The MULTIFAMILY MILLIONAIRE

Achieve Financial Independence by Investing in Small Multifamily Real Estate

Vol. I

BRANDON TURNER

Author of THE BOOK ON RENTAL PROPERTY INVESTING

and BRIAN MURRAY

Author of CRUSHING IT IN APARTMENTS AND COMMERCIAL REAL ESTATE

The MULTIFAMILY MILLIONAIRE

Achieve Financial Freedom by Investing in Small Multifamily Real Estate

Volume I

BRANDON TURNER AND BRIAN MURRAY

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First and Second Place CIPA EVVY Awards 2019

"An insider's perspective, full of encouragement and resources for newcomers… Interested readers will find the book substantially useful as a starting point."

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Brandon Turner and Brian Murray

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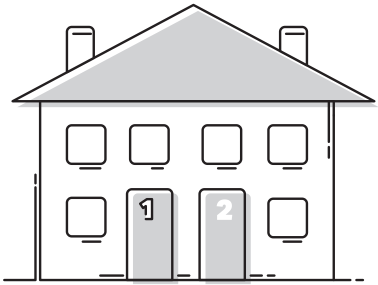

Chapter 1

AN INTRODUCTION TO MULTIFAMILY PROPERTIES

"A decision is what a man makes when he can't get anyone to serve on a committee."

—FLETCHER KNEBEL, BEST-SELLING AUTHOR

There are a *lot* of ways to invest in real estate, such as:

- Buying single-family houses
- Buying storage units
- Buying office buildings
- Buying mobile homes
- Flipping houses
- Building skyscrapers
- Buying/building large apartment complexes
- Buying/building small multifamily real estate

And you know what? There are many highly successful people in all these niches. That's the great thing about real estate—the plethora of choices. But that's also the dangerous thing about real estate: *so many choices!*

As business author Seth Godin once said, "In a world where we have too many choices and too little time, the obvious thing to do is just ignore stuff." When faced with the hundreds of different paths one can take to build a life of wealth and happiness, many people simply ignore them all, give up on their dreams, and go back to doing what they know: watching television, eating bad food, and hoping the government takes care of them in the few years between retirement and death.

But not you.

After all, you're reading a book on buying small multifamily real estate, so the topic obviously pulls at you—and for good reason! Multifamily real estate is one of the greatest investments someone can make and one of the best ways to begin building serious wealth and long-term income.

This book is designed to help you do just that. But first, let's get on the same page.

Defining Multifamily Properties

Multifamily. Multi-unit. Multi-dwelling unit. Apartments. Complexes. Flats.

Many different names, but they all refer to a type of real estate that we'll call "multifamily" throughout this book. A multifamily property is a singularly owned property that contains two or more residential housing units. Each residential area contains, at minimum: a bathroom, a kitchen, and a place for a bed.

Multifamily, therefore, could refer to a five-hundred-unit apartment complex in the suburbs, a duplex in the city, or a fourplex in the country. Multifamily properties come in all shapes and sizes: large buildings, small buildings, and even separate buildings on the same lot. My first multifamily property, the one I mentioned in the preface, contained two single-family houses located on one city lot, separated by a driveway and some dirt and grass.

I also own a three-unit and a four-unit with similar setups. Additionally, I have a five-unit that is located in one giant square building. Then there is the triplex I bought with one unit upstairs, one unit on the main floor, and one in the basement with a completely separate vacation-rental unit in the backyard.

Or take, for example, a property I own that contains fifty different mobile home units, each home independently owned by a resident but each "lot" that the home sits upon owned by me. Or the 126-unit apartment complex Brian Murray owns in New York. Or the house my friend and business partner Ryan Murdock owns that was once a large single-family house but has been carved up and remodeled over the past 140 years and now houses four separate families.

As you can see, multifamily is a broad niche. To cover the full spectrum of opportunities and provide as much value as possible, we are going to divide multifamily investing into two tiers. This book, Volume I of *The Multifamily Millionaire*, with writing led by me (Brandon), focuses on what we call *small* multifamily real estate. Volume II, with writing led by Brian Murray, focuses on what we call *large* multifamily real estate. But that begs the question: What is large, and what is small?

Oftentimes people draw a simple line between small and large properties: four units. They consider anything with four units or fewer to be small and anything five units or more to be large. And when it comes to *lending*, they are not wrong. As you'll learn later in this book, getting a loan on a single-family house, duplex, triplex, or fourplex is different from getting a loan on anything with five units or more.

However, aside from financing, in the real world, buying a fourplex is not all that different from buying a five-unit property. But buying a two-hundred-unit property is *very* different from buying a fourplex. So where do we draw the line? We want to make sure that someone reading this book is equipped to buy a five-unit, an eight-unit, or even a twenty-unit if they so desire. Because it's not that difficult—you *can* do this—even if you're just starting out.

