HOW TO GROW A MULTI-MILLION DOLLAR PROPERTY PORTFOLIO

IN YOUR SPARE TIME

MICHAEL YARDNEY

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ACKNOWLEDGEMENTS

Just as creating wealth is never a solo effort, this book would not have been possible without the support and encouragement of certain people who have contributed to my life in many ways.

In particular thanks to my wife Pam for encouraging me, supporting me in every way and putting up with all my late nights and weekends on the computer. She endures with my almost fanatical attitude to business and property investment and continually encourages me through all the good times and through all the things I still need to learn. I am humbled by her love and devotion, which I try hard but never quite succeed to match.

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I have read almost every book about property ever written, learned lots along the way, and there are many ideas sprinkled throughout this book that I have learned from others. I guess I had to learn everything from someone at one stage, so I am sorry I cannot acknowledge everyone – I really can't remember where I first came across many of my strategies. I must make special mention of American author Robert Allen, who contributed to many of my concepts about wealth discussed in the early chapters of this book.

Thanks to Michael Wilkinson of Wilkinson Publishing for having faith in me and my book way back in 2006, and to Damian Alway for his great editing of the original manuscript.

And finally to you, the reader – thank you for choosing to invest in this book. Please take advantage of the information I have to offer by using it to obtain the financial independence you deserve.

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INTRODUCTION

Whether you have yet to make your first investment or you already own a multi-million dollar property portfolio, this book is for you. It will give experienced investors the opportunity to re-evaluate and fine-tune their current approach and the same information will help new investors get a perspective that normally takes years and years to acquire.

I have been investing for close to 40 years and over that time I have adapted my investment strategies to change. Recessions, fluctuating interest rates and changes in legislation have all taken their best swing at our property markets. Despite all the changes we've experienced and in spite of regular predictions that our real estate markets will collapse, property prices and rentals have continued to increase. In fact they've been doing so for more than 200 years.

With the advent of the Internet and easy access to almost unlimited information and instantaneous news, change seems more prevalent and economic cycles seem shorter. This has led to a band of fortunetellers trying to predict our property markets and property spruikers selling get rich quick through property schemes suggesting new techniques for our changing economic climate.

While there is a lot of information out there, much of it is misinformation. That's one of the reasons why the majority of people who become involved in property investment are not successful in building the financial independence they are seeking.

Fact is most property investors fail. Statistics show that about half of those who buy a property investment sell up within five years. In fact close to 20 per cent of people sell up in the first year or so. And those who hang in there only manage to buy one or two properties and less than one in two hundred investors ever buys six or more properties.

Owning one or two properties isn't really enough. To become financially free you need to own a multi-million dollar property portfolio. This means that most Australian property investors won't achieve financial independence. It also means that if you do what most property investors do, if you invest the way most Australians invest and if you listen to who most investors listen to, then you will get the same results most Australian property investors get!

And you want better than that don't you?

That's why I wrote the first edition of this book back in 2006. I had the aim of giving ordinary Australians a system to become wealthy through residential property investment – a strategy that would allow them to survive changes in the market. As you will discover, this book offers a different approach to property investing than is found in most writings about this topic. While I embrace many of the classic methods used by professional investors, it also contains many ideas and technique not widely used or understood, but which can dramatically affect your results.

I bought my first investment property in 1970 and while I don't know everything about real estate, I have been investing for decades so I have a clue about what works and what doesn't. Although I've been reasonably successful as an investor I would have given anything to have had the benefit of the information in this book earlier in my investing career. Getting the right ideas and then putting yourself in the right environment with the right mentors is a huge shortcut to success.

If you're like most readers you've bought this book because you have a dream. A dream about what your life could be like in the future if you were financially independent. And you're looking for a plan to fund your dream.

My aim in writing this book is to put down a strategy to help you achieve your dream. One that has not only worked for me but for many others who have read earlier editions of this book. This way all Australians can at least get some insight into a successful wealth-making property formula – one that is reproducible and has stood the test of time.

I've been amazed at how many people come up to me as I conduct seminars around Australia, and specifically thank me for the information they have learned from this book and how it has given them a clear path to their own financial freedom.

