30 April 2002

Hi and welcome to your April edition of Financial Independence.

I want to get straight into the action this month as there is a lot to discuss, so let's not delay getting started. Your April topics include:

- The Dangers Of Limited Thinking
- 4 Steps To Fast Tracking Success
- Insider Update On Traralgon 27-Unit Property Deal
- Our Latest Deal – 21 Units In Nambour

Let's go!

The Dangers Of Limited Thinking

This month's Australian Property Investor Magazine (which is available at most newsagents) features an interesting article written by Terry Ryder titled 'Getting Rich Quick'.

In it Ryder poses the question of whether it is possible to make a million dollars in real estate in less than five years or are so-called get rich quick schemes nonsense?

Terry Ryder is the author of a very good book titled 'Confessions of a Real Estate Investor', but on this occasion his article misses the mark of what I would call reasonable and accurate journalism.

Instead of reporting the true rorts that are common place in the real estate market, such as two tiered marketing and 'fly by night' type seminars based on dodgy property strategies, Mr. Ryder spends a lot of time interviewing people who all agree that it's just not possible at all to make a million in real estate.

Some of the quotes from experts included in 'Getting Rich Quick':

"Brisbane real estate agent Patrick Dixon says 'There is no way you can become a millionaire in five or seven years through real estate investment.'" (Page 18)

"Noel Whittaker believes most get rich schemes are a 'total nonsense' but adds 'you are not going to be a millionaire in five to seven years doing it.'" (Page 18)

"Rod Cornish, head of Property Research at Macquarie Bank regards notions of achieving millionaire status in five years as 'just unbelievable'. He says 'This kind of thing shouldn't be allowed.'" (Page 19)

If you were an average investor reading this article you'd most likely conclude that achieving fast-tracked wealth creation can't be done – the experts say so, and continue to spend 45 hours a week working in a job.

And that's OK if that's what you want to believe.

But before we rule off that massive wealth creation through network marketing, share trading, real estate or even olives can't be done, let's complete a little more analysis by studying the psychology of the people making these comments.

Did you notice that the quotes above come from mouth of *employees* and not investors?

In the world of an employee the possibility of creating massive wealth doesn't exist. As Robert Kiyosaki writes in his various "Rich Dad" series of books, employees desire a safe and secure existence.

The limiting mindset of an employee looks to fund life with a pay by the hour job and then relying on superannuation to fund retirement. To them the idea of leveraging off someone else's hard work is not just alien, it's seen in many cases as morally wrong.

Let's expand this concept a little more.

When you borrow money (eg. home loan, personal loan etc.), you are actually borrowing someone else's savings. These savings were originally deposited into the bank in the form of cheque accounts, term deposits etc, which currently attract no / low interest returns.

The bank acts as a clearing-house between investors and depositors. In doing so they provide a point of 'leverage' in that they *create* money, since as each dollar that is received as a deposit is lent on a government regulated multiple. That is, for every dollar of deposits a bank receives, they may lend out (say) $1.20.

Lenders charge a margin on deposit:loan interest rate too, which is the same model that I use as the basis of a wrap; banks do it with money and I do it with property!

Now as an investor, I can add further 'leverage' by borrowing 80%+ of my property purchase price or seek funding to finance the expansion of my business to the next level. That is, I can reduce the cash I need to have to buy a 'deal' by only needing a small percentage of the overall purchase price.

Here's an example of how leverage works:

Original Deposit	Bank	Investor
10 people place $10,000 term deposits (total $100,000) earning 4% (flat) per annum interest	Takes the $100,000 and then lends it out on a multiple, say $120,000, as a loan at 6% (compound) interest	Borrows $120,000 as an 80% deposit on a 'deal' priced at $150,000 yielding 12%

So who is it that contributes the bulk of the deposit money that is needed to fuel the leverage facility identified above that's so critical to investors? It's *employees* to whom the notion of creating massive wealth is seen as risky and unachievable.

Ryder's article is typical of the limited thinking mentality that inflicts employees who lack the vision to see beyond the security of a job. The model put forward for employees is to work hard, invest for the long-term and retire (hopefully) rich.

And yes, this is a formula that should work given time, discipline and guaranteed employment.

BUT, if you DON'T want to work until retirement age, what options or strategies are available?

Answering this question takes you out of the realm of employee and into the topsy-turvy land of investors and entrepreneurs, where deals that can deliver financial independence DO exist.

However there is a massive sacrifice needed to make the transition to become a successful investor. It's this cost that I have attempted to reveal and outline in previous editions of financial independence.