Rather than making a strict distinction between small and large based on a specific *number* of units, we have decided to draw a softer boundary between small and large based on *approach*.

You see, the approach to buying a duplex is not that different from the approach to buying an eight-unit. They require similar processes, people, and skill sets.

There are many different processes, people, and skill sets involved when buying a two-hundred-unit apartment complex. That type of purchase likely involves tens of millions of dollars and the expertise of teams of professionals, with much of the work taking place around long mahogany tables. In practice, investing in large apartment complexes is more akin to buying, owning, and selling a business. Quarterly meetings and quarterly returns. Hierarchies of employees. Fund-raising webinars. Mission statements and business plans. We're certainly not saying large multifamily isn't within reach for small investors who want to go big—because it is—but it requires a different approach. Patience, Grasshopper: We'll get there in Volume II.

Purchasing a duplex, triplex, or something similar, on the other hand, is a simpler process. You'll be using your own cash, a bank loan, a partner, and/or some other more creative methods to finance the deal. You'll be managing the property yourself or hiring a small, local property manager to assist. You won't be forming companies inside companies inside companies. The property will likely be in your own name or the name of an LLC. Small multifamily real estate investing is something an individual can easily do independently with the help of various independent contractors (such as title companies, attorneys, and property managers) brought in to handle specific aspects of the job.

To help clarify how that differs from large multifamily real estate, here's a side-by-side breakdown of some of the differences between investing in small multifamily real estate (which we're focusing on in this volume of *The Multifamily Millionaire)* and large multifamily real estate (which is the focus of Volume II):

SMALL MULTIFAMILY REAL ESTATE	LARGE MULTIFAMILY REAL ESTATE
Likely financed by a local bank	Likely financed by large commercial lenders with assistance of mortgage brokers
Down payment probably self-funded	Down payment probably funded by raising money from investors
Typically managed by owner or small local property manager	Typically managed by large, third-party property manager
Usually local, though long-distance is entirely possible	Usually long-distance, but local is entirely possible
Owner likely knows tenants' names	Owner unlikely to know tenants' names
Repair work to units done by owner or handymen hired by owner	Repair work to units done by contractors or on-site employees
Property rehabs performed by owner or local contractors who handle small-scale projects	Property rehabs performed by contractors who handle large-scale projects
Bank's decision on whether to fund typically based on owner's borrowing strength	Bank's decision on whether to fund typically based on property's business strength
Owner usually involved in daily operation of investment	Owner usually not involved in daily operation of investment

Of course, these are general guidelines. It's entirely possible to see the owner of a two-hundred-unit apartment complex show up in overalls to do their own work. It's also entirely possible to see the owner of a duplex in a suit and running their business entirely as a business, without ever engaging in the daily operations of the property. However, the distinctions above tend to hold true, so we've divided our coverage into two volumes accordingly.

Will the information in this book help you invest in duplexes, triplexes, or fourplexes?

Definitely.

Will it help you take down that twenty-unit you've been driving past for years?

Absolutely.

Will it help you raise $6 million in a 506(c) Reg D Fund with a 65/35 LP/

GP split and an 8/15 percent tiered waterfall for distributions? Eh… for that, you'll want to read Volume II. But start here anyway! This book will give you the *foundation*. The lessons you learn in this book about small multifamily real estate will give you the tools, knowledge, and confidence to eventually move into the big leagues if you want.

And, of course, you don't have to move to the big leagues. Maybe buying giant apartment complexes doesn't sound appealing. That's fine by us. You can build massive wealth and financial independence not only for yourself but also for your children and their children just by effectively buying and managing small multifamily real estate. This book will show you how.

Eight Reasons to Love Small Multifamily Real Estate

We titled this two-volume set *The Multifamily Millionaire* because we believe multifamily real estate is the greatest way for the average person to become a millionaire. It's that simple. Millions of people, for generations, have become millionaires thanks to real estate—even people with less intelligence, fewer connections, and less capital than you.

There are far too many benefits to investing in small multifamily properties to list them all here, so we'll just highlight eight of our favorites.

1. Cash Flow

Let's play a quick grade-school math game. Becky sells cookies. She earns $10 at the bake sale. Go, Becky! But Becky had to spend money on baking supplies. In total, she spent $7. Therefore, how much profit did Becky actually earn? Three dollars. That is Becky's "cash flow," the profit earned after paying all of a business's bills. Becky's cash flow is hers to spend on whatever she wants. The same is true for your cash flow, and it's one of the reasons we love small multifamily real estate so much: It offers the opportunity to earn *a lot of cash flow*.

