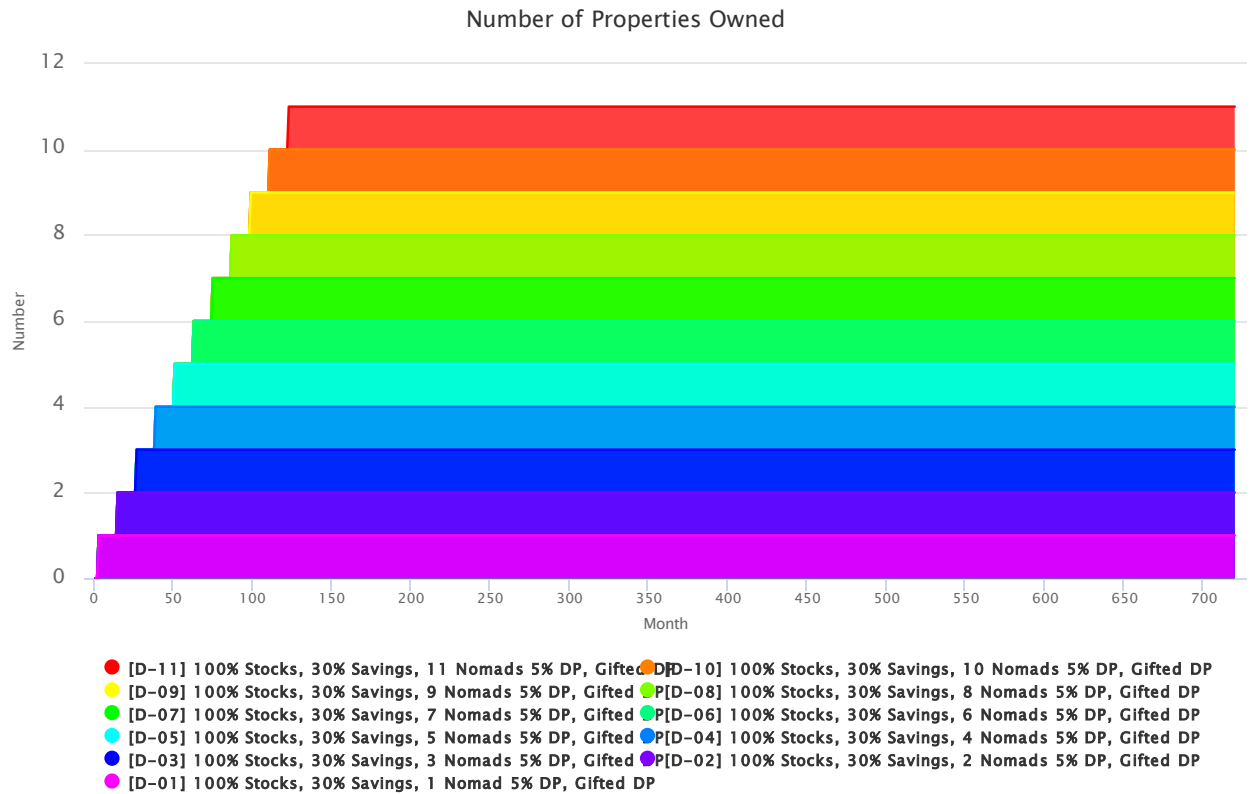


## Up to Full Nomad™

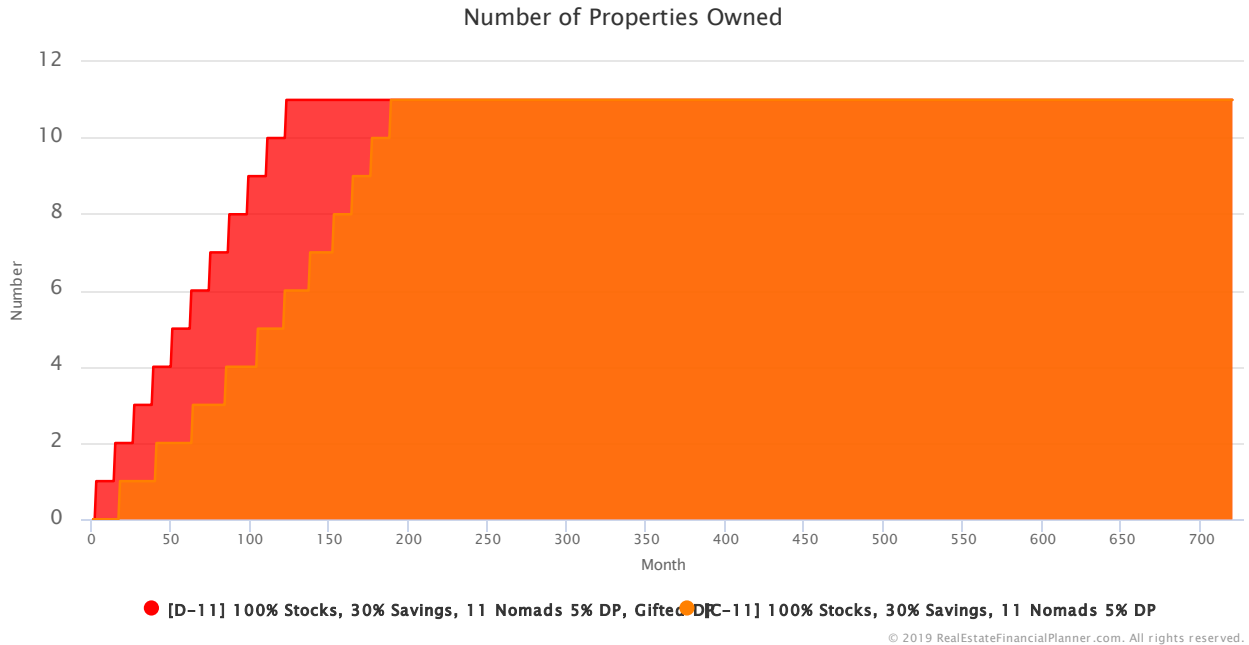
So, let's jump from doing Nomad™ twice to showing you what doing Nomad™ 3 to 11 times looks like.

How long does it take you to acquire the properties? It looks like, since you are receiving gift down payments, you can buy the properties after waiting the minimum 12 months required by the lender for each new purchase.

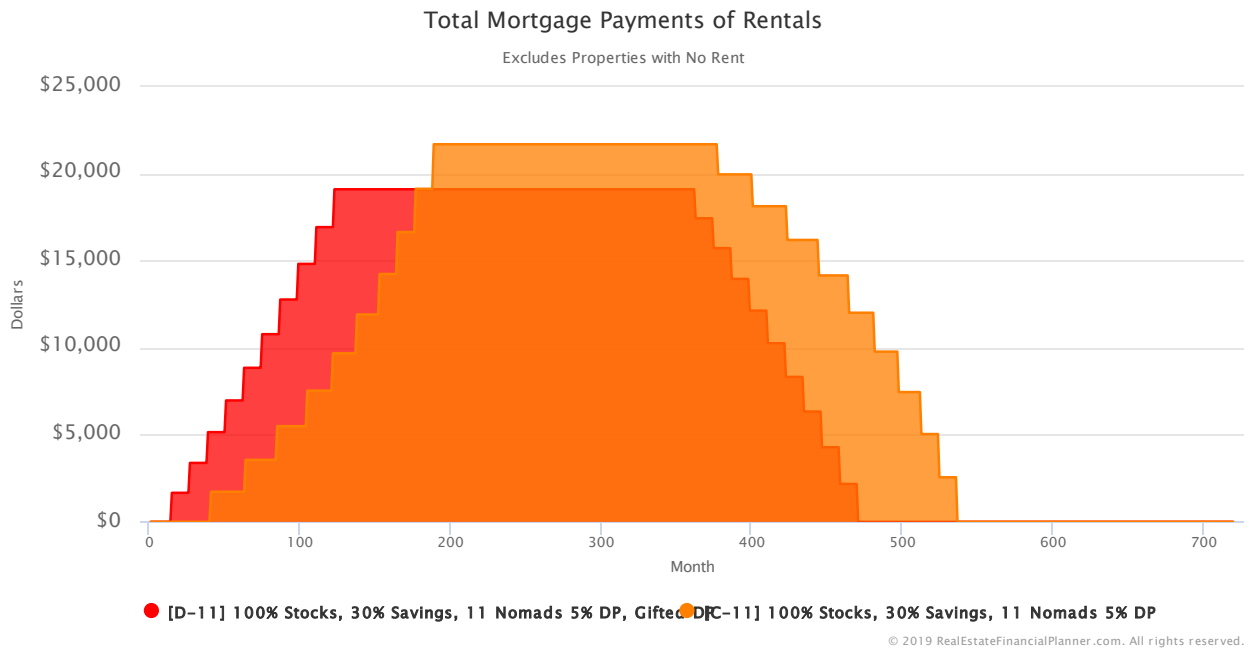




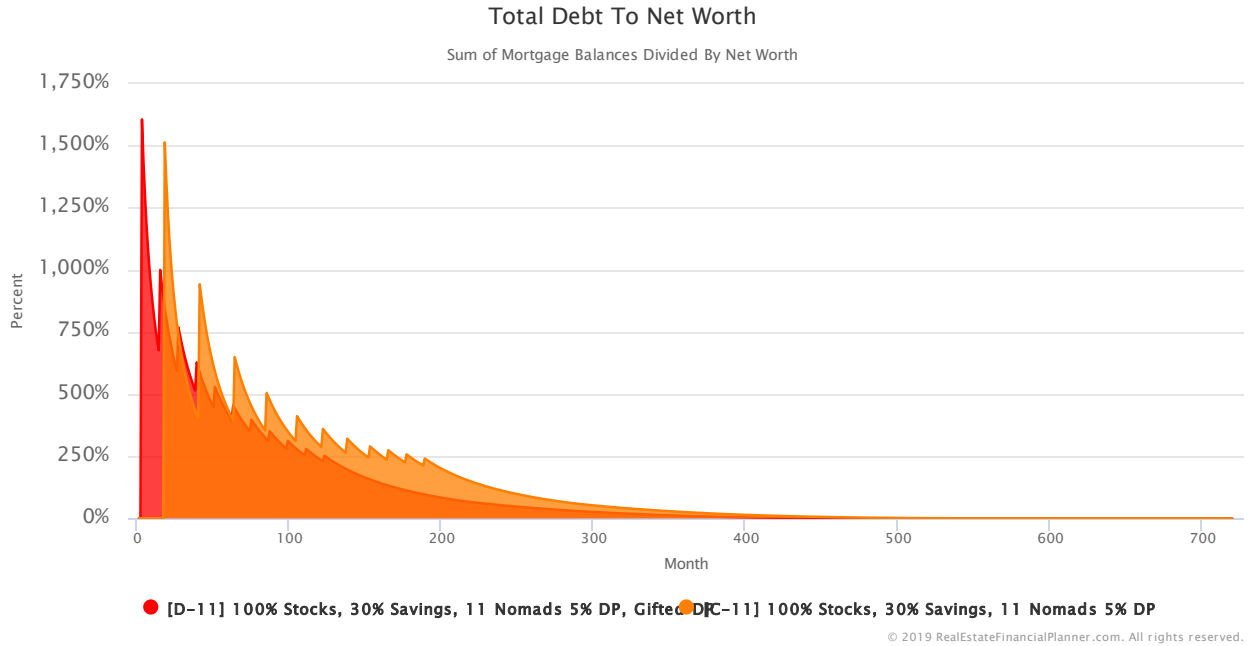
If we compare doing Nomad™ 11 times with gift down payments to saving for the 5% down payments yourself, you can see the time difference in the chart below. You end up acquiring the 11<sup>th</sup> Nomad™ in month 123 with gift down payments versus month 189 when you have to save up for the down payments yourself. This is more than five years faster to get to 10 rentals.



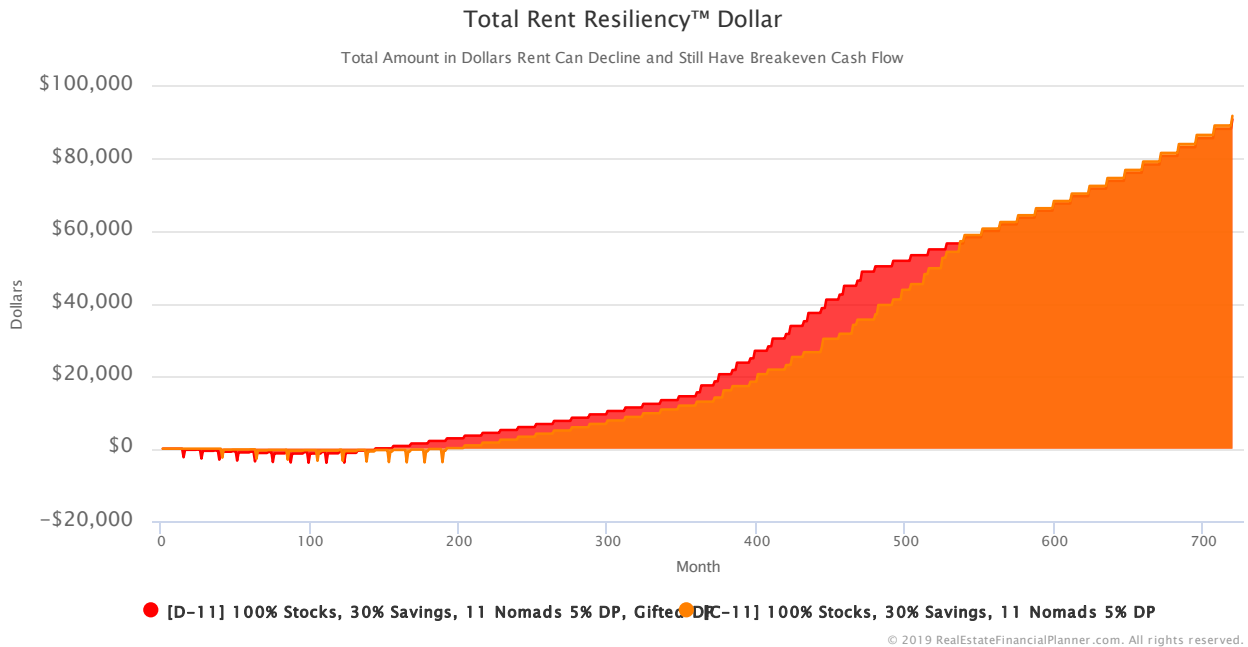
Buying properties sooner means you end up having lower mortgage payments because you are ultimately buying less expensive properties.



You end up with slightly higher risk earlier, again, because you are acquiring properties sooner. For example, here is a chart showing one of our measures of risk: Debt to net worth.



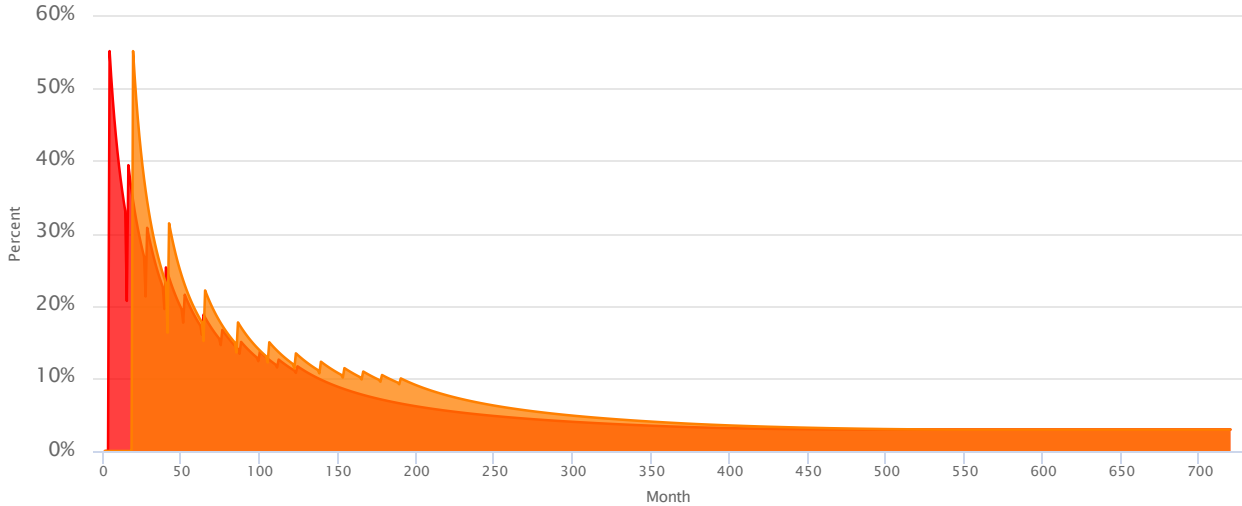
And, here is another measure of risk: Rent Resiliency™ in dollars. This is another term I’ve coined and what it looks at is the amount that the rent you are receiving can decline yet still produce breakeven cash flow. The higher the Rent Resiliency™ the larger the buffer between what you are receiving in rent and the minimum rent you need to be getting to cover all the expenses of owning the property. In this chart you can see that you do have slightly higher risk earlier when you buy the properties more quickly with slightly negative cash flow. However, you have slightly less risk later when your properties are cash flowing better.



You also end up front loading your returns earlier. For example, the following chart shows your overall return on equity from appreciation. By buying properties earlier, you get the boosted, higher returns from appreciation earlier which helps get you to your goals faster.

### Total ROE from Appreciation

Sum annualized Appreciation divided by sum of all Equity in All Owned Properties, As Percent



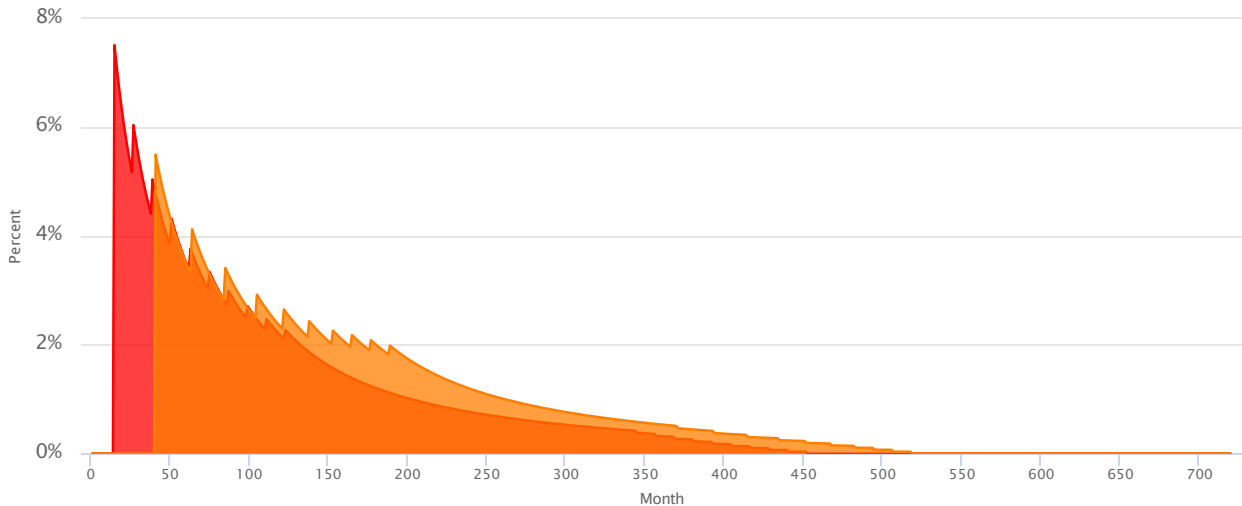
● [D-11] 100% Stocks, 30% Savings, 11 Nomads 5% DP, Gifted ● [C-11] 100% Stocks, 30% Savings, 11 Nomads 5% DP

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The same is true for return on equity for cash flow from depreciation. Buying houses earlier gives you this return boost sooner.

### Total ROE from Cash Flow from Depreciation

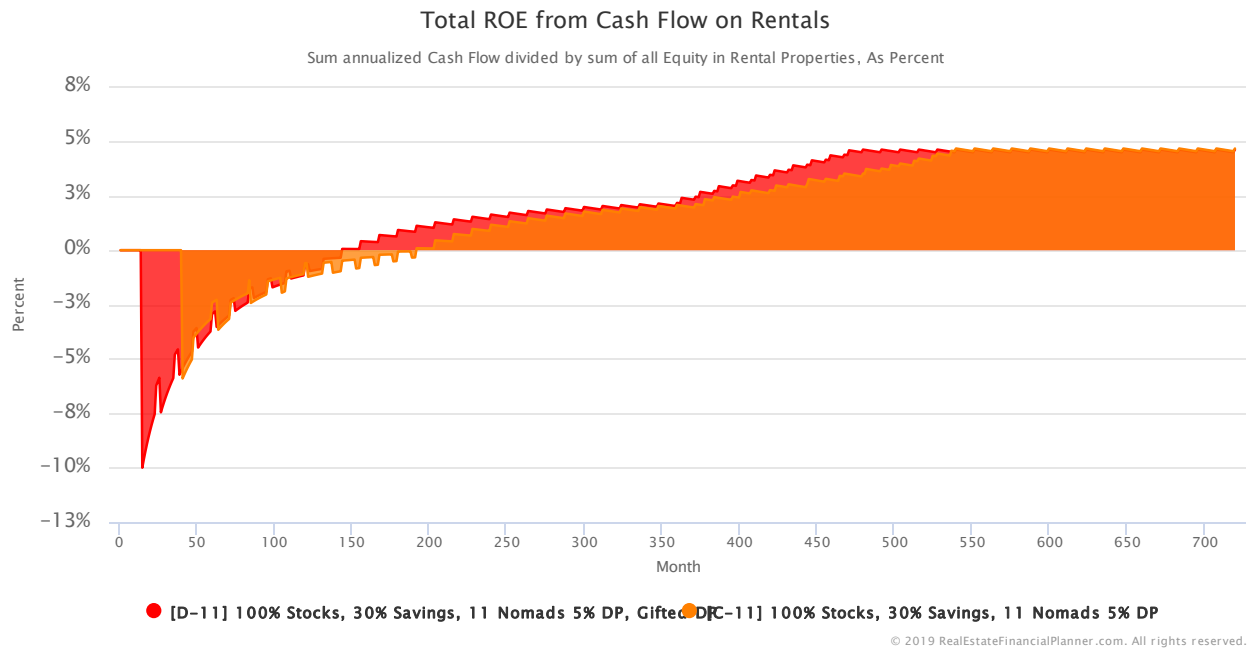
Sum annualized Cash Flow from Depreciation divided by sum of all Equity in Rental Properties, As Percent



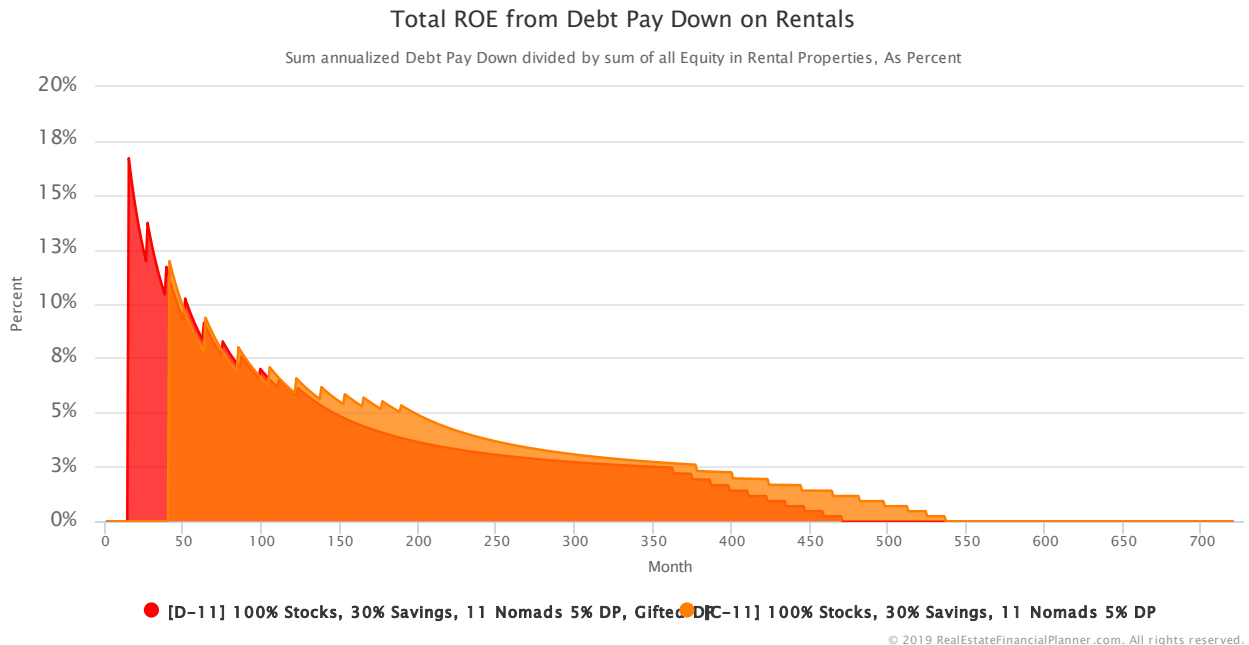
● [D-11] 100% Stocks, 30% Savings, 11 Nomads 5% DP, Gifted ● [C-11] 100% Stocks, 30% Savings, 11 Nomads 5% DP

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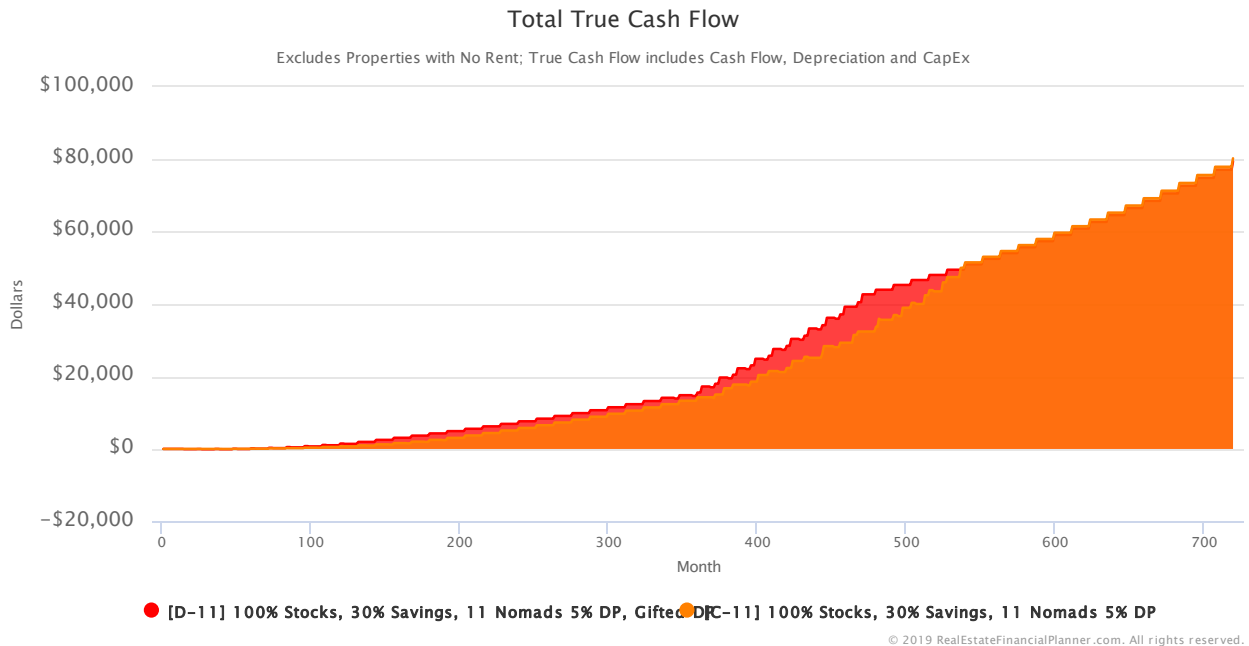
Similarly, your return on equity from cash flow starts negative. It is more negative the more aggressively and quickly you buy properties since you are not delaying as much between them and allowing the rents to increase once you own them. Over time, you get better cash flow sooner on properties you have owned longer, improving your return on equity from cash flow until they are all paid off, when they become equal.



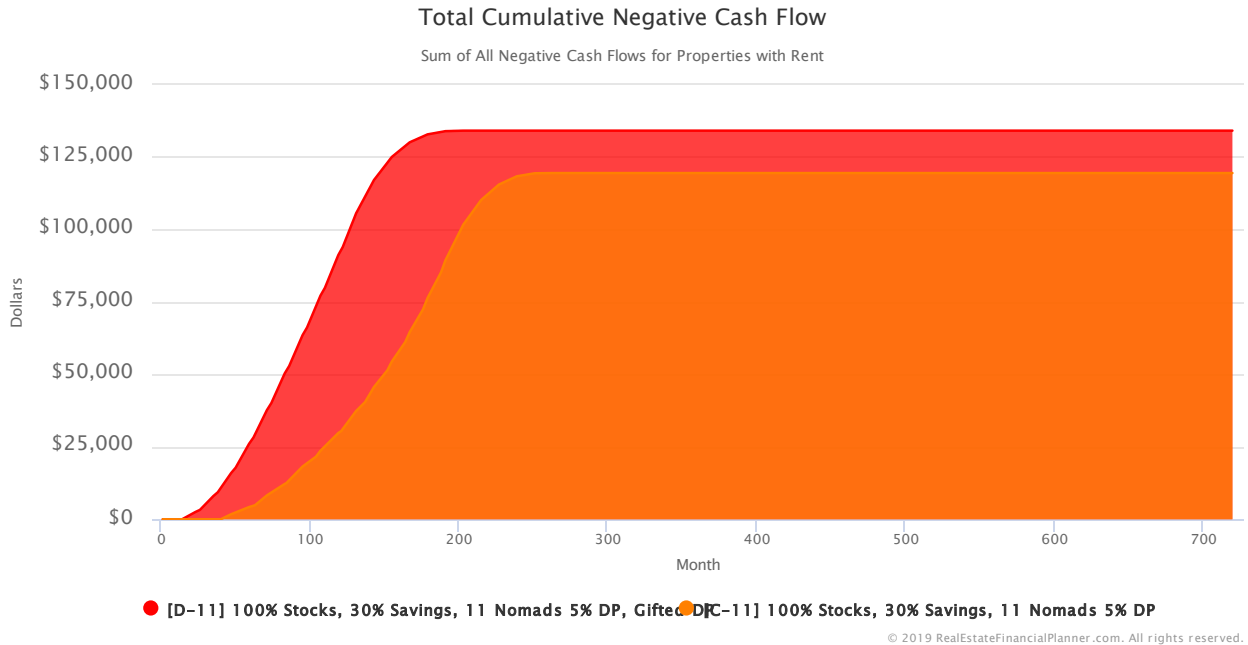
And, I think you knew it was coming, but you get the same front-loaded benefit from return on equity from debt paydown as shown below.



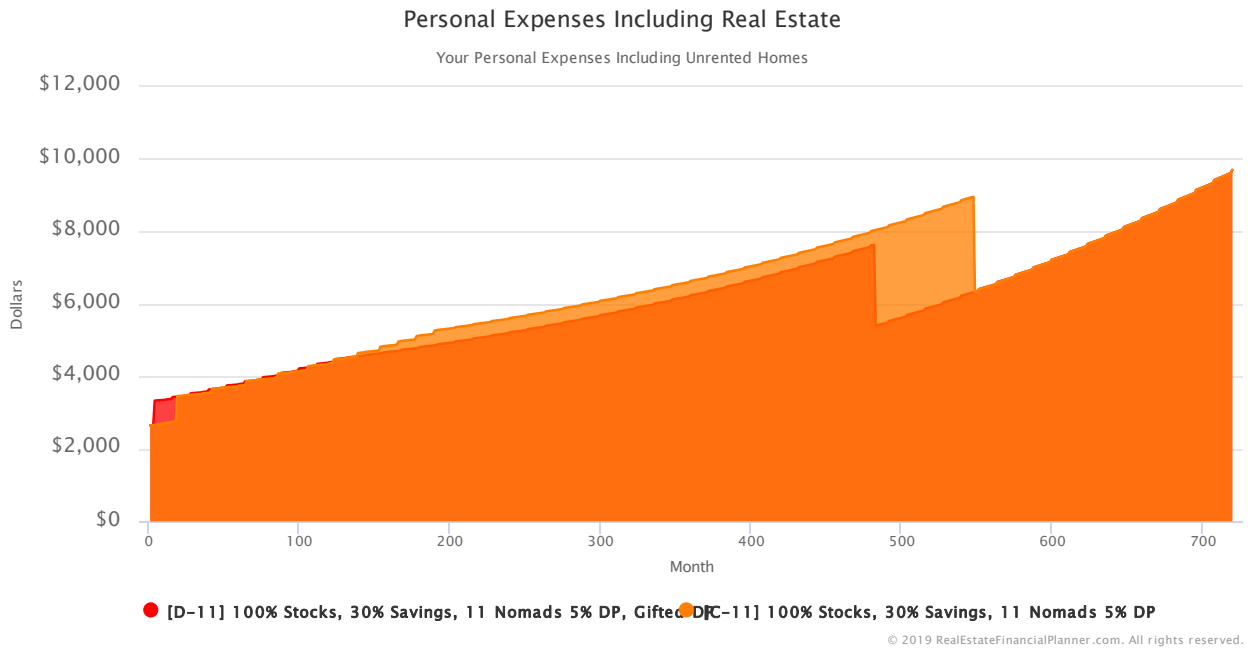
You get better True Cash Flow™ when you are able to buy your properties earlier, as well.



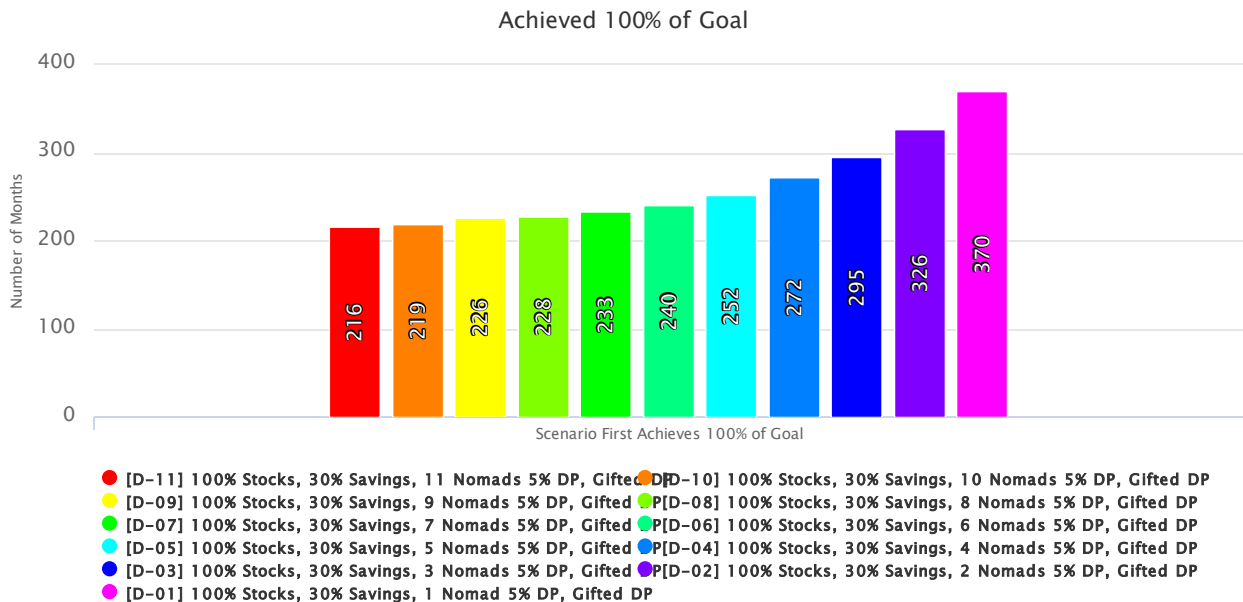
However, you end up having to pay more negative cash flow by buying properties earlier. Here is a chart showing the amount of negative cash flow (not considering the cash flow from depreciation that offsets some to all of this negative cash flow). You wind up paying about \$15,000 more, in total, in negative cash flow by buying properties more quickly with gifted down payments.



Your personal expenses, including the cost of the property you are living in, end up being lower overall when you receive gift money and buy properties faster. Although, you do start paying higher personal expenses earlier because you are buying a property sooner. Also, buying the property earlier, you end up paying off the last property much more quickly. When you pay off the property, your expenses go down. Lower expenses means you are able to save a lot more later, after you've paid off the house.



The following chart shows you how many months it takes you to achieve financial independence for each scenario doing one Nomad™ with gift down payment or no down payment and buying the property at a 5% discount (presumably creatively) through doing Nomad™ eleven times.



Previously, in the last chapter without gift down payments, doing Nomad™ lost its effectiveness of shortening time to achieve FILYP after doing Nomad™ seven times. Adding those extra properties would still improve your standard of living once you achieve FILYP, but it did not get you there faster.

With gift down payments though, each additional property you receive gift down payment money for does increase your speed to financial independence. The fastest you get there now is in 216 months which is 18 years from now. You would be 40 years old.

I know that you are fiercely independent and want to Frank Sinatra it and “Do It [Your] Way”, so let’s assume for the rest of the scenarios that you are not going to receive down payment gift money.

## Model It Yourself

If you want to copy any of the gift money scenarios to your own Real Estate Financial Planner™ account and adjust the assumptions, you can use the links below.

- 100% Stocks, 30% Savings, 1 Nomads, 5% Gifted DP  
<http://refp.io/624>
- 100% Stocks, 30% Savings, 2 Nomads, 5% Gifted DP  
<http://refp.io/625>
- 100% Stocks, 30% Savings, 3 Nomads, 5% Gifted DP  
<http://refp.io/626>
- 100% Stocks, 30% Savings, 4 Nomads, 5% Gifted DP  
<http://refp.io/627>



- 100% Stocks, 30% Savings, 5 Nomads, 5% Gifted DP  
<http://refp.io/628>
- 100% Stocks, 30% Savings, 6 Nomads, 5% Gifted DP  
<http://refp.io/629>
- 100% Stocks, 30% Savings, 7 Nomads, 5% Gifted DP  
<http://refp.io/630>
- 100% Stocks, 30% Savings, 8 Nomads, 5% Gifted DP  
<http://refp.io/631>
- 100% Stocks, 30% Savings, 9 Nomads, 5% Gifted DP  
<http://refp.io/632>
- 100% Stocks, 30% Savings, 10 Nomads, 5% Gifted DP  
<http://refp.io/633>
- 100% Stocks, 30% Savings, 11 Nomads, 5% Gifted DP  
<http://refp.io/634>

If you do end up implementing one of these scenarios, I would strongly advise you to do full Monte Carlo testing as we described in the previous chapter.

To find and copy any of the other scenarios covered in this book, follow the link below.

- <https://realestatefinancialplanner.com/filyp/>



## **Path 5: 20% Down Payment Rentals**

---

Nomad™ seems great: You get to put only 5% down and you get a better interest rate. However, moving every year...maybe, not so great. I get it. Your mother and I have lived in the same home where we raised you and your brother since 2003. I eat the same thing pretty much every day. So, I am as averse to change as the next guy, maybe even more.

What if you still buy a single owner-occupant property to live in, but buy your rental properties differently? What if you decide to forgo putting 5% down doing Nomad™ and instead you just saved up and bought the same properties as rentals with 20% down payments? You'd be getting investor interest rates, which at the time of this writing are 5.125% instead of the 4.375% owner-occupant interest rates we've been using in previous scenarios.

The down payment is more, but the interest rate is higher. How will that impact cash flow? Will it allow you to achieve final independence faster than doing Nomad™? How much faster? These are some of the questions we will answer next.

### **Nomad™ Twice vs 1 Owner-Occupant and 1 20% Down Payment Rental**

We will start by comparing the scenario we already covered in which you Nomad™ twice. We will refer to this as the Nomad™ scenario for the rest of this comparison. You acquire a property to live in, live there until you save up your next 5% down payment and then buy your next property to live in. You convert the first property you live in to a rental. So, you end up with an owner-occupant property and a rental that you once lived in.

We will compare that to buying an owner-occupant with a 5% down payment, then saving up until you have a 20% down payment. You buy the 20% down payment property, but you continue living in the first property you purchased. We will call this the 20% down scenario even though you are still buying a 5% down payment owner-occupant property first.

As you might imagine, you end up buying the first property in the same month in both cases since all our other assumptions are the same. However, when you go to buy your second property, it takes you 30 additional months saving and investing in the stock market, until you have enough to buy the second property with a full 20% down payment instead of just the 5% required with the Nomad™ strategy.

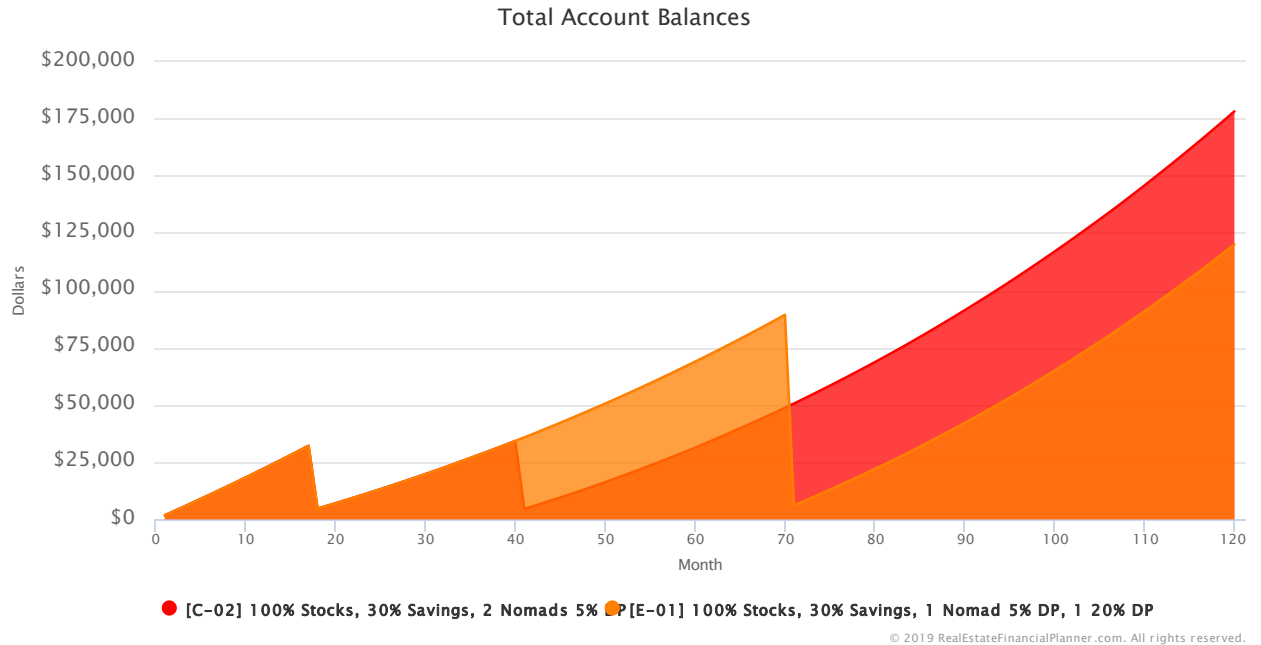


## Account Balances

The account balance charts below show what saving up for down payments, closing costs, and the subsequent purchases of properties look like.

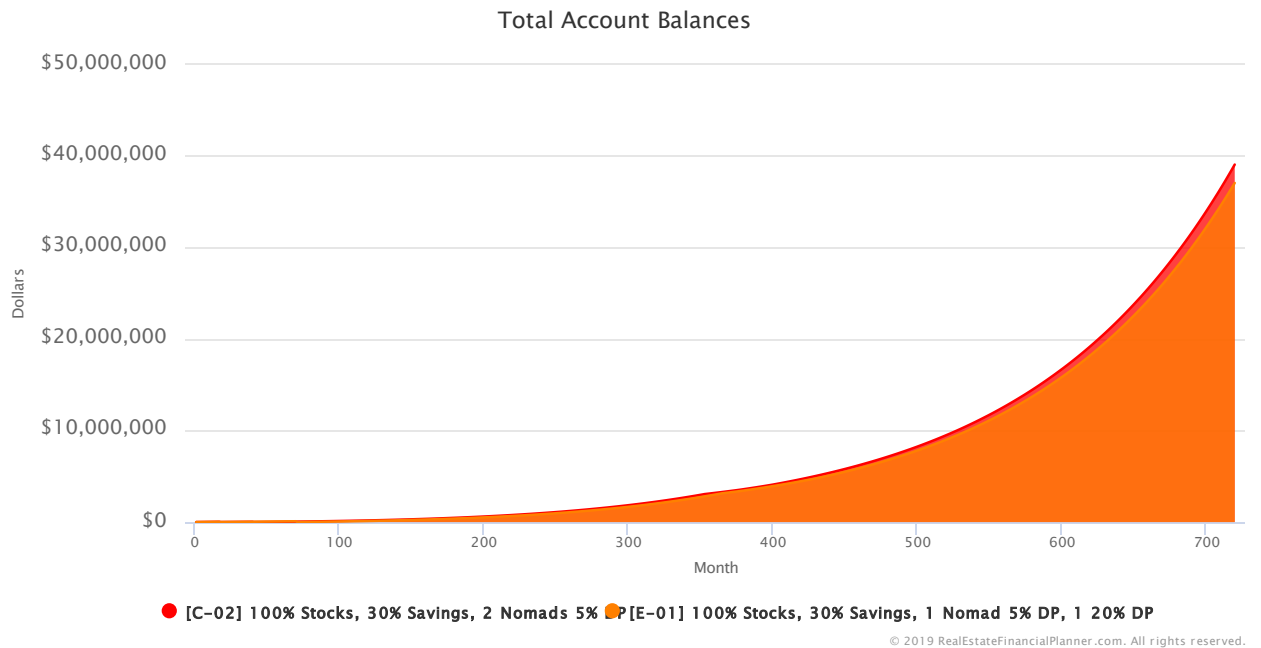
You will notice that the stock market balance for the Nomad™ strategy matches the balance for the 20% down strategy through the first purchase. However, for the second purchase, the bank balance for the Nomad™ strategy only needed to grow enough to cover a 5% down payment plus closing costs. Then, the balance drops when you buy the property.

However, in the 20% down strategy, the stock market account balance continues to grow for the 20% down payment. When you finally save enough for a 20% down payment and closing costs, you purchase the property and the stock market account balance drops.



From here, the stock market account balance continues to grow for each of the scenarios.

By the way, the stock market account balance for the 20% down strategy never overcomes the stock market account balance for the Nomad™ strategy over the entire 60 year run of the scenario. The stock market account balance for Nomads™ is always higher.



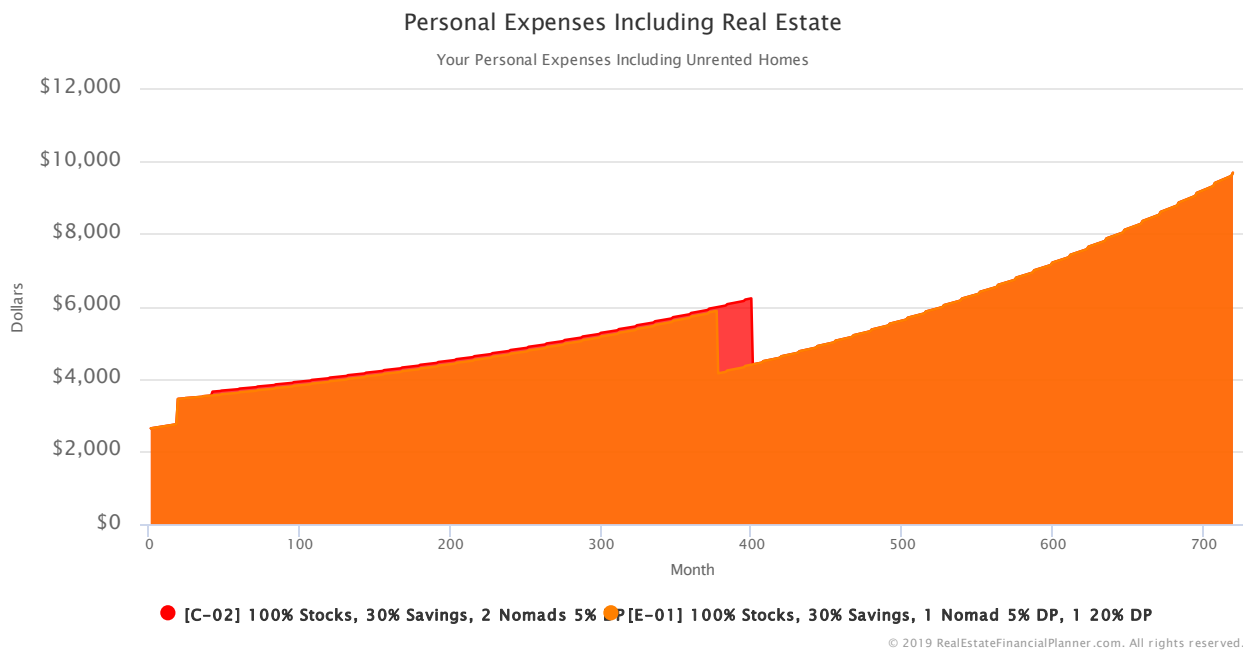
## Personal Expenses

What about personal expenses? With both strategies your first purchase with a 5% down payment is identical. However, with the Nomad™ strategy, you are buying the second property as an owner-occupant. That means your personal expenses to live in that property go up a little when you buy it. You end up saving a little less since your personal expenses are a little higher.

Plus, since you are living in the second property with the Nomad™ strategy, the mortgage does not get paid off nearly as quickly as the first property you bought. That means your personal expenses are higher for a longer period as well.

Of course, with Nomad™ you pay off the first property in 30 years and since that is now a rental, your cash flow on that property increases once you pay off the mortgage. This means you get the full cash flow of that property sooner than you do with the 20% down strategy.

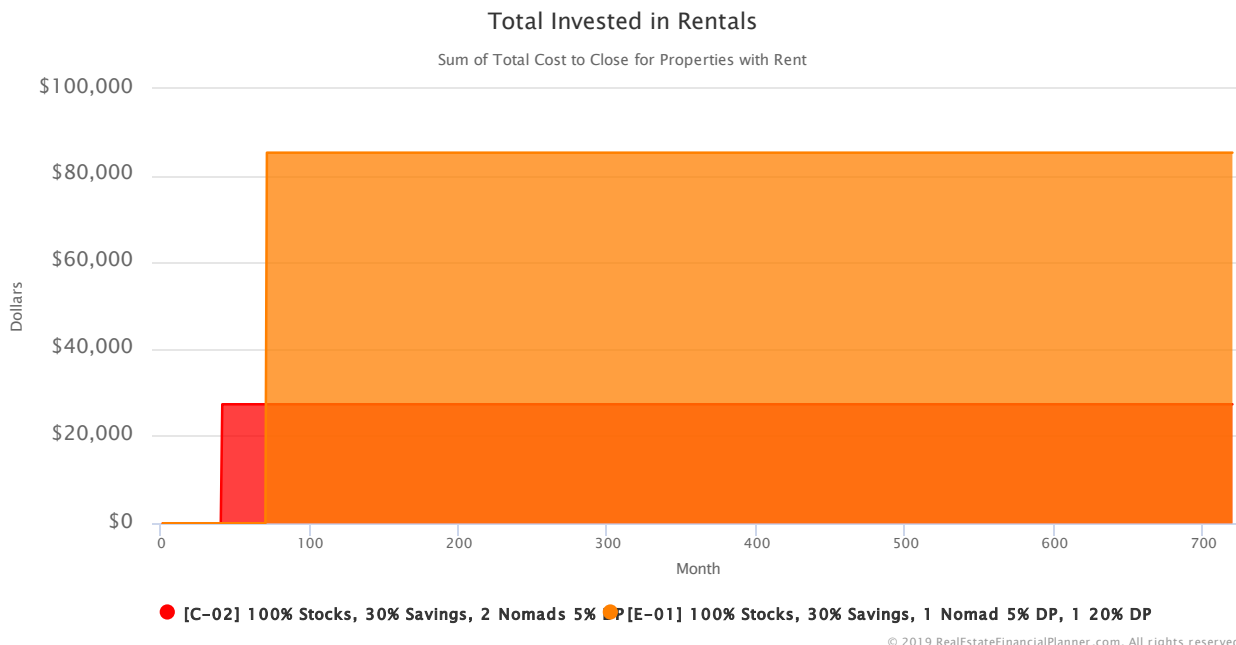
Here's a chart of your personal expenses including real estate comparing the two scenarios.