More so, the necessary transition is something that only you can make. And it's the failure to see and make any progress towards a transition that keeps employees that would-could-should be investors attending seminar after seminar seeking the magical 'this could be it' opportunity to make massive wealth.

See, it's not the 'how' that's important. Surely there are enough rich people who have made fortunes in shares (eg Warren Buffet, Rene Rivkin), businesses (eg. Richard Branson, Kerry Packer) or property (eg. Grollo Family, Frank Lowy, John Gandel).

It's having the faith, courage and frankly the balls to try to make the mental transition into a realm where it's possible to get wealthy by thinking big and taking appropriate action. In this mental state the notion of being an employee is seen as the worst possible outcome.

Making this transition is something that you will be ridiculed for – guaranteed. Although Kiyosaki is doing his best to change the psyche of the average investor, there will always be more people who dream about life on the other side of the investing spectrum but will never have the courage or wherewithal to attempt the transition.

That is, people want to change but are not willing to pay the price, which is leaving the security of being employed.

Getting back to the article – what we have is information written about the world of investing from the perspective of an employee. The conclusion? It's not possible to earn a million dollars in real estate for those who cling to the safe and secure approach to investing that are the predicable and reliable crutches of those living in the realm of an employee.

Perhaps we have journalists, bankers and real estate agents who have tried and failed, and are now bitter towards others more successful. It's like telling someone who has cracked the code for the Rubik's Cube that it's not possible to solve the puzzle in less than 100 moves.

I agree that people need to be warned about the schemes of the unscrupulous and that there is a huge difference between *being* a successful investor and *talking about* what is needed to be a successful investor.

Seminars, information products etc. that disclose the 'how to' will be of limited benefit unless you can first attempt and later seek support along the mental transition that is critical to evolving from employee to investor.

Creating a million dollars in real estate can be done and the Ryder's article acknowledges this with the following quote:

"Kerry Herron… chairman of Herron Todd White says only the extremely lucky or the extremely skilful achieve the kind of rapid wealth promised at get rich quick seminars." (Page 19)

In another article later in the magazine (page 33) the following text appears "We have comment from expert renovator Paul Eslick. He built a multi-million dollar portfolio in just three years…"

It seems it IS possible!

My experience adds further conclusive evidence to this assertion. I have made a million dollars in real estate, which means it is *possible* for you or anyone else to do it too. But *can* you do it? That is a matter of being open to the possibility of allowing your mind to evolve.

Changing the way you think is at least, if not more important, as acquiring a strategy such as property, shares, etc. that someone else has developed, refined or enhanced to make money.

True success is in the way you think.

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4 Steps To Fast Tracking Success

I first met investing duo Bruce Innocent and Denise Sam in November 2000 at the first 'get together' I held in Box Hill. Bruce had earlier e-mailed me after reading a Internet forum post I had made on the 'Rich Dad' site about how I got out of the rat race in 11 months.

In November 2000, Bruce owned four properties but couldn't crack the formula for achieving the fast-track success that David and I had achieved. Today Bruce and Denise own 24 properties and have built an extensive passive income. I have asked Bruce and Denise to contribute a small article that outlines how they have been able to achieve this extraordinary success.

Hello fellow Inner Circle members.

It's a great pleasure to be able to contribute this short outline of how we have been able to build our property portfolio using the advice of Steve and several other mentors.

Just before we begin we'd like to acknowledge the time and effort that Steve and David contribute to making information available in the 'Inner Circle' that you simply can't and won't find anywhere else. If you actually use the information that is published here, you'll quickly conclude that it is priceless, well, it has been for us.

Before we had met or even heard of Steve McKnight we had read Kiyosaki's excellent book 'Rich Dad Poor Dad'. Completing that book was a massive step in our financial independence education as until that point we were unsure of what other possibility existed except working in a job.

Sure, we already had four investment properties, but these were not what you would call successful and one of them would regularly cost us up to $1,000 per month under the guise of a tax efficient long-term asset.

Following on from the book we looked up Kiyosaki's website and found a discussion forum. It was fundamentally American and being Australians we sought affirmation that the information in his book was relevant and could be applied here.

That's when we stumbled across a post that Steve had made titled 'How I got out of the Rat Race in 11 months'. Reading Steve's story of how he invested in property and how he used the wrap process, we were encouraged but at the same time nervous.

We wondered 'OK if it can be done, what could we do next to make it happen?'

Being shy types it took some time to pluck up the courage to e-mail Steve. We half expected no response or worse – a blast for the insolence of attempting to contact someone successful without invitation. Yet we were blown away when he replied politely and even said that we could call and have a chat!