The highlight of many of my business days is when I receive emails from people I've never met telling they have read this book and it takes pride of place on their bookshelf. They tell me that now they "get it" – how it all makes sense now that I've outlined a financial blueprint for them.

Remember ... all the strategies in this book have been proven in real life. They actually work. They are not some theory a property "guru" preaches but does not practise.

But the power of all this information is not in the information itself, it's in the implementation of the knowledge. It's in taking action.

Both my wife Pam and I remain active property investors and developers and we still use exactly the same techniques I will teach you to grow our already substantial property portfolio.

But back to this updated fourth edition ...

As I write this introduction in August 2012 we are living in interesting times. Due to events that started on the other side of the world a few years ago, we have been plummeted into a time of global financial uncertainty, but it is also a time of massive opportunity as we work our way out of the Global Financial Crisis and move into a new property cycle.

The good news is that this is the beginning of a new economic cycle – a new opportunity for you to build YOUR wealth.

What we are seeing now has many of the hallmarks of one of the great wealth building opportunities that come around every so often. These are the times when fortunes can be made for those who are prepared and are "in the game". They are also times when those who are not "in the know" will make the same errors that others have made in the past that will hold them back financially.

Australia is at the beginning of an unprecedented resources boom that will create wealth for all Australians. This is not just another circuit of the economic clock, it's a situation that many people have never experienced in their lifetime ... and possibly a situation we may never experience again for a long, long time!

> The good news is that this is the beginning of a new economic cycle...

This is an opportunity to get set to take advantage of the beginning of a new property cycle that only occurs four or five times in your adult life.

While there will be some great opportunities the rules are different now. We are moving into a new financial era – a time of change. Let's be honest: most of us don't like change – we'd rather have a nice predictable environment for our job security, our businesses and our investments. Unfortunately, all these are subject to the whims of the markets and the economy, and therefore are not predictable.

I felt compelled to update this book when I realised how much the property markets have moved in the couple of years since I penned the last edition. So in this edition I clarify some strategies, expand on others and in fact completely change my opinion on one or two.

The world's economic markets are still in turmoil with some countries suffering more than others. Fortunately the Australian economy has fared well and has been the envy of many other nations, but companies are still going broke, people are losing their jobs and most of us are feeling at least a little uncertain. However our economy is turning around and the good times are returning. And eventually the world economy will once again inflate, which means prices will start going up again and life will become very difficult for the average Australian.

The Europeans and the US government printed billions and billions of euros and dollars to salvage their economies. So did many other countries. When a government turns on the printing presses and floods the markets with more dollars this eventually decreases the value of every dollar – the ones in your pocket and mine as well. When your dollar buys less and less and the cost of everything you buy goes up, this is called inflation. This is good for the government who eventually pays back its debts in cheaper dollars, but it's not good for the average person.

We've moved from a nation of spenders to a nation of savers.

Now this is a simplistic explanation, but many economists concur that inflation will come back in a big way. Give it a while and not only will petrol prices rise again, so will the cost of food and most other items you buy. Yes, we'll have another round of inflation, but it doesn't have to be bad news for you if you own the right type of assets – those that increase in value during inflationary periods – such as residential property.

Inflation rewards borrowers who acquire appreciating assets using depreciating dollars, but disadvantages savers as the value of their money goes down over time. This will set the stage for another significant property boom as more investors will turn back to assets that store value, like residential property, which increases in value during inflationary times.

Currently many Australians have taken their money out of the share market and have put it "safely" in the bank waiting to see how things pan out. Others have paid down their mortgages, their credit cards and other debts, ensuring their family budgets look healthier. We've moved from a nation of spenders to a nation of savers.

Eventually, when confidence returns, they will start to invest their money again.

When looking to invest there will be a flight to quality – to an investment vehicle that is safe and secure. Many investors will remember how the value of their shares plummeted and they will invest in residential property again and this will ensure that the property cycle moves on. Just like every boom paved the way for the next downturn, every downturn sets the stage for the next boom.