## Total Invested in Down Payments and Negative Cash Flow

Do you end up investing more doing Nomad™ or doing the 20% down payment? If you remember, I discussed this with you in general terms earlier. But since we are talking about a specific scenario right now, I can show it to you in charts. I love charts, if you recall.

How much do you need to invest in down payments to be able to buy the rental in both the Nomad™ and the 20% down strategy? The following chart shows you the total amount invested and when it occurs.



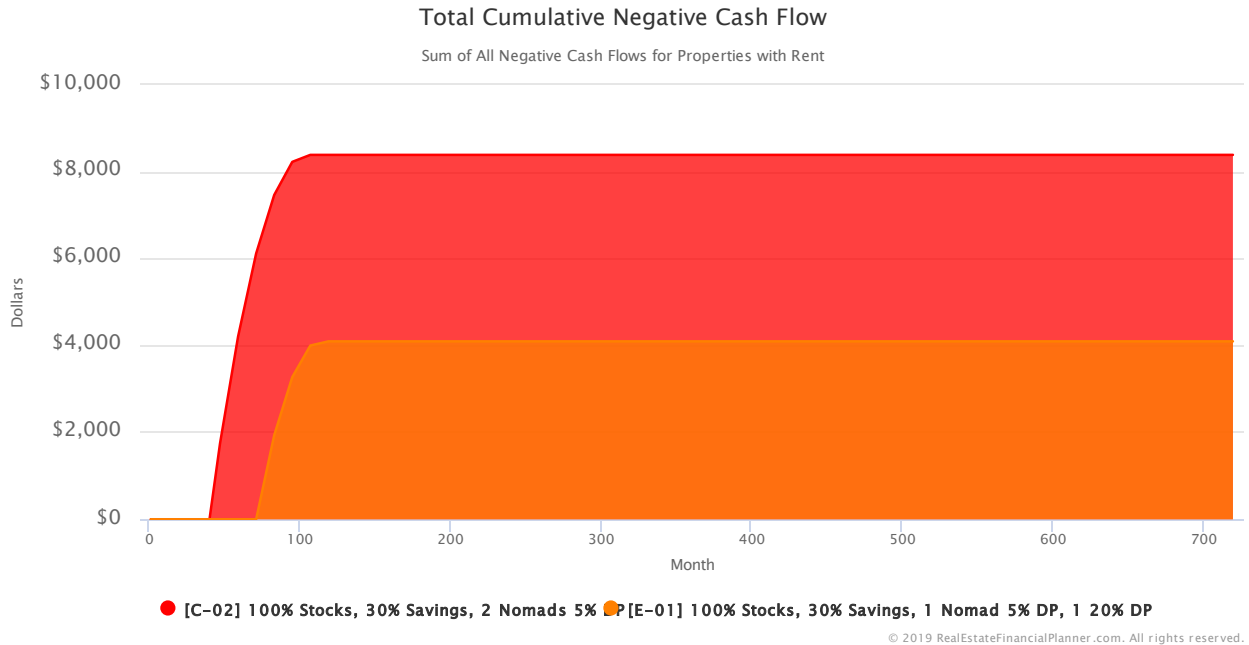
You can see that you make your 5% down payment investment earlier, but the 20% down payment investment happens later and is much larger. It is over four times as large, actually.

But what about negative cash flow? You might expect cash flow to be better if we are putting four times as much down. And you'd be right. However, it is not nearly as much as it might have been if two opposing forces were not also present.

The first opposing force is that we waited to buy the property, so the property is more expensive. That means a higher mortgage and therefore a higher payment.

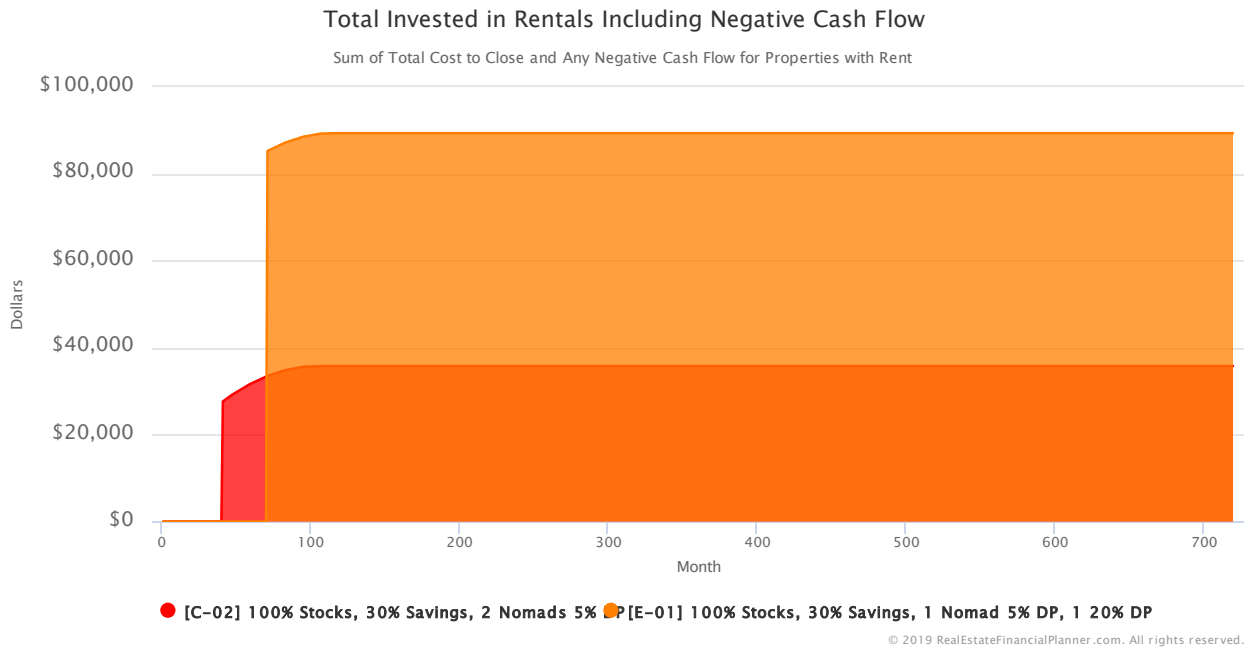
The second opposing force is that owner-occupant interest rates are much lower than investor interest rates. The 20% down payment property was an investment property and so the interest rate is higher. This also means a higher monthly payment.

The following is a chart showing the negative cash flow for each of the two scenarios. It does not account for cash flow from depreciation which will offset much or all of it in these cases.



As you can see, there is almost \$4,000 of negative cash flow even with the 20% down payment property. There is more than twice that for the 5% down Nomad™ property.

But, if we consider both down payment and negative cash flow, which required a larger investment? Glad you asked. Here’s another chart answering that by combining both negative cash flow and down payment into one neat little chart. Seems like I’ve got a chart for everything, doesn’t it?



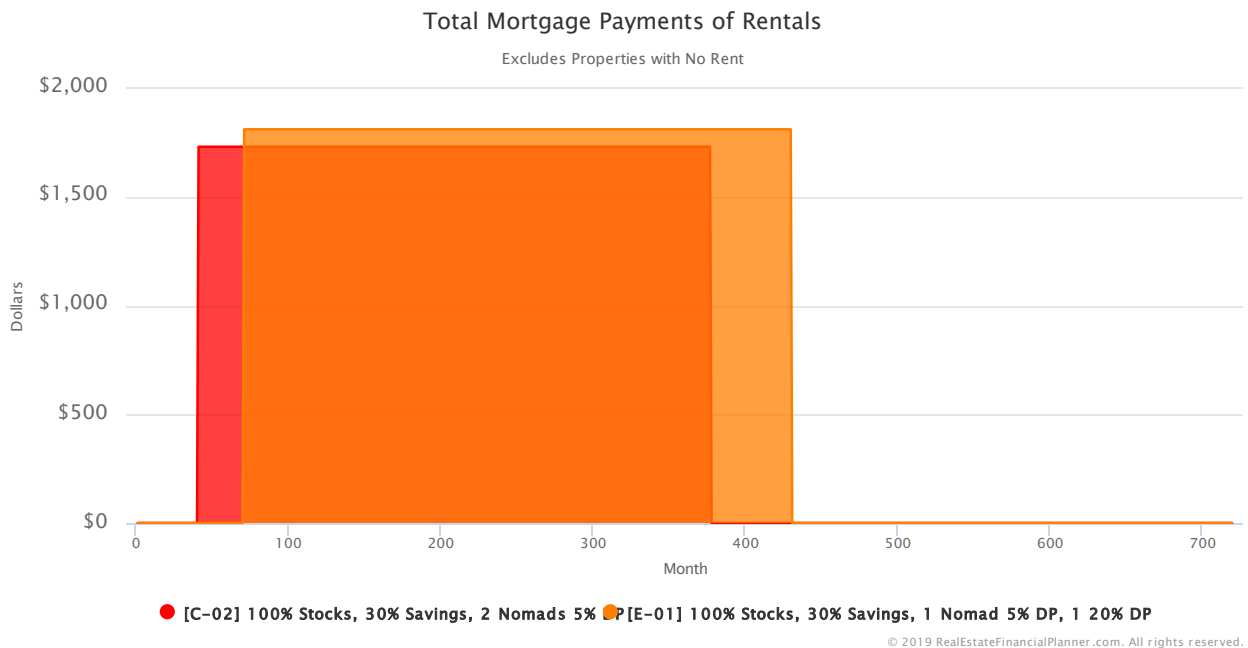


When we look at the chart above, it is clear that you had to invest a lot more for the 20% down payment property. Not quite four times as much, but more than double the investment required to do Nomad™.

That’s interesting. How much is the inconvenience of moving worth to you? \$50,000? What if it were for 10 properties... is it worth \$500,000? Of course, that decision is ultimately up to you.

### Mortgage Payments and Balances

If you recall, I pointed out that since you had to wait to buy the 20% down payment property and since the interest rate is higher, the cash flow is not *significantly* better than the cash flow you might get from buying a Nomad™ property earlier and with a better interest rate. The following chart shows the mortgage payment of each rental property.

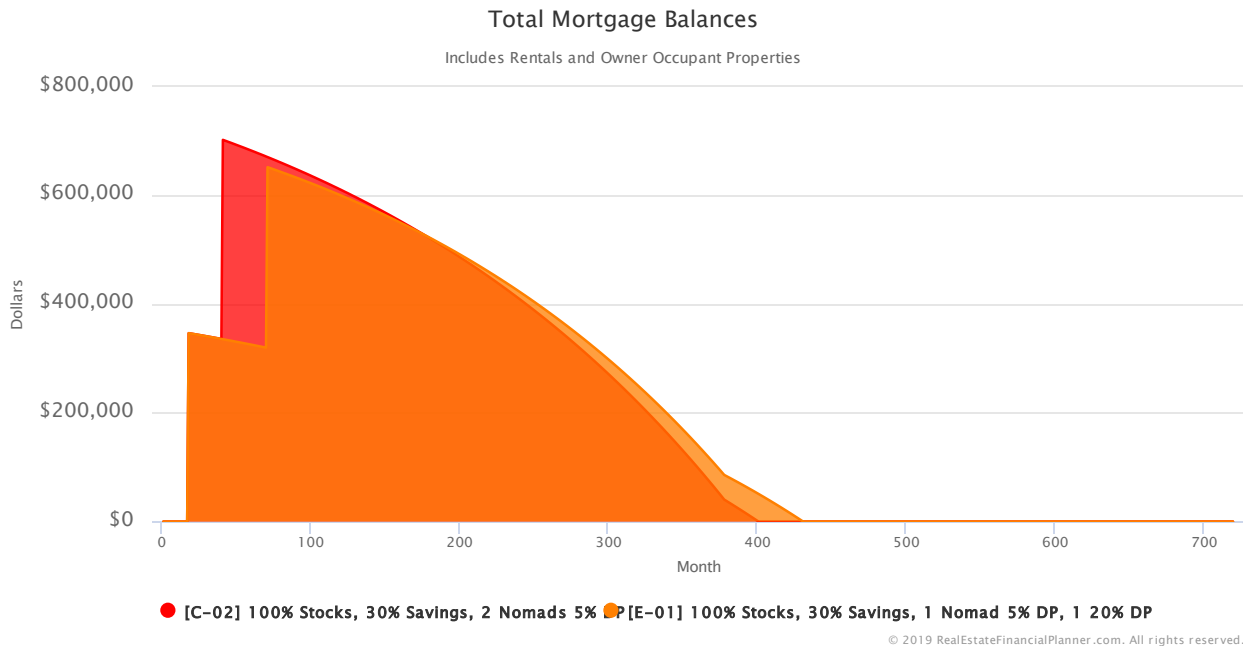


As you can see in the chart above, the mortgage payment for the 20% down payment property is, in fact, higher than the mortgage payment for the first property you bought as a Nomad™ that you originally lived in and then converted to a rental.

As a side note, you can also see the offset in the mortgages as to when each starts and ends. Remember, when the mortgage payment goes away (after you pay off the loan), your cash flow improves. The 20% down strategy has a mortgage on a rental that lasts much longer than the loan on the first Nomad property.

Side Note For Hyper-Observant People: If your eagle eye is looking at when the mortgage payment starts for the Nomad™ one, you may like to know that since this chart only shows mortgage payments on rentals, we only start to display the mortgage payment when it goes from being an owner-occupant to a rental. Even though the mortgage starts earlier, it won’t show up on the chart above until it is a rental.

Speaking of mortgage balances, this chart shows the sum of the mortgage balances for all properties—rentals and owner-occupant properties.



There are a few interesting things to note about this chart. First, you can see that the total mortgage balances for the Nomad™ strategy will give you the largest amount of debt between the two. That makes sense: You are acquiring properties with only 5% down and doing it quickly. With the 20% down strategy, you add a second mortgage, but you are putting 20% down on that purchase. By the time you purchase the second house, you have paid off some of the first loan.

However, there is a difference in how fast you pay off the mortgages as well. You can tell because the lines of the total mortgage balances cross. The Nomad™ strategy starts with a higher total mortgage balance, but we end up paying it off earlier.

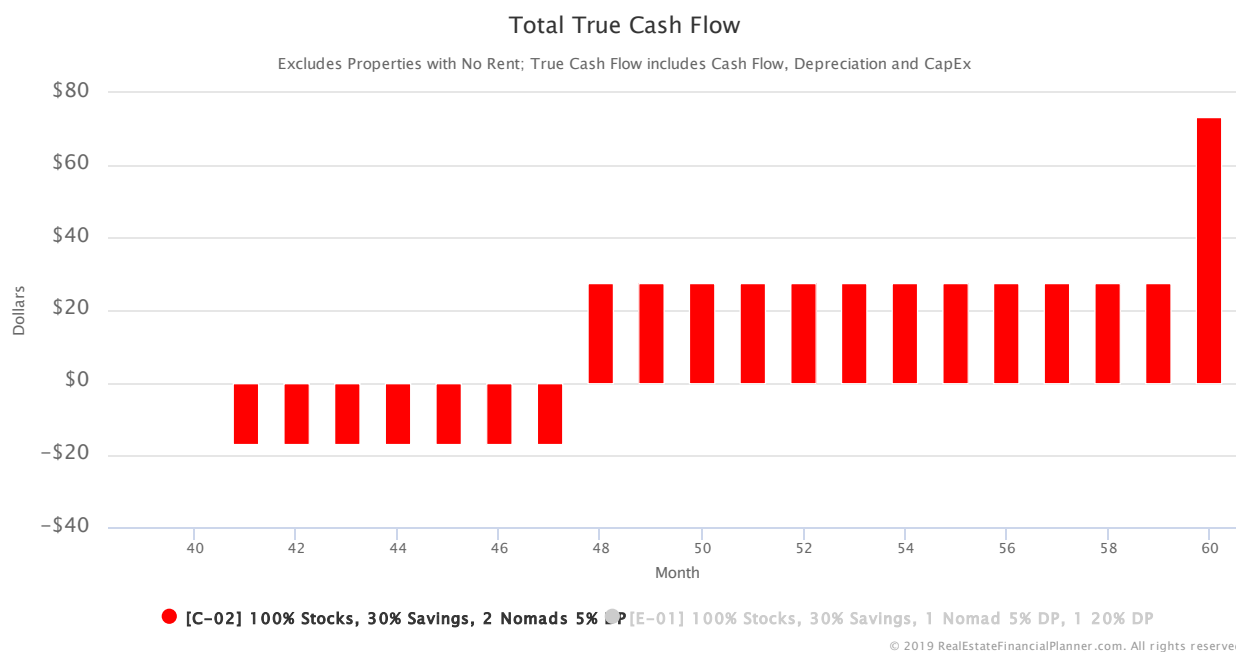
The interest rate of the mortgage is a factor in how quickly a mortgage will be paid off and the slope of this curve. Since the 20% down payment mortgage has a higher interest rate, these curves are not the same.

Let me clarify with another example. If you have two 30-year-mortgages started on the same day they will both be paid off 30 years from when they start. However, if they have two different interest rates, they will have different payment amounts. And, their remaining balances at different months during the loan repayment period will be different. For example, they will have different amounts owed at the halfway point.

## Cash Flow

What about cash flow? Since I already showed you the cumulative negative cash flow generated by the rentals when I discussed the total amount invested, you should already know that both Nomad™ and 20% down will have negative cash flow in this situation. What if we take into consideration cash flow from depreciation though?

If you recall, True Cash Flow™ is cash flow plus cash flow from depreciation minus capital expenses. So, the chart below shows the Total True Cash Flow™ of just the Nomad™ property when it first becomes a rental.



As you can see, there is a period where even with the cash flow from depreciation you have less than \$20 per month in negative cash flow for a few months. Once you renew the first lease, cash flow should improve, and it should be slightly positive with cash flow from depreciation at that point.

In the next chart, I will show you a longer period where we add in the 20% down payment rental to compare.

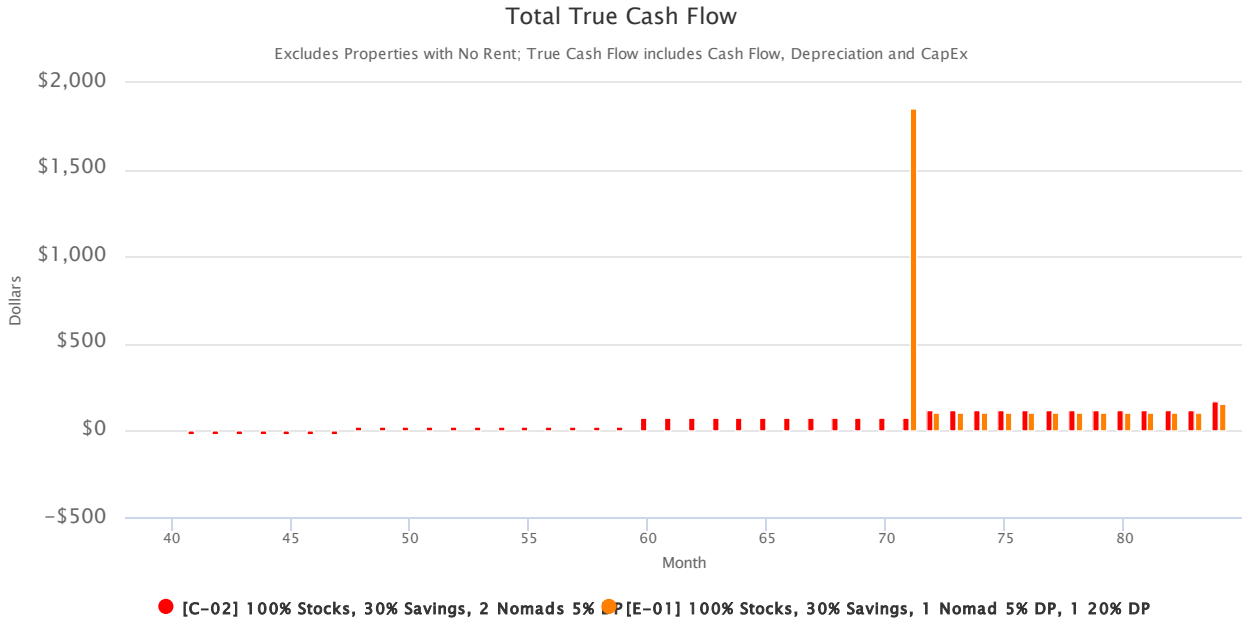
You might notice one month with the 20% down payment property where cash flow is abnormally high. It happens to be the first month we own the property and rent it. Do you know why cash flow is high for the first month?

You might guess that it is the security deposit. That is not it. Since the tenant gets their security deposit back except for any damages they may have made to the property, we don't count that as cash flow. A second guess?

If you guess it is because you make mortgage payments in arrears, a month delayed, you'd be correct.

When you buy a property, you need to have borrowed the money from the lender for 30 days for a payment of interest (and principle) to be due. So, you own the property for 30 days, then, on the first of the next month your payment covering interest and principle for the previous month is due. Taxes and insurance are also due.

So, without a mortgage payment, your cash flow in that first month is abnormally high and that is why that chart appears the way it does.

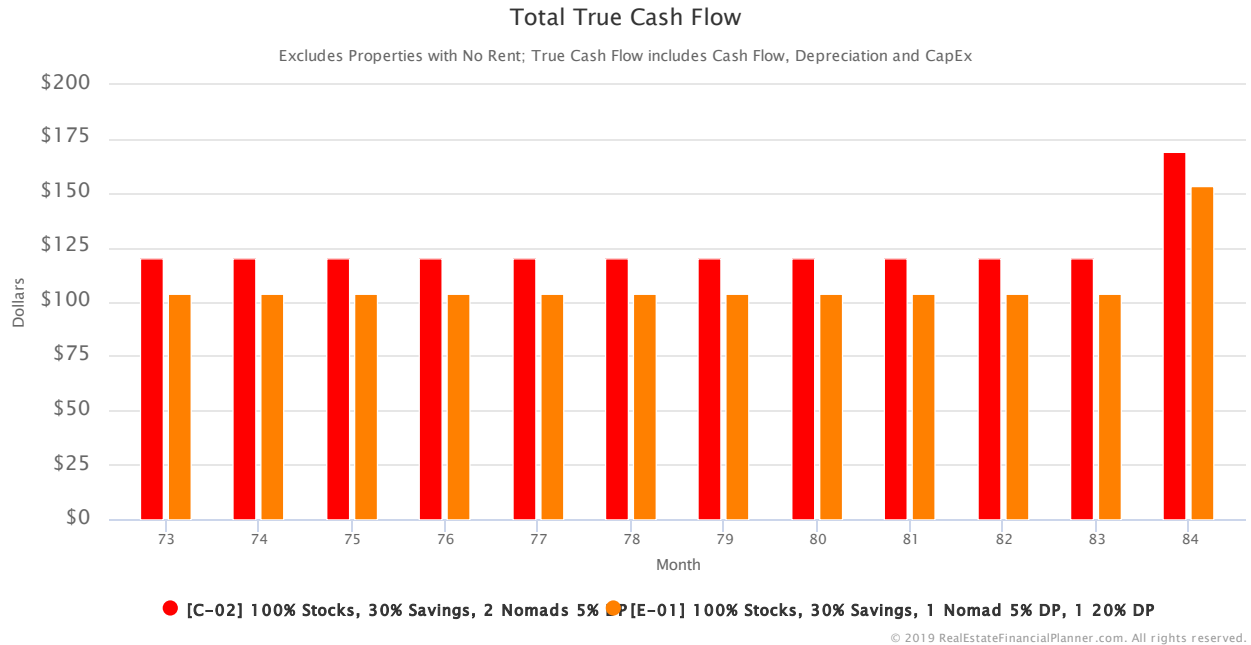


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However, I want to show you the difference in cash flow between the Nomad™ strategy rental and the 20% down strategy rental. It might even be hard to see in the chart above and, since I love charts, I'll even show you another one.

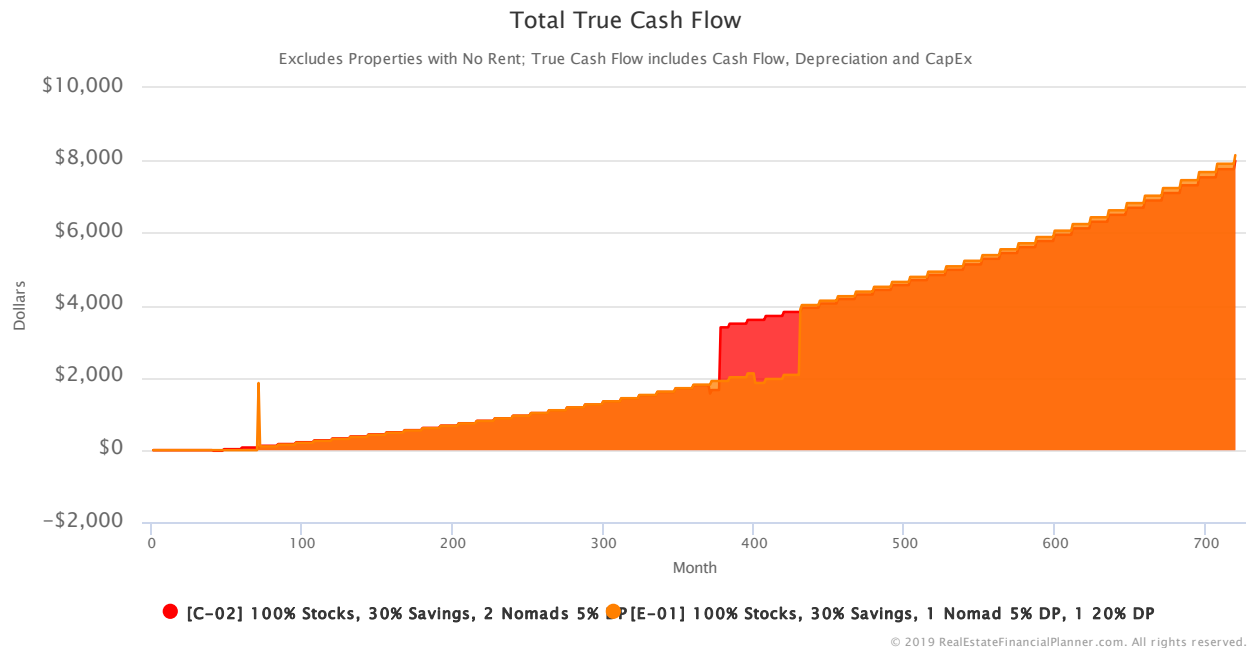
In the chart below, we zoom in to about a year after we buy our 20% down payment rental.

You can see that cash flow on the Nomad™ property is slightly higher than cash flow on the 20% down rental. It is not much, about \$15 or so. But it is still better cash flow than the 20% down rental. We have already discussed why: more expensive property, higher loan amount even with 20% down, and a higher interest rate.



By zooming out to look at a full 60-year view, we can also see that the cash flow for Nomad™ jumps when we pay off that mortgage much earlier than the mortgage on the 20% down property.

Ultimately, once both are paid off, cash flow is very similar.

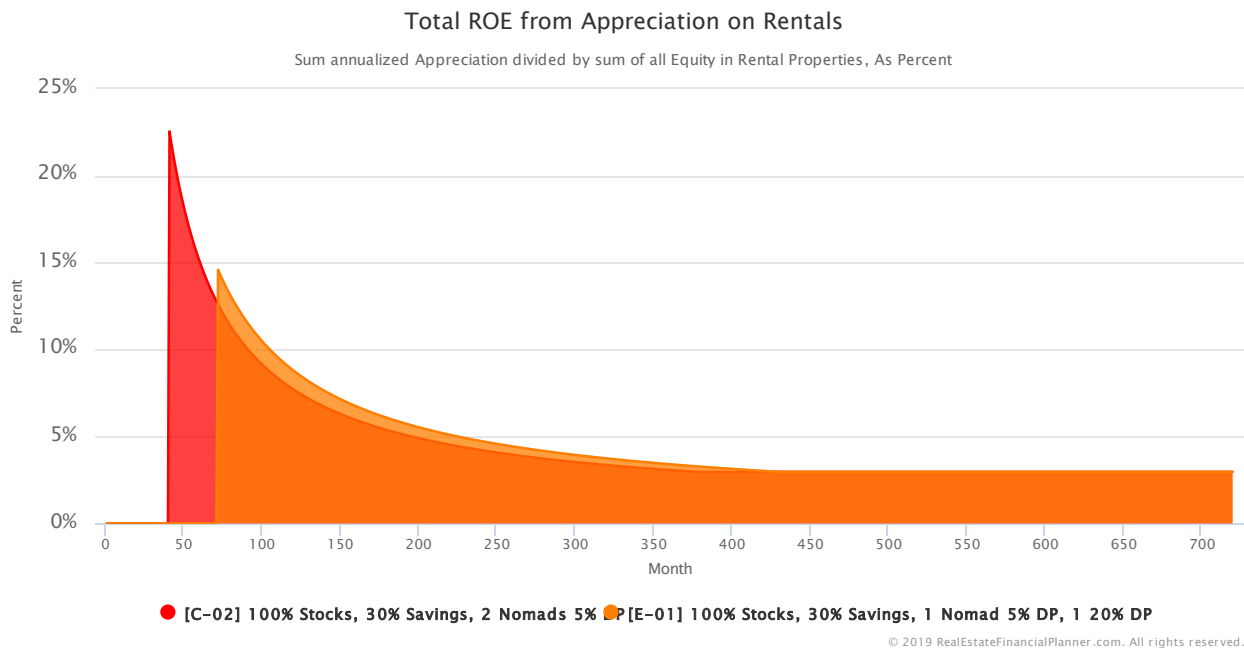


## Return on Equity

How is return on equity impacted when we buy a property later and we put more down on that property to start? Let's look at each of the four areas of return and specifically the return on equity for each.

First, let's start with appreciation. The properties in both Nomad™ and 20% down are appreciating at the same 3% rate. And since they are the same property worth the same amount, that means they are appreciating at the same dollar amount per year as well.

The primary difference between the two scenarios then is really the denominator, or the equity part of the calculation. As you can see in the chart below, there is a much higher and earlier return on equity from the rentals because you both bought earlier and put less into the deal to begin with.



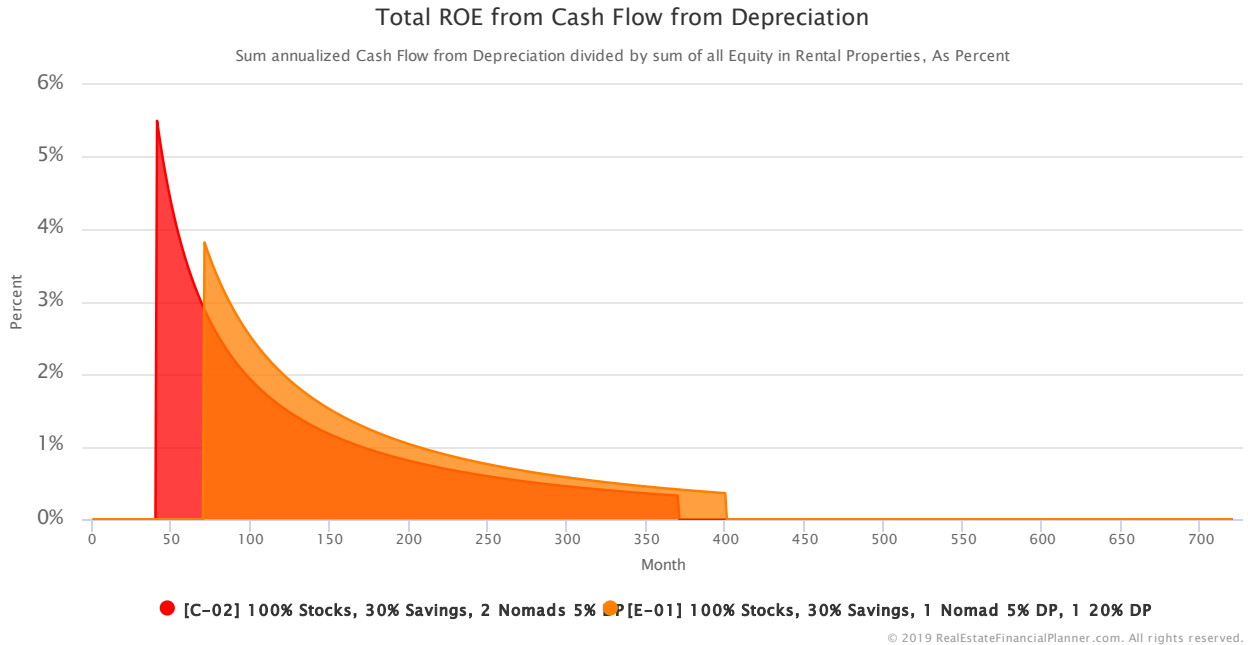
Eventually, the properties both get paid off and you see the exact same return on equity for each.

We might expect something similar with return on equity for cash flow from depreciation.

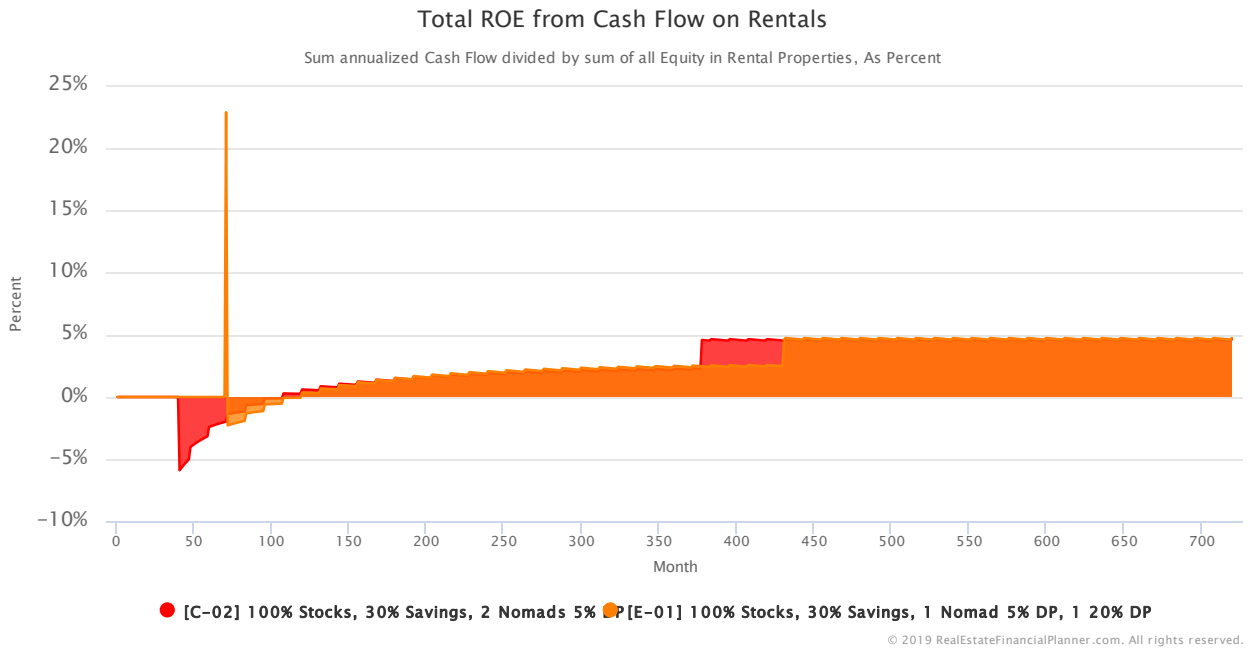
Your cash flow from depreciation is based on your purchase price and your tax rate. If your tax rate is the same (which they are for these models), the only factor then is really what you initially paid for the property minus the cost of the land. The more expensive the building, the more you can depreciate and therefore the more cash flow from depreciation you can get from the property.

In the chart below, you can see that with Nomad™ you get cash flow from depreciation early and since you put less down, you get a higher return on equity from it.

When you wait to buy a 20% down rental, you start getting cash flow from depreciation later and since you put a larger amount down, your equity is greater than it would be for a 5% down property.

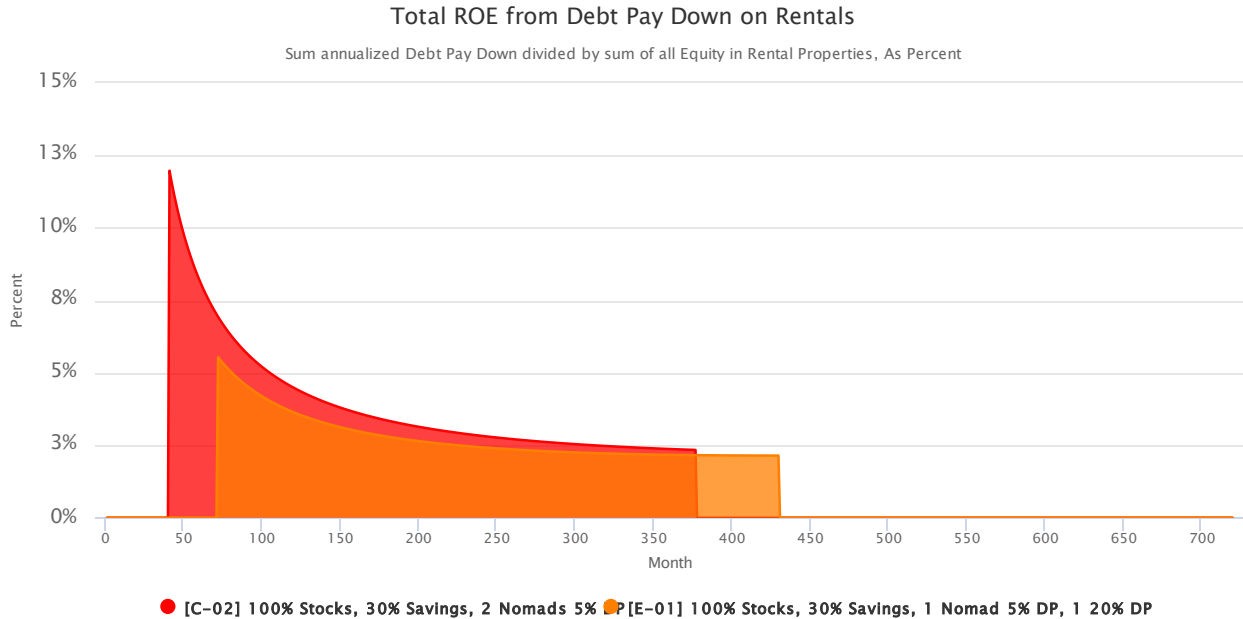


How about return on equity from cash flow? Well, since each starts out with negative cash flow, you have a negative return on equity at first. When you put a smaller amount down, this negative return is amplified, so the return on equity for 5% Nomad™ is greater than the return on equity for the 20% rental when you first buy that one. Then, over time both do increase and become very similar as shown in the chart below.



Eventually, the loan for the Nomad™ gets paid off and you see a bump in return on equity. However, the 20% down strategy is not far behind and when it is paid off the return on equity from cash flow is very similar when comparing the two strategies.

What about return on equity from paying down the mortgage? Same story. You get the return on equity earlier and it is higher with Nomad™. And return on equity from debt paydown starts later and yields a lower return with the 20% down strategy. This is shown in the chart below.



## Risk

Of the two strategies, Nomad™ and 20% down, which one is riskier?

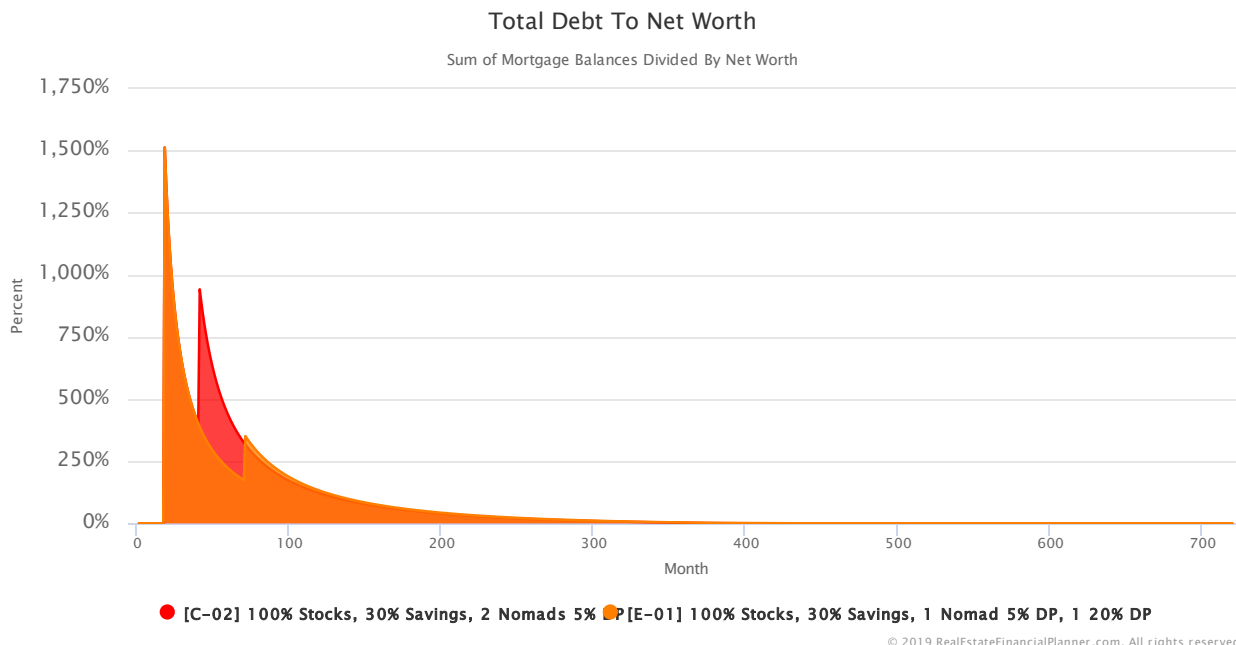
The cash flows are similar so their Rent Resiliency™ profiles are similar, but their debt to net worth profiles are different.

If we look at the chart of debt to net worth below, you can see that the risk for the first purchase in both scenarios is the same. You are buying a property with a 5% down payment while you have very little net worth. That's the shared first peak in the chart below.

However, the risk profiles of these two scenarios diverge at this point. With Nomad™ you take on a decent amount of risk again quickly. In fact, you increase your risk from about 400% back up to 900% or so by purchasing a second property with 5% down quickly.

Compare this to the purchase of the second 20% down payment rental. Right before the second purchase, your debt to net worth risk measurement had been reduced to about 200%, but bumped back up to only 300% or so. That is far less risky than the jump back up to 900% with Nomad™.





This brings up another dimension to discuss: Timing.

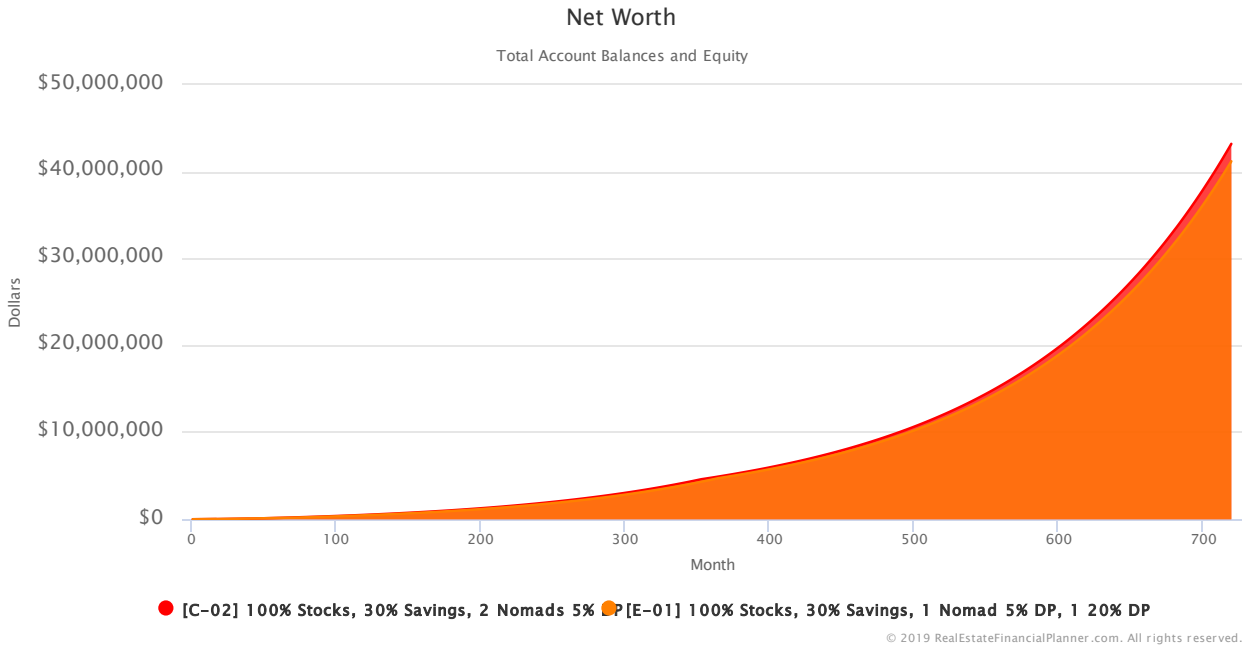
In theory, one might argue the time to take on more risk is earlier in your life when you have the time to correct and learn from mistakes.

It is interesting to point out that when you do buy your second 20% down payment rental property, your risk rises above your then current risk level for having already bought the two Nomad™ properties. Meaning if you look at a snapshot of debt to net worth just after buying the 20% down payment property, the Nomad™ who took the bigger risk earlier and survived has a slightly lower risk measurement than someone who just added a second property with more down payment later.

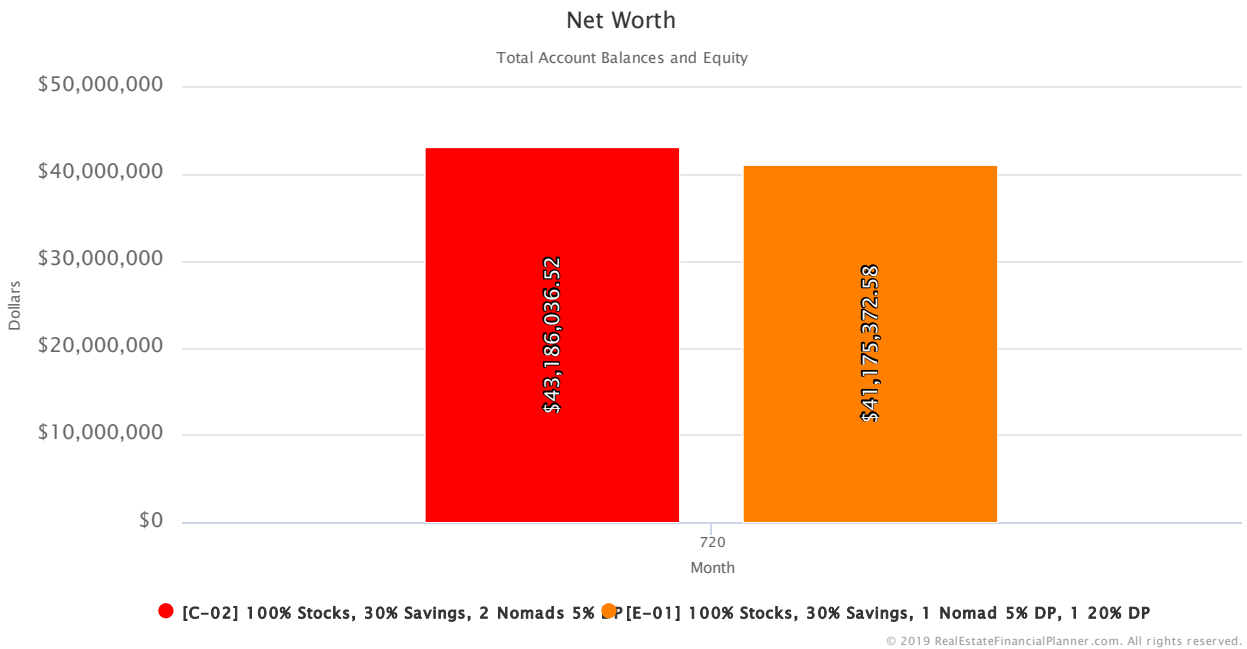
### Net Worth

So, of the two strategies, which one gives you a higher net worth?

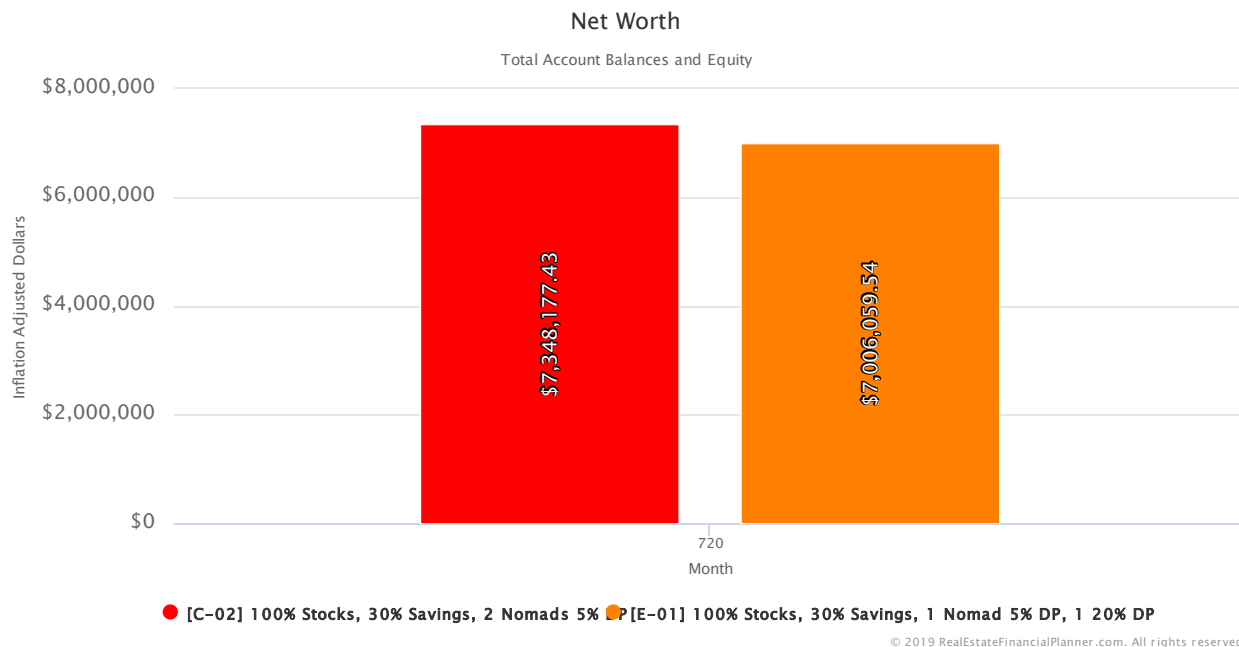
In the chart below you can see the power of buying a property sooner. You get a leveraged asset that can grow in parallel faster with the Nomad™ strategy. This is largely why you end up with a higher overall net worth with the Nomad™ strategy over the 20% down strategy.