When purchased at the right price (which you will learn to do) and managed correctly (which you'll learn to do), small multifamily real estate tends to generate substantial monthly cash flow. Collect enough of these properties and you'll be able to quit your job sooner than you ever thought possible. It doesn't take that many small multifamily properties to give you the financial resources to live an incredible life; it just takes the *right* ones. This book is going to teach you exactly how to find, buy, and manage the right ones.

2. Simple and Low-Cost Financing

A few moments ago, we mentioned that when it comes to lending, banks and lenders draw a line between small and large multifamily properties. Let's discuss that a bit more in depth here. Properties with one, two, three, or four residential units are generally covered by a field of lending known as residential lending, while properties that contain five or more residential units (such as apartment complexes) are covered by commercial lending. Although both types of lending provide a similar service—loans that allow you to purchase real estate—there are some minor, and major, differences between the two. Residential lending often offers better interest rates, less money down, and longer loan terms.

Additionally, commercial loans often contain a provision known as a balloon, which means there is a date by which the loan's remaining principal balance must be paid back, regardless of the term. For example, let's say you have a 5.5 percent interest rate on a $100,000 commercial loan, and it's spread out over twenty-five years. Your monthly payment would be roughly $614. However, even though the loan is spread out over twenty-five years, you might have a seven-year balloon payment, meaning the entire remaining balance of the loan is due at the end of year seven, even though the loan hasn't been paid off. This would require you to either sell or refinance (get a new loan) before that deadline.

Residential financing tends to be much more simple and straightforward, not to mention cheaper, than commercial financing. Thus, another benefit of small multifamily real estate investing is the ability to obtain residential financing—as long as your property has four units or fewer.

3. Abundance of Opportunities

Most markets contain small multifamily properties. As a result, you aren't necessarily looking for a needle in a haystack. In fact, in Chapter Four, we're going to lay out seven different types of small multifamily properties you can look for, including monster houses, cottages, and up-and-downs. Of course, some locations tend to have more small multifamily properties than others, but the bottom line is that you can invest in small multifamily properties just about anywhere.

4. Less Competition

Although you can find multifamily properties in almost any market, most real estate buyers are not looking to buy a small multifamily property; most are looking for a single-family property to call home. They aren't concerned with cash flow or any other financial metrics. Logic and math play second fiddle to the emotional draw of a cute kitchen, a cute front porch, and a cute street for their cute kids to play in.

Therefore, when you invest in single-family real estate, you are competing with buyers who will pay more than they should because emotion tells them to. Emotion is tough to compete against when you're trying to find good investments. (That's not to say single-family houses never work as investments. However, the competition for those that do can be fierce, forcing investors to focus on off-market acquisition strategies and major rehab projects.)

Although you'll face significantly less competition when shopping for large multifamily properties, that competition will be much *savvier*. You'll be going up against teams of well-trained, well-financed, well-educated professionals.

Small multifamily real estate is wedged between those two highly competitive sectors. Armed with the knowledge in this book, you'll be perfectly positioned to take advantage of this real estate sweet spot. You'll be savvier than the average person who's shopping for a home, and you're looking to buy deals that are simply too small for most professionals to consider. As the law of supply and demand dictates, where there is less competition, better deals can be found. Those lucrative small multifamily deals can be your ticket to financial freedom, *fast*.

5. Growth Potential

Imagine being able to wake up each morning when you *want*, not when you *have to*. Imagine spending as much time as you desire with your kids, with your spouse, with your dog. Imagine not feeling guilty when you go to the gym because you have more than enough time. Imagine working hard on work that you love, that energizes you, that allows you to take bigger risks. Never again will you have to watch the clock, waiting for the small breaks your office allows.

These are not pipe dreams. This is real life for Brian and me, and for millions of other people who have successfully invested in real estate. Maybe your idea of financial freedom is different. But that's the best part about financial freedom—you get to choose! Let's be honest: You'd like to have financial freedom (however you define it) sooner rather than later, right? Whether you love your job or want to quit tomorrow doesn't matter. The freedom to choose how to live your life, unrestricted by the conventional need for money, sounds pretty amazing to almost everyone. And here's the thing: With multifamily real estate, you can get there *faster*.

When you invest in multifamily real estate, your portfolio grows more quickly than it would if you were collecting single-family houses. Yet the surprising truth is that it's not twice as difficult or expensive to buy a duplex versus a single-family home. Similarly, it's not four times as difficult or expensive to buy a fourplex versus a single-family home. In fact, it takes about the same amount of work.

If speed is important to you, investing in multifamily real estate will get you to the finish line faster. In Chapter Two we'll delve into a concept we call The Stack, which is perhaps the most effective strategy for scaling a real estate business faster than you could ever imagine. Stay tuned!