As our markets move through the next property cycle and properties in Australia increase in value by millions of dollars, the properties themselves won't care who owns them. So you should be one of these owners. Somebody is going to make money – so why not you, and in this book I'm giving you the knowledge to do that.

The game of property investing is a little like the game of chess. We all have the same pieces on the board. But those players who can see three or four steps ahead are the ones who are going to win.

I'm going to teach you my 4 Stranded Strategic Approach to property investment. This is a system that is well rooted in the real world of property and, while it is not a get rich quick scheme, it has helped me, hundreds of my clients and many readers of earlier editions of this book grow very substantial property portfolios.

While the majority of people will sit on the sidelines, strategic investors are looking for and buying investment opportunities created by our changing times. While this may seem difficult to believe given the amount of negative news bombarding us on a daily basis, the truth is fortunes are always made in times of change.

As you read this book I will be your property mentor and give you the perspective you will need to build your own multi-million dollar property portfolio – one property at a time. And don't worry, it will be easier than you think as you ride the wave of the next property cycle as Australia enters a new age of prosperity fuelled by the resources boom.

Why do I say that?

I'm glad you asked. Read on to find out ...

Michael Yardney

August 2012

LET ME BE YOUR MILLIONAIRE MENTOR

Would you like to become rich by investing in real estate – possibly very rich? Then this book is for you.

You should be aware from the outset that there is no safe way to get very rich from real estate quickly. It takes time, but most Australians who simply have owned their own home for more than a few years have made money. This rise in real estate values meant that many home owners have seen their household wealth increase substantially.

But another group of Australians discovered how to profit in ways other than just owning their own home. They became real estate investors and bought additional properties.

Most investors recognise that the performance of real estate as a financial asset is astonishing. What you may not know is that some of the best opportunities for many years are now available in our property markets. These have been created by the world financial crisis as interest rates have dropped considerably and property values have stagnated or fallen in many parts of Australia.

Through this book I am going to be your property mentor and will argue that over the next decade almost every reader will be able to build themselves a multi-million dollar property portfolio because I am going to give you an insider's view of how the professionals invest in property. This means you will be able to grow your property portfolio faster, yet more securely, than most and in a way that will have the banks support you.

And the real benefit is that you will be able to become financially independent. You may be able to replace your day job with your property income and only go to work if and when you choose.

As your mentor I will show you how to get set for, and take advantage of, the next property cycle, which will create a new group of property multi-millionaires in Australia over the next decade.

You see, in Australia we are witnessing what I call a "perfect storm" – a confluence of a number of fundamental factors that will ensure that as we move out of the effects of the world's financial crisis, property values around Australia will increase significantly. We have:

- A rising population, fuelled by a record number of immigrants as well as a baby boom.
- A shift in the demographic composition of our nation – the types of people who live here, how they want to live and the types of properties they want to live in. We have more single and two people households meaning we need more dwellings just to house the same number of people.
- An ever-increasing shortfall of housing in some parts of Australia, as builders hesitate to construct more dwellings. Currently banks are not keen to lend for speculative construction and even if they were, the cost of constructing new apartments and townhouses in most of our capital cities is too expensive, meaning that the cost of established dwellings will have to increase significantly before new construction starts to relieve our housing shortfall.
- Very low vacancy rates and rising rentals as a large number of potential tenants vie for a dwindling supply of rental properties.
- Relatively low interest rates.
- An improving economy that is likely to remain strong for a number of decades driven by our resources boom.
- Strong yields – the return investors receive on their investment – as flat property prices, increasing rents and lower interest costs all make the cost of owning an investment property more attractive.
- Rising building costs that will make new dwellings more expensive.

There will be a continual strong demand for housing from our various generational groups, including the Baby Boomers who are moving into different types of accommodation, their children; Generation X, and the many immigrants who will need to come to Australia to boost our work force. This will ensure that the long-term fundamentals for our property markets remain excellent and the upturn in the property cycle that is commencing will continue well into the next decade.

As your mentor I want to persuade you to take advantage of the opportunities that will arise in Australia's property markets over the next few years.

AN INSIDER'S PERSPECTIVE INTO THE PROPERTY MARKET

Many years ago I made a decision about my future that I've never regretted. I decided to start exploring ways to become financially independent by investing in real estate.