What is that difference in month 720, year 60? It turns out to be about \$2 million in inflated dollars.

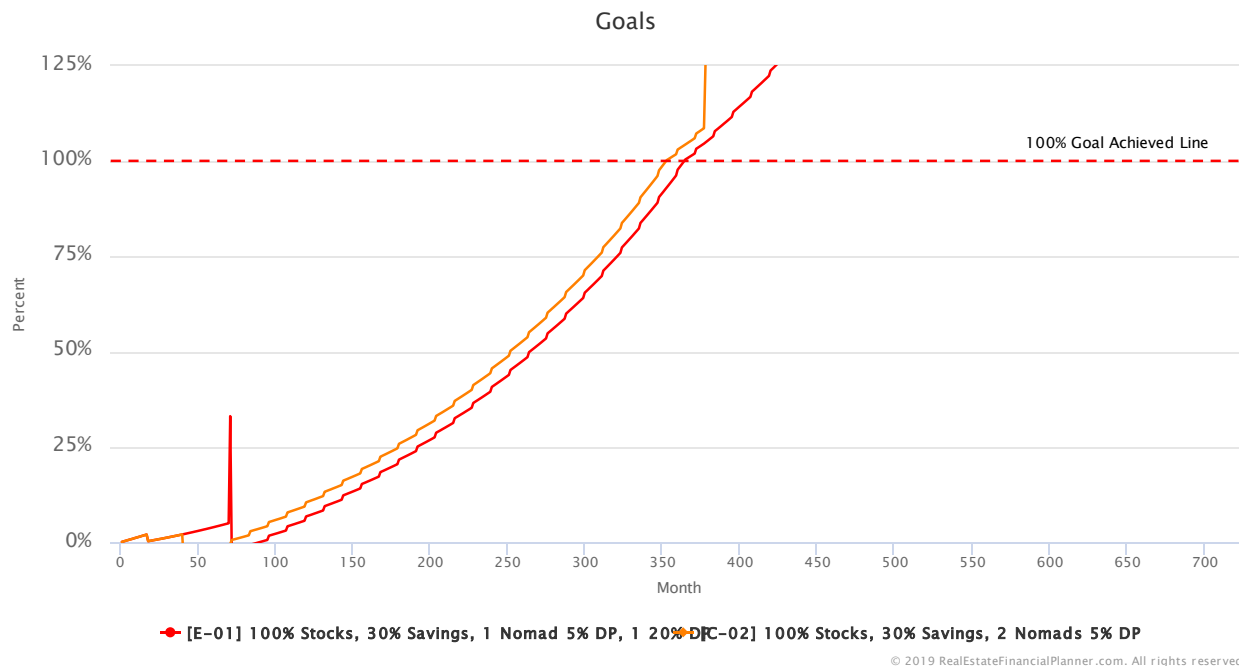


If we adjust back to today's dollars, the difference is a tamer \$340,000 or so. Still, that is a significant difference for just moving once.

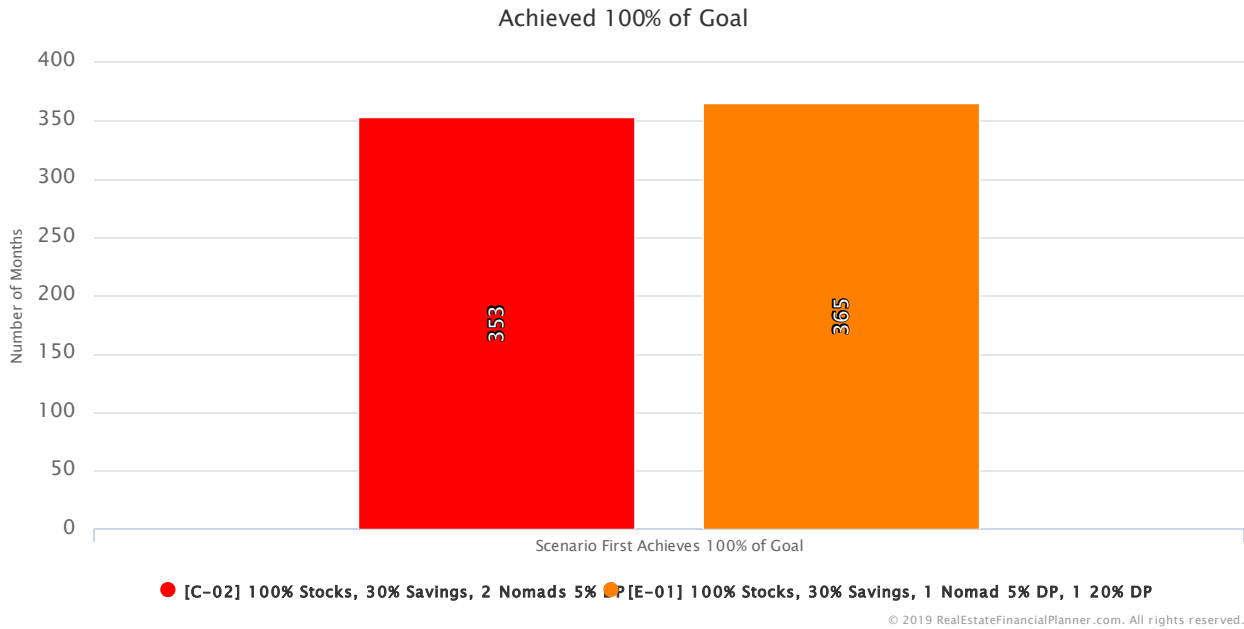


## Goal of Financial Independence

I suspect you are most concerned with when you achieve financial independence and can live your passion. And that makes sense to me. The chart below shows the two scenarios and how they compare to getting you to your FILYP date.



If you want to see what month each strategy hits your financial independence date, when your income from your rentals and the safe withdrawal rate from your stock market accounts can support your target income in retirement, that chart is below.



It turns out you can still hit your financial independence date faster by doing Nomad™. You end up being FI a full year faster by moving once. Move once = financial independence a year earlier.

## Buying More 20% Down Payment Rentals

But does this change if you buy more than one 20% down payment rental?

To answer this question let's look at the outcomes of scenarios in which you buy between one and ten rental properties and compare how quickly you reach FI if you follow the Nomad™ strategy versus if you purchase 20% Down rental properties. Remember, one rental is what we've been comparing above.

- 1 Rental: FI in 353 months with Nomad™ vs 365 months 20% Down
- 2 Rentals: FI in 331 months Nomad™ vs 354 months 20% Down
- 3 Rentals: FI in 314 months Nomad™ vs 348 months 20% Down

Buying additional Nomad™ rentals continues to get us to FI faster with each property. But if you look below you can see that adding a fourth or fifth 20% Down rental has no impact on when you reach FI. So, since it doesn't speed up your path to FI there's no point in buying additional 20% down rentals, right? Wrong. Purchasing additional 20% Down rental properties will still increase your monthly income in retirement and thus afford you a higher standard of living.

- 4 Rentals: FI in 301 months Nomad™ vs 348 months 20% Down
- 5 Rentals: FI in 299 months Nomad™ vs 348 months 20% Down

When Nomading™, after the fifth rental, purchasing additional rentals no longer shortens the time it takes to achieve FI. However, your standard of living still goes up with each rental you buy.

- 6 Rentals: FI in 288 months Nomad™ vs 348 months 20% Down
- 7 Rentals: FI in 288 months Nomad™ vs 348 months 20% Down

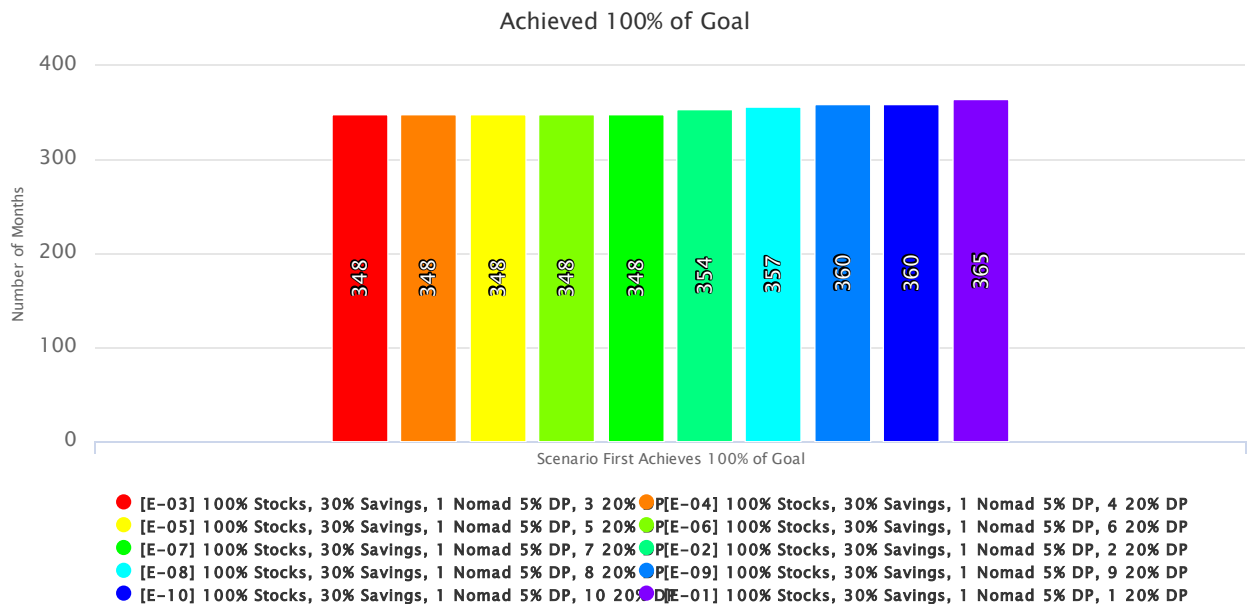
For both Nomad and 20% Down your standard of living is still improving. At this point though, adding another 20% down rental actually slows you down on your path to FI.

- 8 Rentals: 288 months Nomad™ vs 357 months 20% Down

Purchasing a ninth 20% down property makes your FI date another three months slower but continuing to buy additional properties no longer impacts when you achieve FI. However, your standard of living continues to improve from the increased cash flow from each rental property.

- 9 Rentals: 288 months Nomad™ vs 360 months 20% Down
- 10 Rentals: 288 months Nomad™ vs 360 months 20% Down

The chart below shows the number of months it takes to achieve your goal of FI for each version of a 20% down payment scenario buying one through 10 rentals with 20% down plus an owner-occupant with 5% down payment.



What do you want to do? The fastest strategy is still doing Nomad™ seven times or more to get at least six rentals. The more you do beyond seven times does not increase your speed to financial independence, but it does ultimately improve your standard of living over time once you get there.

Are there other ways you can speed up the Nomad™ strategy to make it faster?

This is what we will look at next.

## Model It Yourself

If you want to copy any of the 20% down payment scenarios to your own Real Estate Financial Planner™ account and adjust the assumptions, you can use the links below.

- 100% Stocks, 30% Savings, 1 Nomad 5% DP, 1 20% DP  
<http://refp.io/635>
- 100% Stocks, 30% Savings, 1 Nomad 5% DP, 2 20% DP  
<http://refp.io/636>
- 100% Stocks, 30% Savings, 1 Nomad 5% DP, 3 20% DP  
<http://refp.io/637>
- 100% Stocks, 30% Savings, 1 Nomad 5% DP, 4 20% DP  
<http://refp.io/638>
- 100% Stocks, 30% Savings, 1 Nomad 5% DP, 5 20% DP  
<http://refp.io/639>
- 100% Stocks, 30% Savings, 1 Nomad 5% DP, 6 20% DP  
<http://refp.io/640>
- 100% Stocks, 30% Savings, 1 Nomad 5% DP, 7 20% DP  
<http://refp.io/641>
- 100% Stocks, 30% Savings, 1 Nomad 5% DP, 8 20% DP  
<http://refp.io/642>
- 100% Stocks, 30% Savings, 1 Nomad 5% DP, 9 20% DP  
<http://refp.io/643>
- 100% Stocks, 30% Savings, 1 Nomad 5% DP, 10 20% DP  
<http://refp.io/644>

If you do end up implementing one of these scenarios, I would strongly advise you to do full Monte Carlo testing as we described previously.

To find and copy any of the other scenarios covered in this book, follow the link below.

- <https://realestatefinancialplanner.com/filyp/>

## **Path 6: House Hacking and Side-Hustles**

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A \$350,000 property for you to live in by yourself might be a significant luxury. In our modeling you are buying a \$350,000 property as a Nomad™ and living there for at least a year while you save up to buy your next property. Do you really need a three or, more likely, four-bedroom home to live in by yourself? Probably not.

What if you got yourself a roommate that contributed hundreds of dollars per month toward your mortgage payment? Any extra money you collect from a roommate would look like you got a raise at work. Since you've committed to living at a certain fixed standard of living already, all the extra money from roommates, after paying taxes, would go straight to additional savings.

It would allow you to save for your next down payment and closing costs faster. And, if you are done buying houses, it can be invested in the stock market toward your financial independence.

When you get a roommate or collect income on a property you are living in, this is called house hacking. Some folks house hack by buying a duplex, triplex or fourplex. You can buy a multi-family property easily with your first purchase and still Nomad™ by getting an FHA loan. FHA financing allows you to buy a single-family home, duplex, triplex, or fourplex with just a 3.5% down payment. With rare exception, you can only have one FHA loan at a time, so you can only do it once. If you served in the military or otherwise qualify for a Veteran's Administration (VA) loan, you could buy a second or maybe even third duplex, triplex, or fourplex with VA financing. You will want to talk in detail to a lender that understands the Nomad™ model and the idea of house hacking to get some extra income from your property to do loan planning.

Other folks house hack by collecting income on their properties in other ways. For example, they may rent out an RV parking space on the side or back of their property. They may own their own RV, park it on their property, and allow people to rent that by the night, week, or month. They may rent out their garage or shed as storage. There are several creative ways to collect extra income on a property you own. Depending on what strategy you choose, you should always check the local rules and regulations in your area to make sure you are in compliance, and in some cases, you may need to collect sales tax for short term rentals. When in doubt, check with your attorney and accountant.

Most people, when they refer to house hacking though, are referring to getting roommates or buying a multi-family property and having roommates or tenants pay part, or—in some cases—all of their house costs including their mortgage, taxes, insurance, and maintenance.

I will point out that getting a roommate who might pay you \$600 to rent a room in your property is functionally like getting a side hustle that earns you an extra \$600 per month. In both cases you are earning an extra \$600 per month. In both cases you need to pay taxes on that money. In both cases you will likely need to do a little bit of work to earn the money.

Some people would argue that having roommates might be an inconvenience. I have many clients that have found the opposite to be true. They have found true friends and help in running and maintaining the house in their roommates.

Regardless of whether you decide to get a roommate (or two or three) or you decide to get a side hustle to bring in \$500 to \$2,000 per month, what impact does that have on your ability to achieve financial independence and be able to live your passion?

### Saving Different Percentages of Your Income

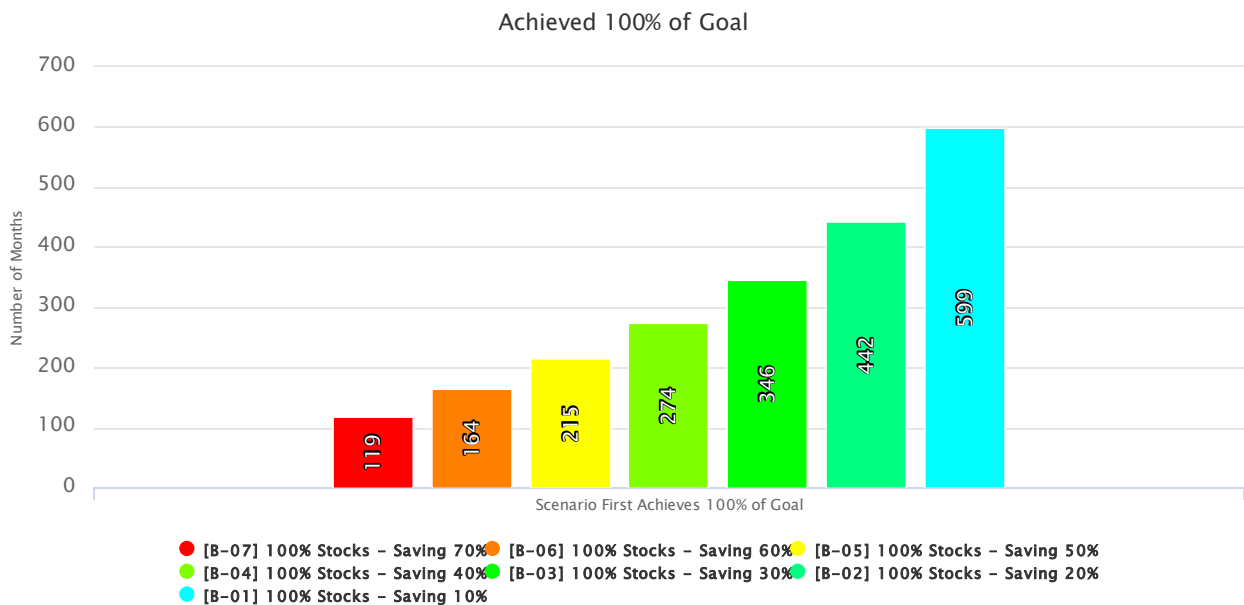
If you recall, way back in chapter two, we discussed the impact of being able to save a larger percentage of your income and the impact this had on achieving financial independence.

In the last few chapters, we have been assuming you are saving 30% of your income, or about \$1,750 per month in the first month. If you get a roommate or side hustle that brings in an extra \$600 per month and pay taxes on it, that’s almost as if you are saving an extra \$450 per month. It’s like saving an extra 7.71% of your base salary from work because you increased your income through a roommate or side hustle and saved that. Instead of saving 30% of your income, now you are saving almost 38% of your income.

If you get two roommates or increase your side hustle to \$1,200 per month, that’s like saving more than 15% of your income. You’ve increased your savings rate from 30% to just over 45%.

If you get a third roommate or increase your side hustle to \$1,800 per month, that’s like saving more than 23% in addition to the 30% you are already saving. That means you are now saving more than half of your income.

I showed you a chart earlier where we looked at the impact of various savings rates on your ability to achieve financial independence and live your passion if you just invest in the stock market.

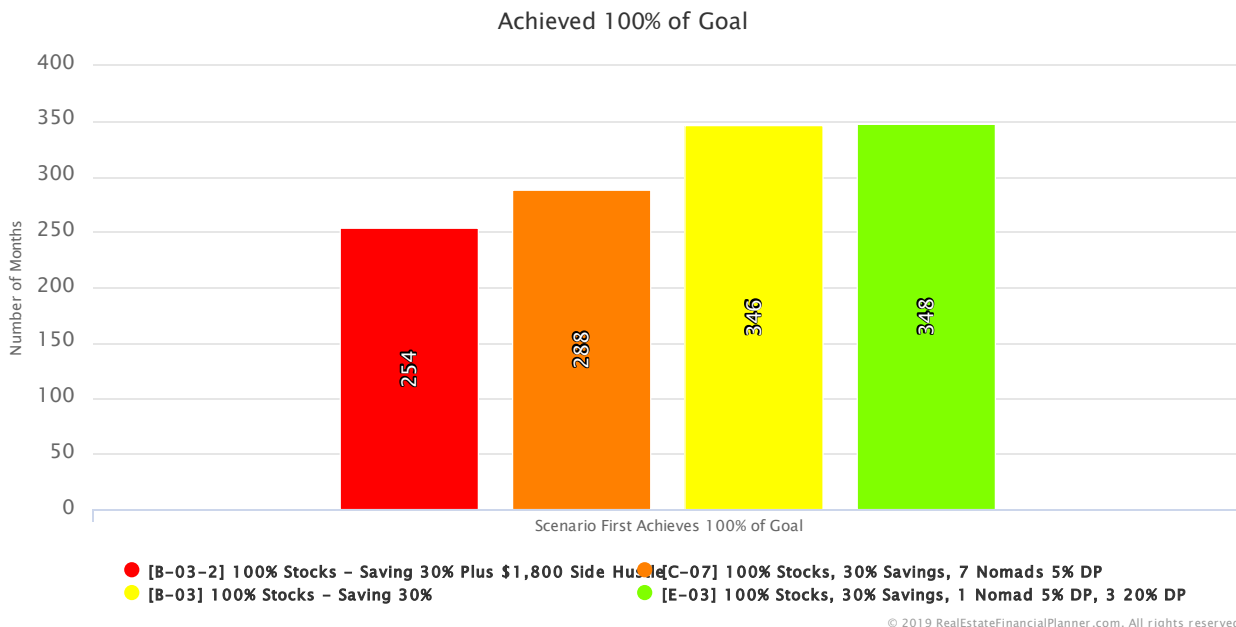




At a 50% savings rate, you could achieve financial independence in a mere 215 months. Realize though that we also reduced your target monthly income in retirement to be just 50% of your original income. That is a different, lower standard of living than you'd have saving 30% and living on 70% of your income.

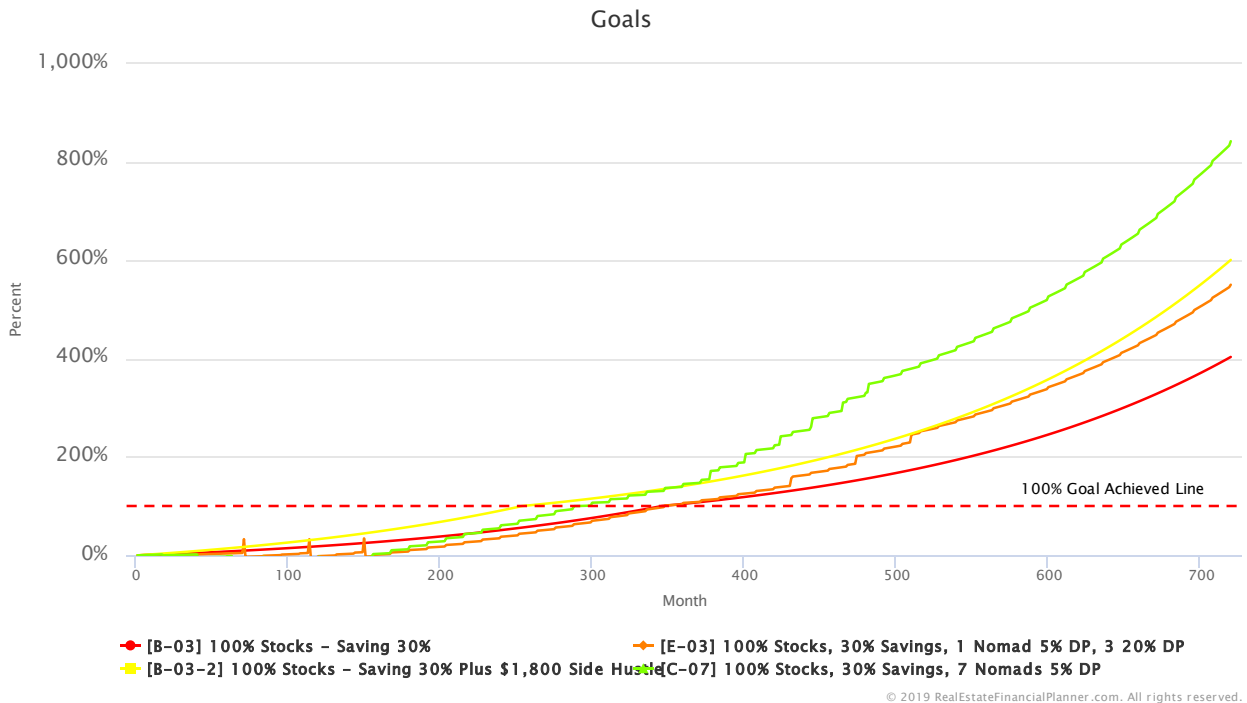
If we go back and keep the same 70% standard of living but add an extra \$1,800 per month side hustle to the earlier scenario where you were investing just in stocks, it turns out it takes you 254 months to achieve financial independence.

The following chart shows a quick comparison of some of the better performing scenarios we have covered up to this point.



It appears that extra \$1,800 in side hustle investing 100% in stocks seems to be the scenario that gets you to financial independence fastest. It is almost three years faster than traditional Nomad™ with seven properties (six rentals). It is 92 months faster than just saving 30% and it is 94 months faster than buying a property to live in then buying three 20% down payment rentals.

It is important to realize this is a one-dimensional answer to the question, though, because it does not account for standard of living once you hit financial independence.



The highest overall standard of living comes from doing Nomad™ seven times. Followed by the extra \$1,800 per month in side hustle with 100% stocks; you are saving a lot more, faster. Then the three 20% down payment rentals. The worst, as you might have guessed, is just saving 30% and investing in stocks.

## 11 Nomads™ With and Without Roommates or Side Hustle

Let's compare four scenarios. First, the scenario we have already covered, where you are doing 11 Nomads™ with no roommates or side hustle.

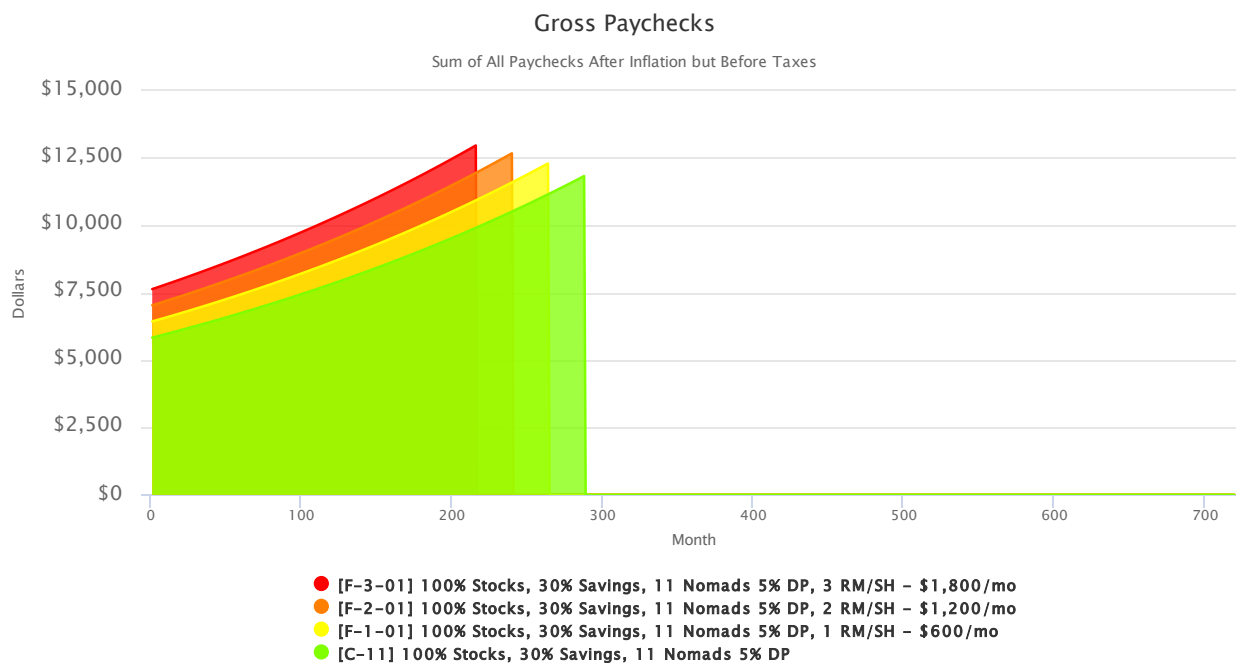
But we will also do the same 11 Nomads™ wherein we will consider getting one roommate or a \$600 per month side hustle. We will also consider two roommates or \$1,200 per month in side hustle. And finally, we will consider you getting three roommates or \$1,800 per month in side hustle.

In each case of having roommates or a side hustle, we assume that you keep your roommates or side hustle until you achieve financial independence and then you stop. The faster you achieve financial independence, the sooner you stop having roommates or the side hustle.

I will chart all four scenarios together as we compare them.

### Gross Income and Amount Saved

We model the rent from roommates or income from a side hustle as another paycheck in the Real Estate Financial Planner™ software. So, we can see the extra income from roommates or side hustle when we view the chart of your gross paychecks.



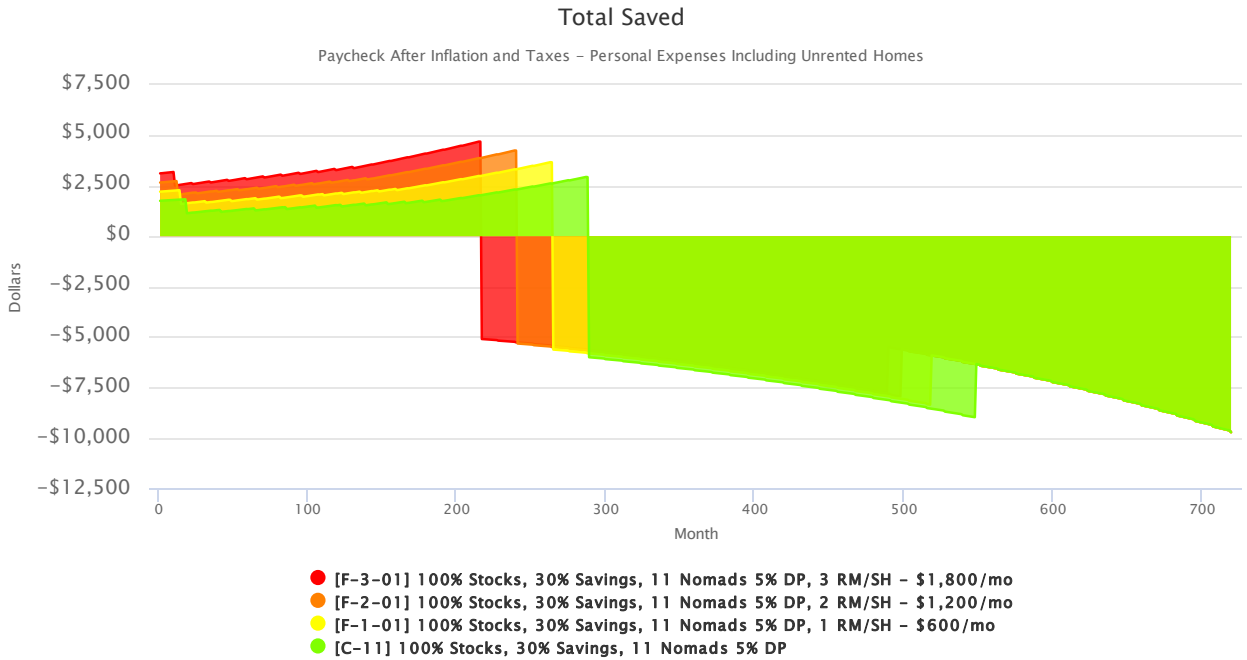
In the chart above you can see the extra income you are receiving in the four different scenarios we set up. You will also notice that once you achieve financial independence, we have assumed that you stop receiving both your regular paycheck from your job and the extra income from your roommates or side hustle.

A side note, but probably one we should explore together and maybe in another separate book: There is probably a version of reality where you could stop working your job even slightly before you officially achieve financial independence, especially if you continue with roommates or your side hustle during that period. For example, if you know that your rental properties will ultimately be increasing in rents, you could start spending some of the cash you have stored in the stock market at a rate greater than your official safe withdrawal rate. You realize that the balance in your stock market accounts would be declining by withdrawing more than your safe withdrawal rate, but your real estate assets would still be growing and eventually the rent from the properties (especially as they get paid off) would more than make up for it.

You could play with this model by copying the scenario into your Real Estate Financial Planner™ account and forcing your job income to stop earlier than your financial independence date. Again, probably an entirely separate book but something to discuss over the holidays together.

Back to these four scenarios. I just finished showing you the amount you are bringing in between your job and your roommates or side hustle. But how much are you saving? That is the chart below.

In this chart I show you the exact amount that you are saving in each of the scenarios we are comparing. The more roommate and side hustle income you have the more you save, and also the sooner you achieve your financial independence date and stop saving altogether from these income sources.

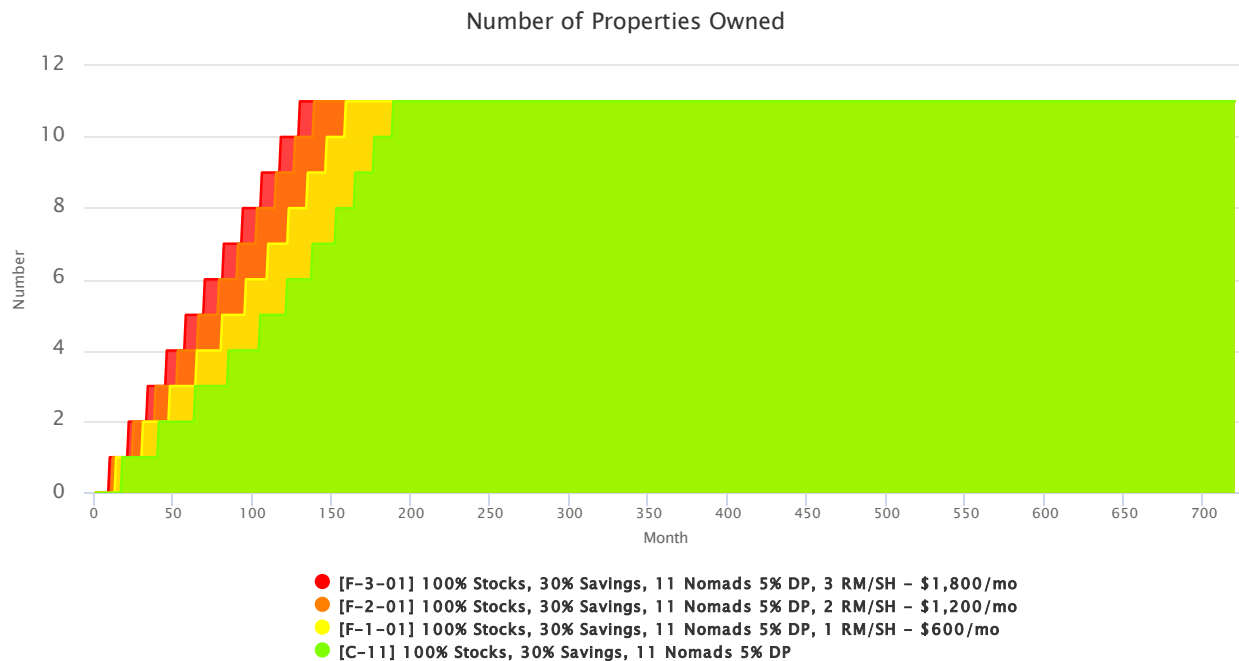


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### Number of Properties Owned and When

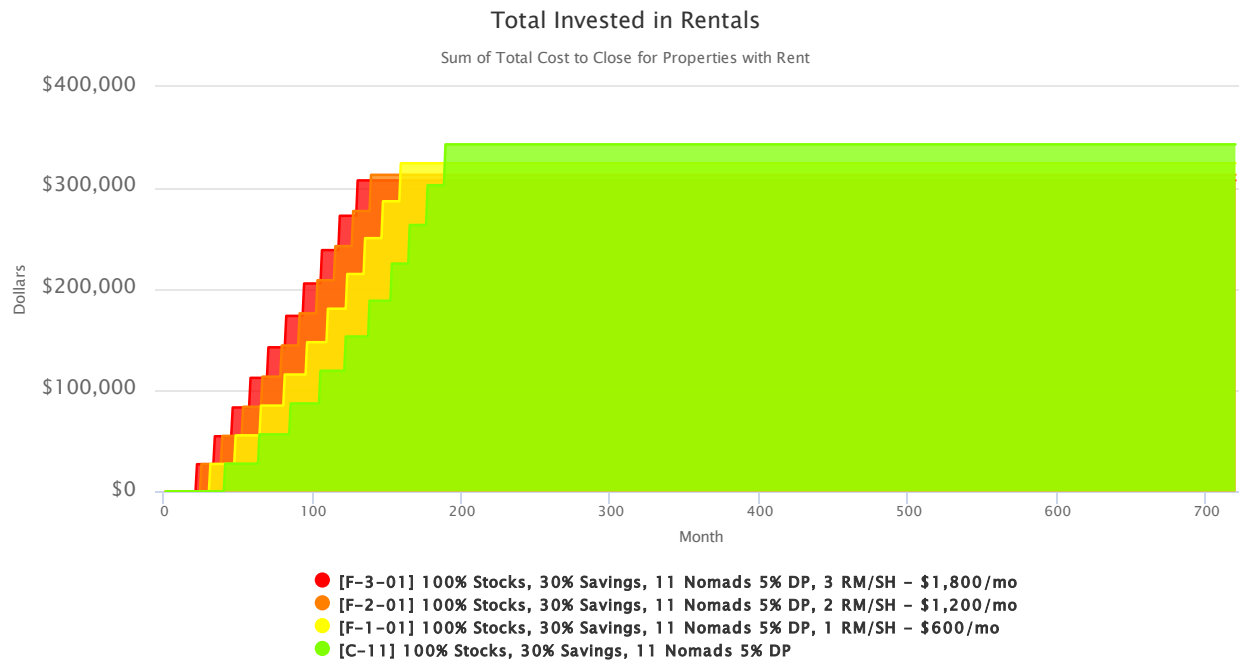
Because you are saving more and sooner by having roommates and/or side hustles, you end up being able to save for your down payments and closing costs faster. That means you end up buying properties faster as well. This is shown in the chart below.

In the chart, you can see when you add properties to your portfolio and the total number of properties you have.



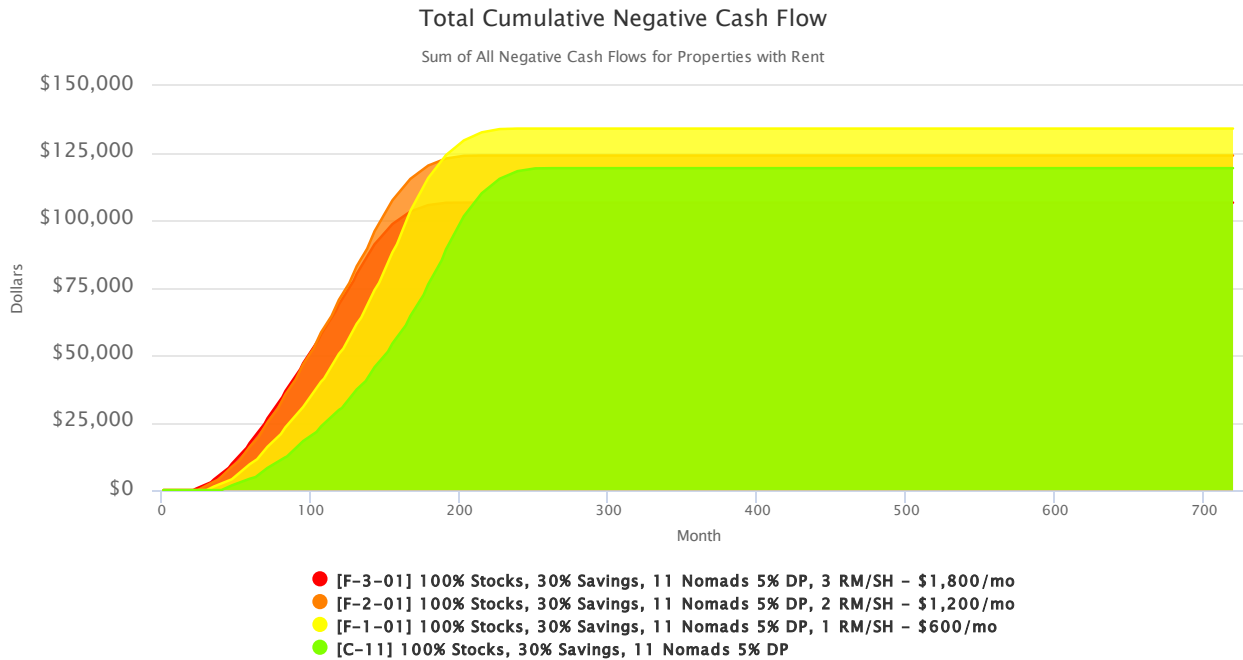
## Total Invested Including Negative Cash Flow

Let's look at a chart showing the total amount you invested to acquire your rentals.



The chart above shows the total of both down payment and closing costs to acquire your rental properties. Since you are saving more and faster by having roommates and/or a side hustle, you buy properties sooner. This means that you buy them when they are less expensive, which means the amount required for your down payments is slightly lower.

What about negative cash flow? This is shown in the chart below.



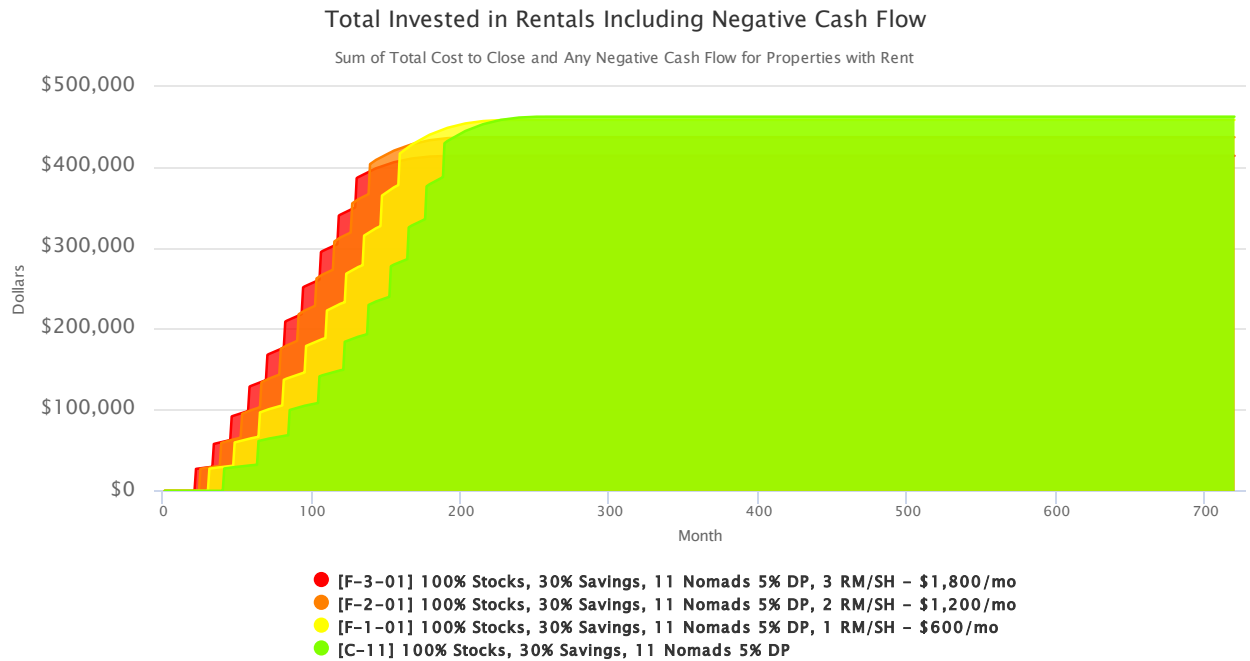
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Before I go into explaining this chart, I want to remind you that most, if not all, of this negative cash flow is offset by cash flow from depreciation. So, you are not coming out of pocket for the amount shown.

Back to the chart, it should not surprise you that buying the properties fastest by having three roommates and/or a side hustle means that you have the least amount of negative cash flow. What might surprise you, as it did me, was that not having any roommates and/or side hustles produces less negative cash flow than having \$600 or \$1,200 per month in extra income. Why? It is because it takes you longer to buy properties with no roommates or a side hustle and that gives the properties you are living in time to generate higher rent before converting them to rentals.

If you would like to see a combination of both the down payments and closing costs plus the negative cash flow summed on one chart, I will show you that next. The chart below displays the total amount invested to acquire your rentals including down payment, closing costs, and any negative cash flow.

When you combine everything, a trend appears, showing that it requires less overall investment with more income coming in from roommates and/or side hustles.



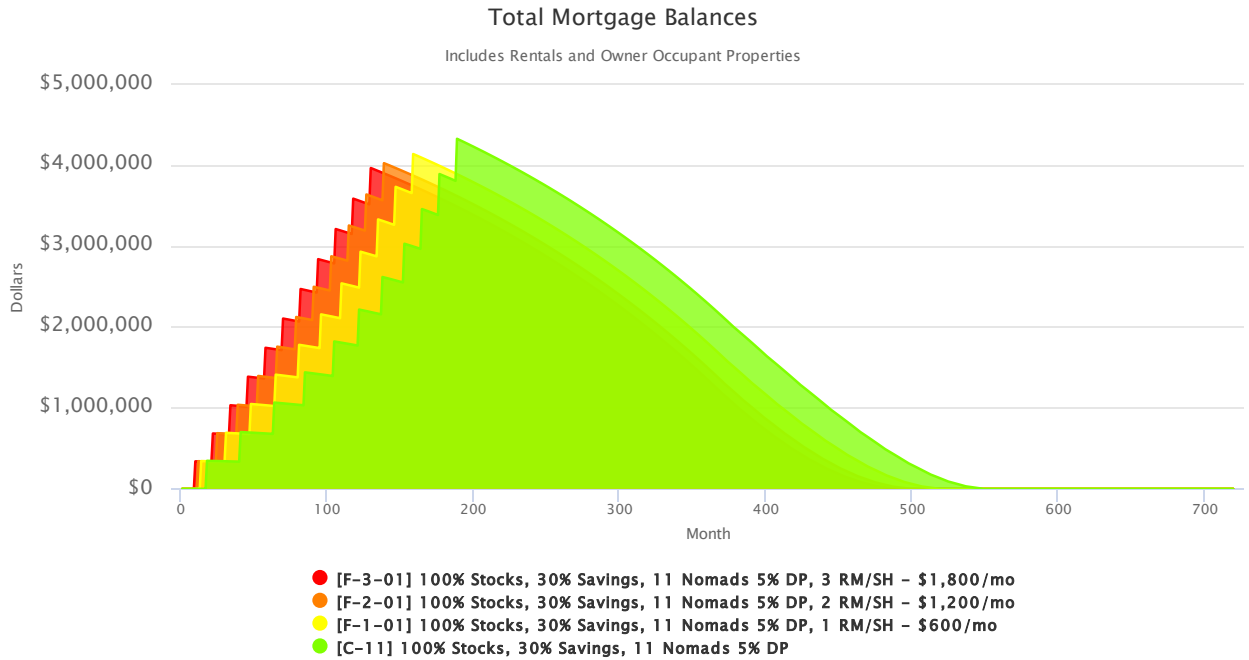
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### Total Mortgage Balances and Payments

The faster you acquire properties, the less expensive the properties are when you acquire them. That also means you will have a lower mortgage balance than if you waited.

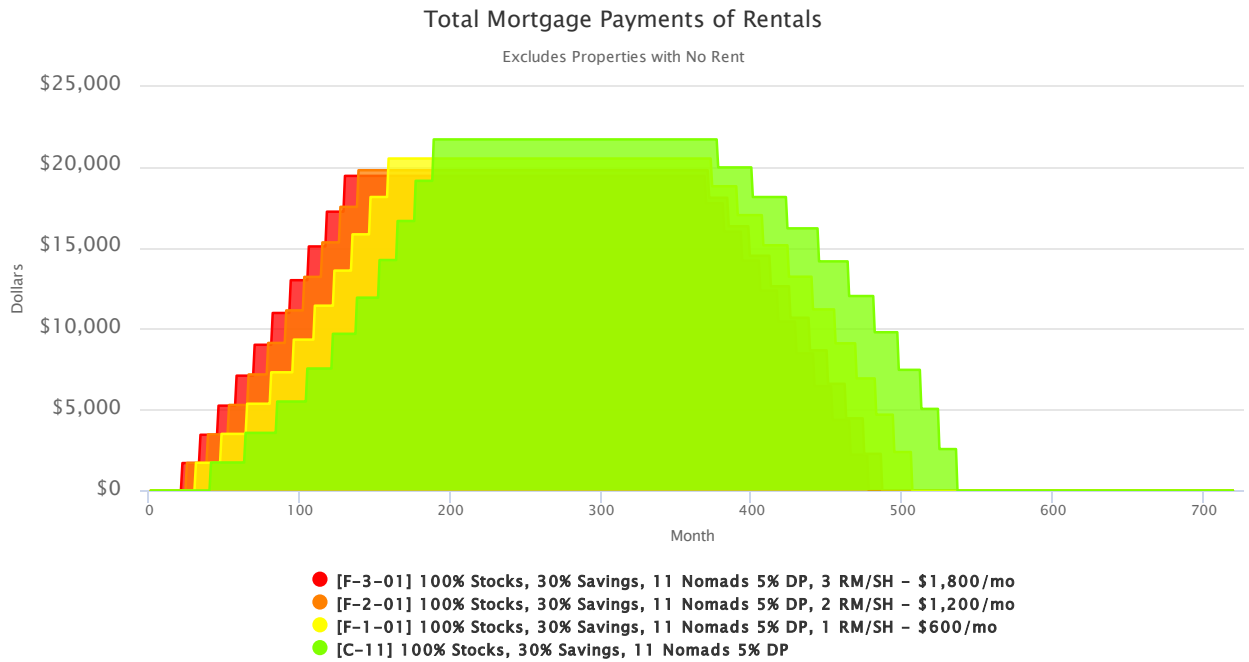
In the chart below, you can see the total mortgage balance for all properties (owner-occupant and rentals).

Since you are getting 5% down payment loans for all properties, the difference shown on the chart is primarily from the price of the property purchased. The chart shows the benefit of buying properties earlier by having the money for down payments and closings costs sooner from roommates and/or side hustles.



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Similarly, since we are assuming that the interest rates are the same for each loan, you can see the benefit in terms of mortgage payments as well in the chart below.



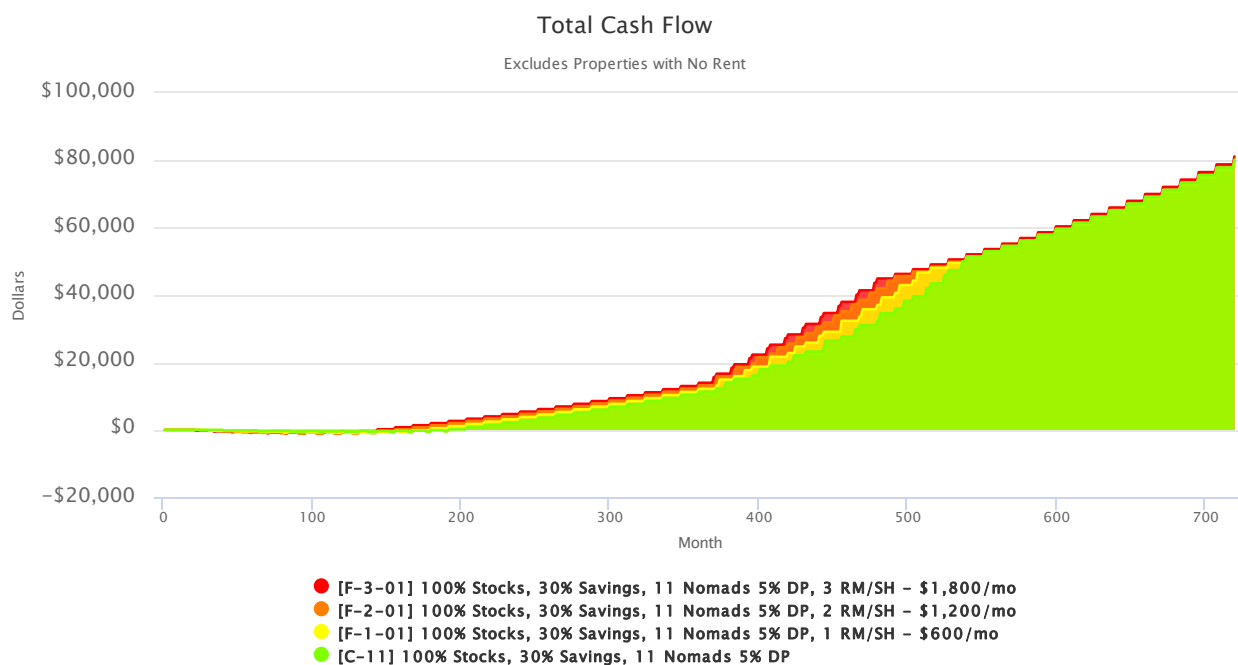
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## Cash Flow

With a slightly better mortgage payment, the cash flow you ultimately get after overcoming the initial negative cash flow is better from being able to buy properties sooner and at lower prices.