We took him up on that offer and afterwards shook our heads at the paths that life can lead us on when we have the courage to take action. Really, if we hadn't plucked up the courage to e-mail Steve then I'm not sure whether we'd have the same degree of success that we enjoy today.

Our story continues in that we have continued to be guided by mentors such as Steve and David (both directly through their friendship, the Inner Circle and other information projects they have created such as the Wrap Library), Robert Kiyosaki (through his books, tapes and website), and John Burley (through his book).

The result? Today we own 24 positive cashflow investment properties that provide substantial passive income.

Not that it has been easy and without the occasional expensive mistake from time to time. But if we can do it using nothing more than guidance, perseverance, reassurance, some good-luck and also a willingness to take action – then you can too.

Looking back, we believe that our success stems from having a plan that involved four stages, which Steve has conveniently turned via marketing speak into 'The Four Steps To Fast Tracking Your Success'. To assist you to achieve the kind of results that we have we'd like to share these four steps with you as set out below:

Step One: Acquire Knowledge And The Learning Process

Your desire to achieve a different life must come from a passion, and your passion can only be ignited when you believe in something and feel that it can be a possibility in your life.

So in order to work out what are the alternatives (in a financial sense) from your current situation, you need to have to seek mentors and look at the outcomes they have achieved and the way they have done it.

This translates into becoming educated or increasing your knowledge by seeking out information that you don't know. Think about this for a minute.

In our case we had four investment properties, yet we continued to succumb to the living beyond our means and using credit cards to finance the shortfall.

We'd often spend oblivious to the obligation to repay. When payment came due we simply didn't find the funds - a term we've heard applied is 'we had more month than money'.

Our change in mindset began with a commitment to seeking a new mental diet of financial independence based knowledge that we could use to overwrite our old strategy that was keeping us poor.

This included books (principally by Kiyosaki and Burley), websites (http://www.richdad.com and http://www.propertyinvesting.com) and seeking mentors (such as Steve through this Wealth Tips Online service).

One of the most valuable things this new information delivered was a frank and honest review of our money situation at the time and the realisation that what we were doing was not a sustainable formula for success.

We needed to regain control of our spending, a task we completed while also discovering the various creative investing strategies that other people have used to make money.

In summary, step one is a learning process that we recommend must last at least six months. During this time you need to assess your financial position, control your spending, create some sort of savings plan and also capture information that is often available for free (Internet) or low cost (such as books, games etc.).

Without this new knowledge and a reprogramming of your financial brain, the best you can hope for is more of the same of what you have currently got.

Step Two: Put The Team Together

You may not have realised yet, but your team starts with yourself. So, do you want to or can you afford to be the weakest link?

The answer is 'obviously not', so this again reinforces the need to invest in your financial education.

You must assume responsibility as the leader of your team, which means you must know the outcome your team is working towards in intricate step-by-step detail.

Other members of your team may include:

Business or Joint Venture Partners – a business or JV partner doesn't need to be someone that you'd like to be the best man or matron of honour at your wedding. It should be someone who can bring to the table different skills or resources that complement yours.

Accountants – Our first financial model for an investment property was a three line Excel spreadsheet that was pretty much rent, expenses and profit. Then we sought the help of an accountant to help us to build a more realistic financial model, create a plan that was to become the vision for our team and also establish what records should be kept and for what purpose.

The taxation consequences of your investment will impact your bottom line. It is important to be pro-active rather than reactive when it comes to finance. You should consult with your accountant before a problem gets out of hand.

Legal Experts – The first time we approached our commercial lawyer about wraps he was less than enthusiastic about the concept. But we pushed him to study up (at our expense) and a short time later he was convinced that the idea had merit.

Sometimes your team of advisers will begin with people whom you already know from other circles in your life. For example, our lawyer was already a good friend that we knew through a mutual passion in music.

Finance Providers – At one time in our property investing experience we had four deals all lined up to settle on the one date, only to be told about a month before that our already approved finance had been cancelled higher up the bank chain.

Shocks like this test the resolve of a business partner relationship, but it is in hard times that the weaknesses of your business are exposed. It is a good idea to have a number of potential finance providers who are all interested in your business, as this allows you to shop around for the best deal.

Mentors – You need to have people around you whom you can mentor and who can mentor you. This is critical since someone independent to your deal can review it with fresh eyes and potentially see holes in your plan or perhaps better ways to make your investment more profitable.

You have to be pro-active in finding mentors, as people won't approach you. For example, we had to approach Steve and now we are starting up an informal investing club in our area with about six other people and copious amount of coffee and hot chocolate.