6. Opportunity to Buy from Bad, Burned-Out, or Checked-Out Landlords

People get into real estate for a variety of reasons, and many don't have the same level of excitement as you do. In fact, plenty of current landlords never wanted to be a landlord, or have long since discovered they just don't enjoy it. They may have inherited a property and have no idea what they are doing. Perhaps some bought into the idea that real estate investing was a quick and easy way to strike it rich, but have been unwilling or unable to do what is necessary to make the investment work.

Regardless of *why*, many landlords are burned out. The reason is that owning rental properties is *not* an entirely passive activity, especially at the beginning. It requires skills, knowledge, and persistence. It may also require you to make difficult decisions, miss important events, and continually educate yourself on best practices and legal changes, among other things. But this doesn't mean you shouldn't take the plunge. On the contrary, some of life's most worthwhile pursuits are found on the road less traveled. The easy path isn't always the right path, and the right path isn't always the easy one.

Now, we don't say this to scare you. Landlording can eventually become passive, and there are many ways to make it simple and easy.

Just like in sports, mastery comes after significant and continual personal improvement. If you read books, create systems, make and learn from mistakes, and do it all over and over, in time, landlording becomes easier and even fun. But for the many, many landlords out there who have not put the time into becoming good at their job, it can be hell and cause burnout.

One landlord's burnout is another landlord's opportunity. In fact, most of the properties we have purchased over our careers have been from failed landlords. Whether the landlord failed completely and the property was foreclosed, or the landlord simply gave up and sold the property at a discount to get out from under it, our best deals have come from burned-out or neglectful landlords. There are many opportunities for the ambitious real estate investor to buy these deals, turn them around, and make a killing.

7. House Hacking Potential

One of the best ways for new investors to get started in multifamily real estate investing is through a strategy we call "house hacking." House hacking means that the homeowner lives in one unit and rents out one or more units of their property so they can live there more cheaply than normal—maybe even for free. The story from the preface was based on house hacking. The income from the rented units can sometimes cover your entire mortgage payment and more, allowing you to essentially live for free. This is the power of house hacking, and small multifamily properties make it possible.

Now, why would anyone choose to invest in a rental property where they have to live in one of the units? What makes this option so appealing to new investors? Three words: low down payment. Earlier, we talked about the differences between residential and commercial lending, including how residential lending tends to be cheaper and easier to obtain. To take this concept a step further, residential lending becomes even better when the borrower is planning to live at the property. In the United States (and many other nations), homeownership is strongly encouraged, with the government even assisting in making this dream a reality for many people.

The U.S. Government does this through lending programs that offer loans with very low down payments. The most common example is the Federal Housing Administration (FHA) loan, which requires the borrower to put down only 3.5 percent of the purchase price. On a $200,000 purchase, that could be just $7,000 down. In addition to the FHA program, many banks now offer other loan products with low down payment options that have some unique advantages over the FHA program for just a slightly higher down payment.

Compare that to a residential loan for a property the owner is not living in. Down payment requirements could be as high as 30 percent on those non-owner-occupied loans, meaning that same $200,000 purchase could require up to $60,000 as a down payment! (Don't worry if you don't have that kind of money to invest in your next property. Later we'll discuss several different strategies for financing multifamily real estate, no matter how much you currently have in your bank account.)

Furthermore, although these owner-occupied loans are obviously designed for an owner to live in the property, the owner doesn't have to live there forever. Generally, the house-hacking owner must intend to live in the property for at least one year. After a year, you can move on to bigger and better things, but—get this—you get to keep the loan in place. In fact, after a year of living in that small duplex and collecting rent from my friend, I moved (into another duplex, actually) and began renting out my former home for $550 per month. Fourteen years later, I still own that property, which continues to provide significant monthly cash flow to my bank account. And it all started with a house hack.

8. Gateway to Larger Deals

We've already established that building a portfolio is important and the sooner you build a large portfolio, the sooner you become financially free. Therefore, perhaps one of the most important reasons to invest in small multifamily real estate is that those small multifamily deals become a *gateway* to larger deals.

Some real estate personalities advise their followers on social media to never buy a small deal, ever. "Start with fifty or a hundred units," they say. But that's like telling a brand-new runner to just sign up for the Boston Marathon! Starting with large multifamily real estate can be dangerous if you do not have the knowledge, experience, contacts, or capital to compensate for all the things you do not yet know. When first building a portfolio, you will make mistakes—no matter how closely you follow the advice in this book. However, would you rather go 10 percent over budget on a $20,000 rehab or 10 percent over budget on a $2,000,000