It is important for me to note, and for you to realize, that we are not showing your roommate rent and/or your side hustle income on the cash flow charts. We are adding that as an extra “paycheck” in the Real Estate Financial Planner™ software.



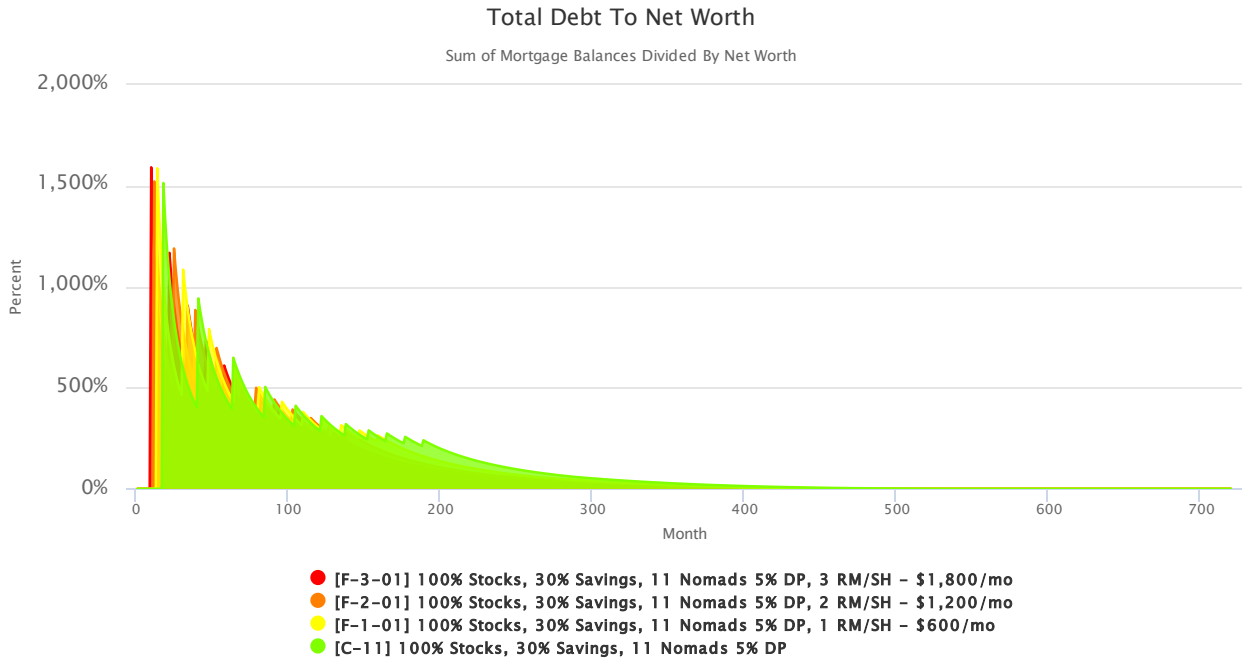
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From the chart above, you can see that eventually, when the properties are paid off, the cash flow from the properties—regardless of the scenario—tend to become essentially the same.

## Risk

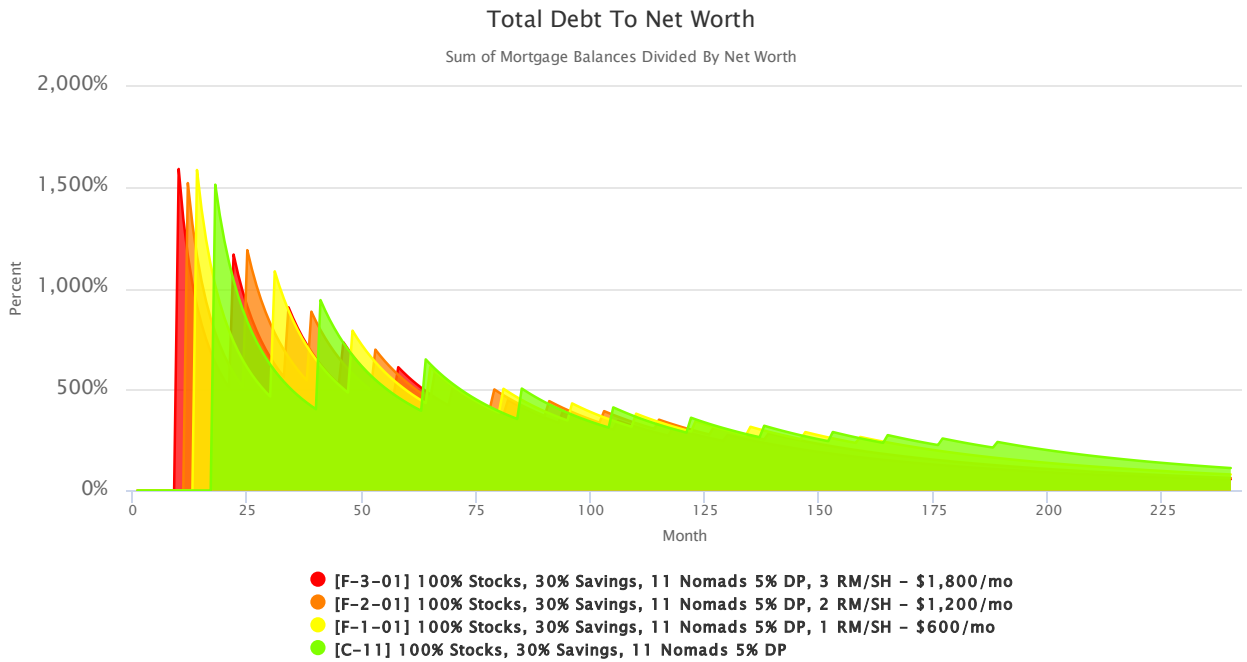
What about risk? Is it riskier to have roommates and/or get a side hustle?

One of our measures of risk has been debt to net worth. Below is the chart of debt to net worth that compares the four scenarios we’ve been discussing.



There are two factors to consider here. First is timing of the risk and the second is the magnitude of the risk.

Let's zoom in a bit on the chart to get a closer look at these factors.

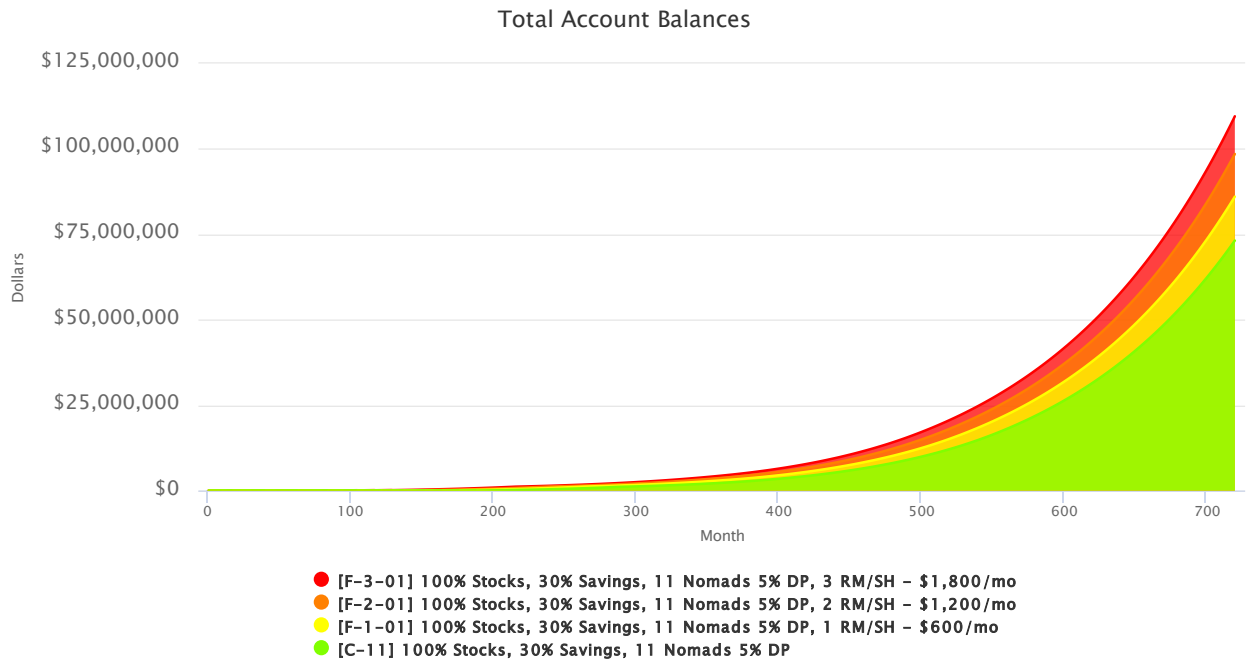


In the chart above you can see that having roommate and/or side hustle income moves your risk up in time. You end up taking on risk earlier. Should something go awry, you have more time to recover.

However, if you do not have roommate and/or side hustle income you end up having slightly higher net worth as you acquire properties later. This means that the magnitude of your risk is lower when you add on more debt to a higher net worth. This would mean that not getting roommates and/or side hustle income would mean lower risk as it slows you down a bit.

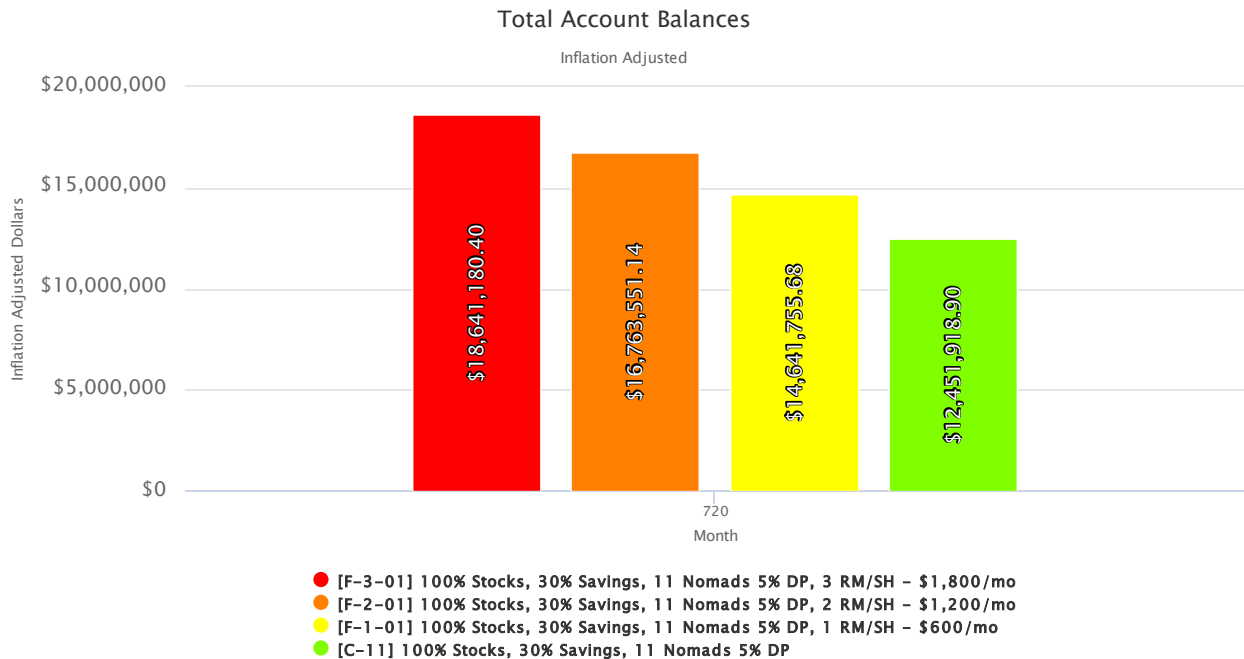
### Stock Market Account Balances

How much difference do roommates and/or side hustles make to your stock market account balance? The following chart shows your total stock market balance comparing the four scenarios.



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While the differences might, at first blush, appear significant in the chart above, that chart is in raw, inflated dollars. If we adjust back for inflation to today’s dollars, the chart below shows the true difference at the 60-year point.



The difference, in today's dollars, between no roommates and one roommate is only \$2 million dollars. Is that a luxury you are willing to pay for? If you get three roommates, it is almost \$6 million more versus not getting roommates at all. Is not having roommates until you achieve financial independence worth \$6 million dollars in today's dollars to you?

Again, these are personal decisions you need to make for yourself.

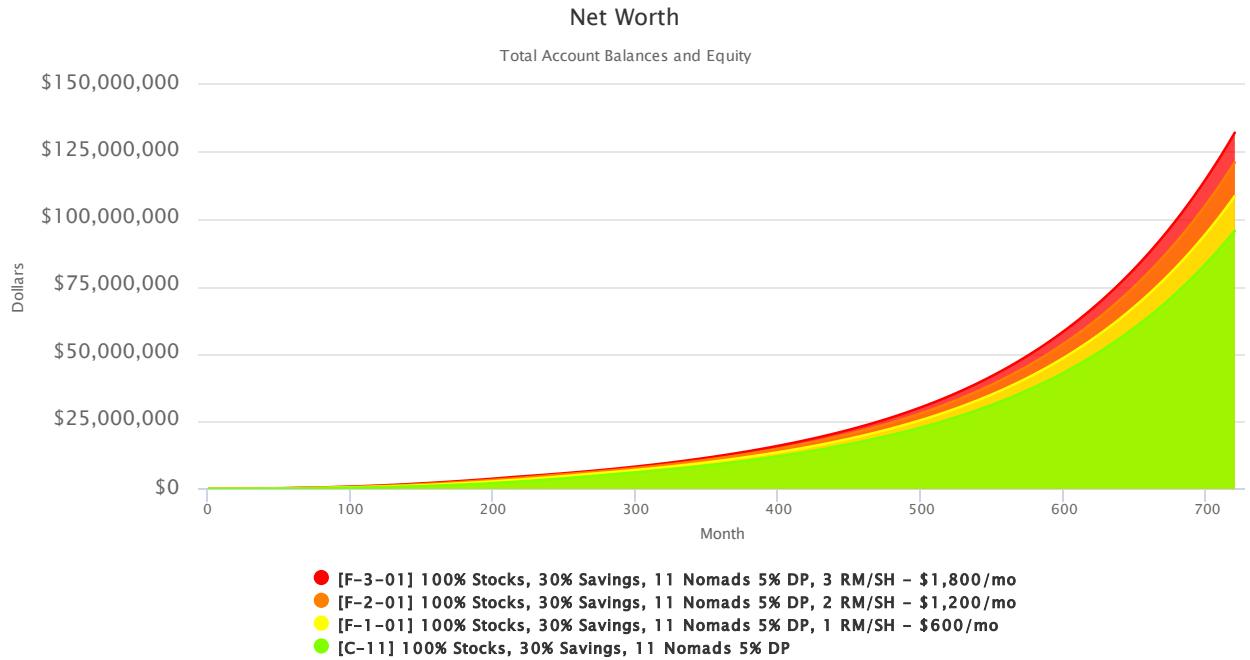
## Net Worth

What impact do roommates and/or side hustles have on your overall net worth? It's more than just your stock market balance alone. It also means buying your properties sooner.

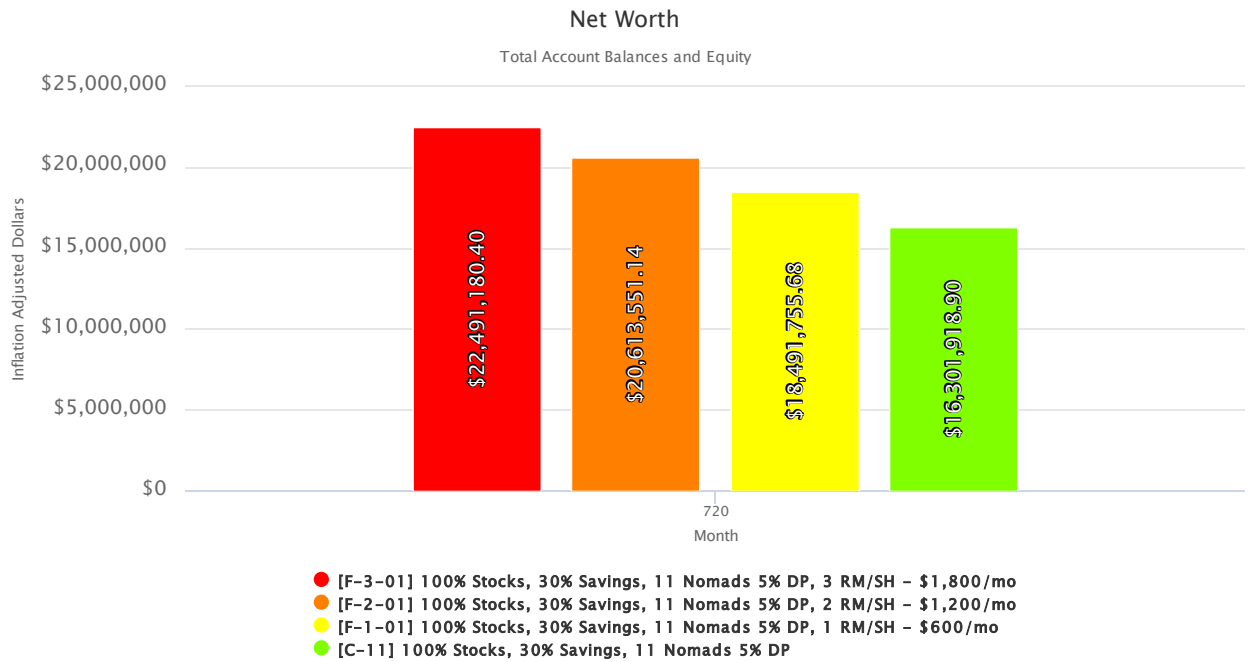
I'll share with you a little secret about how to think about future real estate values in inflated dollars and adjusted back to today's dollars. You buy a \$350,000 property today, and it keeps pace with inflation. Even if the property is worth \$1 million dollars in the future (in inflated dollars), it is still like owning a \$350,000 property today.

So, since we are talking about buying the same 11 properties as a Nomad™ and even though you are buying them at different times, the value of those properties when we adjust back to today's dollars is still \$350,000. That's regardless of when you bought them. Once you've paid off the mortgages on them, they all contribute the same amount to your net worth regardless of when you bought them.

So, the net worth numbers should add the same equity from the 11 properties. We can look at net worth in the chart below.



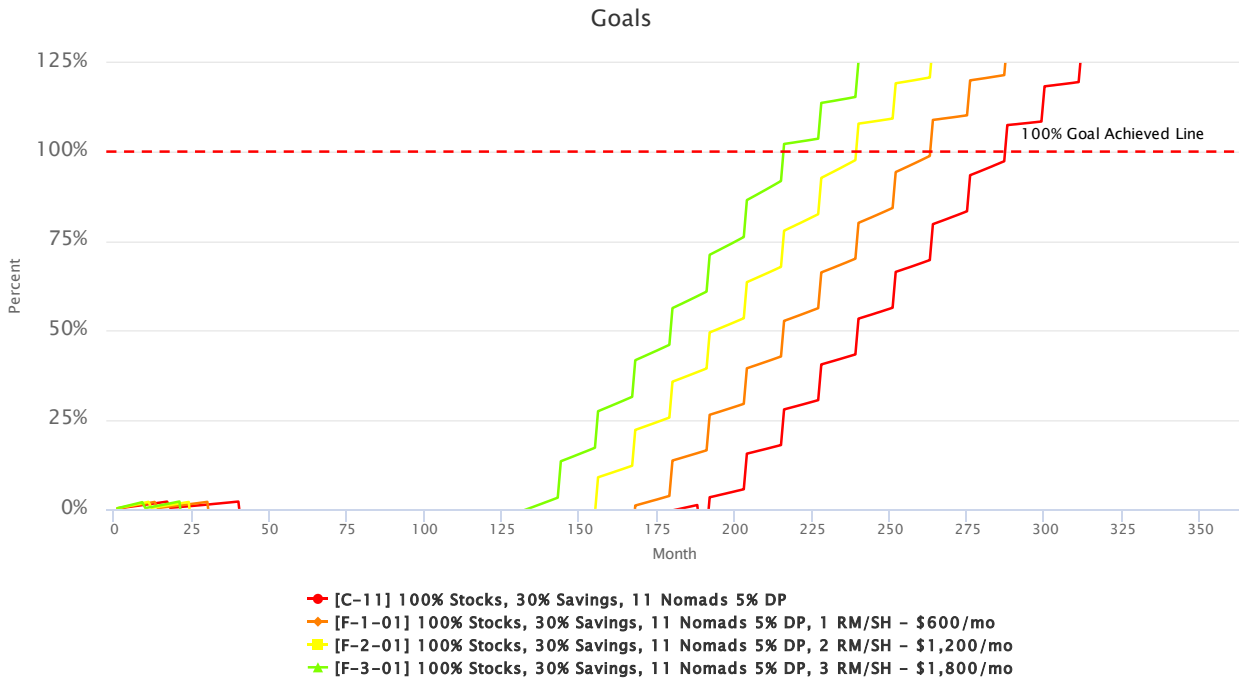
If we look just at the inflation adjusted values in month 720, 60 years out, this is the chart showing those values.



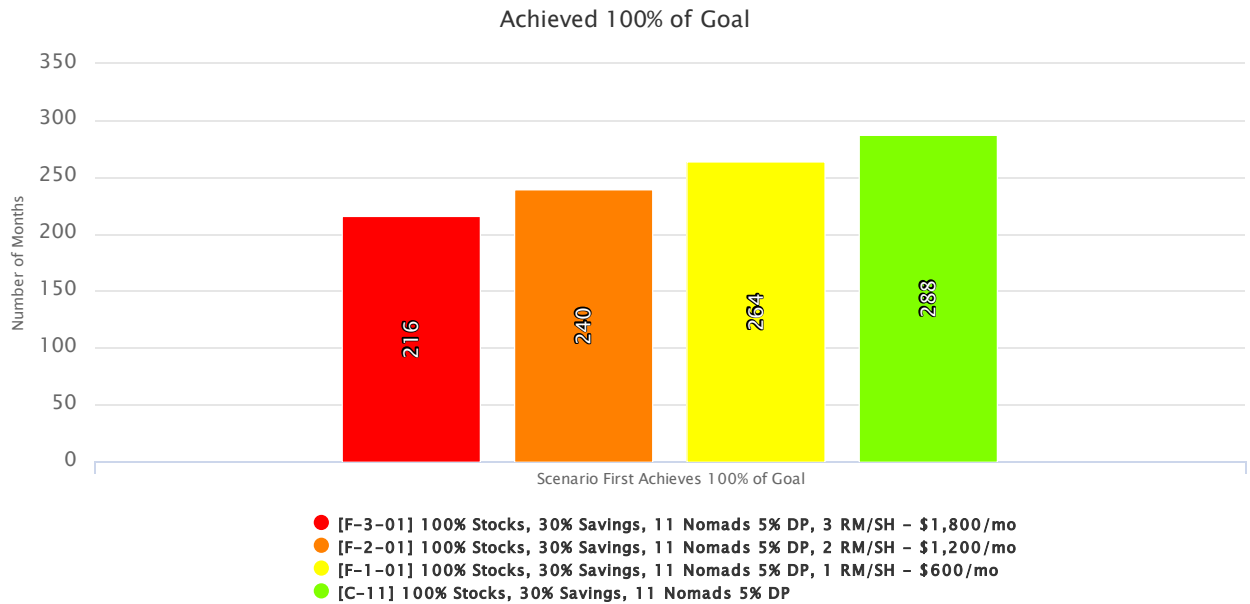
Again, it is approximately the same \$2 million difference for having roommates or not having roommates and the same \$6 million difference between no roommates and having three roommates.

### Goal of Financial Independence

I suspect you are primarily interested in how quickly getting roommates contributes toward your goal of achieving financial independence. So, let’s look at the chart that shows how fast we get to FI with the four scenarios.



If we want to look at a chart comparing what month each hits your financial independence date, you can see that having just one roommate and/or a side hustle allows you to achieve financial independence two years faster. Each additional roommate you get shortens the time to your goal by an additional two years.



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## Limiting Time with Roommates and Side Hustle

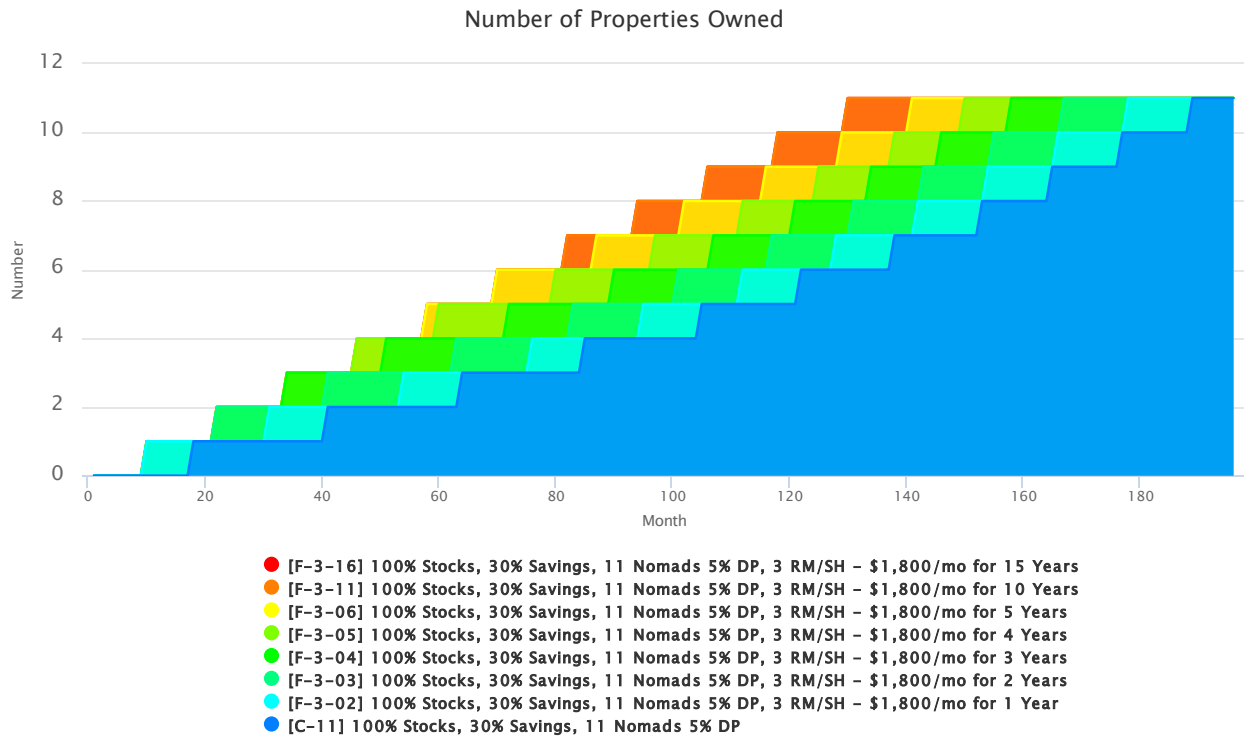
What if you say, I'll try the roommate thing, but I'm not sure I can do it for 20 years. That is what we will cover next.

I will show what happens if you are willing to get three roommates or a side hustle that brings in \$1,800 per month for just 1 year, 2 years, 3 years, 4, years, 5 years, 10 years, and 15 years.

## Number of Properties Owned and When

The following chart shows you how quickly you can acquire properties for having three roommates and/or an equivalent side hustle.

As you can see getting a roommate even for one year, does make a difference. You can buy properties quicker. The longer you have roommates the longer that positive impact lasts since it helps you buy the subsequent properties more quickly.



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## Net Worth

What impact does having roommates—even for a brief period—have on your net worth?

I'll skip over showing you the non-inflation adjusted chart of net worth and jump right to discussing the inflation adjusted, today's dollar benefit, of getting three roommates for just a single year.

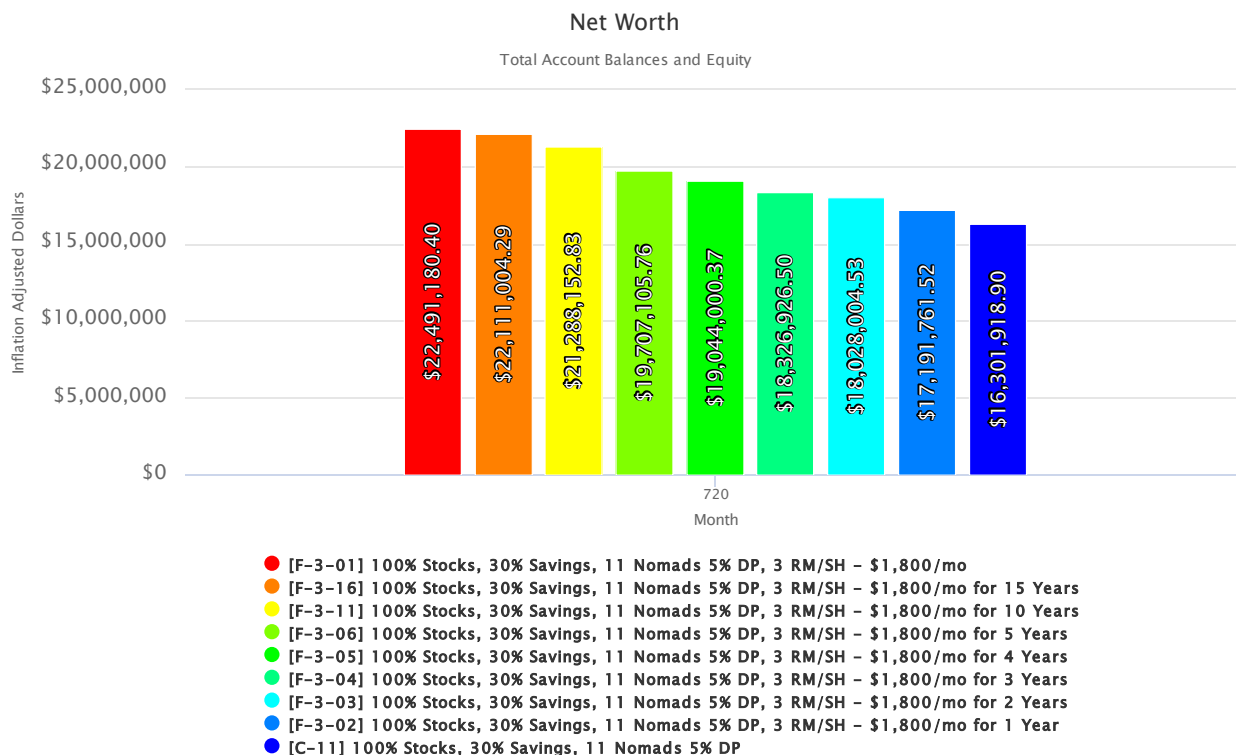
Well, as you can see in the chart below, the difference in dollars between having three roommates for a single year is a cool \$900K in today's dollars. To help you understand this difference, I will change how I present this to you.

What if I posed the question to you like this: Would you be willing to get three roommates and live with them for a year, if I gave you \$900,000 toward your retirement? While I realize this is twisted because it is \$900,000 60 years in the future, the question is valid.

Having three roommates for an extra year (two in total) adds approximately an additional \$800K.

Look at the chart below to get a feel for what getting roommates for even short periods gives you and the luxury tax that not having roommates costs you.





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## Goal of Financial Independence

Really though, it is not net worth. It really comes down to how quickly you can achieve financial independence.

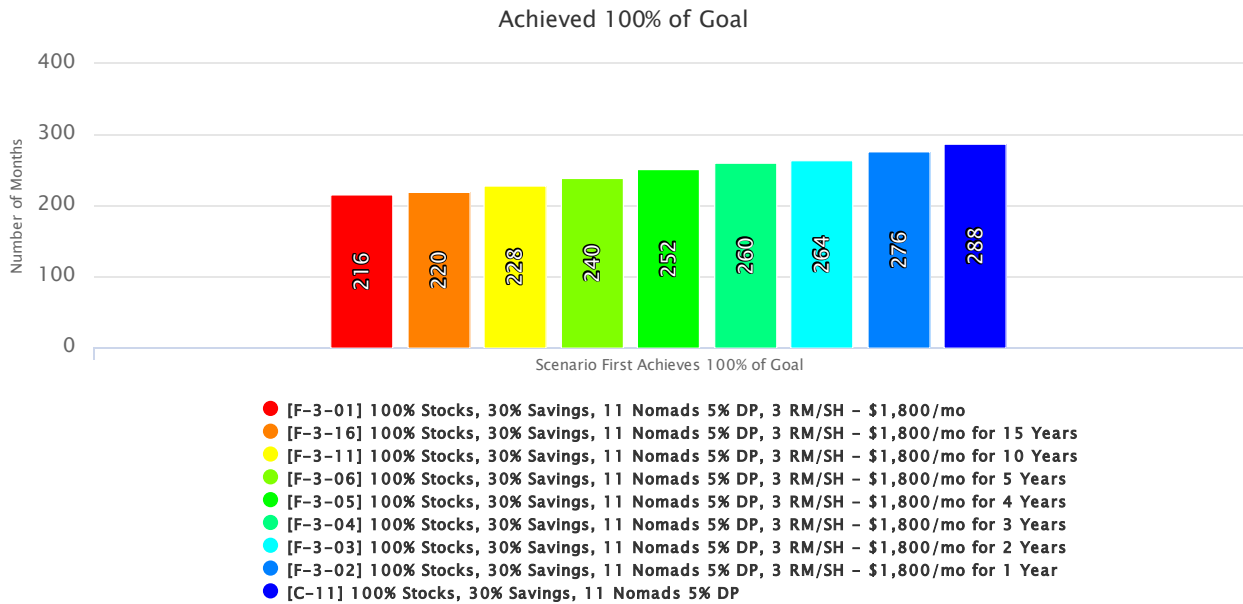
Having three roommates for just a year, allows you to achieve financial independence a year faster than not having roommates.

Roommates for two years will save you another year.

Roommates for three years only saves you four months, but four years will save you an additional eight months. Going from roommates for two years to four years will save you a full year (four months and eight months combined).

Having roommates for five years, buys you another year of speed allowing you to achieve financial independence in 240 months, or 20 years. You could be financially free by 42 if you do Nomad™ 11 times and have three roommates for five years.

Personal question: Is that worth it to you?



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## Model It Yourself

If you want to copy any of the roommate and/or side hustle scenarios to your own Real Estate Financial Planner™ account and adjust the assumptions, you can use the links below.

- 100% Stocks, 30% Savings, 11 Nomads 5% DP, 1 RM/SH - \$600/mo  
<http://refp.io/645>
- 100% Stocks, 30% Savings, 11 Nomads 5% DP, 2 RM/SH - \$1,200/mo  
<http://refp.io/646>
- 100% Stocks, 30% Savings, 11 Nomads 5% DP, 3 RM/SH - \$1,800/mo  
<http://refp.io/647>
- 100% Stocks, 30% Savings, 11 Nomads 5% DP, 3 RM/SH - \$1,800/mo for 1 Year  
<http://refp.io/648>
- 100% Stocks, 30% Savings, 11 Nomads 5% DP, 3 RM/SH - \$1,800/mo for 2 Years  
<http://refp.io/649>
- 100% Stocks, 30% Savings, 11 Nomads 5% DP, 3 RM/SH - \$1,800/mo for 3 Years  
<http://refp.io/650>
- 100% Stocks, 30% Savings, 11 Nomads 5% DP, 3 RM/SH - \$1,800/mo for 4 Years  
<http://refp.io/651>
- 100% Stocks, 30% Savings, 11 Nomads 5% DP, 3 RM/SH - \$1,800/mo for 5 Years  
<http://refp.io/652>
- 100% Stocks, 30% Savings, 11 Nomads 5% DP, 3 RM/SH - \$1,800/mo for 10 Years  
<http://refp.io/653>
- 100% Stocks, 30% Savings, 11 Nomads 5% DP, 3 RM/SH - \$1,800/mo for 15 Years  
<http://refp.io/654>

If you do end up implementing one of these scenarios, I would strongly advise you to do full Monte Carlo testing as we described previously.

To find and copy any of the other scenarios covered in this book, follow the link below.

- <https://realestatefinancialplanner.com/filyp/>



## Path 7: Paying Off Mortgages with Cash Flow

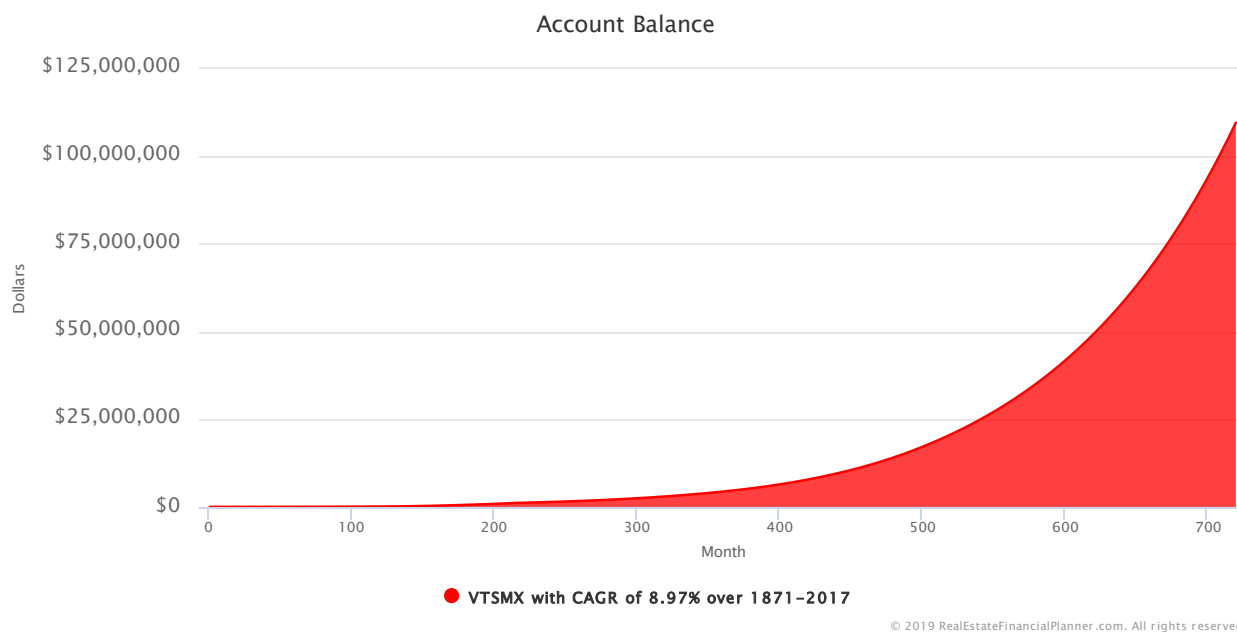
In all the scenarios we have covered so far, you end up with a significant balance in your stock market account. Perhaps you are wondering—as I did—what would happen if you took some of that money you had invested in stocks and used it to pay off the mortgages on properties you own instead.

That's what this chapter is about.

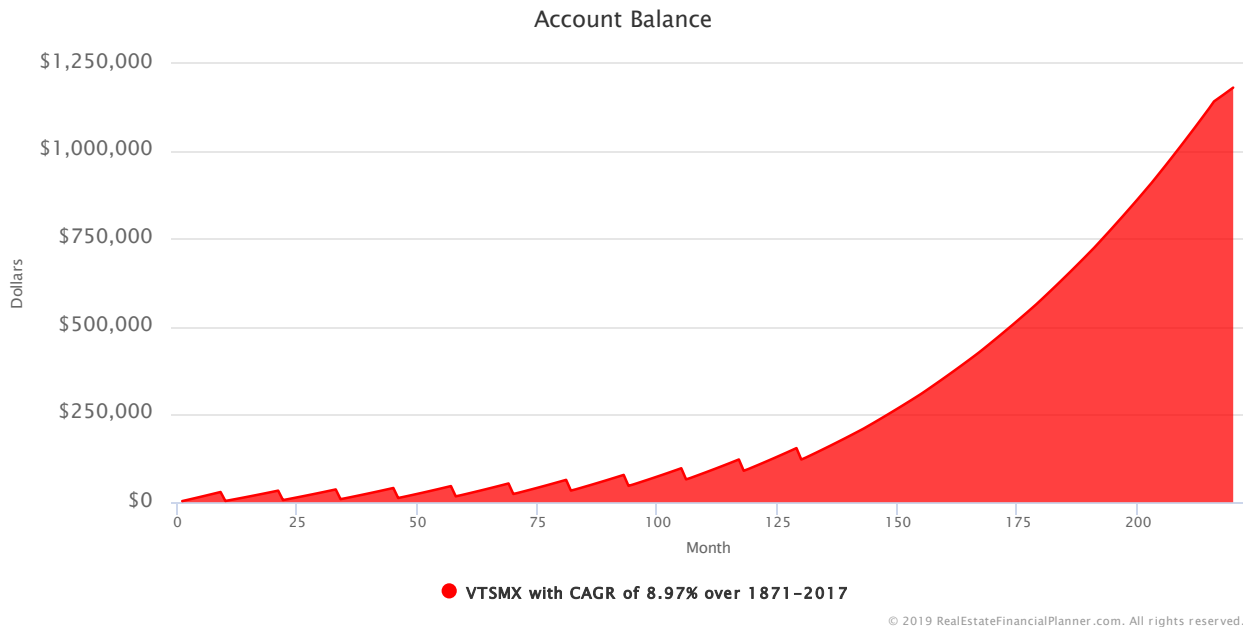
We will keep the same assumptions. You are:

- Saving 30% of your income each month.
- Investing 100% of your extra money in the stock market (no bonds).
- Earning a fixed rate of return in the stock market of 8.97% per year.
- Buying properties as a Nomad™ each time you have saved up a 5% down payment and have lived in the current property for at least a year.
- Getting either three roommates or a side hustle that brings in \$1,800 per month and continuing this until you achieve financial independence.

With those assumptions, how much money do you end up having in the stock market account in the scenario from the previous chapter? Remember, this is the amount of money that you could use to pay off the mortgages on your properties earlier.



In this scenario, without paying off any loans early, you are achieving financial independence in month 216. If we zoom in on this chart (remember how much I love my charts), you can see how much you have around month 216.



Zoomed in, you may notice that as you are acquiring properties your stock market balance is not high at all. It is only after you stop using the stock market balance to buy additional properties that the balance really starts to grow.

By the time you hit financial independence and start pulling money from the stock market for living expenses, you have just over \$1.1 million dollars invested in the stock market (in inflated dollars). That's really like having approximately \$670,000 dollars if we adjust for inflation.

## Options For Paying Off Mortgages

If you are going to pay down your mortgages faster with extra money, there are several options you could use to determine which order to pay off the mortgages.

You could sort the properties or loans by:

1. Interest Rate
2. Capitalization Rate
3. Loan Balance
4. Order of Purchase

And for each of these options you could decide to pay off either the highest or lowest first.

If you opted to pay off the loans by interest rate, you would very likely choose to pay off the highest interest rate loans first to save yourself the most interest over time.

In our scenarios in this book we are assuming all the interest rates on the loans are the same, so you can ignore interest rate as a prioritization option for the examples in this book.

You could choose to pay off the properties with the best capitalization rate. This means you would pay off the loan on the property that will give you the highest return on your investment when paid off. This would result in you earning the highest dollar amount on the property you paid off.

Since all the properties are identical for this book, this option too is not a viable choice.

The third option—and the one we will be examining first—is the loan balance. With this option you have two choices:

1. Pay off properties with the highest loan balance first; or
2. Pay off properties with the lowest loan balance first

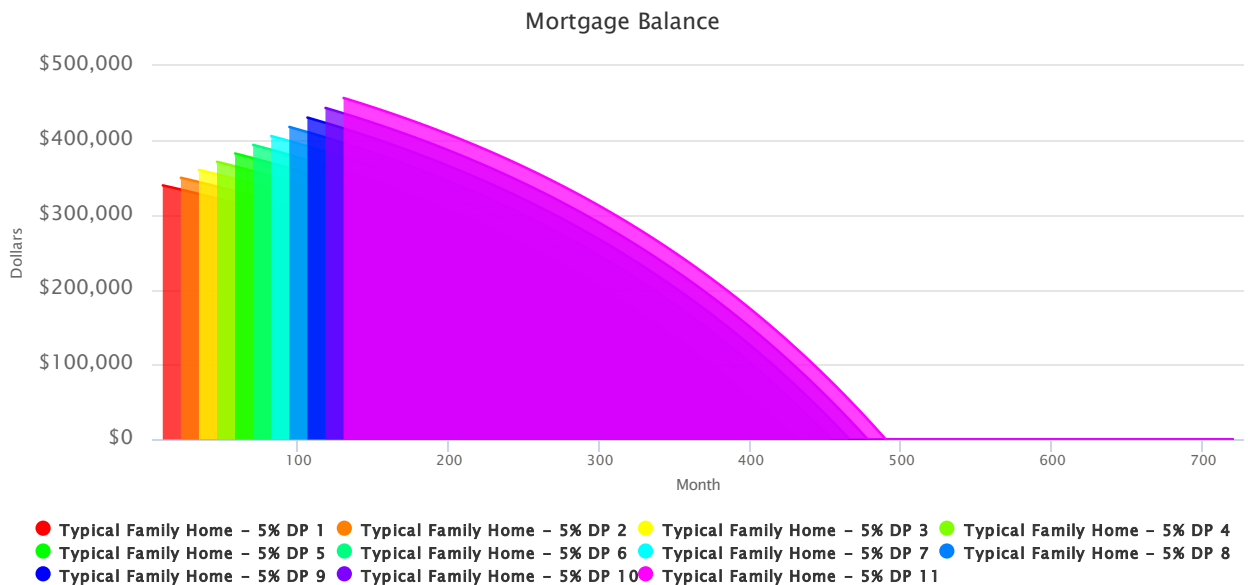
We will look at both, but I will warn you that it might not be what you think.

### Highest Loan Balance First

If you decide to pay off the highest loan balance first, you will be applying any extra money you have in your stock market account to pay off the current highest mortgage balance.

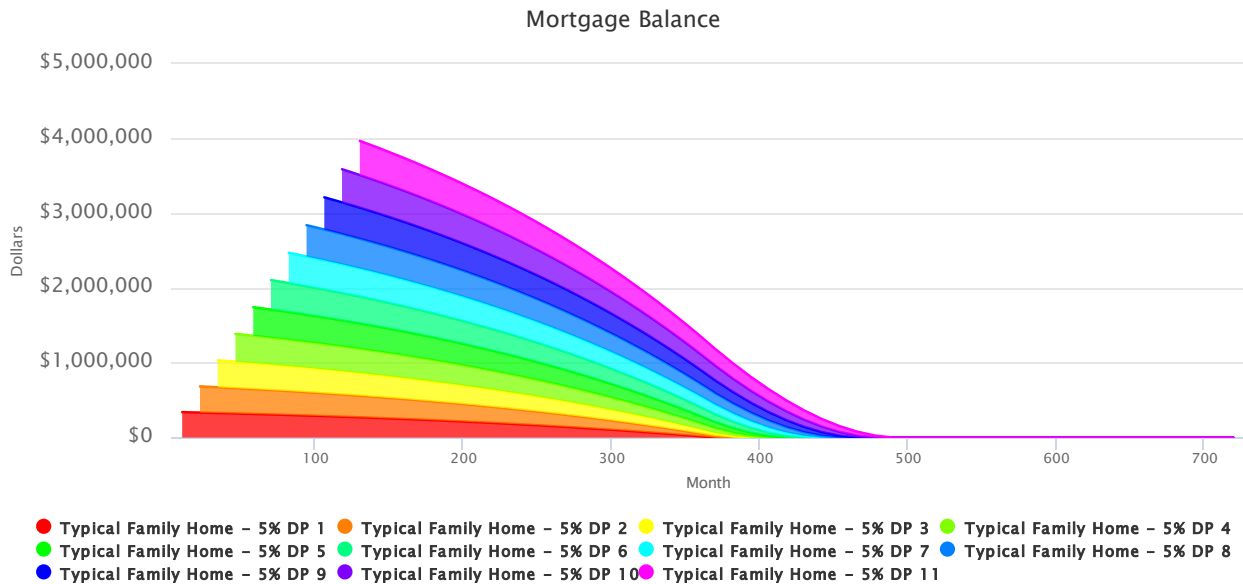
**IMPORTANT NOTE:** You are not selecting the property that had the highest mortgage balance to begin with and sticking with that property until it is paid off. That is “order of purchase” and is the option we will look at next.

The loan balance of the mortgage for each of the properties, if we did not make additional principle payments, looks like the following chart.



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Of course, we could stack them on top of each other to show the sum of all the mortgages. This is shown in the chart below.



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Each month, you will look at your stock market account balance. If you have more than a certain amount in set reserves, you take that extra money and make a lump-sum payment to the then current highest mortgage balance.

How much should we set as the minimum amount to keep in reserves? For this book, I set it to be an inflation adjusted \$120,000. This means that over time the amount increases to keep pace with inflation. Why did I pick this number? It just happens to be an amount that will not interfere with saving for down payments and closing costs while you are acquiring the properties. When you copy the scenario to your own Real Estate Financial Planner™ account, you could just as easily delay starting this pay down rule until after you have purchased all your properties and reduce the minimum reserves.