Remember that your team begins with YOU. You don't need to be the one with all the skills, but you do need the vision and the ability to bring the rest of your team into unison.

If you want to be a participant rather than a leader then you will find it difficult to gain momentum.

Step Three: Secure A Reliable Stream Of Income

We don't want to hose you down, but a reality check requires that while you build multiple streams of passive income you need a secure and reliable stream of income against which a financier will lend against.

And in most cases this will be in the form of a j-o-b or continuing the slog as a business owner!

Sure, we'd like to both stop working, but if this happens then we let the rest of our team down (remember that we are the most important players in our team) since we have not yet posted a winning score on the board.

We keep an eye on the number of total hours a week that we work and can see the progress toward our goal when we work less hours without suffering a loss in lifestyle.

Step Four: Take Action

We know many people who want to be financially independent but are too busy working to ever make a start.

Trust us, making a start is the hardest part and there is always a reason for not beginning. We finally understood that the market will never be perfect, but that didn't matter so long as we had a plan, the team to support us and the reliability of a steady flow of income from our jobs.

And while we didn't know it at the time, our first tentative step into the world of investing actually began when we decided to control our spending and repay the nasty credit card debts that had build up from our lifestyle expenses being higher than our incomes.

We have come to realise that any action creates a reaction, which facilitates more action. Continual action builds up momentum in the form of ongoing reactions (finding deals, learning in the field etc.) which empowers you to always progress towards your goals. You only stop progress when you stop taking action.

But if you never make a start, or if you don't react to successes or setbacks along the way, then don't ever expect change to occur since you'll always remain a spectator in the quest for financial freedom.

Earlier we mentioned how we wondered whether 'it' – financial independence - could be achieved. Now we are two years down the investing track we can say the answer is 'yes', yet our success hasn't happened without sacrifices and some expensive mistakes.

The four steps we've outlined above have laid a foundation for current and future success. We're confident that you can replicate our results, provided you develop a plan, build a team, secure regular income to finance your deals and lastly take action. Good luck!

Thanks Bruce and Denise for sharing your thoughts and strategies. Remember that Bruce and Denise can be contacted through the Inner Circle forum if you have any questions or comments.

Insider Update – Traralgon Properties

Last month I outlined the basic strategy for the 27 units that David and I purchased for $510,000.

You may remember that the overall aim of the project was to sell off 11 of the units to recoup all of our renovation costs, plus our deposit and thus leave us with 16 positive cashflow units on 80% finance for effectively no money down.

Over the past month I have been busy building a financial model to work from and finding contractors who can complete the renovation by our settlement date – 5 July 2002. I have secured early access and found a great builder to do the work who is due to start on 2 May 2002.

I have also placed the following ads in various papers to attract leads - being investors who want to purchase the 11 units:

Ad #1:

CASHFLOW POSITIVE FROM DAY ONE! Rare opportunity to secure 11 units (individual titles) currently returning over 10% per annum + capital gains. I need to sell quickly and use the proceeds in another urgent venture. Will consider carrying back finance to make this a 'nothing-down deal' for the right person. Find out more today - call me (David) on [mobile]. Call now.

Ad #2:

A GREAT PROPERTY INVESTMENT! Currently earning over 10% per annum + capital gains. Here's your limited opportunity to secure 11 units (individual titles) renting between $70 and $80 per week. Properties are undergoing partial cosmetic renovations so depreciation benefits are available. This is a true positive cashflow opportunity that will go quickly. Find out more by calling Dave on [mobile]. Do it now or risk missing out.

As I write this e-mail I am also building this project as a case study for all Inner Circle members. There are digital photos and my financial model which will be uploaded soon. I'll also provide regular updates about the status of the project so members can see the progress and how the deal unfolds. Stay tuned for more information!

Latest Deal – 21 Units in Nambour (Queensland)

On 12tApril 2002 David and I signed a contract to purchase 21 units in Nambour - a small town west of the Sunshine Coast for $530,000.

I first spied this deal while surfing the Internet (realestate.com.au) back on 21st January 2002 with an ad that said:

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INVESTMENT ---BLOCK OF FLATS
$550,000
NAMBOUR
Prime investment opportunity to purchase this block of 21 flats. The
flats are a mixture of 1,2 and 3 bedrooms and have been well
maintained.  This position is elevated with views over town.  Gross
income when fully let is $96,200 and netting approximately 13.5%
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We called up the agent and found out that only one of the units was vacant and that the current annual rent was $91,260.

Based on this we submitted an original offer of $520,000 cash on a $5,000 deposit and balance due in 90 days. The vendor rejected this as too low and they countered at $535,000.