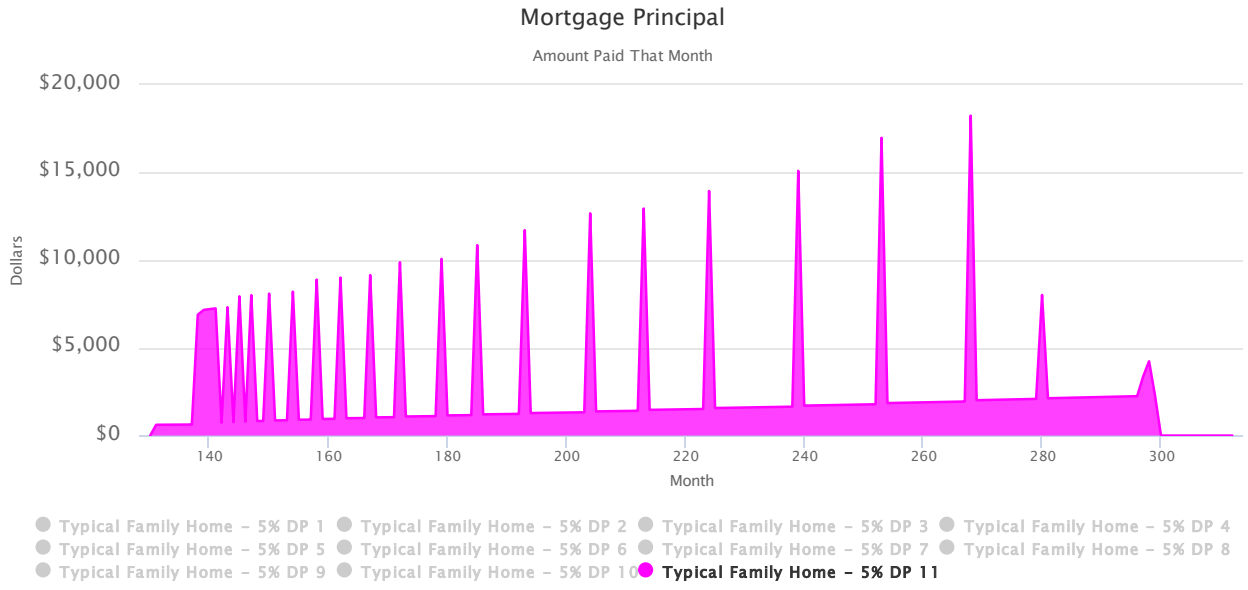
Setting your reserves to \$120,000 for owning 11 properties also happens to be conservative. In an ideal world, you would have six months of principle, interest, taxes, insurance, maintenance, property management, and HOA expenses in reserves for each of your properties. Some folks would argue that having six months of all expenses for the first property is prudent, but the chance of you needing six months—at the same time—for all 11 properties is very low. Thus, they would contend that you don't need a full six months for all your properties.

That decision, and your comfort with risk, is ultimately up to you.

Back to paying down the loans.

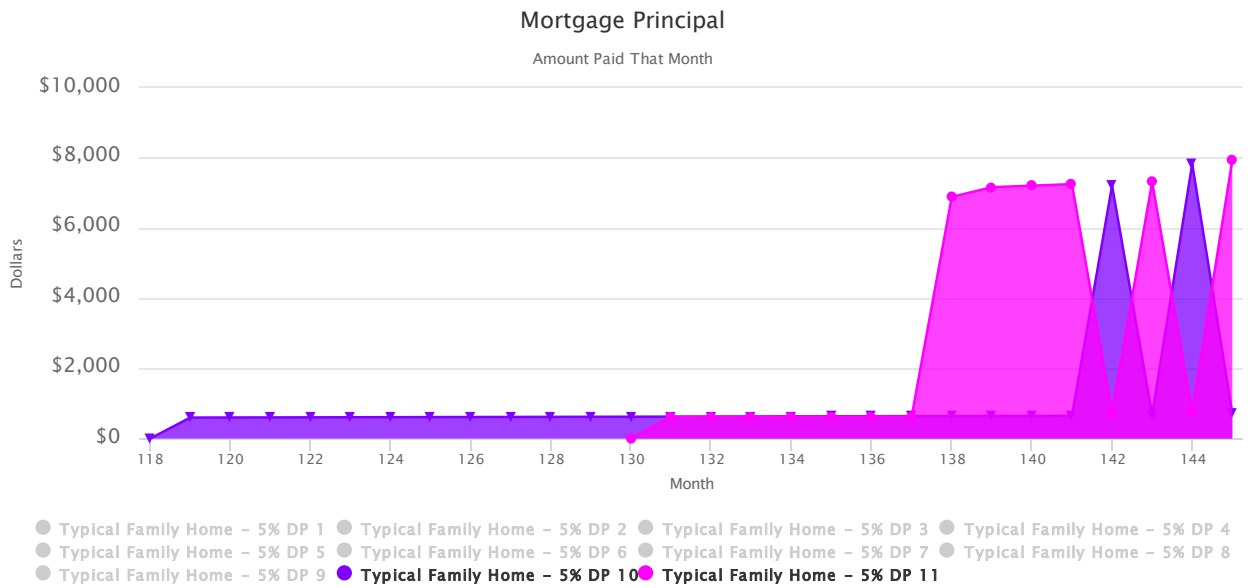
If you apply all your extra cash each month above an inflation adjusting \$120,000 to your highest loan balance for that month, you end up making extra principle payments which reduce the amount you owe. For example, here's the principle payment you make on the last property you purchased.



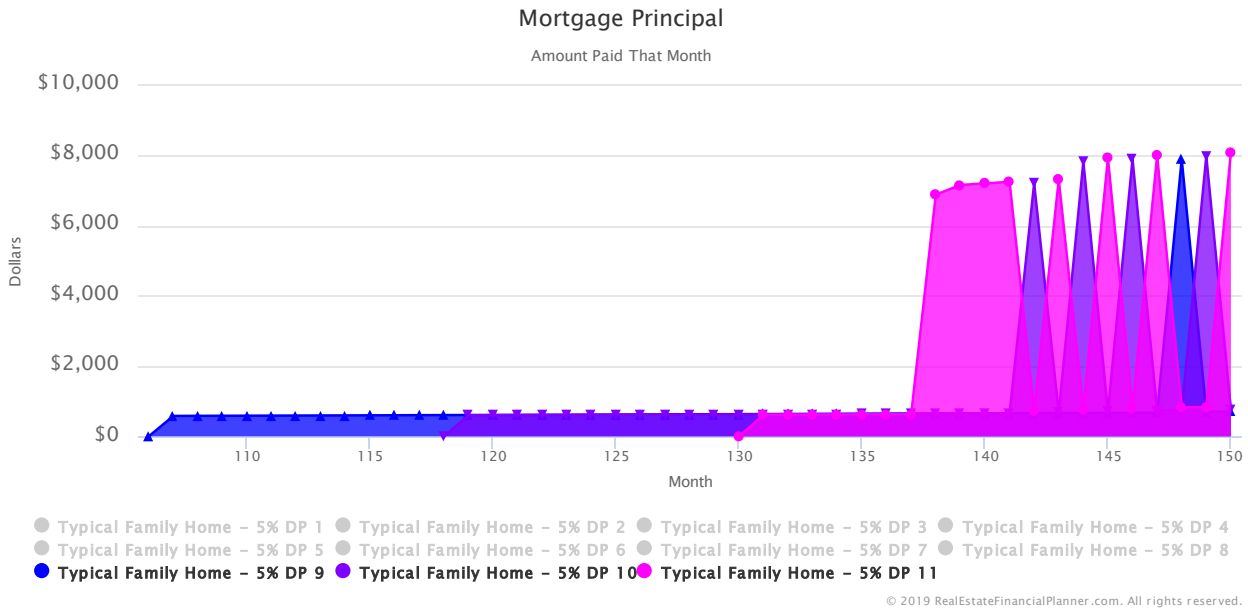


You will notice that you are making the minimum mortgage payment for the first seven months or so while you bring your stock market account balance up above the minimum. Then, the first month you have more than the \$120,000 (adjusted for inflation) in your stock market account, you make an additional principle payment to pay down your loan on this property faster.

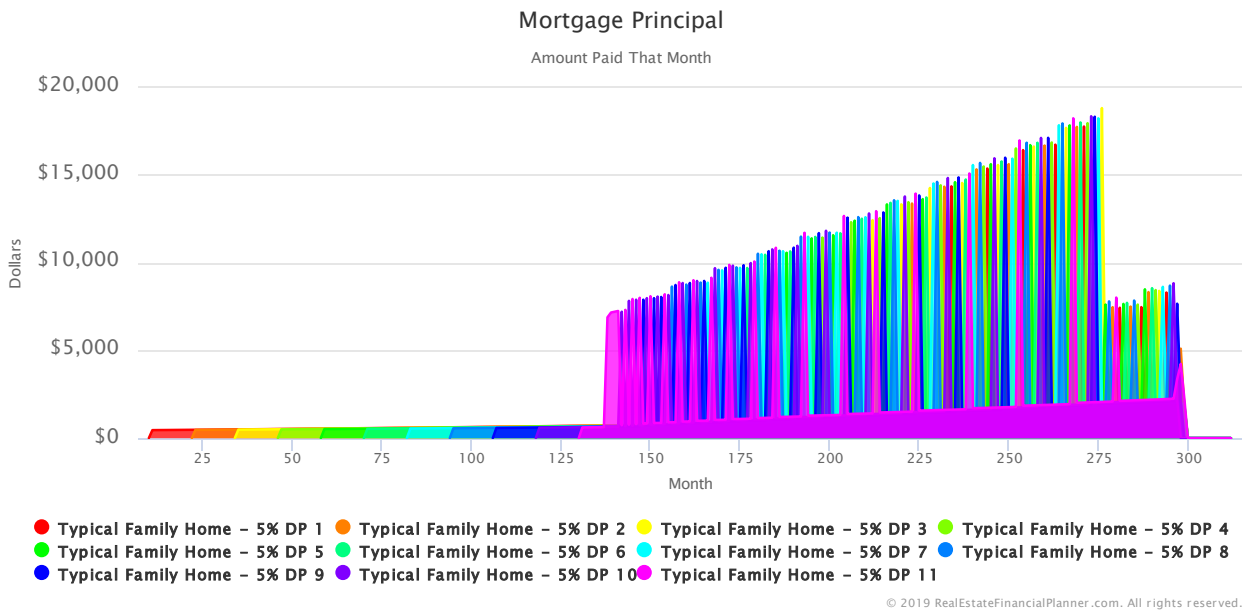
For the next four months or so, you make extra principle payments on this property and reduce this loan. However, after that you realize that this mortgage no longer has the highest balance. So, in the fifth month you decide to use all the excess cash you have above \$120,000 toward the then highest mortgage balance for property 10.



The next month, property 11 once again has the highest mortgage balance so you decide to work on paying that one off. You keep alternating back and forth between property 10 and 11 until you reduce those mortgage balances to be below the balance on property 9.

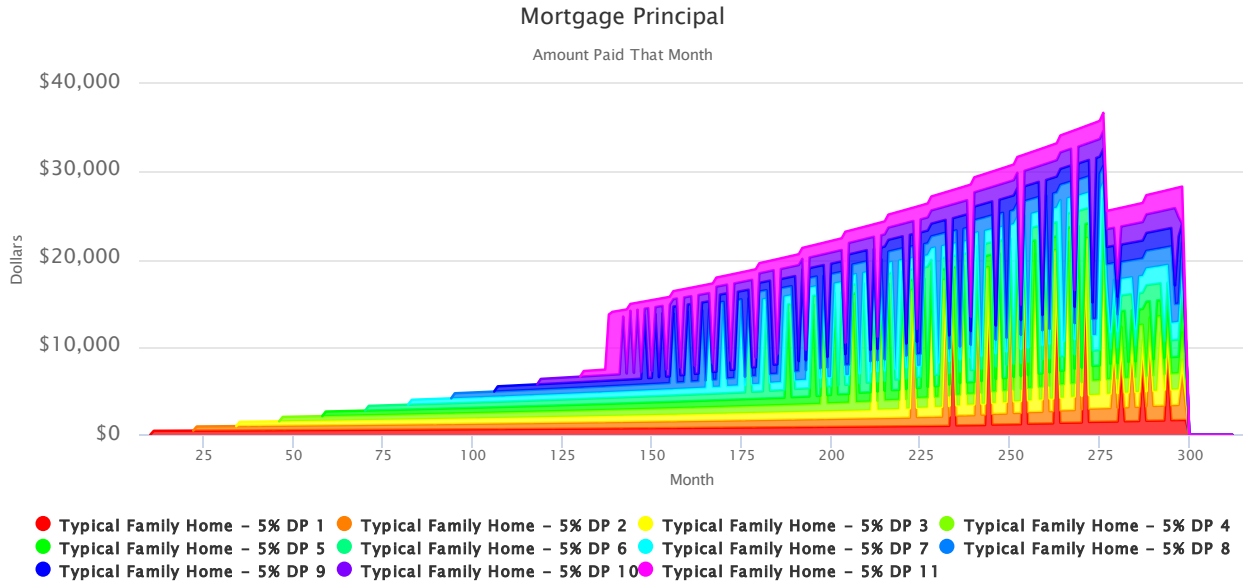


This pattern continues until you are making extra principle payments on all 11 properties as shown in the chart below.



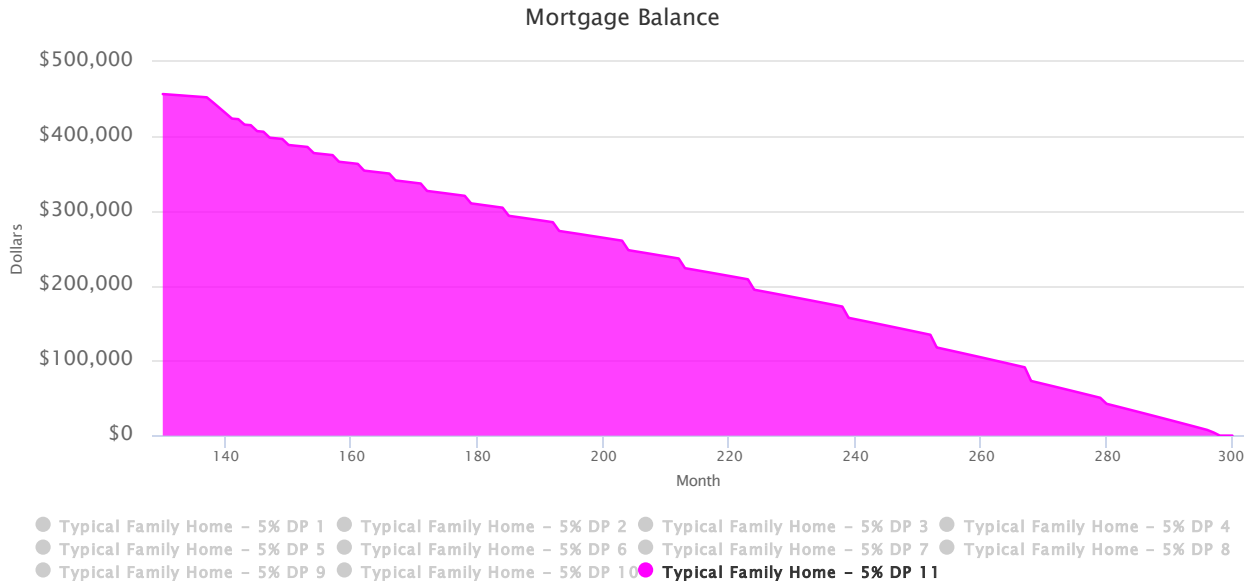
In the later months when you end up paying off a property entirely you will take the extra money and apply it to the next highest mortgage balance. Remember, we are still paying a little bit of principle on

each loan with the normal, minimum payment. You can see this more clearly if we stack the principle payments like we are showing in the chart below.



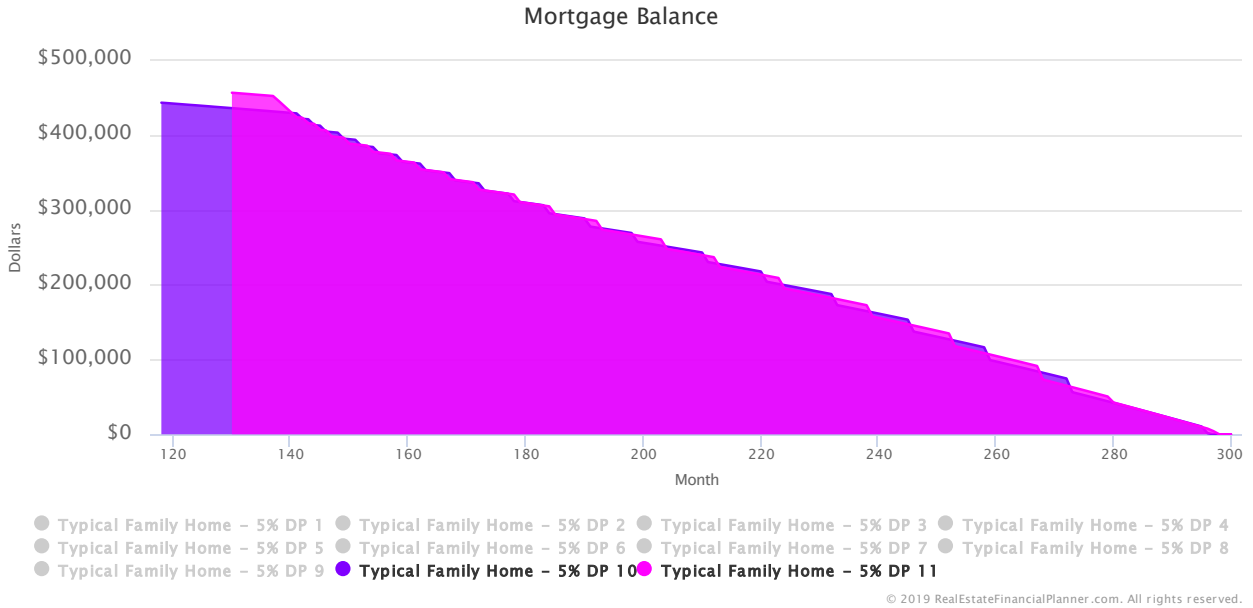
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By the time we get to about month 300, we have paid off all mortgage balances. Because we are “rotating” through the different mortgages, making extra principle payments to whichever has the highest balance that month, the mortgage balances tend to all payoff around the same time. The chart below shows you the last mortgage you acquired when you purchased your last property.

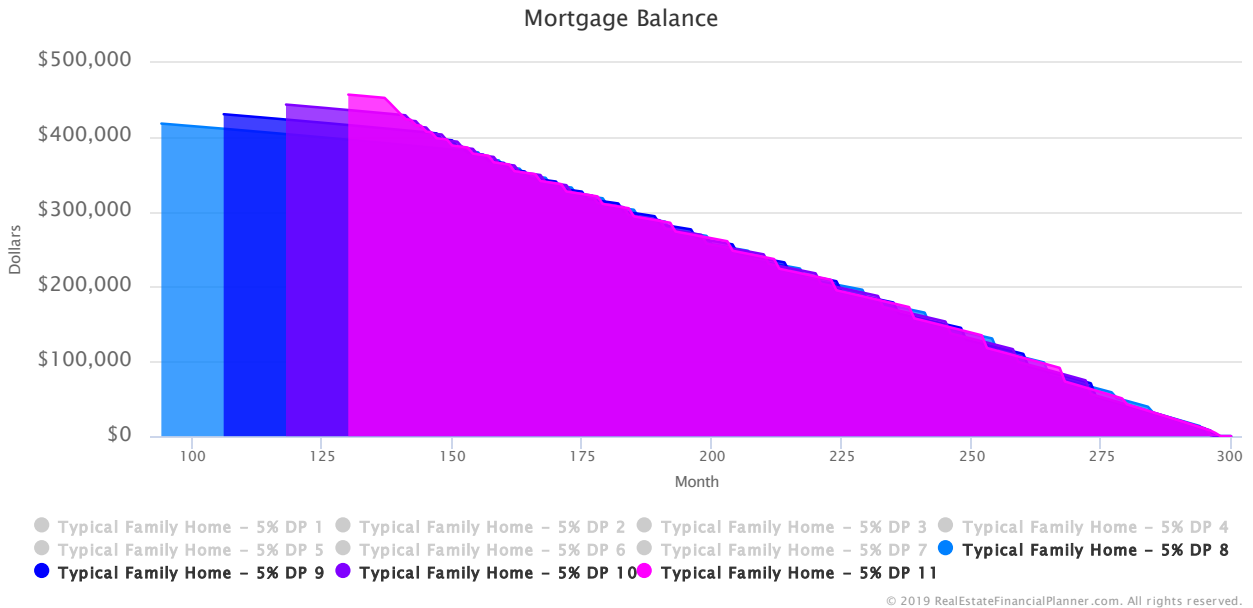


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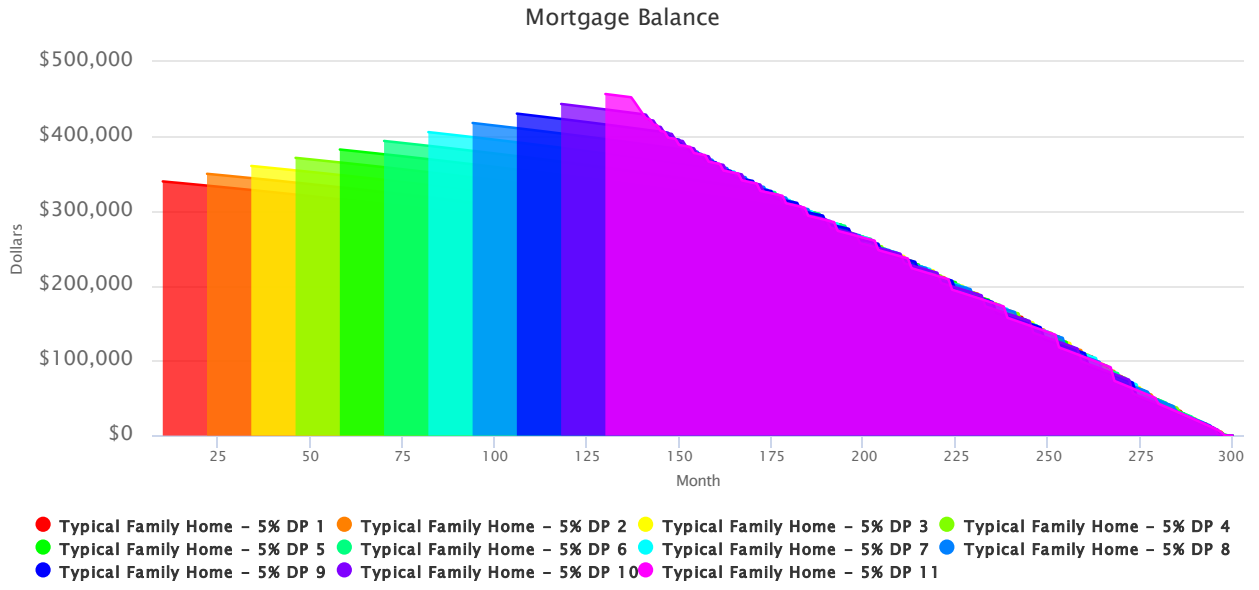
If you compare this to the chart I showed you earlier of what it looked like when you were not making additional principle payments, you can see this loan pays off much more aggressively. In the chart below, I will show you property 10 as well.



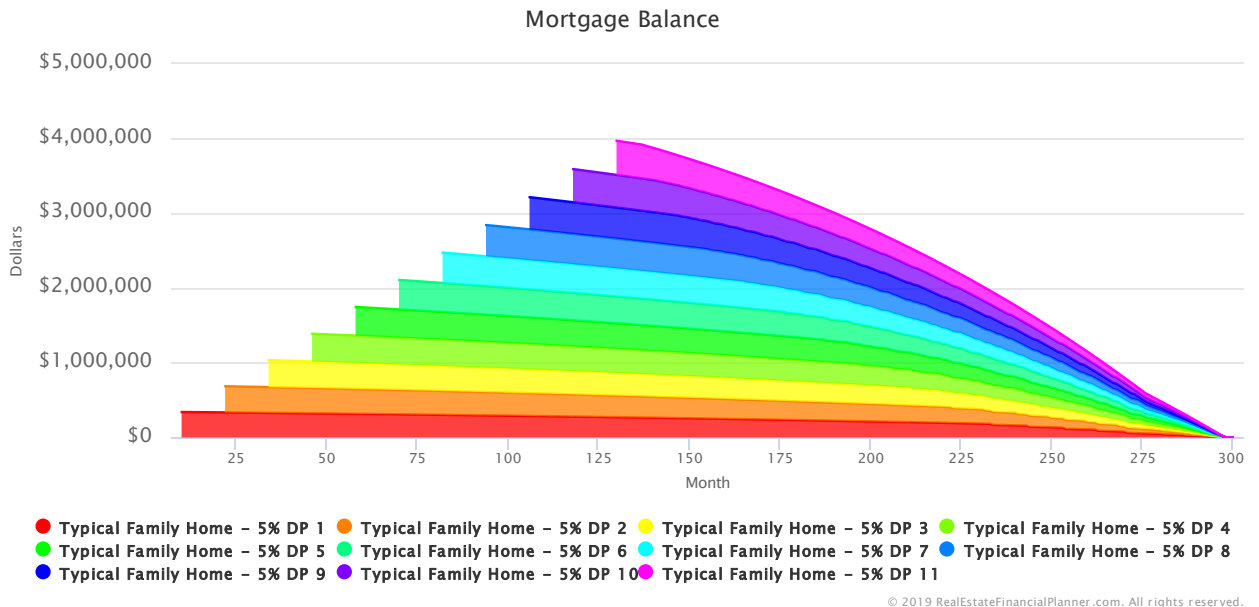
If we add in property eight and nine, you will see how we are alternating between which loan has the highest balance each month.



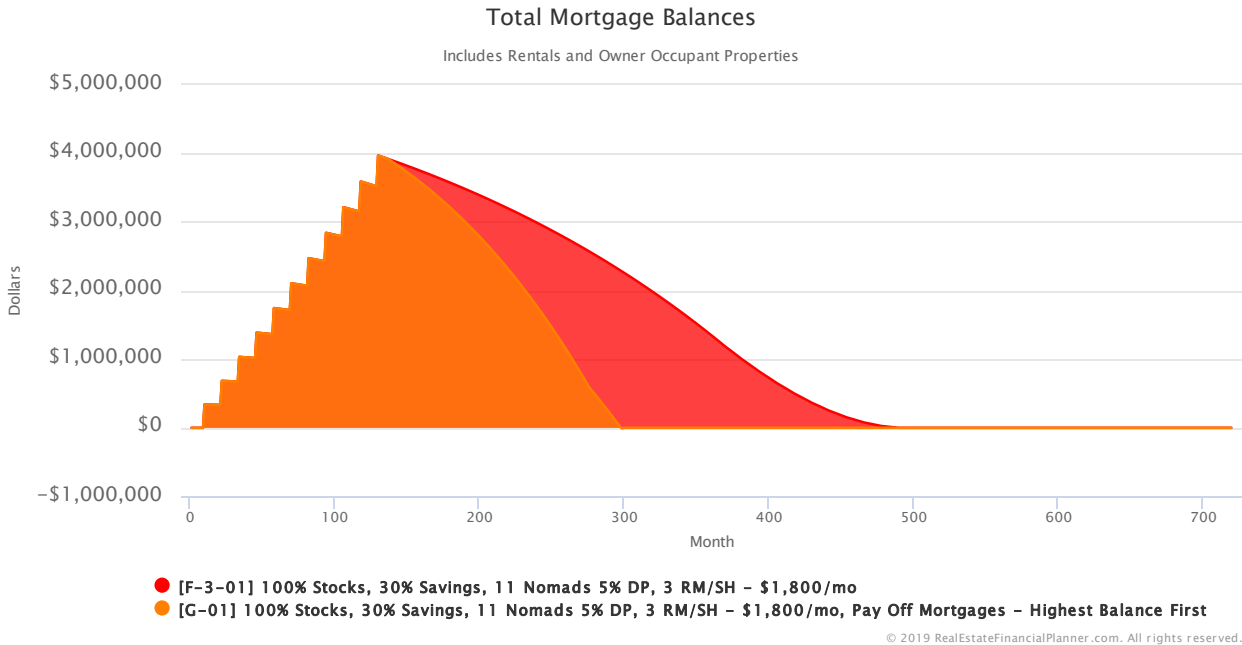
And finally, the following chart has all the mortgages on a single chart.



If we stack them on top of each other to show the total amount owed, you can see this payoff strategy from a different perspective.



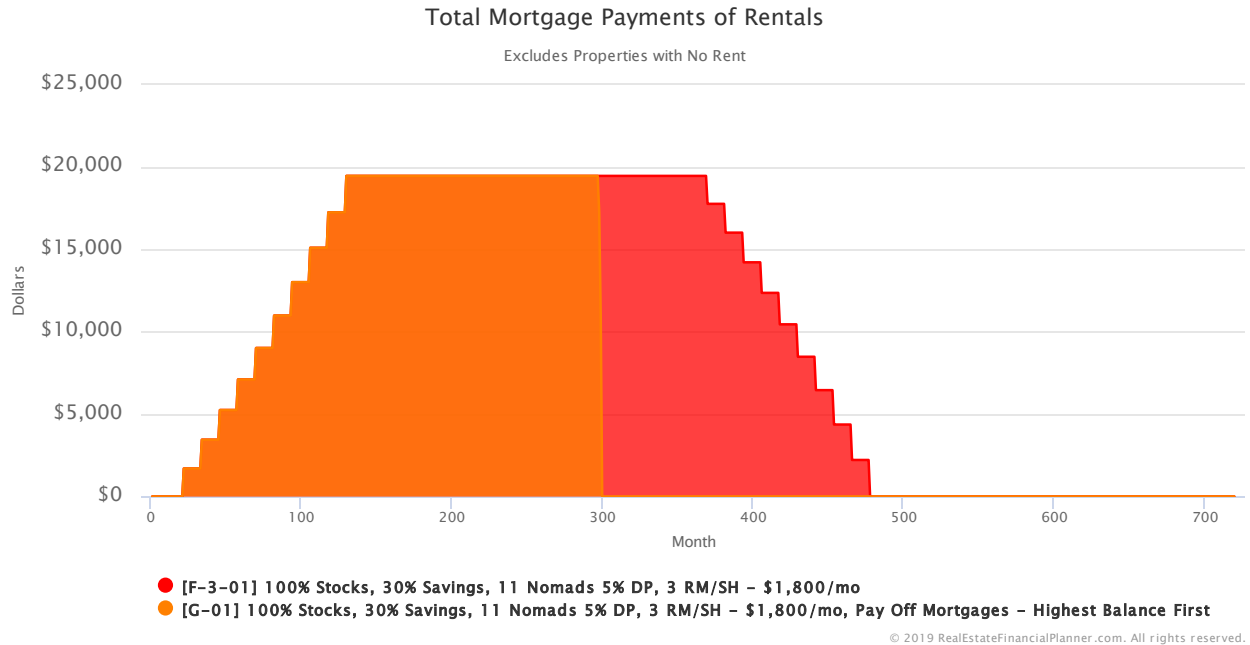
As you pay down loan balances, you owe considerably less than you did if you did not pay extra principle on the highest mortgage balance. The following chart compares making extra principle payments to the scenario we covered in the previous chapter in which we did not make additional payments and let the mortgages pay off over time.



The chart above shows that you start at the same mortgage balance, which is at its peak right after you acquire your 11<sup>th</sup> property. However, with aggressive mortgage pay down, you pay off the mortgages much sooner than if you just let the mortgages pay off naturally over time.

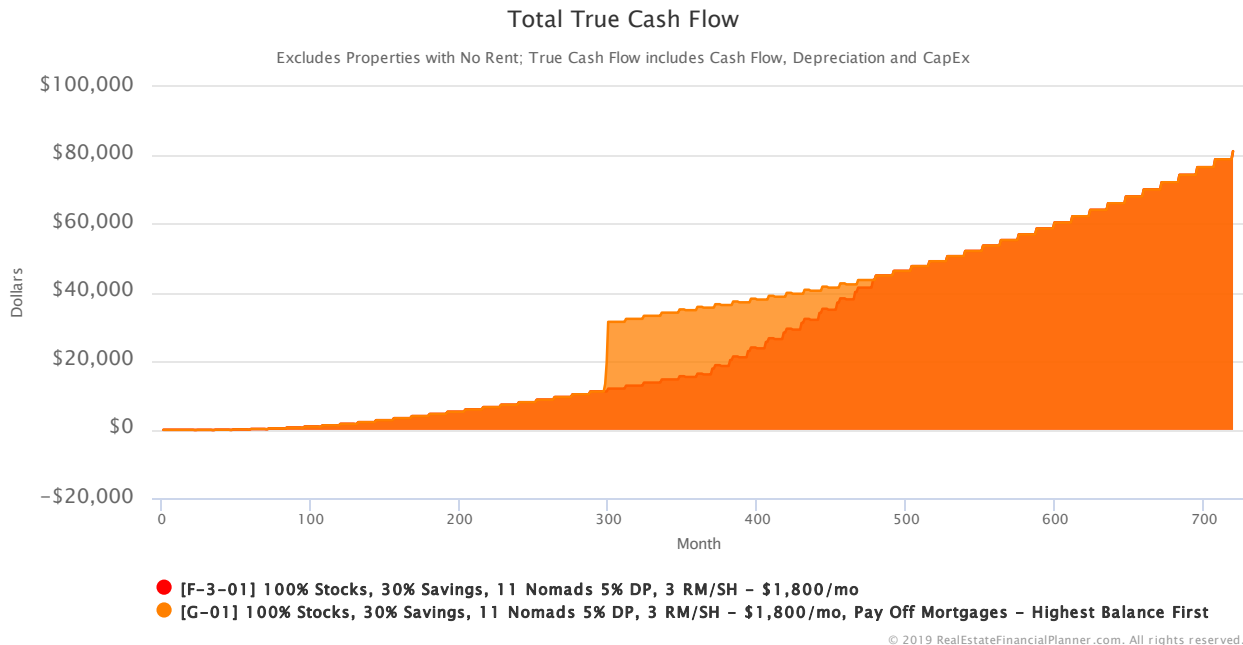
With a lower mortgage balance, you also end up paying less in mortgage interest.

And, since you pay off the mortgages all around the same time, you go from having all your mortgage payments to having none in a matter of a few months. If you compare this to letting the mortgages pay off naturally over time, you can see a drastic difference.



I will make a few comments that are obvious to me but may not be to everyone else. Things like how much the property appreciates, rent, and how much depreciation you get are identical whether you are paying off loans early or not. Furthermore, things like the mortgage payment and cash flow on the property are identical until the loan is paid off.

It is not until you pay the loan off in full that you see any improvement in your cash flow on the property. However, if you do pay off your mortgages early, you will see a huge bump in cash flow. You can see this in the chart below.



Eventually, both scenarios—paying off loans early and letting the loans pay off naturally—end up in the same place for cash flow. That’s because you are dealing with the same properties, bought at the same time. The only difference is whether you have paid off the loans early.

However, this extra cash flow will help you achieve financial independence since it can count toward hitting your minimum target monthly income in retirement. Remember though, the extra money you would have had in the stock market can no longer be used with your safe withdrawal rate to contribute to your financial independence income.

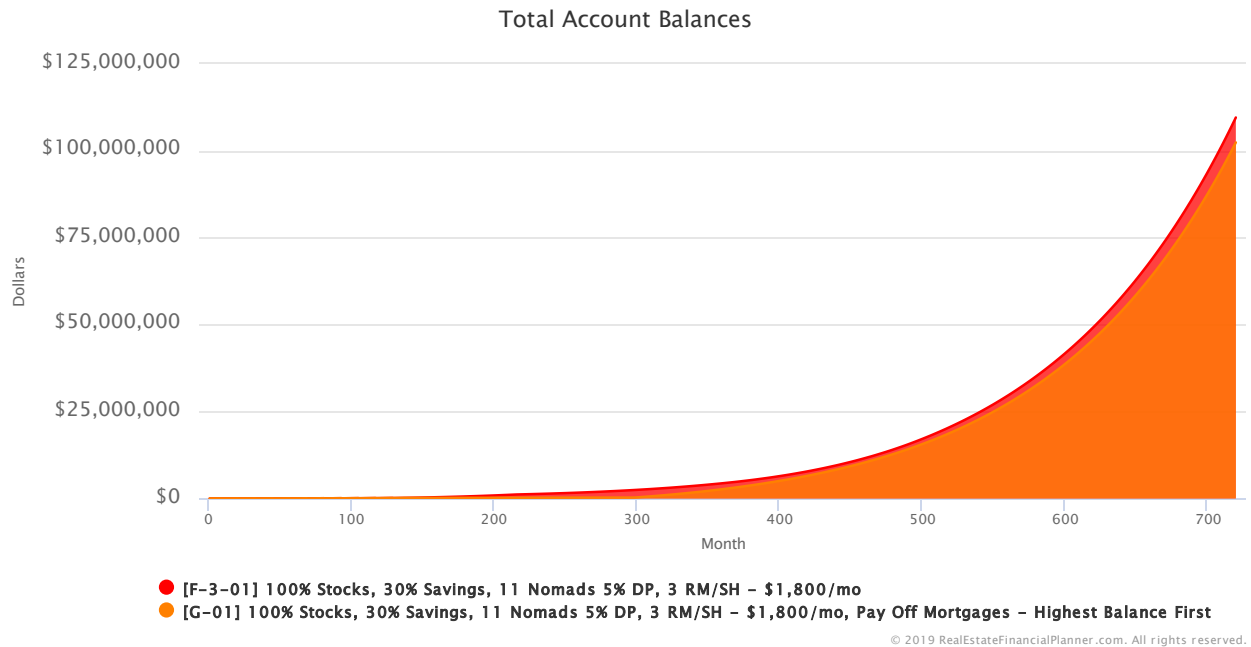
In a moment I will share with you a chart comparing your stock market account balances with paying loans off early (with the highest loan balances first) compared to not paying them off early at all.

If you look at the chart below, you will see that the stock market account balance is higher when you do not take money from our stock market investments and use it to pay down mortgages on properties. And that, I believe, makes sense: you have less money invested in the stock market growing at the 8.97%.

However, as you can also see in the chart below, if you look closely, the extra cash flow you get from the properties once they are paid off does help to replenish some of the money used from the stock market early on.

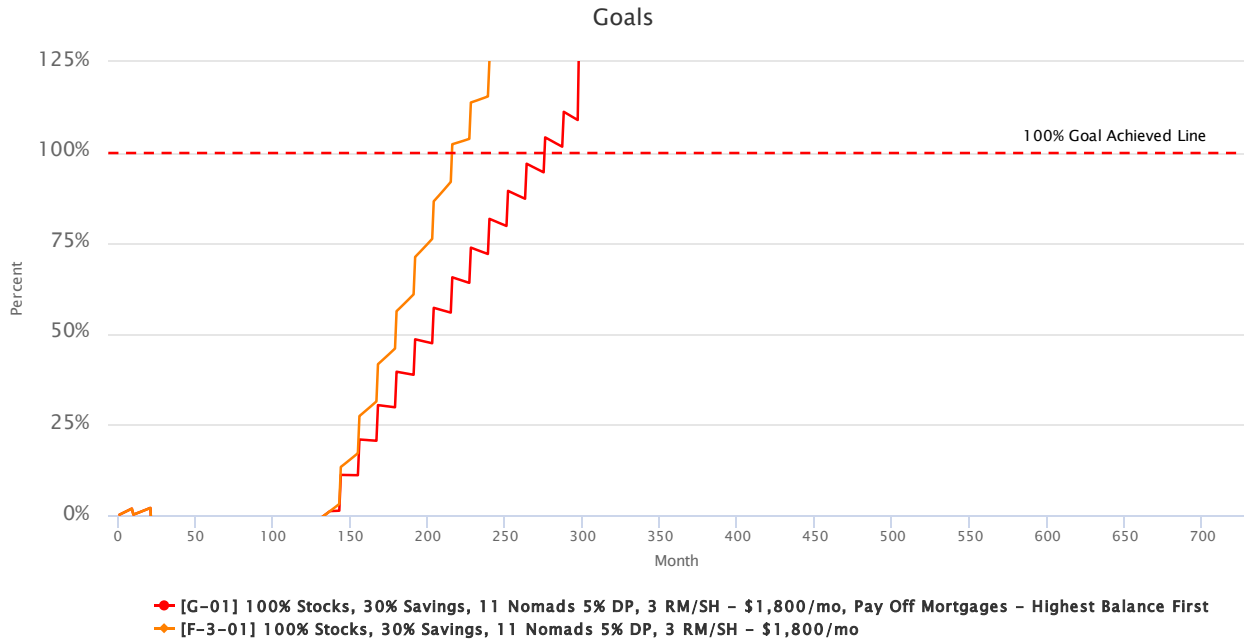
By the time you get to month 720 the difference between the stock market balances in the two scenarios is about \$1.2 million in today’s dollars. This is roughly the same difference in net worth as well.





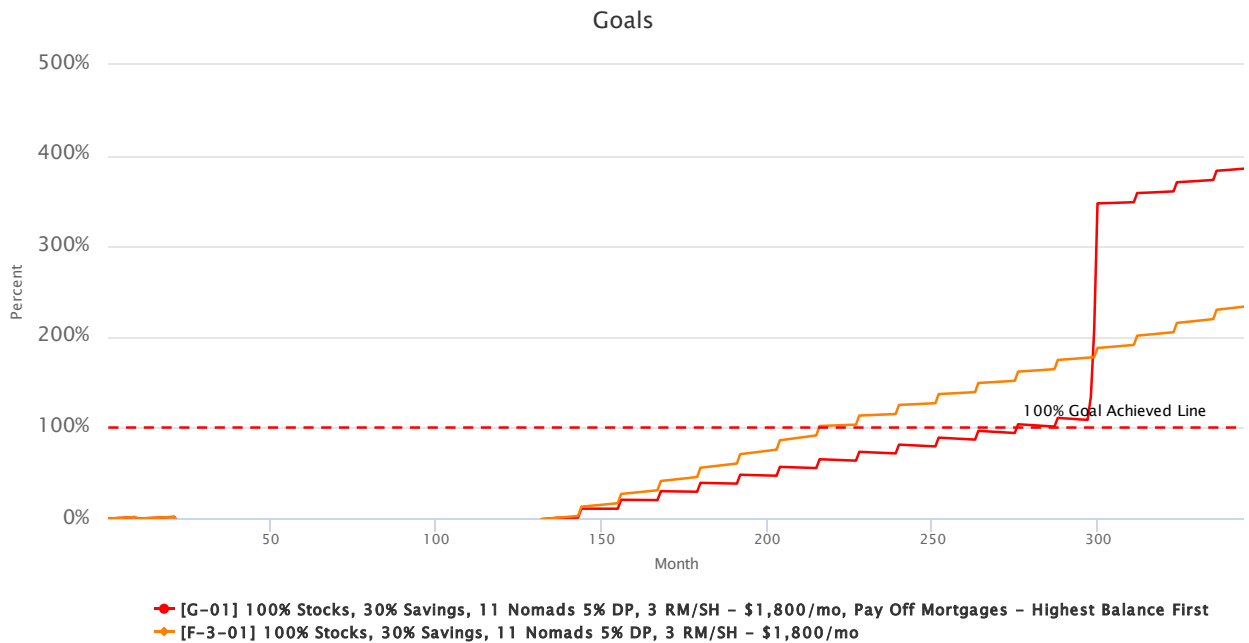
But while the account balance and net worth are not improved by paying off the loans early, surely taking the money and paying off the loans more aggressively will get you to financial independence more quickly? Not so fast.

By rotating through the loans and always paying off the highest loan balance each month, you are executing perhaps one of the least optimized ways of paying off the loans. It actually takes longer to hit financial independence by paying off loans in this manner.



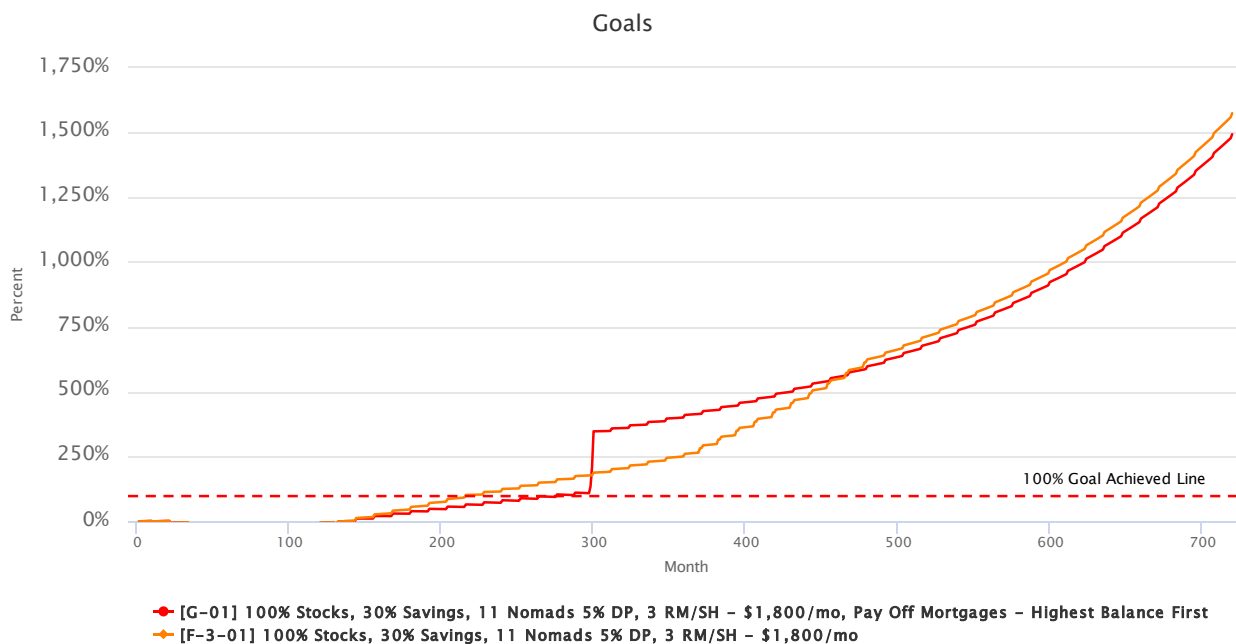
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Now, you do get an improved standard of living when you do pay off the mortgages—a higher standard of living than if you did not try to pay off the loans earlier. You can see this is an expanded view of your goal.



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But even that's not the whole story. If we look at your entire 60-year scenario timeframe, these scenarios swap again later a little before month 500 as seen in the chart below.



From that point on, you could enjoy a higher standard of living by not trying to pay off your loans early.

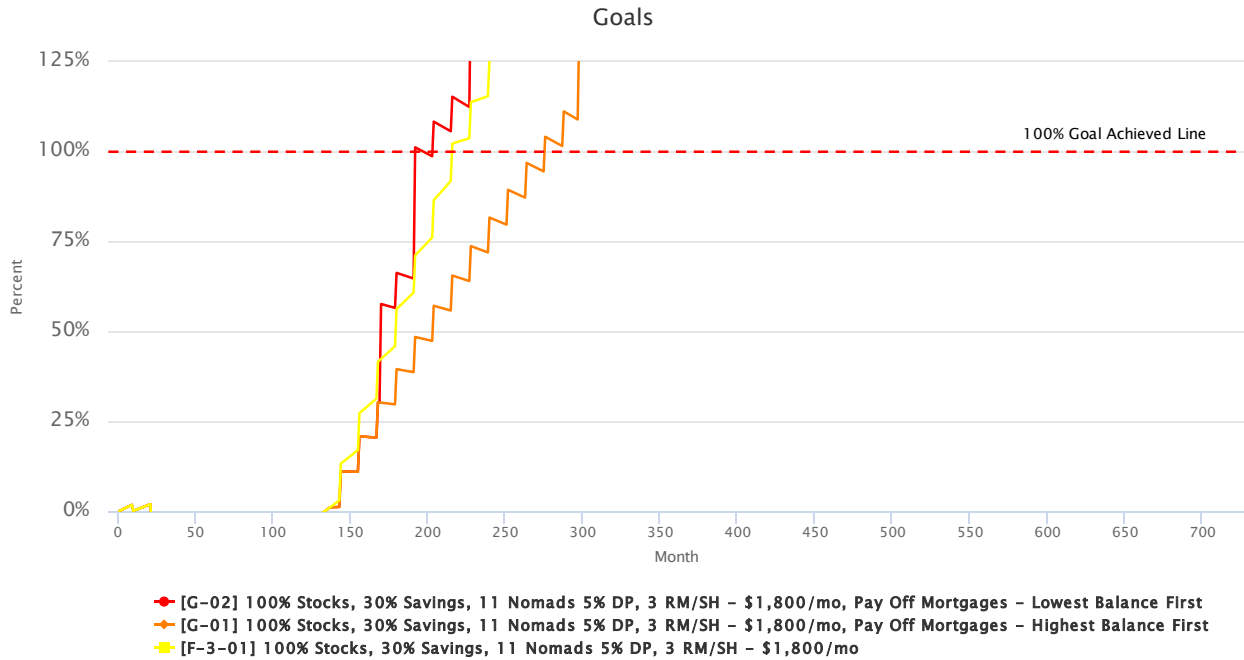
You know that this is not the end of the discussion though, don't you? You realize if we change the order that we pay off loans, it will probably impact the results, right?

## Lowest Loan Balance First

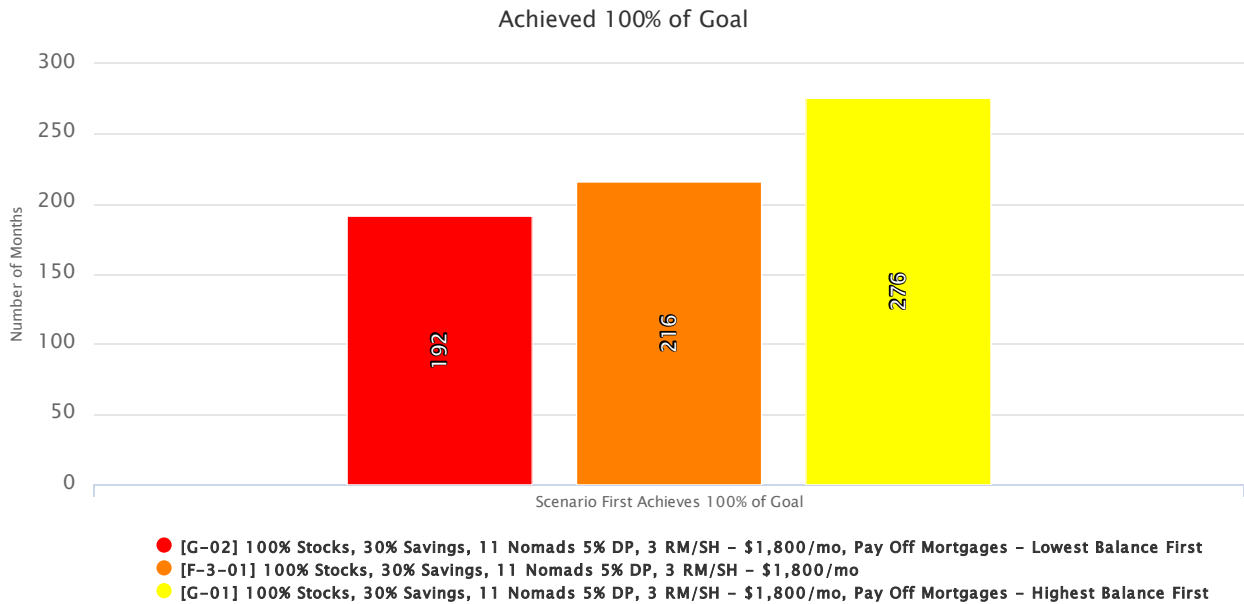
What if instead of paying off the highest loan balance each month, you decide to pick the lowest mortgage balance and pound away at that one until it is paid off? Then, once that one is paid off and you have improved cash flow, you start working on the next lowest loan balance? Would that be any different?

I'm going to jump right to the punch line and tell you, yes.

If you look at how quickly you can achieve your goal of financial independence, paying off the lowest balance first has a huge impact.

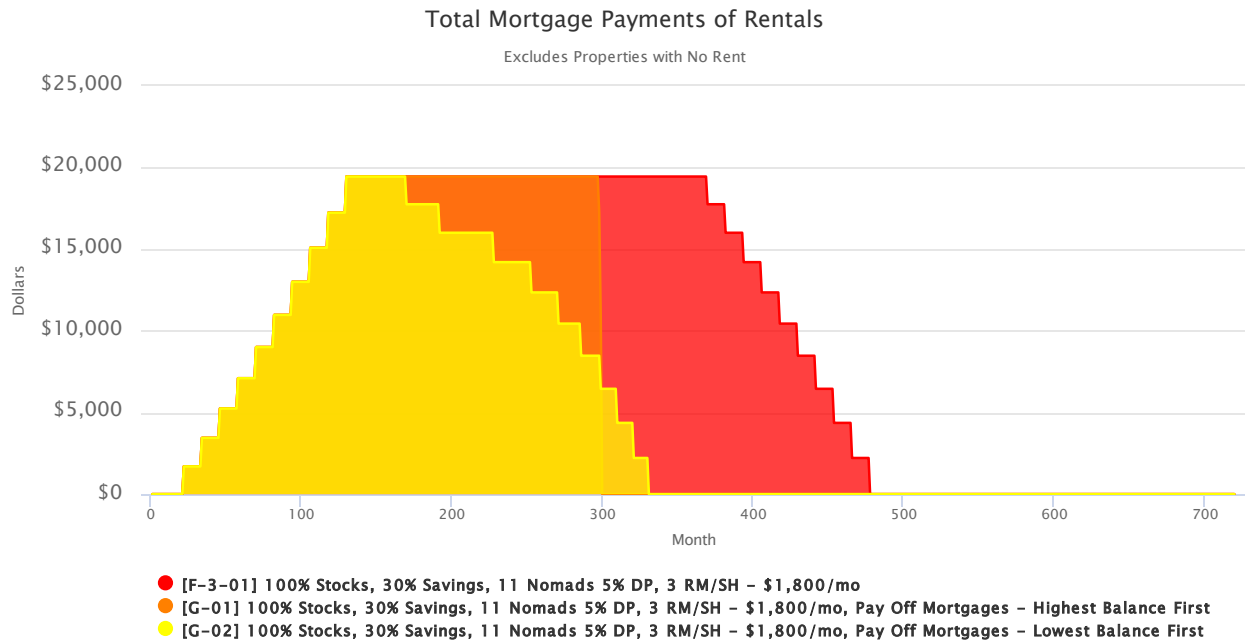


It makes it even faster to achieve financial independence than not paying down the loans at all. It took 216 months to achieve financial independence before we began modeling paying off loans. By paying off the mortgage with the lowest balance first, you are able to reach your financial independence goal to be able to live your passion two years faster in just 192 months.



Why? One reason is that you pay off the smallest loan balance which eliminates that mortgage payment and frees up big chunks of cash flow with each loan that you pay off.

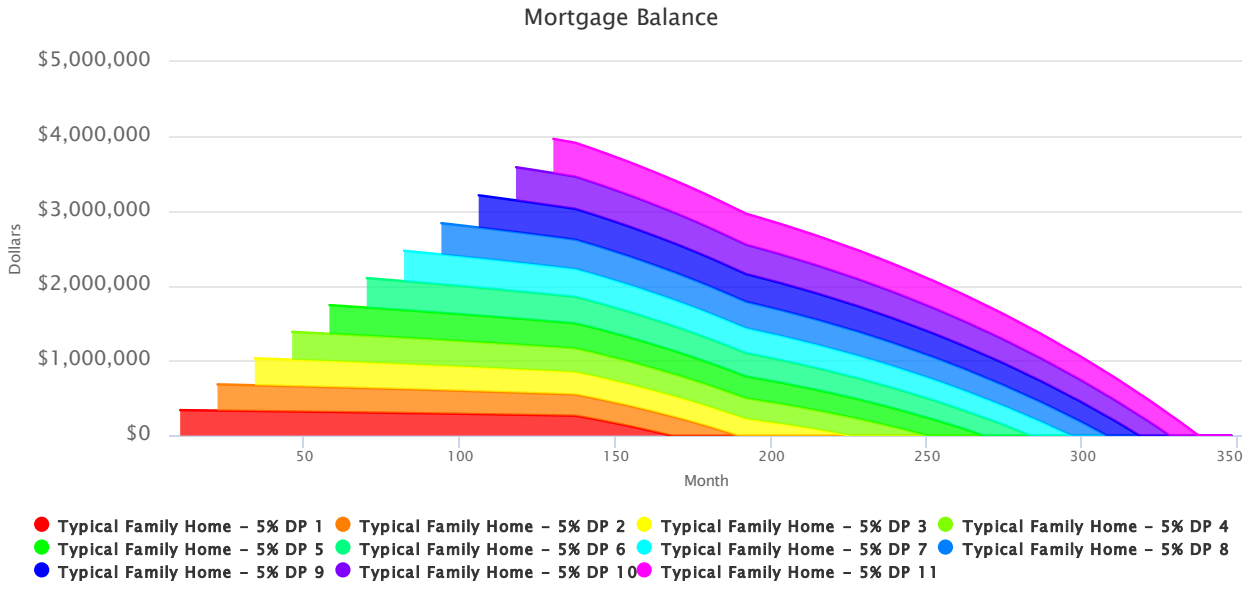
You can see that in the following chart which shows the total mortgage payments of rentals and as you pay off the smaller loans, your total mortgage payment obligations go down.



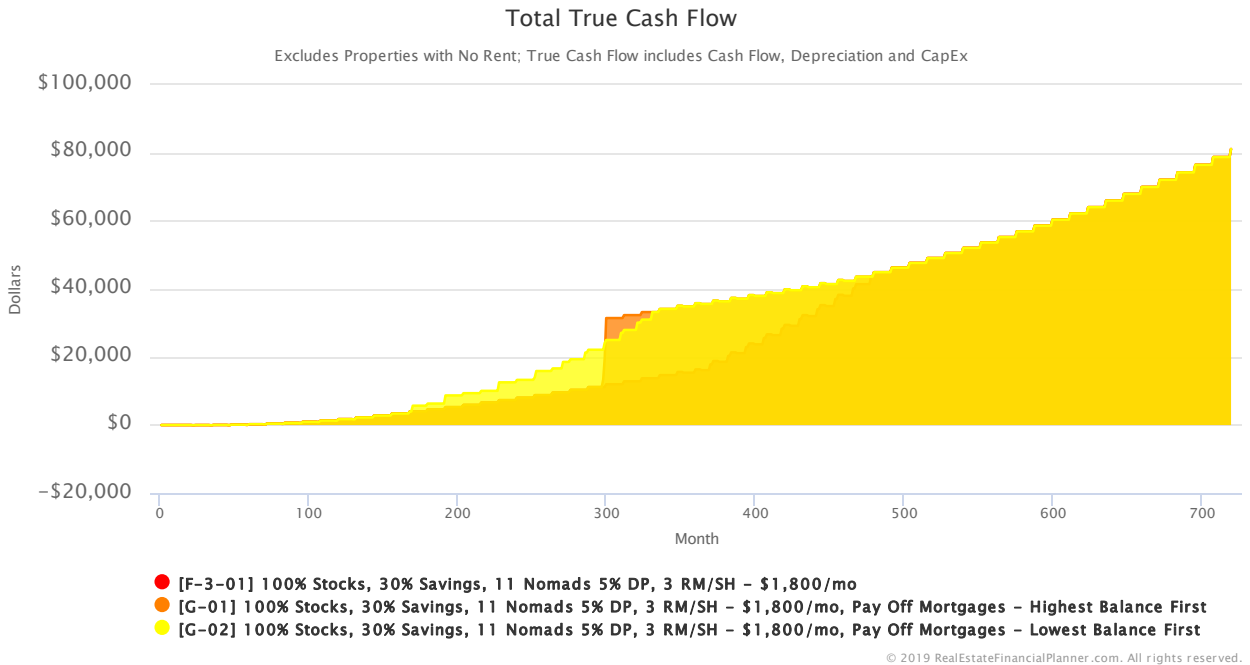
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This is much faster than waiting for the mortgages to pay off naturally. Plus, instead of having all the mortgages pay off around the same time—which happened when you paid off principle on the highest balance each month—you get the benefit of freeing up cash flow as each loan is paid off.

You can see this when we look at the stacked chart of the individual mortgage balances below.



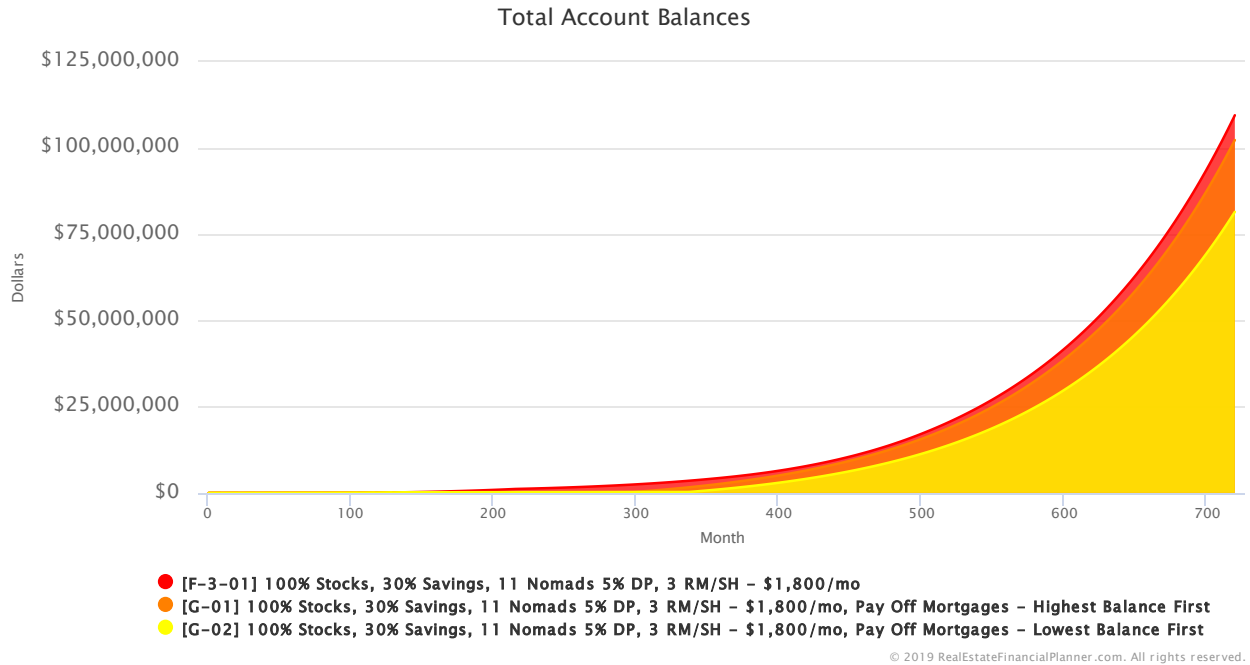
You can also see the impact on True Cash Flow™ in the chart below.



Cash flow improves earliest when you pay off those smaller mortgages and rid yourself of some of the mortgage payments as fast as possible.

Achieving financial independence faster means your job income stops sooner and therefore there is a cost to your savings. Plus, we are assuming that when you hit financial independence you stop with your roommates and/or side hustle as well.

The following chart shows your comparative total stock market account balances when you pay off the highest balance, lowest balance, or let the loans pay off naturally.



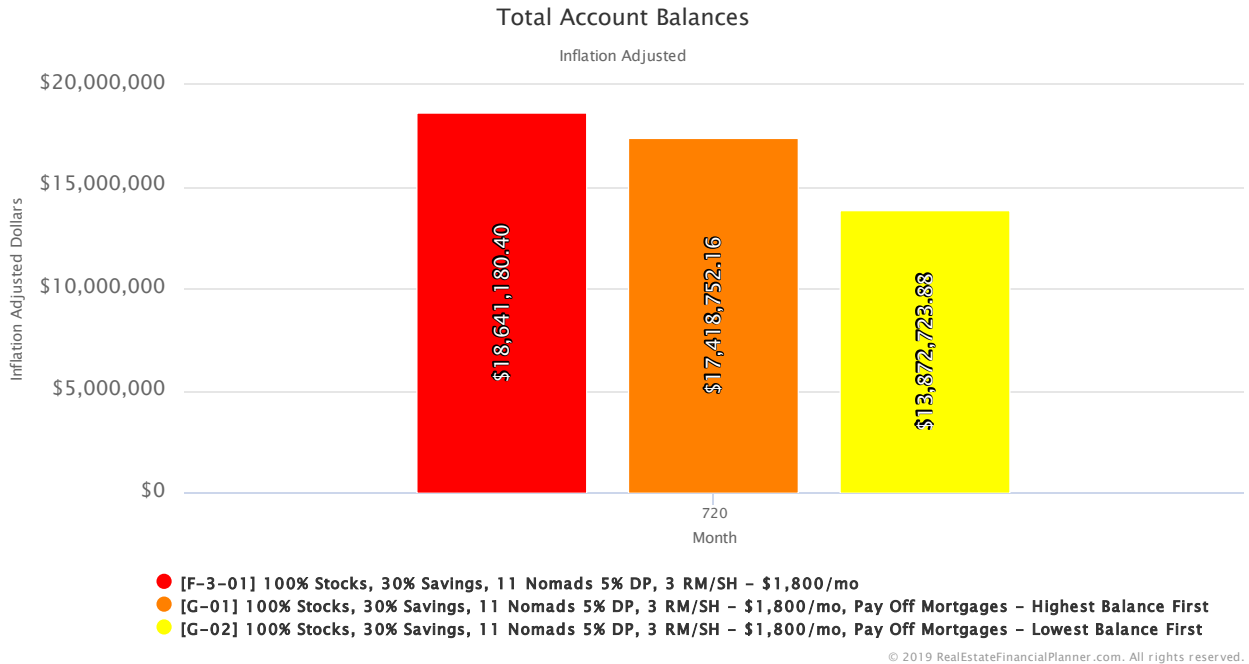
You can see that the highest account balance is from letting your loans pay off naturally. You end up with about \$3.5 million dollars less in net worth in today’s dollars if you pay off the lowest balance first.

Why?

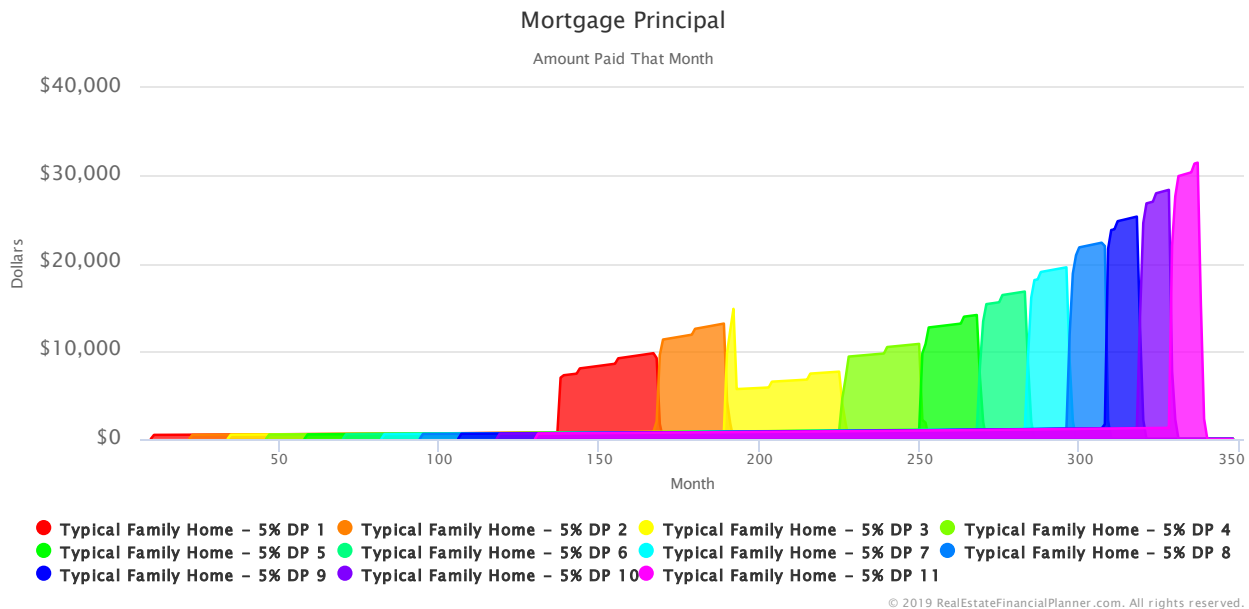
You stop working and earning two years earlier. That’s part of it. But also, you continue to take all the extra money you have and keep paying down low interest rate loans. If you weren’t paying down the loans, your money would be growing in the stock market at 8.97%. Pay down a 4.375% mortgage and earn 4.375% on your money or leave it invested at 8.97% in the stock market? That’s the choice you must make.

You do get to financial independence faster by paying down your loans, but you end up with a much lower account balance doing so.

One could make a case for you to stop paying off your loans once you first hit your financial independence and let the remaining mortgages at that point pay themselves off naturally. I will leave that for you to model yourself using the Real Estate Financial Planner™ software.



If you want to see the impact of losing your job income and its associated monthly savings, plus your side hustle or roommate income, you can see it clearly in this chart of the amount of mortgage principle paid on each loan.

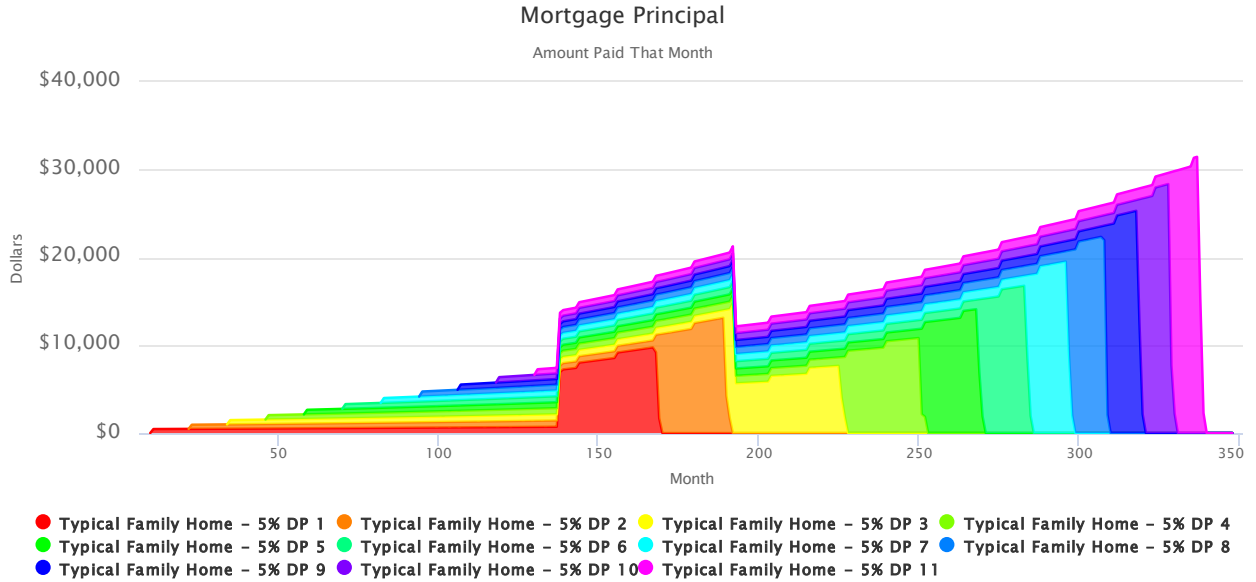


In the chart above you can see that once we've acquired all the properties, met our \$120,000 inflation adjusted buffer, and start to pay down the loans, the amount of extra principle is significant. But shortly after we pay off the second mortgage and make some payments on the third, the amount we are paying

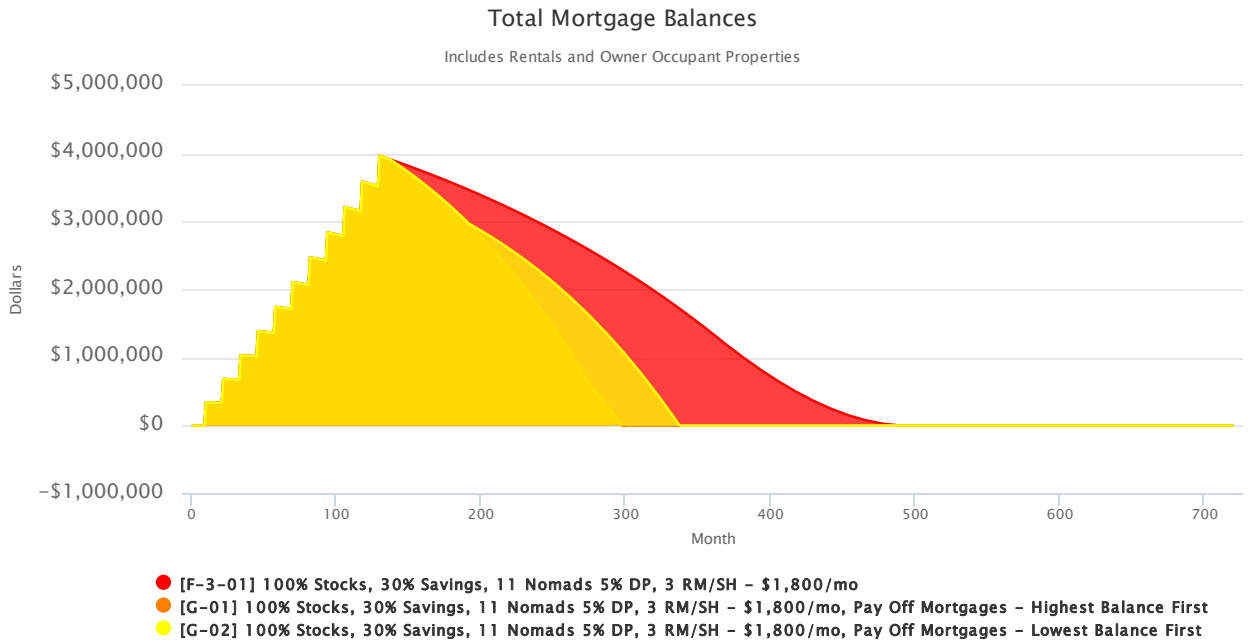


in principle each month drops considerably. That’s when we hit financial independence and stop having extra money from our job, and side hustle or roommate income.

The chart below shows the same chart except we are stacking the total amount of principle paid so you can see how much is applied to each property.

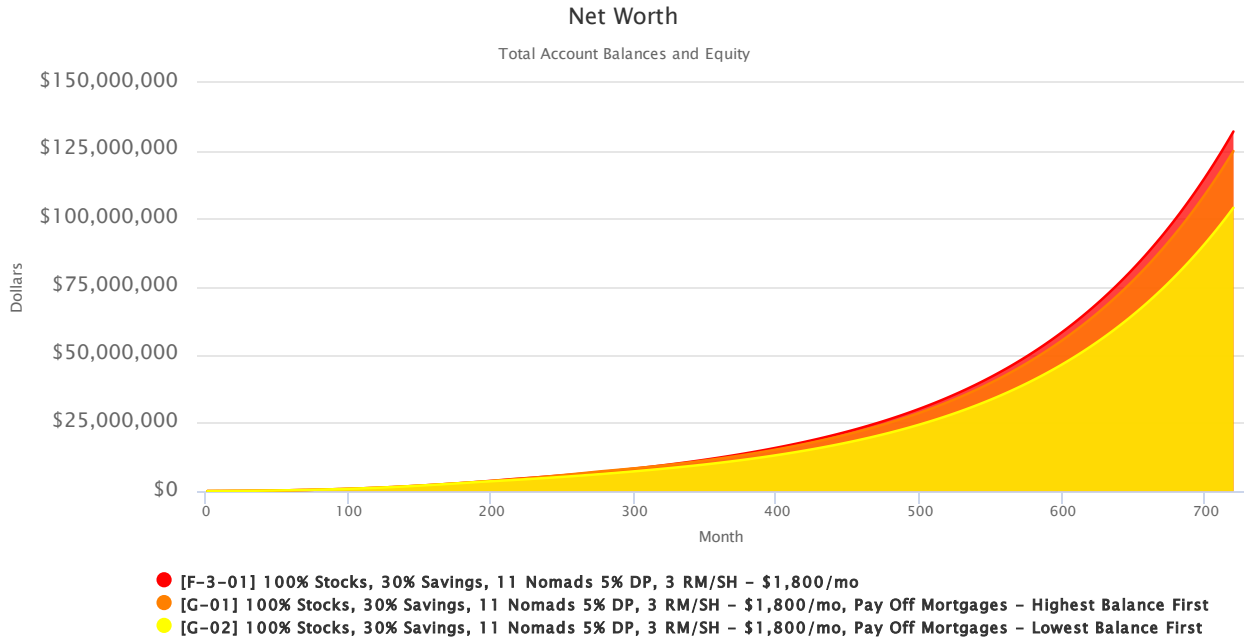


You can see this in the scenario summary of mortgage balances as well in the chart below.

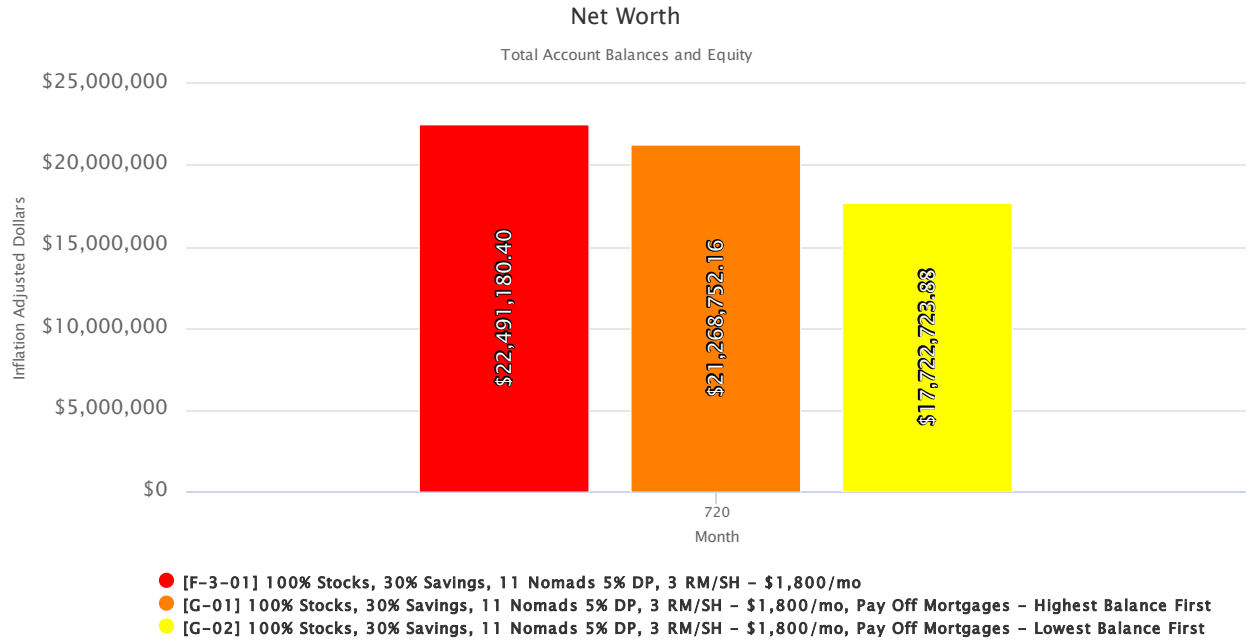


You would expect the total mortgage balances to go down at about the same rate if you are paying the highest balance or lowest balance. But you can see in the chart above that the speed of loan pay off slows considerably with the lowest balance first scenario. Again, this slow down occurs when we no longer have the job, savings, side hustle income and/or roommates coming in to help pay down loans faster.

We have already looked at stock market account balances and in the chart below you can see a similar impact on net worth.

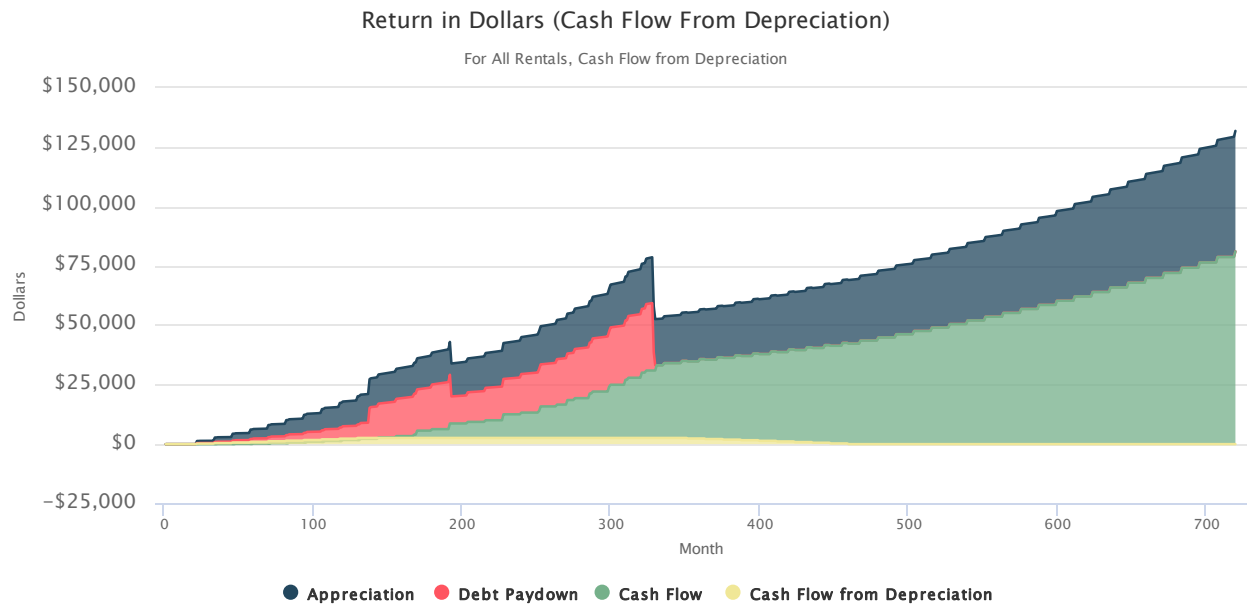


The divergence in net worth is mostly the same as the difference we saw in the stock market account balances.



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One more thing I want to mention about paying off loans early is that this impacts your Return On Investment Quadrant™ numbers as well. The following chart shows the return in dollars as you aggressively pay down your mortgages.



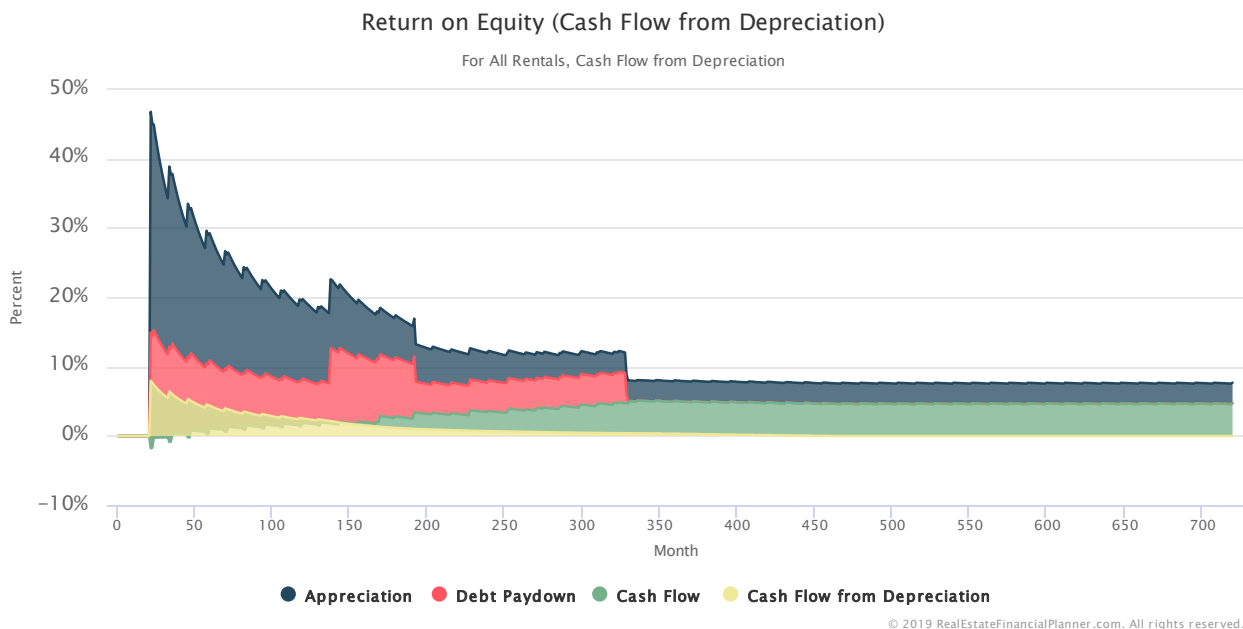
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In this chart you see your debt pay down return end earlier than normal and your cash flow improve faster than normal. Again, your appreciation and cash flow from depreciation remain unchanged.

If we look at the sister chart of return on equity, you can see that your return from paying down loans on your equity again ends earlier than usual. Also, since your equity is increasing faster, your return on equity declines more quickly, and as loans get paid off, we see bumps in return from cash flow on equity.

Of course, return on equity from appreciation and depreciation would have remained the same in raw dollars. However, because equity is increasing faster than even appreciation, return on equity and cash flow from depreciation return on equity are declining more rapidly than in previous scenarios.

Since you are focused on achieving FI, don't get hung up on return on equity. I just wanted to share this information to give you perspective! The goal is to have cash flow that meets your needs for leaving your job.



## Model It Yourself

If you want to copy any of the scenarios in which we pay down mortgages faster to your own Real Estate Financial Planner™ account and adjust the assumptions, you can use the links below.

- 100% Stocks, 30% Savings, 11 Nomads 5% DP, 3 RM/SH - \$1,800/mo, Pay Off Loans From Cash Flow – Highest Loan Balance First  
<http://refp.io/655>
- 100% Stocks, 30% Savings, 11 Nomads 5% DP, 3 RM/SH - \$1,800/mo, Pay Off Loans From Cash Flow – Lowest Loan Balance First  
<http://refp.io/656>

If you do end up implementing one of these scenarios, I would strongly advise you to do full Monte Carlo testing as we described previously.

To find and copy any of the other scenarios covered in this book, follow the link below.

- <https://realestatefinancialplanner.com/filyp/>



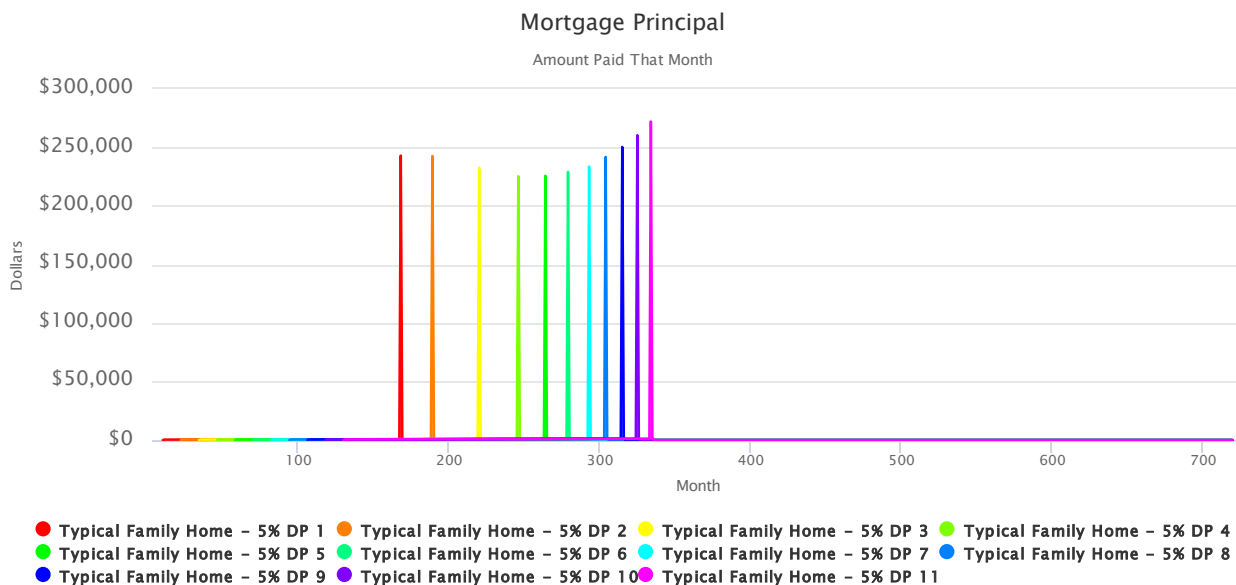
## Path 8: Paying Off Mortgages—But Only In-Full

In the previous chapter we discussed taking any extra cash above a certain threshold in your stock market account and using that money to pay down mortgages faster. In this chapter, we are going to add just one small additional twist.

Instead of making small additional principle payments each month that you have extra money, you will wait until you have enough in your stock market account to pay off the entire loan in a single payment. When you have enough to pay off the entire loan, then and only then, will you pay it off.

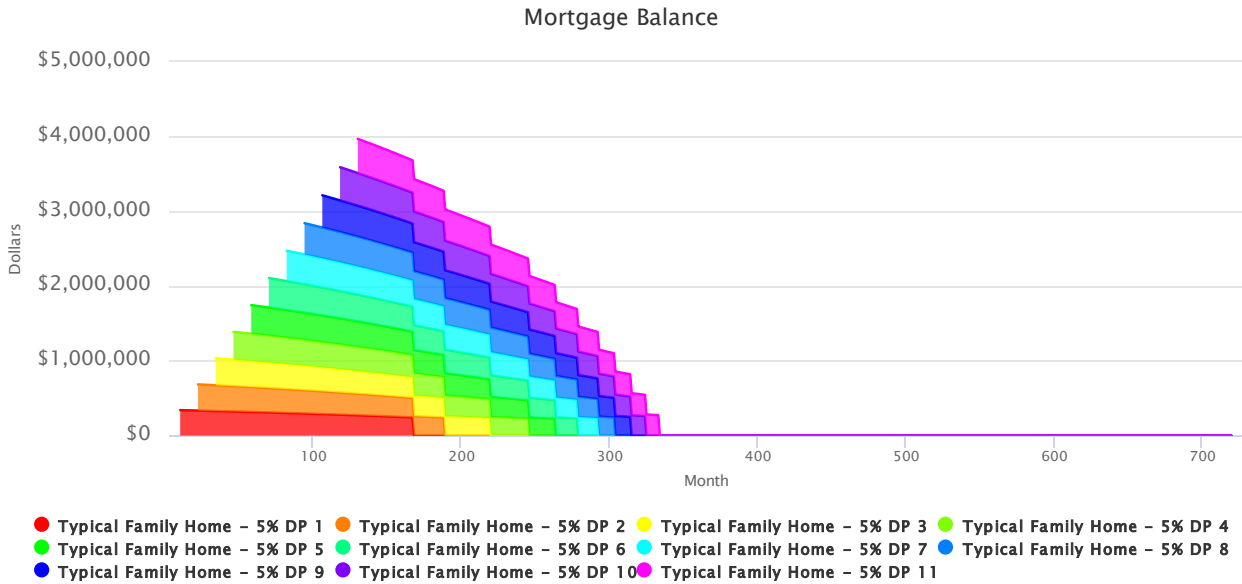
Since we will have enough to pay off the lowest balance loan first, we will assume that this is the one we start with.

In the chart below you can see that instead of the smaller, more consistent monthly extra principle payments, there are spikes of mortgage principle payments each time that you have enough saved up in the stock market account to completely pay off a mortgage.



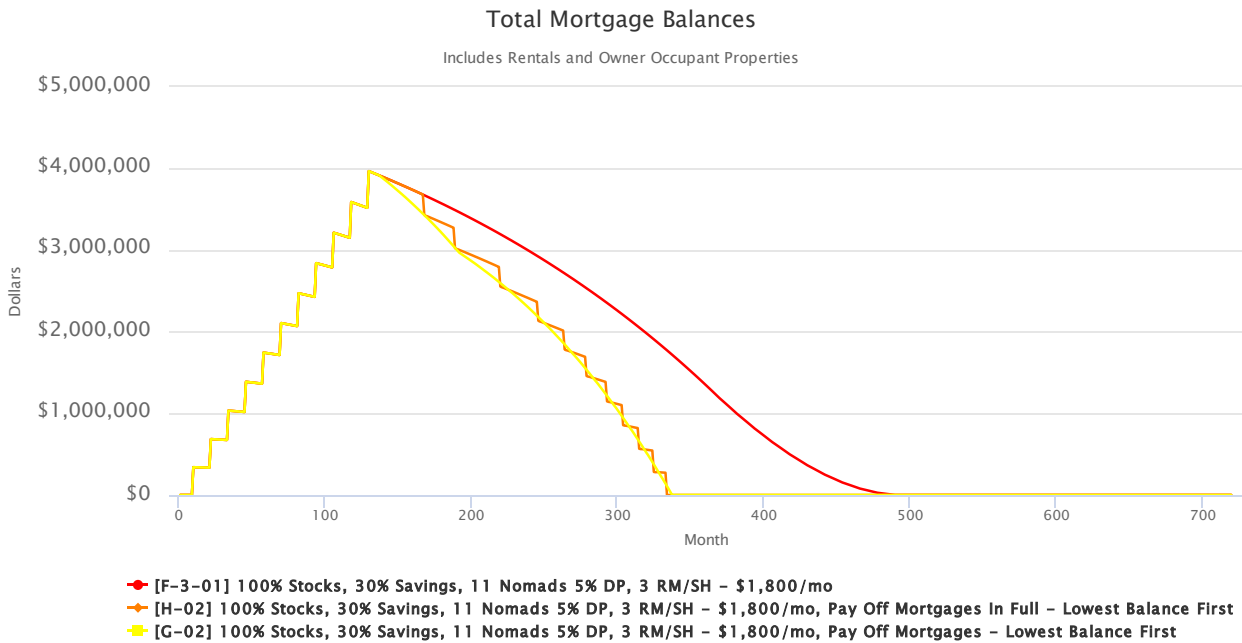
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In the chart below, you can also see the individual mortgage balances over time. As each loan is paid off in a single month, that mortgage balance goes to zero until your total mortgage balance for all properties is zero.



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If you would like to compare the total mortgage balance for the last three key scenarios: no extra pay down, more aggressive mortgage pay down monthly with the lowest balance mortgages first, and paying down mortgages but only in-full, you can see that in the chart below.

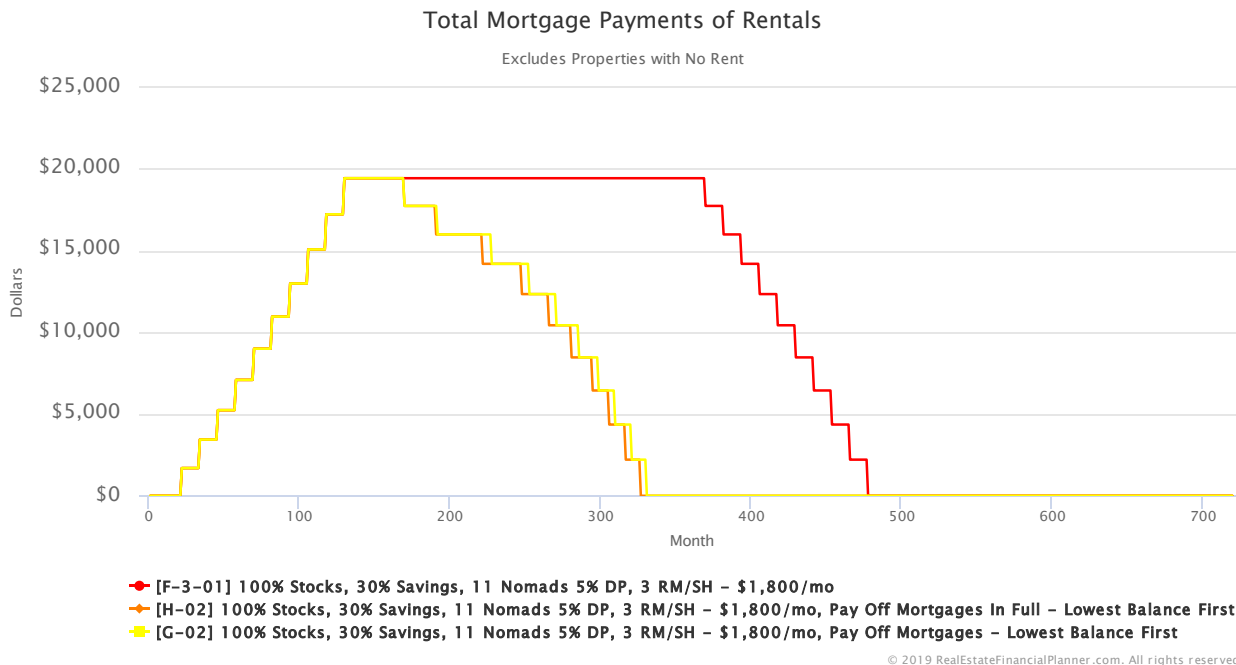


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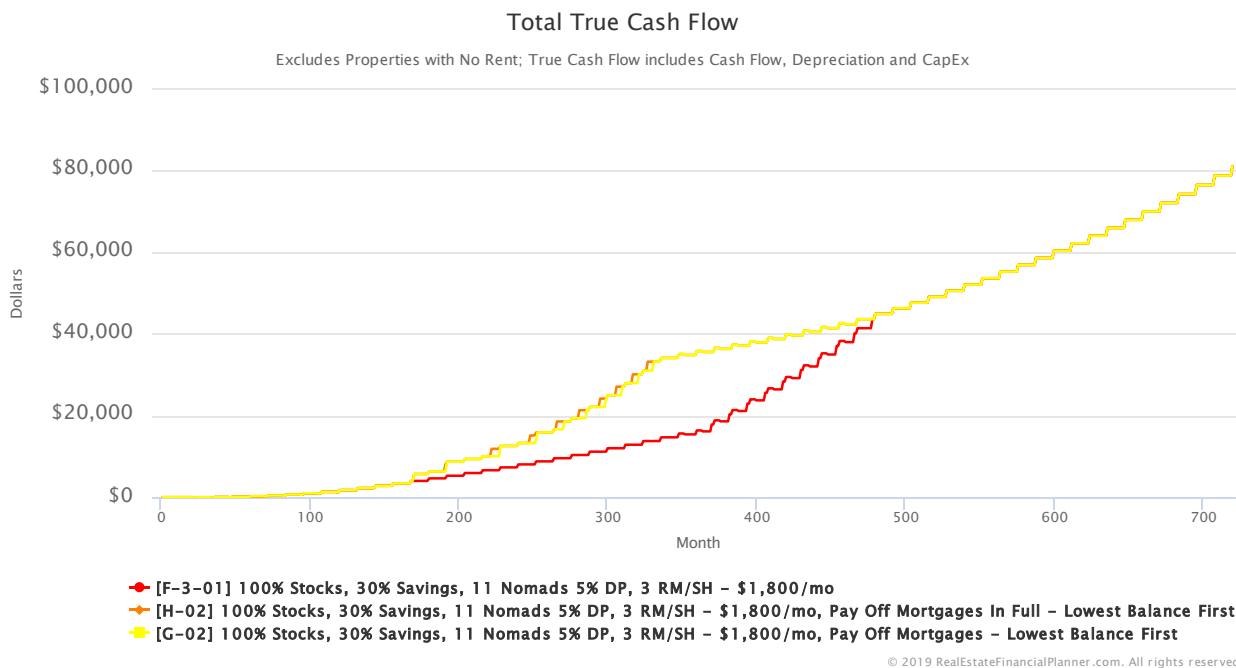
While it takes longer for you to pay off mortgages if you do not pay extra on the principle, there is not a huge speed advantage to paying off the mortgages in-full compared to paying off the mortgages with any extra cash flow monthly.



The chart below shows the total of all the mortgage payments you have on all your properties in any month and you can see a slight benefit to paying off mortgages in-full. There is a small increase in speed of payoff. This is likely caused by allowing your money to remain invested in the stock market at a higher interest rate of 8.97% rather than just getting the benefit of not having to pay 4.375% on the loan.



How does this impact cash flow though?



The chart above shows True Cash Flow™ and you can see that because the loans are paid off a bit faster, you have a very slight improvement in cash flow from paying off the properties in full versus the scenario where you are paying them off monthly. Again, whether you pay your loans off monthly with cash flow, or all at once, is about the same comparatively. However, both are better for cash flow than letting them pay off on their default minimum payment schedule.

There is a discussion I would like to have about paying mortgages off monthly or all at once. There are advantages to each.

An advantage to paying off your mortgages monthly is the money is no longer at risk of a stock market decline. It has been spent to lock in a 4.375% guaranteed return. It is guaranteed because if you pay down your mortgage, you are no longer paying the 4.375% to your lender. You no longer need to make that interest payment and therefore you save yourself 4.375%.

An advantage of keeping your money in the stock market is that you may get a higher return than the 4.375% interest rate of your mortgage as a return. The disadvantage is that there might be a year the stock market declines and you end up getting a negative return and losing some of your principle investment that you could have used to pay off your mortgage.

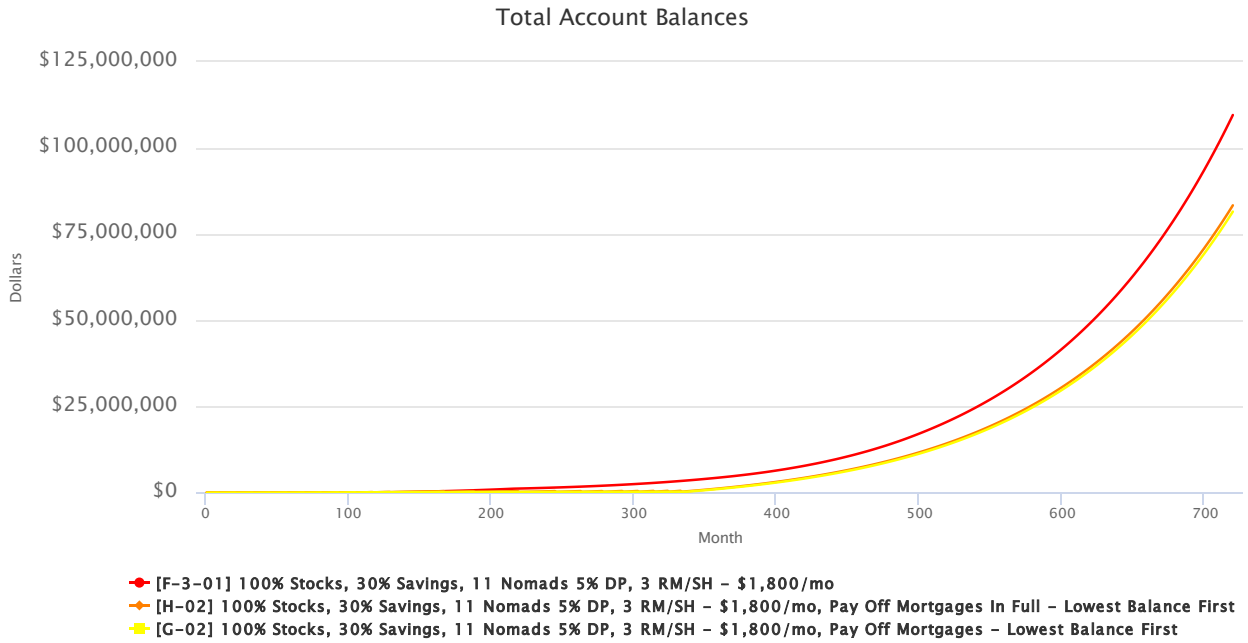
A disadvantage of paying off your mortgage though is that the money is less liquid once you have trapped it as equity in the property. Sure, you could, in theory, sell the property or refinance the property to access the equity. There is likely a significant cost and time commitment to sell the property. So, make sure you consider that. Plus, if you decide to refinance, that assumes you can qualify and that lenders are offering that type of loan. There are times when credit is tighter than others and you may not be able to easily do a cash out refinance. Also, interest rates may have gone up considerably higher than the interest rate you currently have on your mortgage and you may opt not to refinance in order to keep the lower mortgage interest rate.