We countered again at $535,000 broken up between $500,000 cash and a $35,000 second mortgage which was verbally accepted by the vendor.

With the passage of events in our business this deal was put on hold as we prepared for the national speaking tour we completed that was promoted Break Free Events. One event that we were going to speak at was on the Sunshine Coast, which suited our plans because the venue was in the vicinity of Nambour so we could inspect the units.

It was a very sunny day as David and I made the drive from Brisbane to the Sunshine Coast with a detour via the Big Pineapple and into the town of Nambour.

Sadly though, upon our arrival the agent informed us that he'd sold the property for full price the day before to someone from Canberra who had flown up the day she spied the deal and signed a contract there and then. Sure, we had a verbal agreement but we hadn't signed anything and as such we missed out at the eleventh hour.

Yes, we were a little disappointed, but nevertheless left the door open for the agent by mentioning that we are still interested if the deal fell.

Sometimes being an investor is about learning lessons that only come from experience. For example, the pain associated with missing out on this deal led me to hasten stitching up the Traralgon deal, which had also been on the table for a few weeks, the second I got back to Melbourne (which was the Thursday before Good Friday).

It was a good thing that I did because when I called the Traralgon vendor on the Thursday, he'd just come back from lunch with a purchaser who had inspected the property four times but couldn't sign a contract until next week because his business partner hadn't seen it.

I was able to arrange a meeting for Saturday where I signed a contract (with a subject to finance clause) and do to those potential purchasers what someone else had done to us on the Nambour deal.

We didn't hear anything from the Nambour real estate agent and just assumed that the deal was proceeding and that we missed out. Then a few weeks later the agent rang up and advised that the purchaser couldn't get finance, his offer had fallen over and asked 'were we still interested?'

Sure we were! But at different terms to our original offer since we had already committed funds to the Traralgon deal.

There was some haggling about the revised offer before we agreed on:

- Cash price
- $530,000
- Six month settlement
- Subject to finance and building / pest inspection

I often say the negotiation is a matter of being flexible on terms or price but not both.

In this case we secured the property for $5,000 less than our earlier agreed counter offer but with no second mortgage. Yet we did delay the settlement for six months, by which stage we should have recouped our deposit and renovation costs from the Traralgon deal (by selling the 11 units) which we can reuse to finance our deposit for this investment.

Furthermore, following on from the building and pest inspection we negotiated for the vendor to complete renovations and improvements that will cost at least $5,000, again bringing down our real cost and improving our return.

A quick financial budget on this deal reveals:

Rent (based on current figures and vacancies for that area)	$86,700
Loan Repayments (80% finance, P&I, 7%, 25 years)	($35,883)
Management Fees	($5,500)
Rates Etc.	($18,000)
Insurance	($1,000)
Repairs (5% of total rent)	($4,335)
Other Allowance For Contingencies (10% of total rent)	($8,670)
Total Cashflow / Passive Income	$14,312
Cash Needed (20% Deposit)	$106,000
Nett Cash On Cash Return	13.50%
Forecast Capital Gains	5% per annum

This is a big deal in the scheme of our property investing, but it illustrates the progression of our investing business as David and I graduate from small single family homes to bigger and more cashflow positive properties.

In this deal we were again reminded of the importance of taking action. It only came to our attention in the first place because we:

- Downed pens and calculators and took the time to search the Internet.
- Built a team of professionals in Queensland (real estate agent, lawyer, bankers) who guided us on the appropriate procedure for the laws in that State.
- Have regular income from our accounting business and other investments that can be pooled to provide income which the bank needs to see in order to lend us money.
- Took action (eventually in this case) to secure the deal.

These four points are what Bruce and Denise identified in their contribution to this edition and to which I completely endorse and fully agree with.

It would be a good idea for you to take a blank piece of paper, divide it into quarters and then write down what you are doing to plan, build a team and earn secure sources of income that a financier would lend against. Finally, outline what specific action you will take to get or keep you in the game!

This month's Financial Independence has been focused on helping you mentally prepare for the challenge of becoming an investor.

I'd like to reiterate that how (that is, the strategy you adopt) you become financially independent isn't as important as the change in thought pattern and belief that you deserve success. This is the essence of becoming money attractive.

I have had a lot of fun writing this edition and a perfect way to close is to remind you that success comes from doing things differently.

Have an awesome month and I hope to see you on the forums.

Regards,

Steve McKnight

P.S. You should have received your first Hot Topic tape by the end of the first week of May. I'll be very interested to hear your feedback.