In general, you can lock in a lower return at the cost of some liquidity by paying down your mortgages with extra principle payments. If you opt to continue investing in the stock market, you might get a higher return by speculating, and you do keep more liquidity.

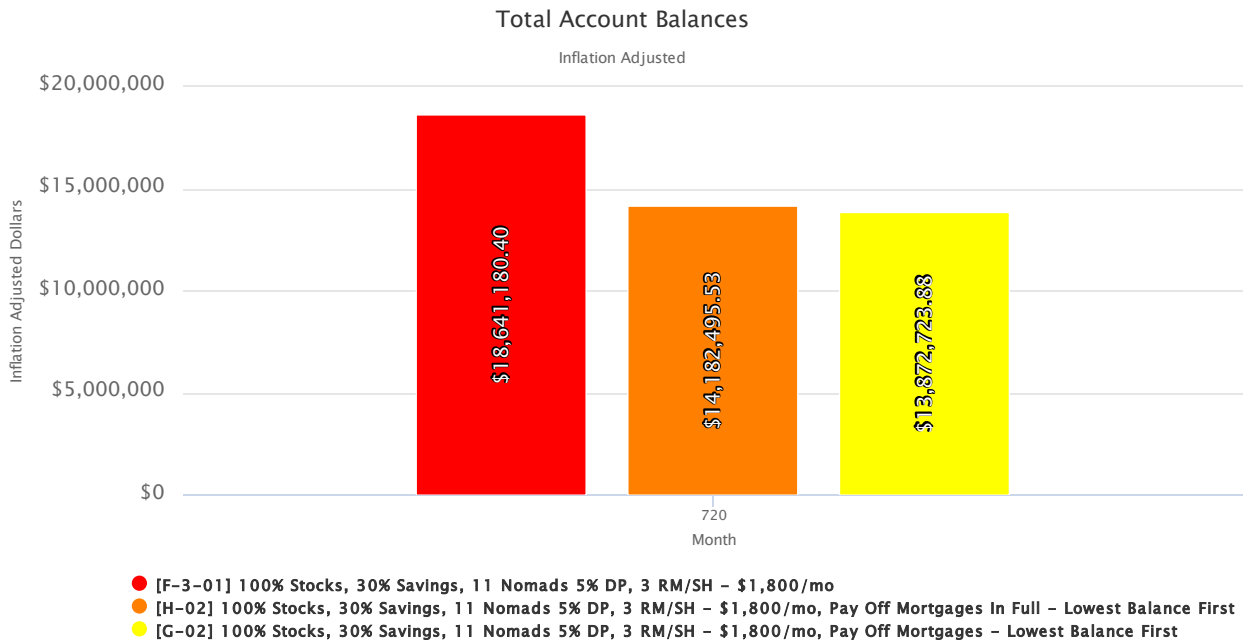
You can test how this might work for yourself with the Real Estate Financial Planner™ software too and model the risk of market declines. One additional point to consider when playing with these options yourself is that paying down mortgages when you intend to buy additional properties may not be the best option. It might be better to keep that extra money for future down payments because it may be harder to access the equity you gained by paying additional principle when you need it for a down payment.

Again, these are all things for you to consider yourself.

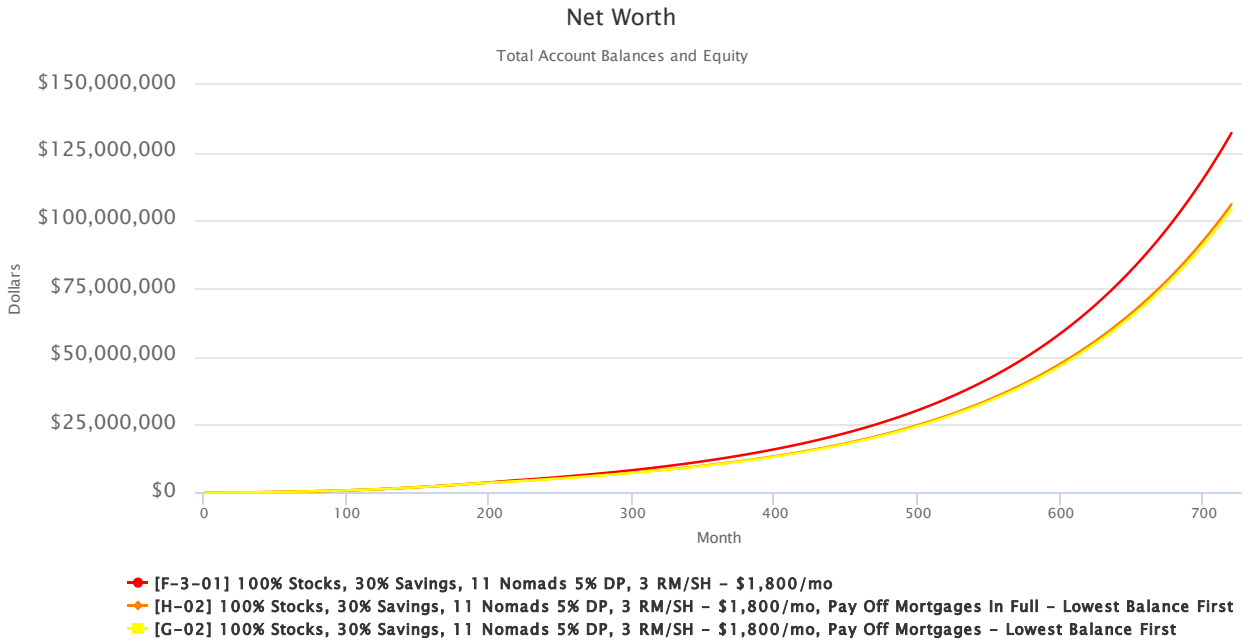
Back to our comparison of paying off properties with cash flow or in-full. Let's look at stock market account balances. If you are paying off loans by making additional principle payments—either in-full or monthly from cash flow—in both cases you end up with a lower stock market account balance than if you just let the mortgages pay off at their default, minimum payment rate. You can see this in the chart below.



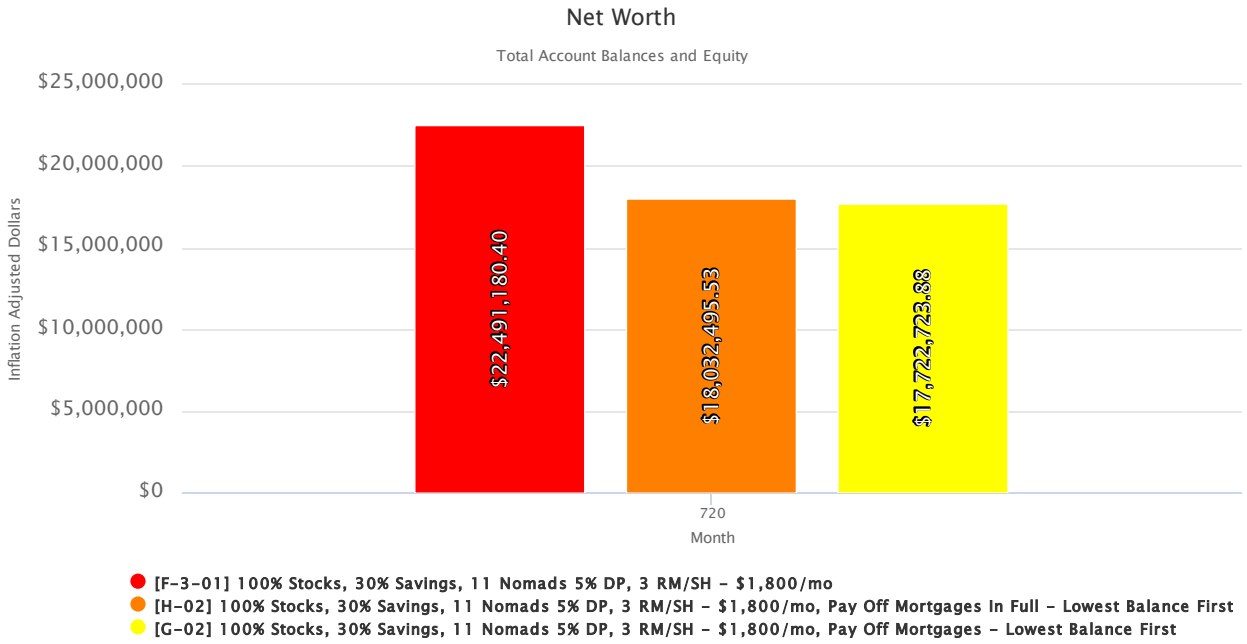
How big of a difference is it? If we look at month 720 and adjust back to today's dollars you can see the comparison below.



How about net worth? Is that like stock market account balances? Yes, yes... it is. You can see this in the next chart which shows net worth from the different scenarios.

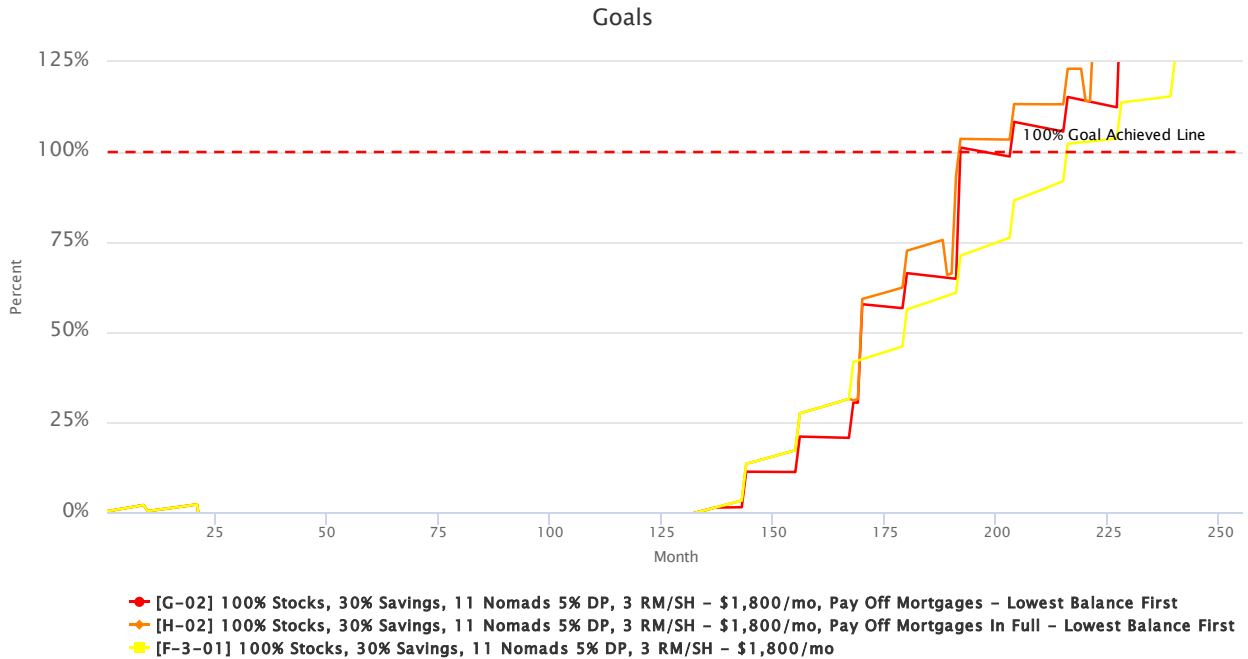


If we look at month 720, 60-years in the future, and adjust back to today’s dollars you can see the difference in net worth in the chart below.



What is interesting though is that while you end up with a higher net worth by not paying additional principle on your mortgages, you achieve financial independence faster by paying down your loans with extra principle payments.

But does waiting to make a one-time mortgage pay off allow you to be financially independent faster than paying a little bit of extra principle each month? Check out this next chart to find out.



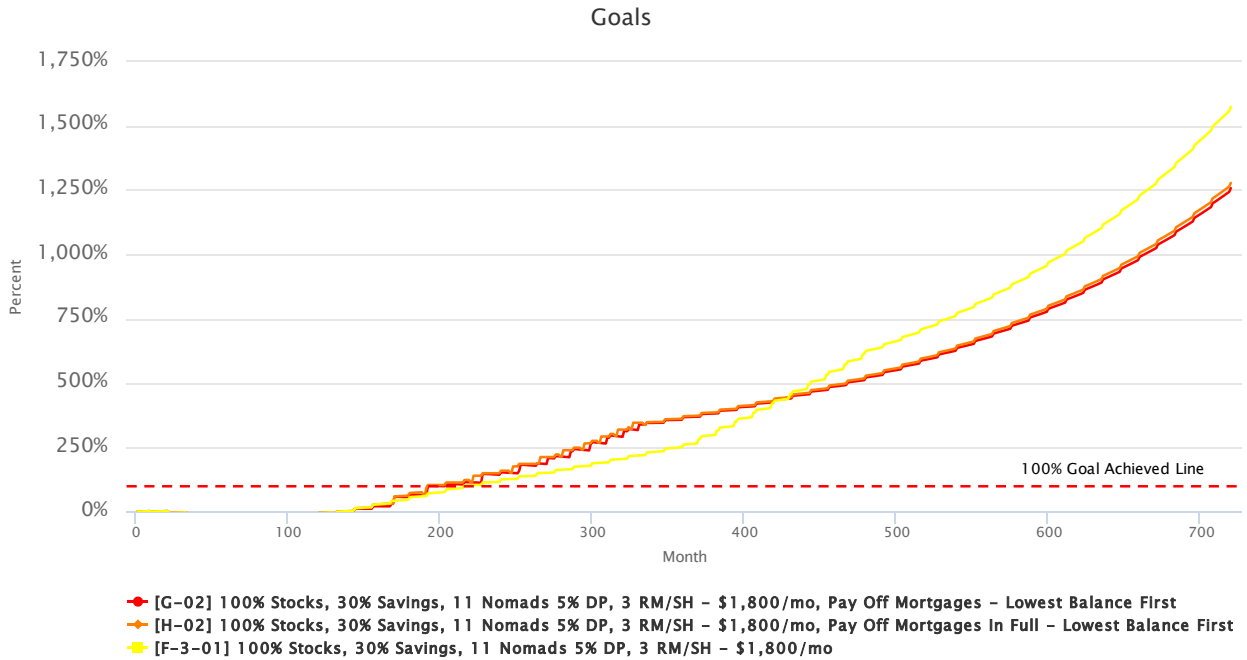
The answer is not really. It takes about the same amount of time to achieve financial independence whether you make extra principle payments monthly from cash flow or just wait until you have enough to pay off the entire property in-full.

Remember when we discussed account balance and net worth before? You can see the impact of that higher stock market account balance in the zoomed-out version for your goal of financial independence.

You can enjoy a higher standard of living (a larger percentage of the goal achieved) with the scenario where you did not pay the loans off faster.

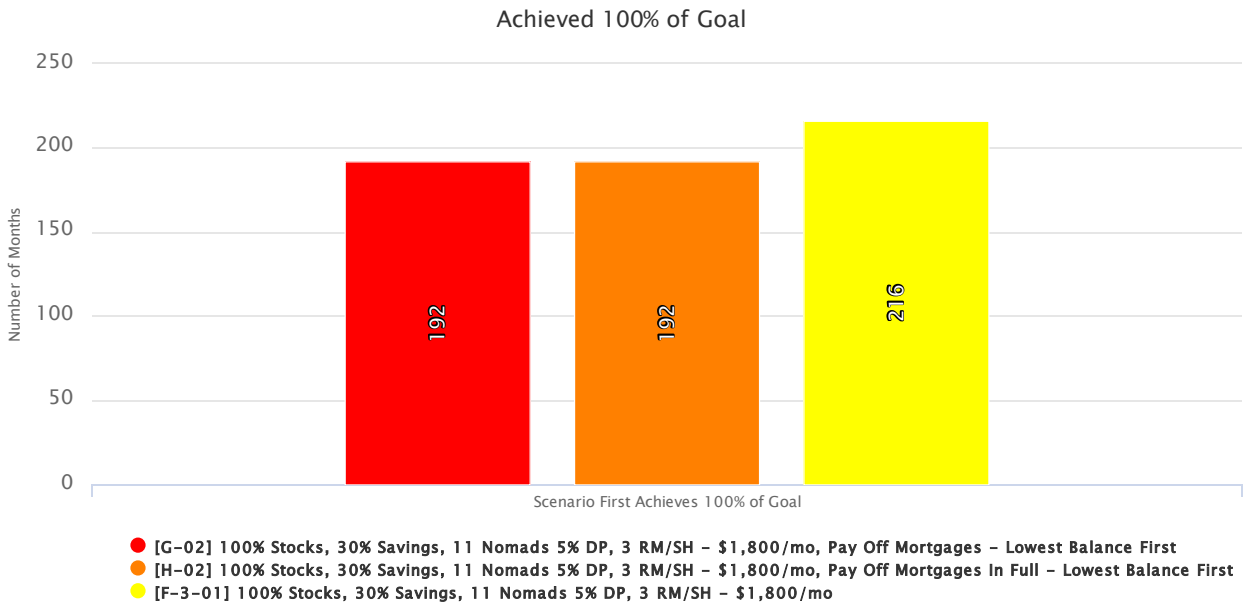
As I mentioned previously, this begs the question of whether you should continue to pay off your mortgage at an accelerated pace once you hit your financial independence number.

It also brings up an interesting question of whether you could “coast” into financial independence by tapping into your stock market account balance more aggressively than your defined safe withdrawal rate knowing that you have rental income that will be increasing as you pay off mortgages. This is a more aggressive strategy in my opinion, but one you could test with the Real Estate Financial Planner™ to see how it might work in a variety of market conditions.



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To summarize, as you can see in the chart below, your time to achieve FILYP is the same with this specific set of assumptions regardless of which way you pay off your loans faster: monthly or only in-full.



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## Model It Yourself

If you want to copy the payoff mortgage in full scenario to your own Real Estate Financial Planner™ account and adjust the assumptions, you can use the link below.

- 100% Stocks, 30% Savings, 11 Nomads 5% DP, 3 RM/SH - \$1,800/mo, Pay Off Loans In-Full – Lowest Loan Balance First  
<http://refp.io/658>

If you do end up implementing this scenario, I would strongly advise you to do full Monte Carlo testing as we described previously.

To find and copy any of the other scenarios covered in this book, follow the link below.

- <https://realestatefinancialplanner.com/filyp/>





## Path 9: Fewer Properties

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Earlier in the book, we discussed buying different quantities of properties. We started with just renting then added a single property we owner-occupied.

Next, we added one rental property. After that, we added several rental properties.

Throughout the previous chapters, we have primarily been discussing 11 Nomad™ properties: one to owner-occupy and 10 rentals.

Is it possible that buying fewer properties could help you achieve financial independence and live your passion sooner? How will it impact your standard of living when you do stop working solely for money?

That's what we will discuss next.

So far, the fastest strategy for achieving financial independence has been to buy 11 Nomad™ properties (one to owner-occupy and 10 rentals) and then aggressively pay additional principle payments—either monthly from cash flow or in big chunks to pay mortgages in-full. Either scenario took 192 months to achieve financial independence.

Let's see how buying fewer properties will impact the speed to FILYP.

In all the cases below you still:

- Invest in stocks at 8.97% per year.
- Save 30% of your income.
- Put 5% down as a Nomad™ when you buy properties.
- Have a side hustle or roommates bringing in an extra \$1,800 per month.
- Pay off mortgages in-full starting with the lowest balance.
  - There is one exception where you are paying off mortgages monthly with cash flow.

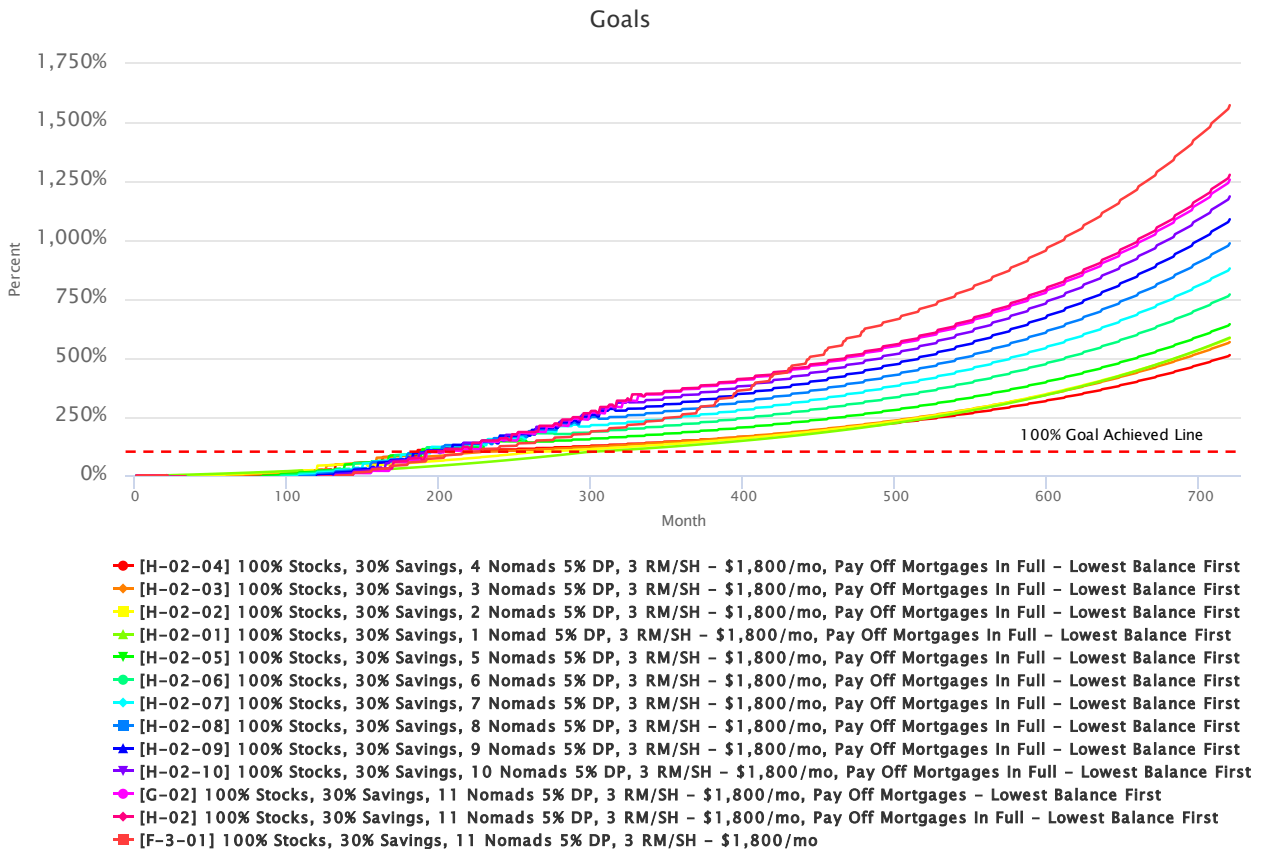
Here are the scenarios ranked in order of speed to financial independence going from longest to shortest:

1. If you buy just 1 Nomad™, no rentals, and live there, you achieve financial independence in 24 years and 9 months (297 months). You would be able to stop working and live your passion at age 47.
2. If you buy 2 Nomads™, one owner-occupant and one rental, you achieve financial independence in 21 years and 10 months. You would be able to start living your passion at 42 years old.
3. If you buy 3 Nomads™: one owner-occupant and two rentals, you achieve financial independence in 18 years and 11 months. You could live your passion at age 41.
4. Your next fastest scenario would be to not pay off mortgages ahead of schedule at all. Just do 11 Nomads™ resulting in one owner-occupant and ten rentals. You achieve financial independence in 18 years. You'd be 40 years old, and with 10 rentals, your standard of living over time would be one of the best of all the scenarios since you'd have cash flow on 10 free and clear rentals eventually.

5. There is a 7-way tie for the next scenarios. All of them take 16 years or 192 months. You would be able to be financially independent by 38 years old. The scenarios are:
  - a. 6, 7, 8, 9, 10 or 11 Nomads™ paying off mortgages in-full
  - b. 11 Nomads™ paying off mortgages monthly from cash flow
6. Your second fastest scenario is to buy 5 Nomads™: 1 owner-occupant and 4 rentals. This gets you to financial independence in 15 years and 9 months (189 months). You'd be 38.
7. And the fastest scenario is to buy only 4 Nomads™: 1 owner-occupant and 3 rentals. This gets you to financial independence in 15 years and 6 months (186 months). You'd still be 38.

## Goal of Financial Independence

You can see a chart showing each of these scenarios and how they measure your progress toward your goal of reaching financial independence.

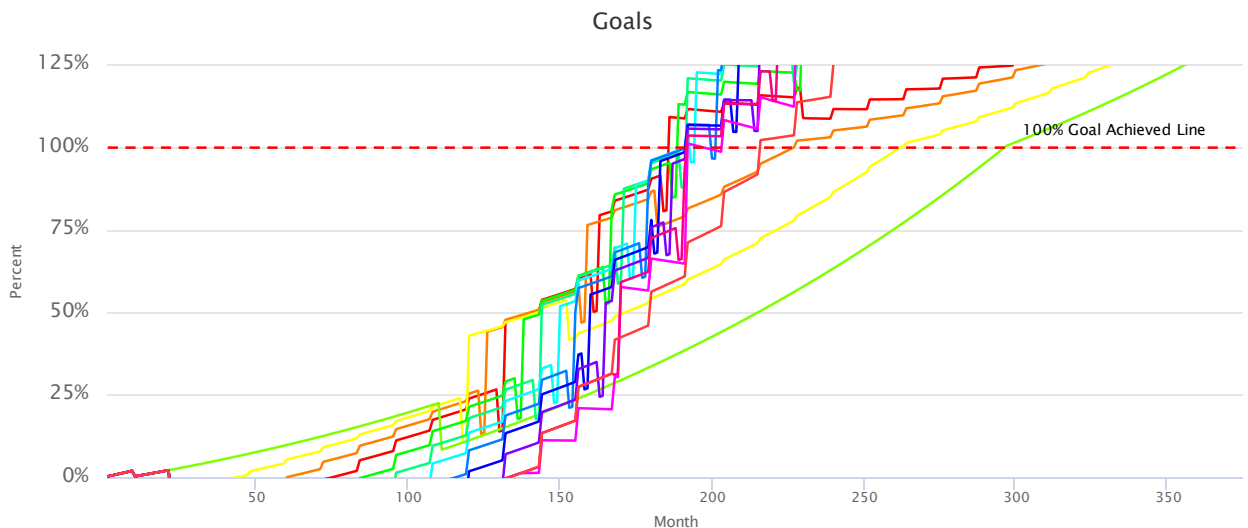


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One important thing to note about the busy chart above - first to financial independence does not mean highest standard of living in retirement. The highest standard of living, shown by the line that is the highest for the majority of your time after you achieve financial independence, results from buying 11 Nomads™ and making the minimum payments on your mortgages letting them pay down naturally.

In general, the more properties you own—and specifically the more rental properties you own—the higher your income is after you reach financial independence and pay off those mortgages.

If we zoom in a bit to look at when they first hit 100% of your goal of achieving financial independence, we can see how they cluster.



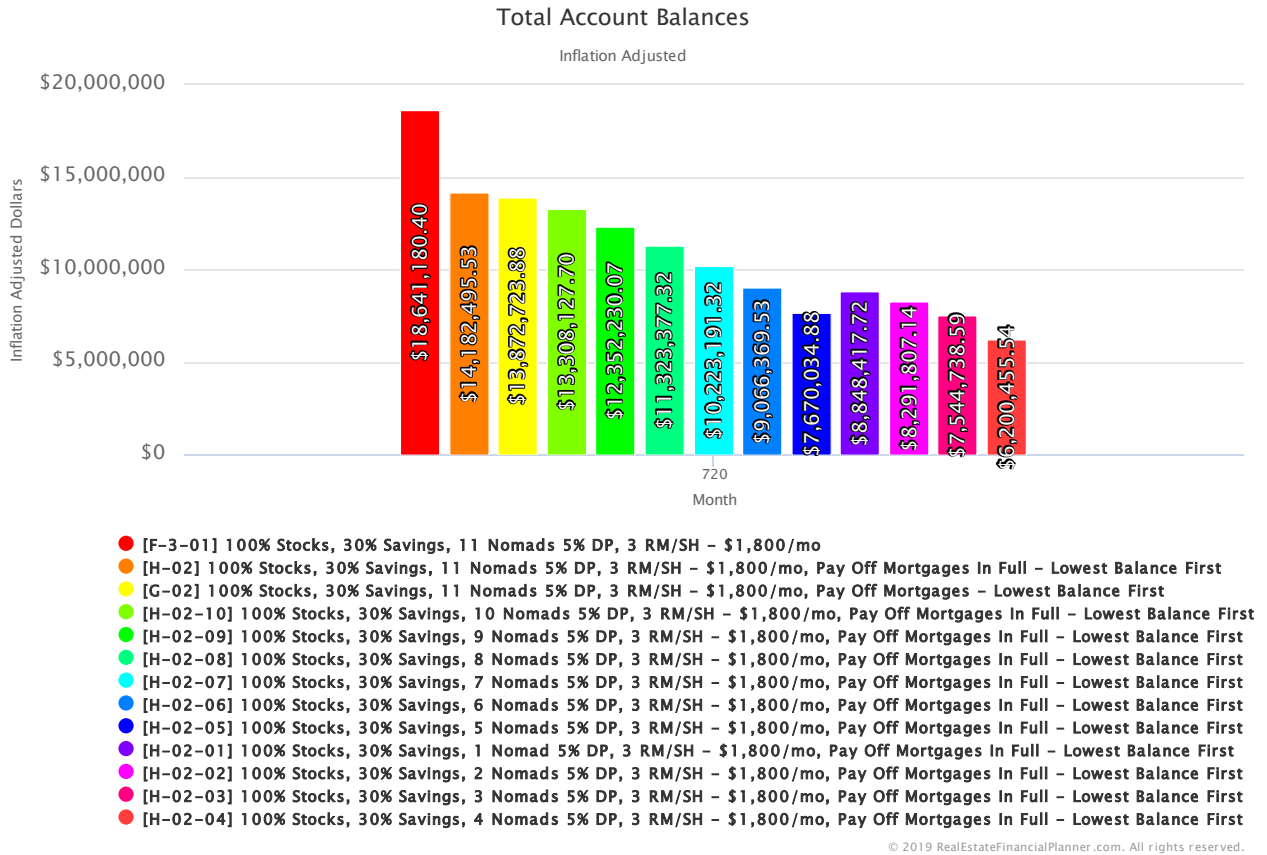
- ◆ [H-02-04] 100% Stocks, 30% Savings, 4 Nomads 5% DP, 3 RM/SH – \$1,800/mo, Pay Off Mortgages In Full – Lowest Balance First
- ◆ [H-02-03] 100% Stocks, 30% Savings, 3 Nomads 5% DP, 3 RM/SH – \$1,800/mo, Pay Off Mortgages In Full – Lowest Balance First
- ◆ [H-02-02] 100% Stocks, 30% Savings, 2 Nomads 5% DP, 3 RM/SH – \$1,800/mo, Pay Off Mortgages In Full – Lowest Balance First
- ◆ [H-02-01] 100% Stocks, 30% Savings, 1 Nomad 5% DP, 3 RM/SH – \$1,800/mo, Pay Off Mortgages In Full – Lowest Balance First
- ◆ [H-02-05] 100% Stocks, 30% Savings, 5 Nomads 5% DP, 3 RM/SH – \$1,800/mo, Pay Off Mortgages In Full – Lowest Balance First
- ◆ [H-02-06] 100% Stocks, 30% Savings, 6 Nomads 5% DP, 3 RM/SH – \$1,800/mo, Pay Off Mortgages In Full – Lowest Balance First
- ◆ [H-02-07] 100% Stocks, 30% Savings, 7 Nomads 5% DP, 3 RM/SH – \$1,800/mo, Pay Off Mortgages In Full – Lowest Balance First
- ◆ [H-02-08] 100% Stocks, 30% Savings, 8 Nomads 5% DP, 3 RM/SH – \$1,800/mo, Pay Off Mortgages In Full – Lowest Balance First
- ◆ [H-02-09] 100% Stocks, 30% Savings, 9 Nomads 5% DP, 3 RM/SH – \$1,800/mo, Pay Off Mortgages In Full – Lowest Balance First
- ◆ [H-02-10] 100% Stocks, 30% Savings, 10 Nomads 5% DP, 3 RM/SH – \$1,800/mo, Pay Off Mortgages In Full – Lowest Balance First
- ◆ [G-02] 100% Stocks, 30% Savings, 11 Nomads 5% DP, 3 RM/SH – \$1,800/mo, Pay Off Mortgages – Lowest Balance First
- ◆ [H-02] 100% Stocks, 30% Savings, 11 Nomads 5% DP, 3 RM/SH – \$1,800/mo, Pay Off Mortgages In Full – Lowest Balance First
- ◆ [F-3-01] 100% Stocks, 30% Savings, 11 Nomads 5% DP, 3 RM/SH – \$1,800/mo

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## Stock Market Account Balances

How much does each scenario end up with in your stock market account? I’m glad you asked.

The chart below shows you the stock market account balance 60-years (720 months) into the scenario. I have gone ahead and adjusted the chart for inflation back to today’s dollars.

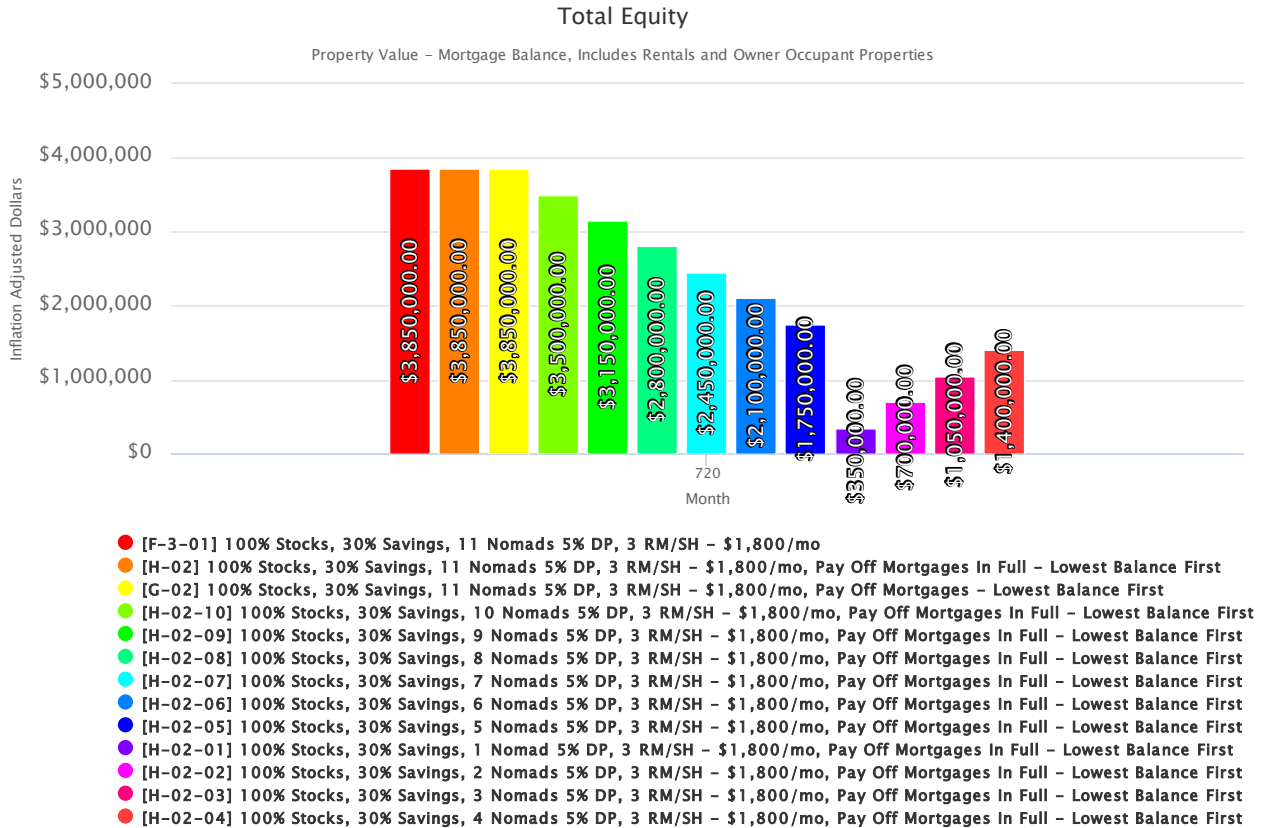


As it turns out, the scenario with 11 Nomads™ following the standard re-payment schedule results in \$18.6 million dollars in your stock market account. The next highest balance is \$14.1 million from the 11 Nomads™ paying off the mortgage in full lowest balance first scenario. The worst performing scenario for your stock market balance is the one with four Nomads™ paying off the mortgage in full lowest balance first.

### Real Estate Equity and Net Worth

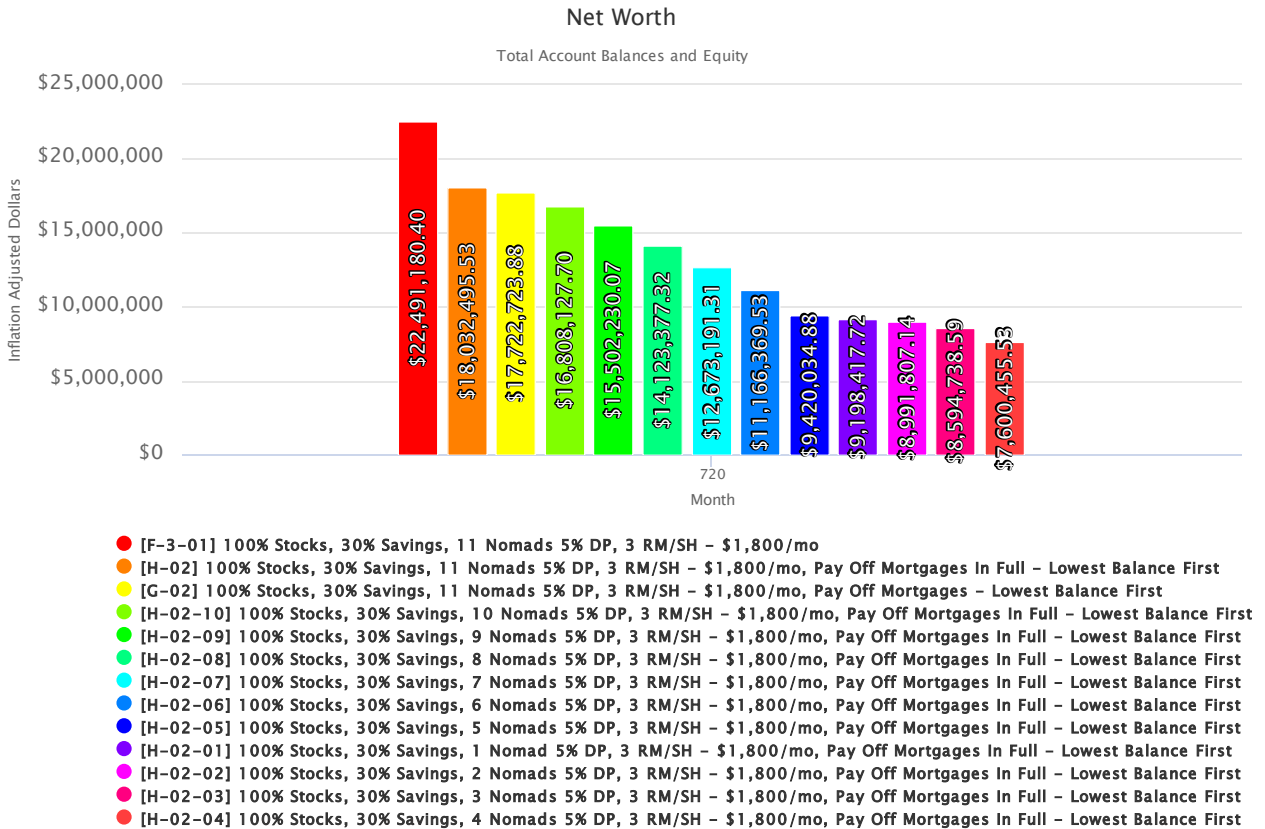
Now that we are playing around with the number of properties owned as well, the stock market account balance is just one factor included in calculating net worth. You also need to consider the value of the properties you own. In general, the more properties you have, the larger your net worth will be.

If we look only at the total equity you have in each of your properties, you can see the inflation adjusted equity for each scenario in the chart below. We are showing month 720.



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If you'd like to look at your net worth for these scenarios, the following chart summarizes your net worth at 720 months, 60-years in the future, adjusted for inflation back to today's dollars.



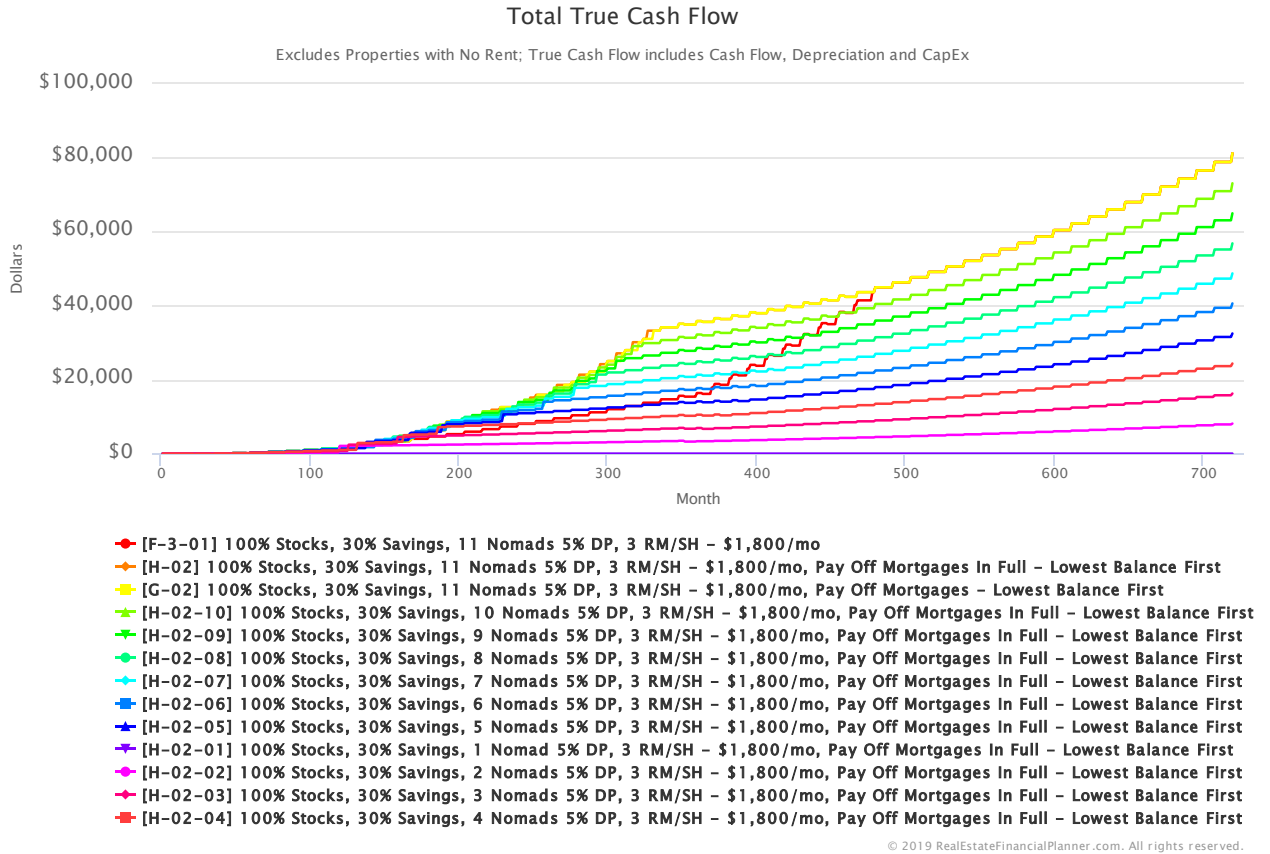
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## True Cash Flow™

Net worth isn't everything. In fact, when you are living off the income from your assets, many folks would make a compelling argument that cash flow is even more important than net worth.

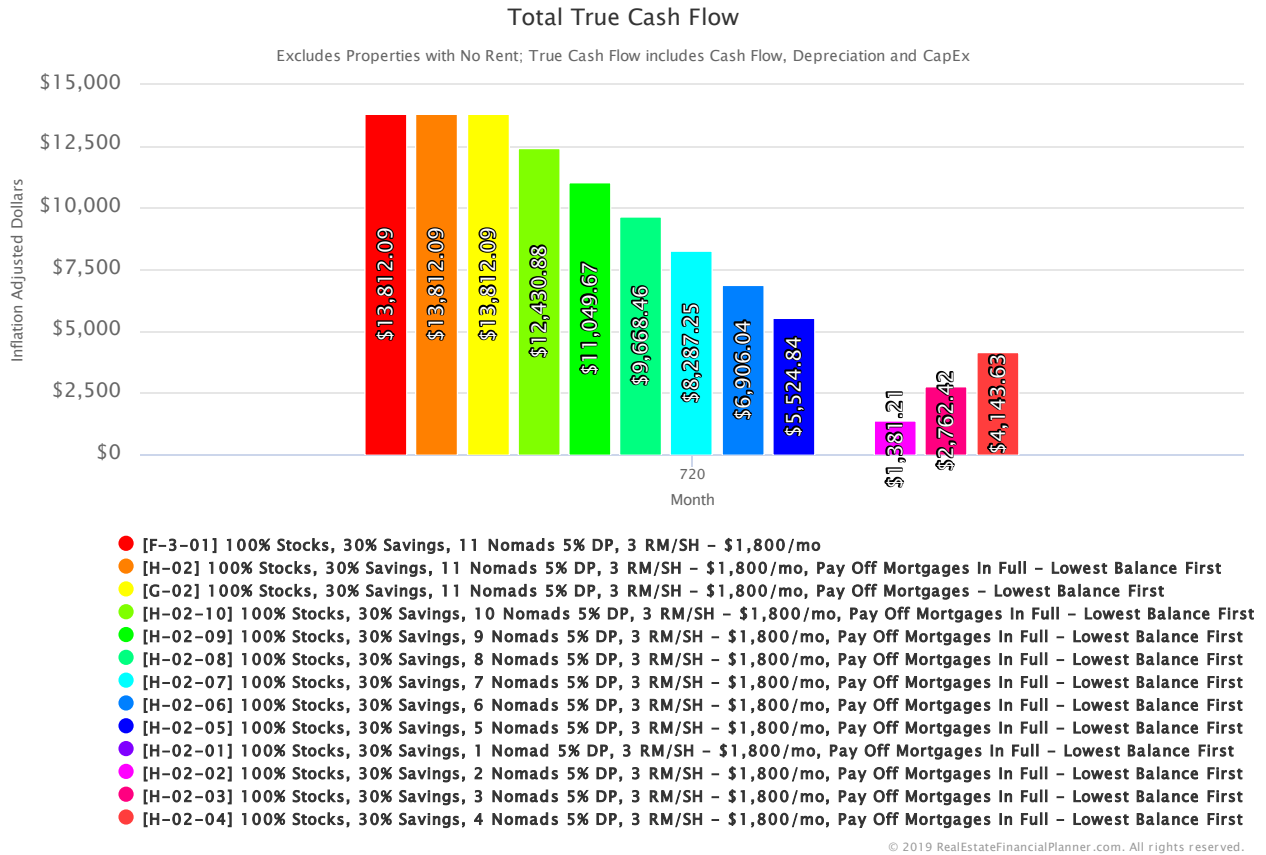
The more rental properties you own the more True Cash Flow™ you are likely to have once the properties are paid off.

We can see this reflected in the chart below which shows your True Cash Flow™ for your properties over time.



If we adjust back for inflation to today’s dollars, 10 rentals, in month 720, looks an awful lot like \$13,000 per month in free and clear cash flow after all expenses. Remember, there are no more mortgages, so you do not have the expense of principal and interest on loans. You do still have taxes and insurance which are already included in that calculation. We are also taking into account vacancy and maintenance on the property. If you were to hire a property manager, you’d need to add that in by modifying the property in the Real Estate Financial Planner™ software. Or, you can estimate that you are paying about 10% of gross rents or about \$2,000 of that \$13,000 per month in property management.

No matter how you look at it, you can look at the chart below to see the minimum number of properties you’d need to own to hit your target monthly income of just over \$4,000 for financial independence. Remember too that this does not factor in your stock market balance at all.



## Model It Yourself

If you want to copy any of the variable number of properties scenarios to your own Real Estate Financial Planner™ account and adjust the assumptions, you can use the links below.

- 100% Stocks, 30% Savings, 1 Nomad™ 5% DP, 3 RM/SH - \$1,800/mo, Pay Off Loans In-Full - Lowest Loan Balance First  
<http://refp.io/942>
- 100% Stocks, 30% Savings, 2 Nomads™ 5% DP, 3 RM/SH - \$1,800/mo, Pay Off Loans In-Full - Lowest Loan Balance First  
<http://refp.io/943>
- 100% Stocks, 30% Savings, 3 Nomads™ 5% DP, 3 RM/SH - \$1,800/mo, Pay Off Loans In-Full - Lowest Loan Balance First  
<http://refp.io/944>
- 100% Stocks, 30% Savings, 4 Nomads™ 5% DP, 3 RM/SH - \$1,800/mo, Pay Off Loans In-Full - Lowest Loan Balance First  
<http://refp.io/945>
- 100% Stocks, 30% Savings, 5 Nomads™ 5% DP, 3 RM/SH - \$1,800/mo, Pay Off Loans In-Full - Lowest Loan Balance First  
<http://refp.io/946>



- 100% Stocks, 30% Savings, 6 Nomads™ 5% DP, 3 RM/SH - \$1,800/mo, Pay Off Loans In-Full – Lowest Loan Balance First  
<http://refp.io/947>
- 100% Stocks, 30% Savings, 7 Nomads™ 5% DP, 3 RM/SH - \$1,800/mo, Pay Off Loans In-Full – Lowest Loan Balance First  
<http://refp.io/948>
- 100% Stocks, 30% Savings, 8 Nomads™ 5% DP, 3 RM/SH - \$1,800/mo, Pay Off Loans In-Full – Lowest Loan Balance First  
<http://refp.io/949>
- 100% Stocks, 30% Savings, 9 Nomads™ 5% DP, 3 RM/SH - \$1,800/mo, Pay Off Loans In-Full – Lowest Loan Balance First  
<http://refp.io/950>
- 100% Stocks, 30% Savings, 10 Nomads™ 5% DP, 3 RM/SH - \$1,800/mo, Pay Off Loans In-Full – Lowest Loan Balance First  
<http://refp.io/951>
- 100% Stocks, 30% Savings, 11 Nomads™ 5% DP, 3 RM/SH - \$1,800/mo, Pay Off Loans In-Full – Lowest Loan Balance First  
<http://refp.io/658>

If you do end up implementing one of these scenarios, I would strongly advise you to do full Monte Carlo testing as we described previously.

To find and copy any of the other scenarios covered in this book, follow the link below.

- <https://realestatefinancialplanner.com/filyp/>



## Path 10: Selling Some Properties

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*"What has been will be again,  
what has been done will be done again;  
there is nothing new under the sun."*

*– Ecclesiastes 1:9*

I love to read older books on real estate investing. As the Good Book says, "There is nothing new under the sun." I find it fascinating to see how folks from decades ago saw the real estate market and the plans they outlined. Some of them are as true today as they probably were when they were written. Some have not aged nearly as well.

In this chapter, I will share with you an idea I first saw presented in a book from 1983 called *Creating Wealth* by Robert G. Allen. I have never been able to replicate the math the author did in the book and some of his assumptions I find highly suspicious, but I've been enchanted by the idea presented since I first read it.

In the book he assumed you were buying homes priced between \$50,000 and \$75,000... which did he use? Not sure; it is unclear to me even looking back at it prior to writing this book. I went to great lengths earlier to show you that you are buying \$350,000 properties, and that you can change this assumption (or the myriad of other assumptions I have made) by copying the scenario to your Real Estate Financial Planner™ account and modifying it as you see fit. To directly address that voice inside your head thanking me: You are welcome.

Properties, according to Robert Allen, would appreciate at an average rate of 10% per year. Based on research by Case and Shiller, this seems to be highly optimistic to me. Remember, we are using 3% per year, the same rate as inflation. This is much more conservative.

In the book, he has you buy two properties a year over a 10-year period. Oddly, at the end of the 10 years, the properties are all worth a range of values from \$81,000 to \$130,000. I have a difficult time understanding how this is true. Are you buying progressively worse properties every year? In other words, did you buy two \$50,000 properties in year 1, but when properties went up 10% to \$55,000 in year 2, did you find a cheaper, lower quality property and buy a \$50,000 property in year 2? Sounds like a horrible plan to me... you keep buying lower and lower quality properties. In our modeling, we have been buying comparable properties each year.

How is he coming up with down payments to buy these properties? He is the author of another book on how to buy properties with no down payment using creative financing strategies. And, I guess if you did opt to use those strategies you could buy two per year. For the Nomad™ modeling we did, we more

realistically modeled you saving up money for the 5% down payment and moving into the property to get owner-occupant financing.

The part of *Creating Wealth* I did like was the idea of acquiring properties over time then selling off some of the properties to pay off the loans on the properties you kept. You end up with fewer properties, but properties that are free and clear of any mortgages with much higher cash flow. It is that idea that I have modeled for you.

## Assumptions

For our modeling, I am using the following assumptions that should be familiar to you at this point:

- Saving 30% of your income each month.
- Investing 100% of your extra money in the stock market (no bonds).
- Earning a fixed rate of return in the stock market of 8.97% per year.
- Buying properties as a Nomad™ each time you have saved up a 5% down payment and have lived in the current property for at least a year.
- Getting either three roommates or a side hustle that brings in \$1,800 per month and continuing this until you achieve financial independence.

In previous chapters, we have discussed paying down loans aggressively. For this chapter, we will not be using that strategy. Instead, you will acquire 11 properties via the Nomad™ strategy (10 rentals and one to live in). Then, we will wait until you have enough equity and cash invested in the stock market to be able to sell some of the properties and pay off the remaining ones. We will only do this if, after you sell the properties and pay off the remaining ones, you have enough cash flow and money invested in the stock market at your safe withdrawal rate to meet your inflation adjusted target monthly income for financial independence.

## Costs of Sale

In *Creating Wealth*, Allen talks about making sure you use after tax and after inflation dollars. I find his assumptions of 20% for taxes on the sale of the property questionable as well.

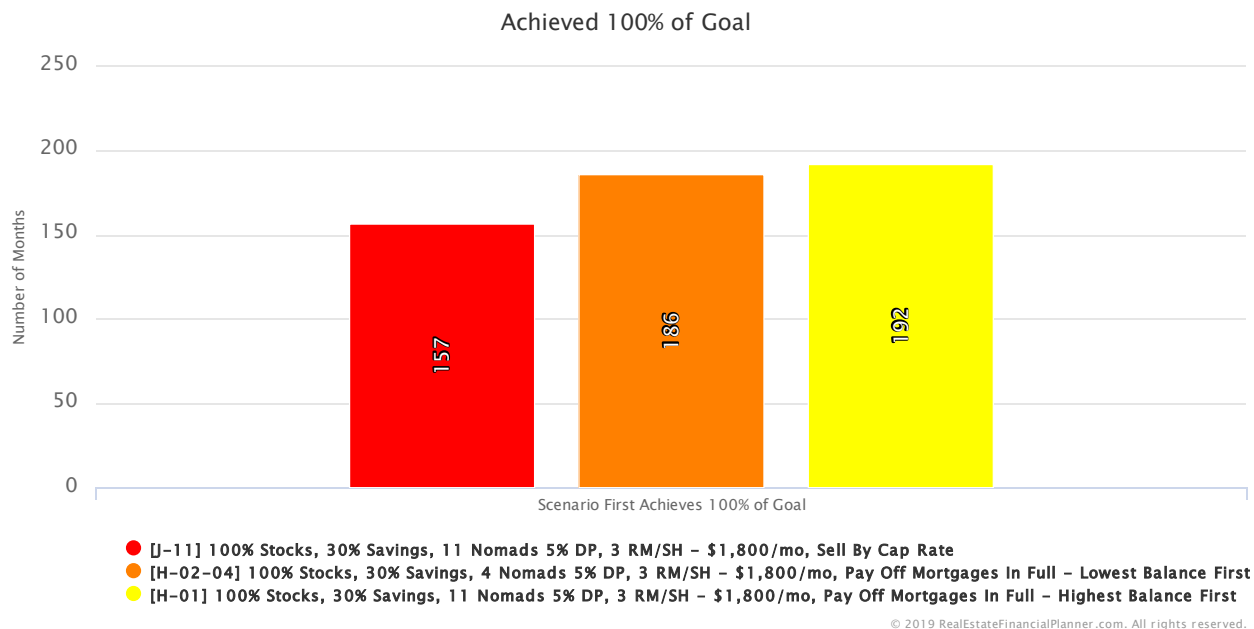
For our modeling, we do consider the following expenses when you sell a property:

- Real estate commissions – 6% of the sale price.
- Closing costs – 1% of the sale price.
- Depreciation recapture tax – 25% of the total depreciation you took on the property.
- Capital gains tax – 15% of the gain you had on the property.

All of these are adjustable when you copy the scenario into your own Real Estate Financial Planner™ account. This allows you to model variations on this strategy that we opted to omit in this book. For example, perhaps you decide to sell your properties on a lease-option instead of with a real estate agent. You might be able to reduce your real estate commission on the sale to zero if you were willing to do all that extra work. This might allow you to reach financial independence even earlier than I am about to show you.

## Achieving Financial Independence

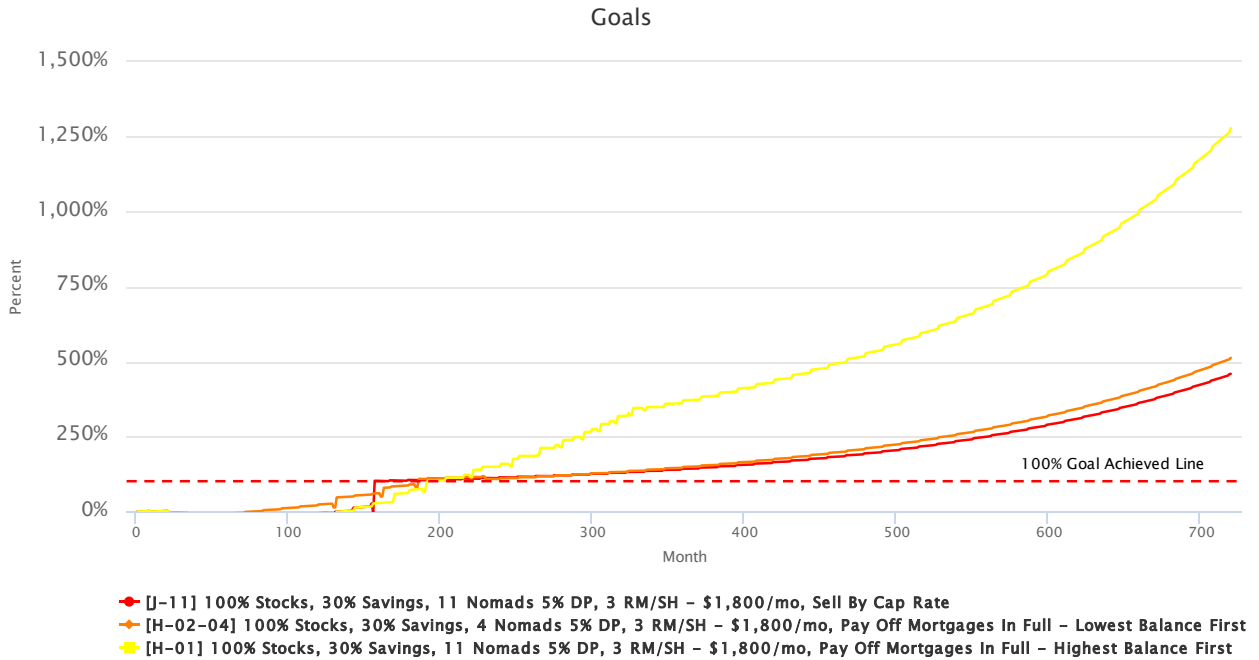
At this point, I think you will appreciate me jumping to the punch line and telling you that selling off some of your properties to pay off the remaining properties will get you to financial independence faster than even our previous front-runner: buying four Nomads™ and paying off mortgages in-full.



By selling some properties and paying off the remaining ones, you can achieve financial independence in as little as 13 years and a month, down from 15 years six months.

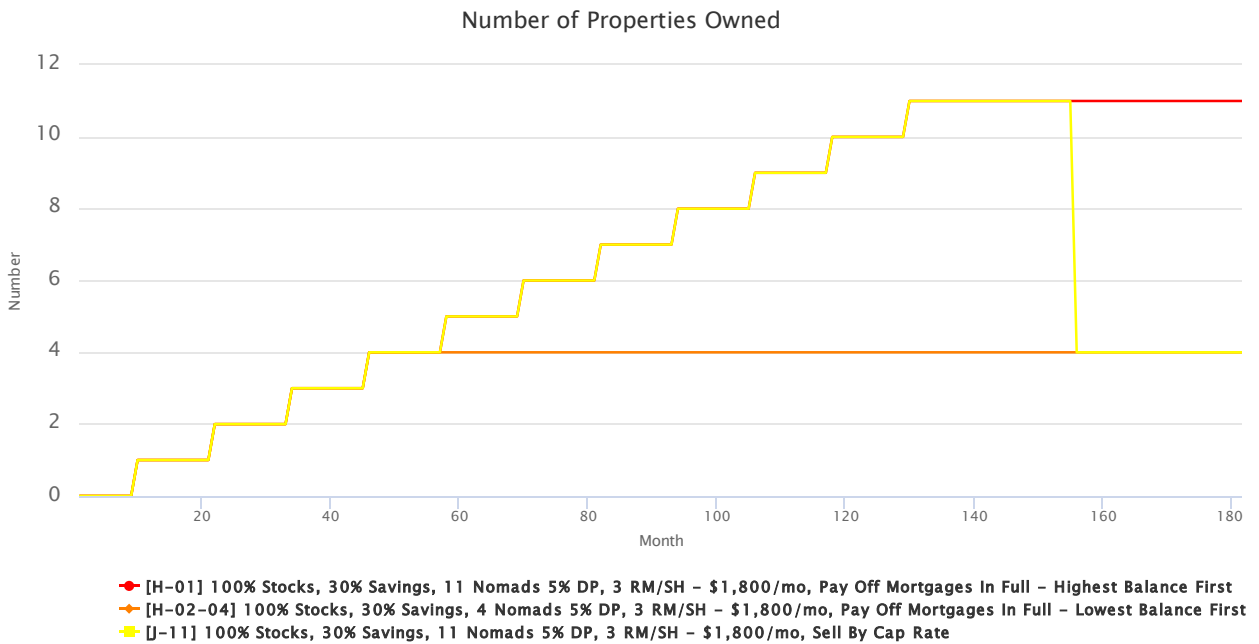
However, as you might have guessed, selling properties results in a potentially lower standard of living than keeping all 11 Nomad™ properties. Look at the chart below showing the percent of your target monthly income for financial independence. You can see that while selling properties is worse than keeping all 11 Nomad™ properties, it is better than just buying four Nomad™ properties.

Of course, you could decide to buy 20% down payment rentals even after you achieve financial independence with extra money you would then have saved in the stock market to boost your cash flow and improve your standard of living.



## Number of Properties Owned

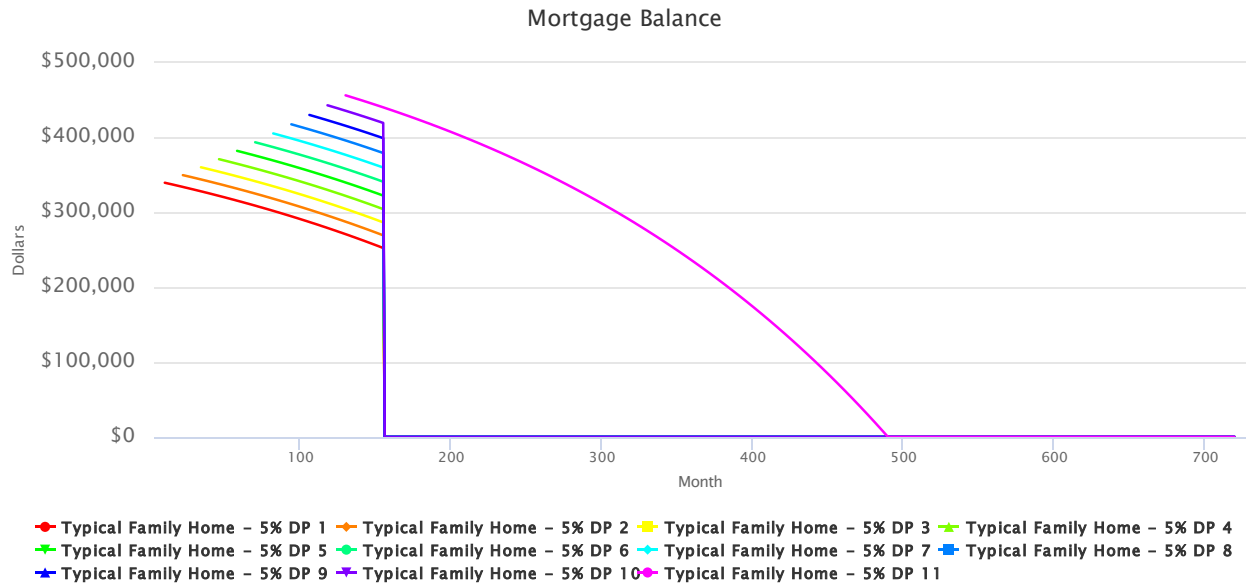
So, how many properties do you end up keeping if you are selling off some?



The chart above shows you the number of properties you own over time. You build up to owning 11 Nomad™ properties, but ultimately sell off 7 of them to pay off 3 rental properties. You keep the mortgage on the property you are living in and let that pay off based on your normal mortgage payment schedule.

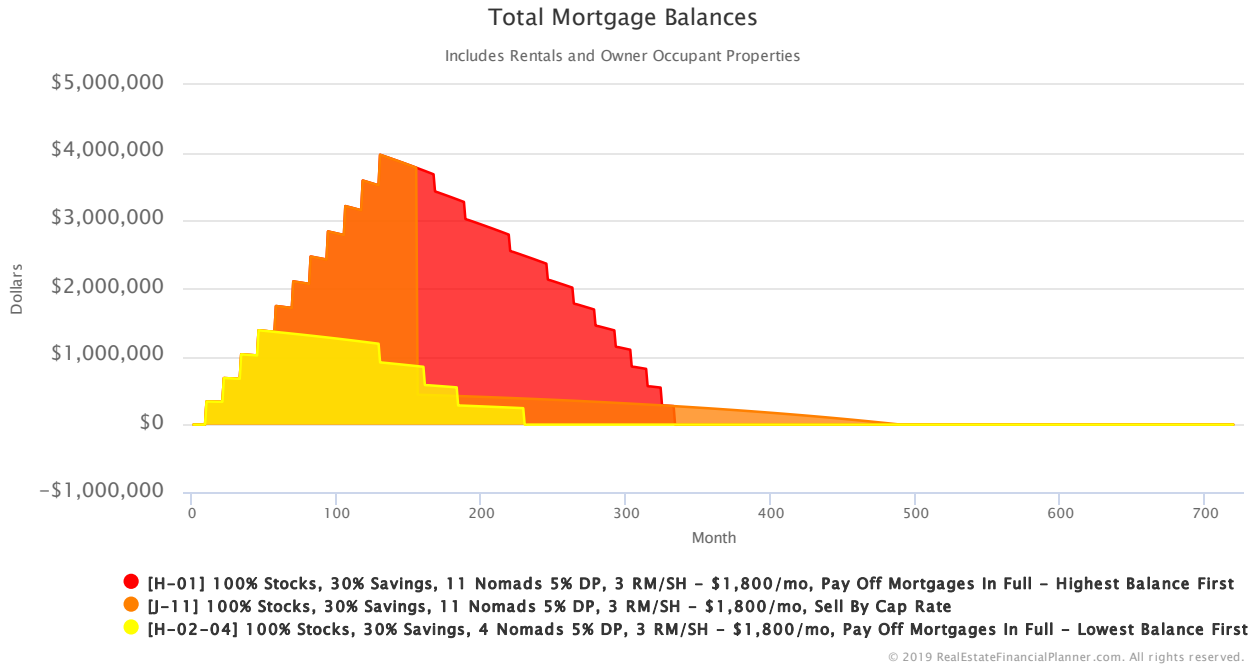
### Mortgage Balances

When we reach the point where you can sell some properties and pay off the mortgages on the others to achieve financial independence, you end up paying off 10 mortgages (seven on properties you sell and three on properties you keep).

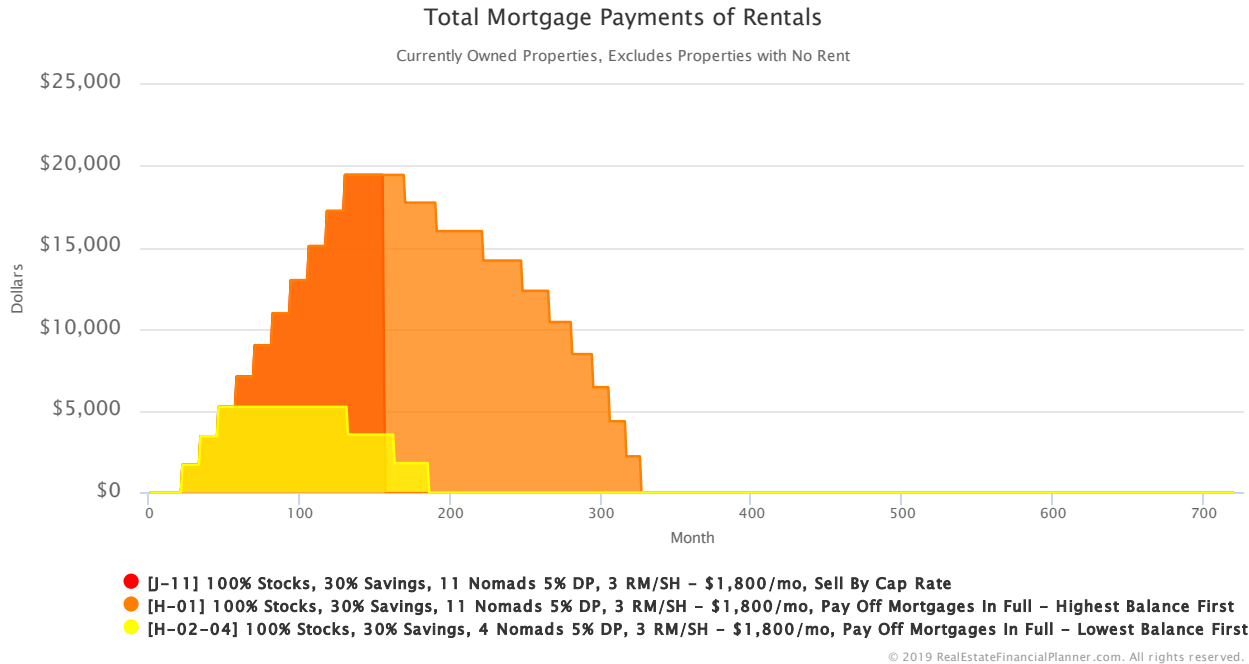


The last mortgage, on the property you are living in, gets paid off over time.

If you'd like to see the total mortgage balance of all the loans combined comparing the three scenarios, you can look at the chart below.



When you sell off the properties, you rid yourself of all mortgage payments on your rentals. Of course, you still have a mortgage on the owner-occupant property you live in.



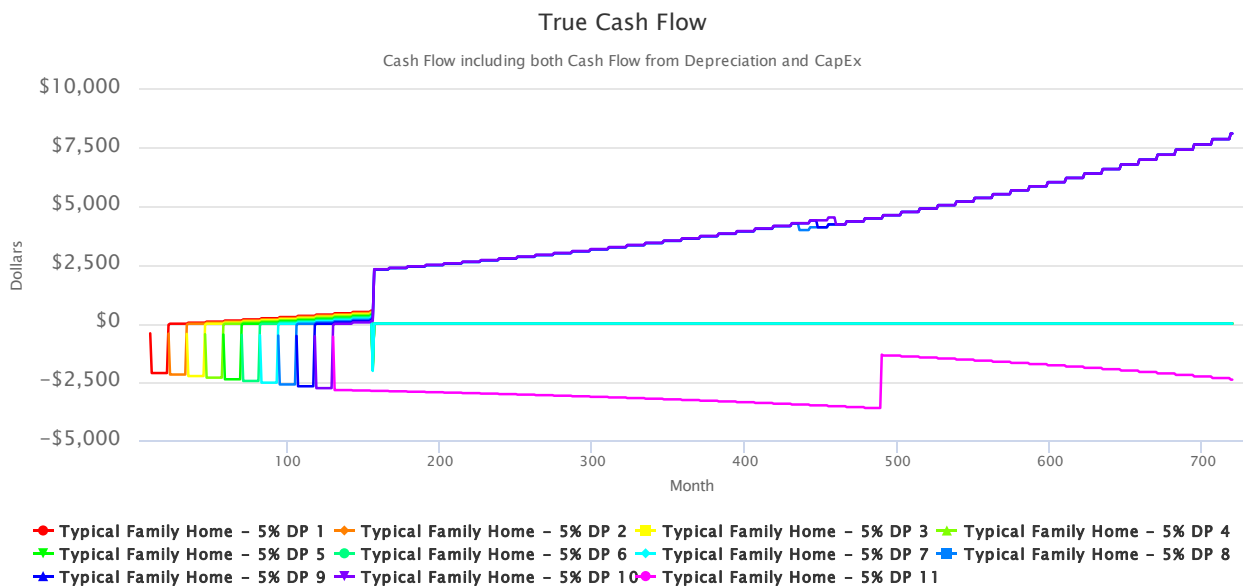


## True Cash Flow™

We discussed that you either have three roommates paying \$1,800 per month or a side-hustle bringing in \$1,800 per month. We are not automatically assuming that you have \$1,800 as rent on the property you are living in. Instead we are just modeling it more generically as an extra \$1,800 in income.

Because of that, each time you buy a new property as a Nomad™ you are living in that property and have negative cash flow for it. When you buy your next Nomad™ property and move into it you then convert the previous property to a rental, and you start getting some income on the property to offset the expenses.

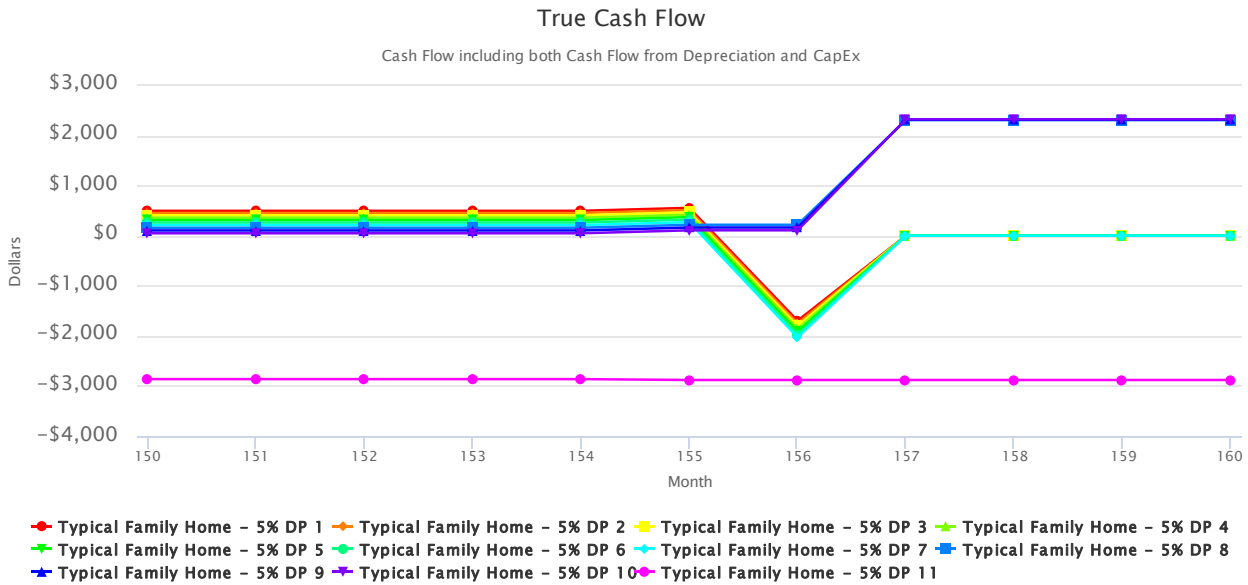
In the chart below you can see each new purchase and the negative cash flow from living in that property for a little over a year. For the last Nomad™ property you purchase you have negative cash flow until almost month 500 when you pay off the mortgage and it becomes less negative. At that point you are only paying for property taxes and insurance on the property because your mortgage payment is gone.



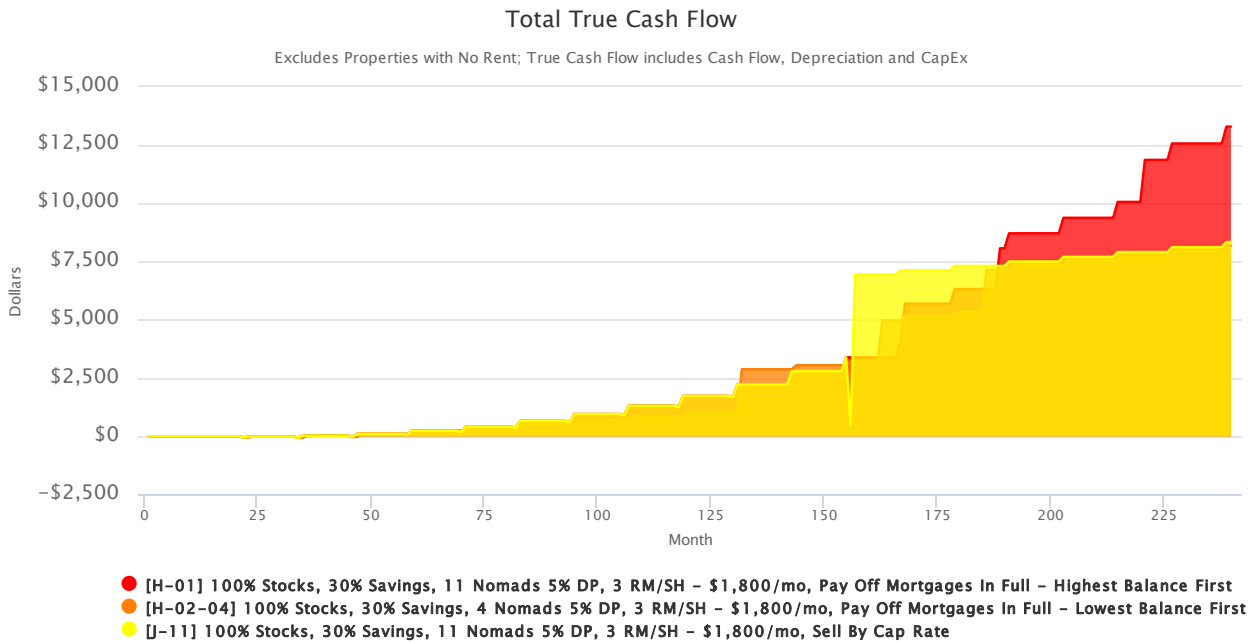
You can also see a bunch of activity around month 157 when you sell off the properties and pay off the remaining three rental property mortgages.

At that point, you have a month of negative cash flow on each of the seven properties you are selling. Why? Because mortgages are paid in arrears, remember? That means even though you sold it in month 157, you still owe a mortgage payment in that month for interest that accrued from the previous month. In reality, this comes out on the closing statement as part of the total pay off amount on the loan, but I do show it on True Cash Flow™ since you don't have any income from rentals for that month (the new owner gets that), but you really need to make that last payment even if it is technically at closing as part of the loan payoff amount. You can see this negative cash flow dip as the downward spike on the chart below.

In that same month, you had made your regular mortgage payment on the properties you are keeping as rentals, so True Cash Flow™ for that month is about what it has been. However, as you can also see clearly in the zoomed in chart below, the very next month—when you no longer have a mortgage payment—the True Cash Flow™ on the three remaining rentals bumps up to over \$2,000 per month (in inflated dollars).

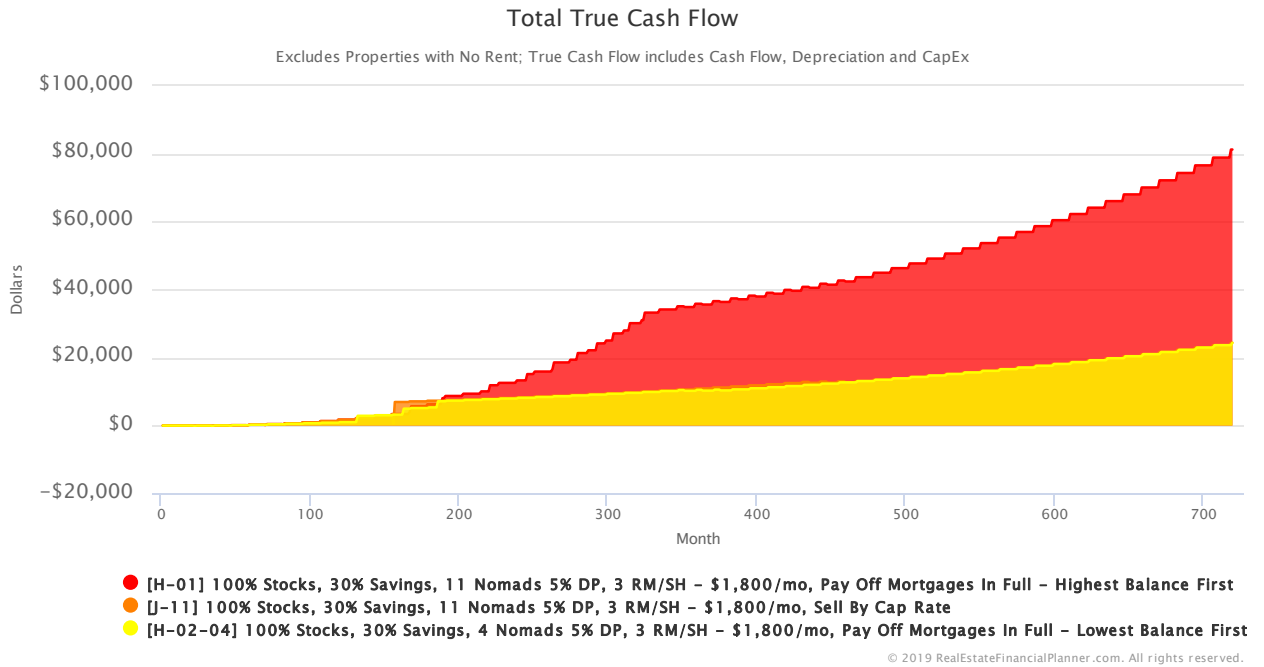


Let’s look at the total True Cash Flow™ of all the properties in the three scenarios we’ve been comparing.

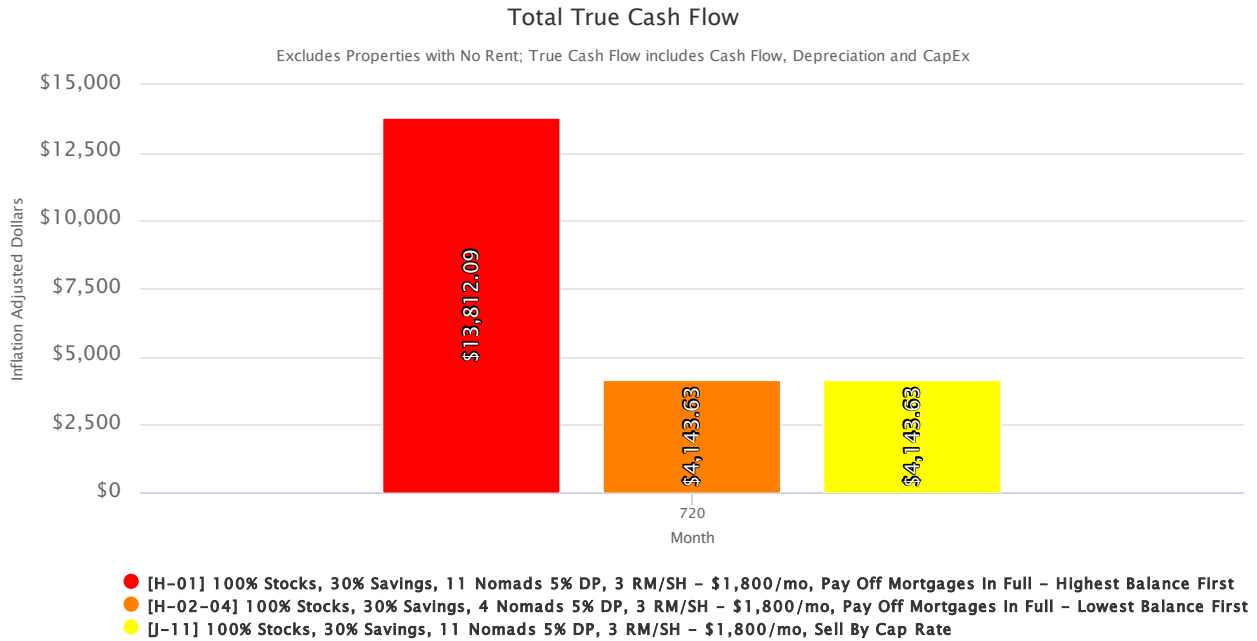


As you can see in the chart above, if you only buy four Nomads™ and pay off the mortgages in-full you get a cash flow boost when you pay off your first property between months 125 and 150 on the chart above. But really, the big jump in True Cash Flow™ by using the equity in the properties you are selling happens around month 157. This pushes you over the edge of achieving financial independence.

Ultimately, True Cash Flow™ is best if you keep all 11 Nomads™. See the chart below.



But, if we adjust back to today's inflation adjusted dollars, you can see the relative amounts of True Cash Flow™ 60 years in the future, in month 720.



## Debt to Net Worth

Of the three scenarios we have been discussing and comparing in this chapter, all of them start off with the same risk profile when considering debt to net worth because all three of them buy the same first four Nomad™ properties.

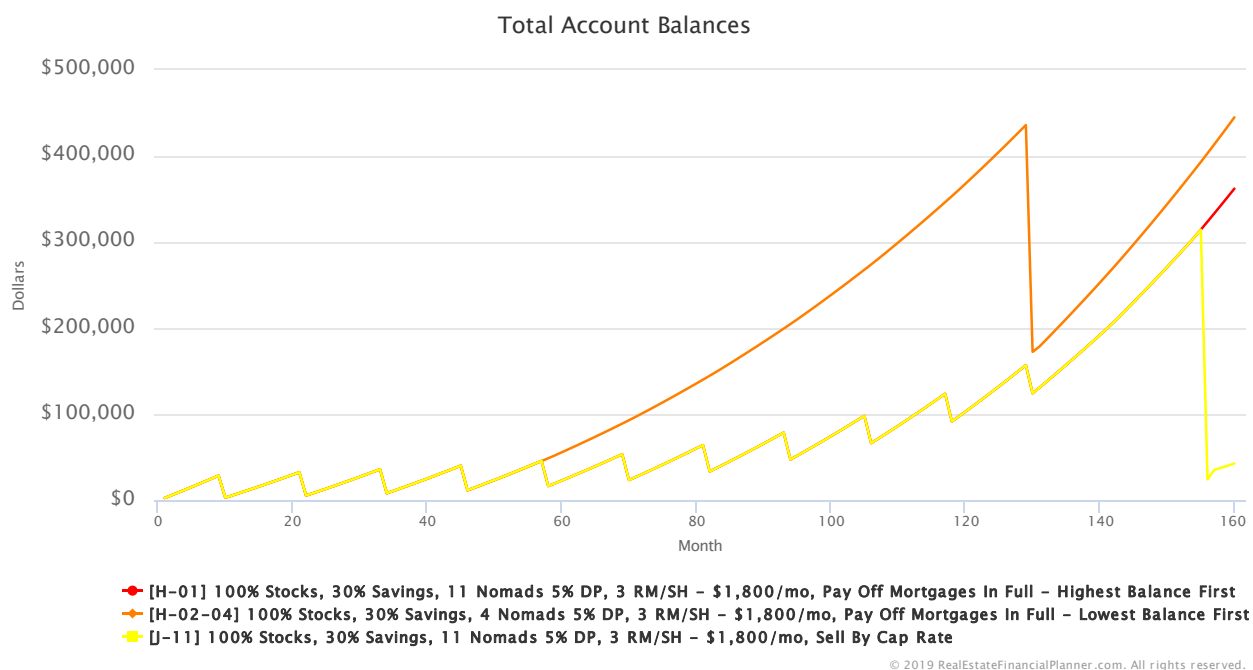


However, if you stop buying more properties, your risk continues to decline. In that way, buying only four Nomad™ properties, is the least risky strategy. Continuing with Nomad™ and buying 11 properties in the two other scenarios is riskier.

When you decide to sell off seven of your properties, your risk declines—even lower than if you just bought the four Nomad™ properties and stopped buying. This is because you took your equity and paid off three of the four properties you owned so your total debt goes way down.

## Stock Market Account Balances

When comparing the three scenarios, which one ultimately gives you the largest stock market account balance? I will get there, but first let's zoom in and look at the stock market account balances through just after you sell off some properties.



In the chart above you can see the jagged sawtooth periods of saving up the 5% down payment to buy your next Nomad™ property then investing that in buying a property and seeing your stock market account balance decline.

You can see how your stock market account balance grows when you stop buying at four Nomad™ properties between approximately month 60 and about month 130. Around month 130 is when you have finally saved up enough to pay off the first property in-full. Then, your stock market account balance grows again until somewhere off the chart above, you save up enough to pay off another mortgage in-full.

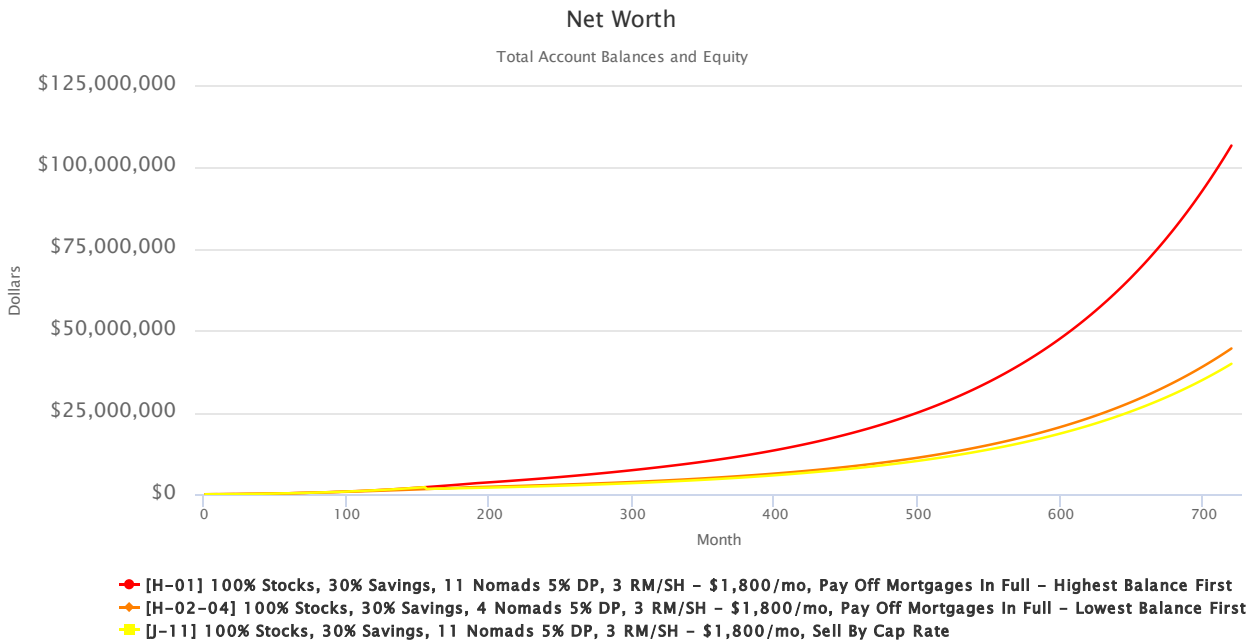
In the other two scenarios, you are buying 11 Nomads™, but with the scenario selling off properties, your stock market account balance falls significantly when you sell off properties and use your stock market account balance to pay off three properties.

Ultimately, as you would probably expect, your stock market account balance grows largest when you keep all 11 Nomad™ properties. The stock market account balance is lowest for the scenario where you sell off properties.

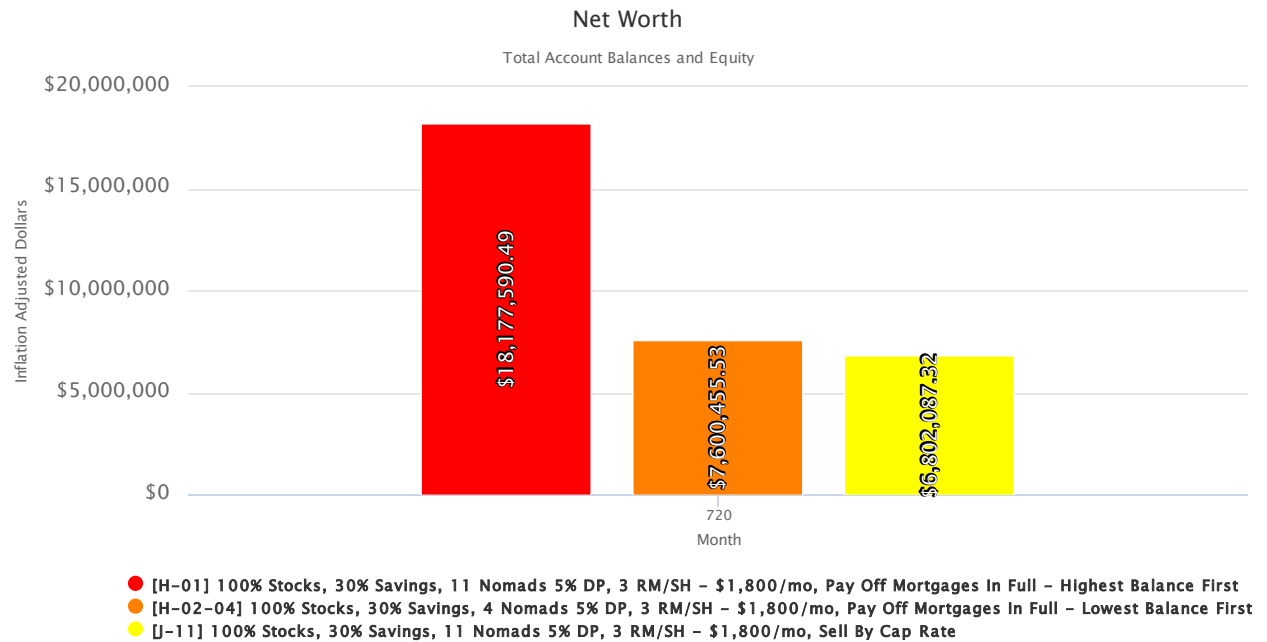
## Net Worth

Similar chart patterns occur with Net Worth. Your highest net worth is reached when you keep all 11 Nomad™ properties. Selling properties to pay off other ones results in your lowest net worth overall.

The following chart shows you the summary over the entire 60-year period.



I suspect you are also curious about what the actual numbers are, adjusted for inflation back to today’s dollars, in month 720. That’s the chart below.



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## Model It Yourself

If you want to copy the scenario for selling properties to your own Real Estate Financial Planner™ account and adjust the assumptions, you can use the link below.

- 100% Stocks, 30% Savings, 11 Nomads 5% DP, 3 RM/SH - \$1,800/mo, Sell By Cap Rate  
<http://refp.io/661>

More important than ever, if you do end up implementing this scenario, I would strongly advise you to do full Monte Carlo testing as we described previously.

You can find a complete list of all the scenarios covered in this book on the following page.

- <https://realestatefinancialplanner.com/filyp/>





## Conclusion

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We just finished an epic journey together. Did you enjoy it as much as I did? Do you agree that the biggest understatement of the entire book is, I love charts? I hope so.

We began our journey together talking about very traditional investing via stocks and bonds. I shared with you what you might expect in terms of how long it would take to achieve financial independence so you could live your passion based on whether you invested in all stocks, all bonds, or some mix thereof.

Next, we looked at the impact of how much you save from your paycheck each month has on achieving financial independence. The more you save—up to a practical point—the faster you achieve financial independence. Later, we also learned about house hacking with roommates and side hustles which can effectively increase the percentage you are saving toward retirement.

I shared with you the amazingness that utilizing the Nomad™ investing strategy can have on your financial independence.

We looked at the impact of having very generous parents (or being able to structure very creative nothing down financing) on your speed to financial independence.

In case you did not realize amazingness when it presented itself to you, I compared 5% down payment Nomad™ to 20% down payments where you don't need to own occupy the property.

Then, after the detailed discussions on house hacking with roommates and side hustles, I took you down the rabbit hole with Alice to discuss a variety of methods for paying off mortgages faster.

We also examined your standard of living after you reach financial independence and how buying fewer or more properties can impact your standard of living and your speed to first achieving financial independence.

And, because I love charts so much and really could not help myself, I wrapped up by discussing what happens if you bought more than you needed and sold off properties to minimize time to financial independence.

Along the way, I showed you more charts than you realized could possibly exist for looking at your personal financial plan. Perhaps most importantly, I empowered you to not just accept my assumptions as is. Instead, I explained that you could copy any of the scenarios we discussed into your own Real Estate Financial Planner™ account in order to drill down into whatever details interest you.

Plus, you can modify any of my assumptions once you copy it to your account.

- Received a promotion and a raise?
- Voluntary demotion or move to a less stressful job?
- Move to an area with less expensive properties? More expensive?
- Better cash flowing properties? Worse cash flowing properties?
- Interest rates went up? Interest rates got better?

- Want to mix some Nomad™ with some 20% down payment properties?
- Want to add any properties or cash you might inherit from mom and me to your account?
- Want to see what impact Social Security might have?
- Fewer roommates? Bigger side hustle income?
- Buy extra houses once you hit financial independence?
- Able to buy houses at a discount?

Just about any other question or scenario you can imagine and want to test, you can with the Real Estate Financial Planner™ software. Just copy the closest one to what you want to test to your account and then start modifying.

In conclusion: I am excited for you. I love you and I am looking forward to on-going discussions with you about this and other topics in the future.

## Acronyms and Abbreviations

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Throughout the book, I have often employed the use of acronyms and abbreviations instead of repeating commonly used phrases.

For example, instead of saying “financial independence” hundreds of times, I frequently chose to use FI.

In most cases, I will show you the abbreviation or acronym right after I use it for the first time. For instance, the first time I mentioned “financial independence and live your passion”, I displayed it as follows “financial independence and live your passion (FILYP)”. From then on, I tended to use the abbreviation FILYP.

This page serves as a short list of the abbreviations and acronyms I have used in case you stumble upon one and can’t find its original use.

- CAGR = Compound Annual Growth Rate
- CapEx = Capital Expenses (capital improvements to properties)
- FHA = Federal Housing Administration (a type of loan)
- FI = Financial Independence
- FILYP = Financial Independence and Live Your Passion
- FIRE = Financial Independence, Retire Early
- HH = House Hacking
- HOA = Homeowner’s Association
- NOI = Net Operating Income
- PMI = Private Mortgage Insurance
- REFP = Real Estate Financial Planner™ software
- SH = Side Hustle (Part-time Job)



## Glossary

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- **Appreciation:** an increase in the value of an asset over time. This can occur for several reasons including increased demand or lessening of supply. This is the opposite of depreciation.
- **CAGR:** compound annual growth rate which is used to measure the annual growth rate on an investment which provides a constant rate of return.
- **Capital Expenses (CapEx):** funds used to upgrade and maintain physical assets. These may include repairs to the property or the purchase of a new appliance such as a furnace or dish washer.
- **Capitalization Rate (Cap Rate):** this is the ratio of a property's net operating income compared to its value. It is calculated by taking the income from a property minus all the expenses—except your debt payments—divided by the purchase price of the property.
- **Cash Flow:** the money coming in on a property in the form of rent.
- **Cash Flow from Depreciation:** the tax rate charged on your income times the depreciation you can claim for the rental property.
- **Depreciation:** an income tax deduction that allows a rental property owner to reduce their taxable income. For residential rentals this deduction is based on the value of the building (not including the land value) and can be claimed for 27.5 years.
- **Financial Independence:** when your net cash flow from rentals, side hustles, or roommates plus a safe withdrawal rate of any non-real estate investments (stocks, bonds) less your expenses meets or exceeds your desired standard of living.
- **House hacking:** this is a strategy for having others pay for your primary residence. In this book we focus on accomplishing that through sharing your primary residence with roommates.
- **Inflation:** the general increase in prices and decline in purchasing power of money over time.
- **Monte Carlo Simulation:** a technique relying on repeated random sampling to predict the probability of different outcomes for processes involving random variables.
- **Net Operating Income (NOI):** All the income from your property minus all your expenses. Expenses usually include maintenance, insurance, taxes, utilities, vacancy costs, and property management.
- **Net Worth:** total balance in all bank accounts plus the equity you have in the properties you own minus any debts or liabilities.
- **Nomad™:** the process of acquiring rental properties through purchasing a property as an owner occupant, living there for a year, purchasing another owner occupant property, and then converting the previous one into a rental.
- **Rent Resiliency™:** the amount that the rent you are receiving can decline while still yielding breakeven cash flow. The higher the Rent Resiliency™ the larger the buffer between what you are receiving in rent and the minimum rent you need to get to cover all the expenses of owning the property.
- **Return on Equity (ROE):** calculated by adding up cash flow, appreciation, debt pay down, and tax benefits and dividing that by the equity.
- **Return on Investment (ROI):** the gain or loss on an investment relative to the amount of money invested.

- Side Hustle: any source of additional income outside of your regular job or cash flow from rental properties.
- True Cash Flow™: cash flow which factors in the cash flow from depreciation. To get this number take cash flow, plus cash flow from depreciation minus capital expenses (CapEx).

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