As I write this today I've been at it for close to 40 years. As a real estate investor and property developer I've bought sold, leased, developed, built and project managed residential, commercial and industrial real estate worth hundreds and hundreds of millions of dollars. I am CEO of one of Australia's premier independent property groups – **Metropole Property Strategists** – and I've made many millions of dollars for myself and my family, as well as creating wealth for our clients.

It's been an amazing journey and, while I don't claim to be the world's greatest real estate expert, I have a wealth of experience and knowledge that has created massive profits for hundreds of clients.

Increasingly these days I'm dedicating a lot of time to writing, speaking at seminars about property investment and the psychology of success throughout Australia and South-East Asia, helping others to find their own way on the path that I've taken.

As your mentor and as a property "insider", I'm ready to share this information with you, and have sprinkled this book with exclusive insider tips. I also have special bonuses available for you at www.TheBookOnPropertyInvetsment.com.

So, why did you pick this book up and why should you read it? I'm guessing that it's because you've made a decision too. If you're ready to start a life-changing journey by exploring ways to invest in real estate over the long term then you will find that what you have in your hands is an invaluable guidebook that can help direct you as you take your first steps on what should be an incredible journey.

For those of you who already own investment properties there are plenty of advanced property investment strategies in this book including a number of concepts I haven't seen written in property investment books before.

To help you I'm going to share some of my own story and lots of insights into how you can build a multi-million dollar property portfolio. Initially, you will be able to do it in your spare time, while you have a day job. Eventually, you will have a choice of whether you go to a day job at all.

But remember that this book is not only about the money. It's about giving you choices. It's about your lifestyle. Ultimately it's about your freedom!

IT'S A BRAVE NEW WORLD FOR PROPERTY INVESTORS

When I wrote the first edition of this book in 2006 there were a lot of people who were too scared to invest in real estate. One of the biggest property booms in recent memory had come off the boil and prices were slumping. Negative talk dominated the media, and many investors were wondering how they could have been so stupid as to have believed in wealth creation through property, and wondered whether prices would ever increase again. Some commentators were suggesting that the property bubble had burst and that it was all over for many years.

At the time I had a clear response: there would be another property boom and it would be even stronger than the property boom of the late 90s and early 2000s.

A brave call? Not at all

> This will be the blueprint to your financial freedom.

At the time I'd been in this business for more than 36 years and I'd learned to appreciate the cyclical nature of markets and how to ride the peaks and troughs. I've invested through and survived five complete cycles and I can say with certainty that the sun will come up again tomorrow and property prices will continue to grow over the long term.

Looking back now, I was a lone voice in the media, predicting our property markets were about to turn. I have since been proven correct with most parts of Australia experiencing an amazing boom in 2006 and 2007. I was right not because I'm so smart, but because that's the way property cycles work. And throughout this book, I'm going to use the lessons of history as our teacher to pave your way for the future, giving you confidence to make your own investment decisions.

Of course, at the time of writing this fourth edition (August 2012) the market has turned once more. We are coming out of a two-year property slump commencing in early 2010. Prior to this slump the price of the average home in some of our capital cities experienced two or three years of strong capital growth, some increasing in value by over 25 per cent. Then we experienced the aftermath of world financial crisis and with concerns that the European financial markets could melt down, banks became more conservative and once again property fell out of favour as Australians stashed their cash, saving rather than spending.

It's interesting how the cycle moves on. Each property boom sets us up for the next downturn. Each property slump sets us up for the next boom.

If you want to become a successful investor you can't afford to wait until the next boom is evident. You should get set for it, because by the time the press and the general public becomes aware of the upward trends in our property markets, the big profits will already have been made.

Right now, as you're reading this, there has never been a better time to get your ship in shape and ready to catch the next wave. Last time we were at this point in the property cycle fortunes were made.

BRAVE VERSUS CRAZY

Don't worry. I'm not trying to play down the seriousness of the effects of the international financial problems on the Australian economy or our finance markets. Nor am I an incurable optimist and I'm not asking you to be either. I know what it's like to be on the cusp of making a big decision involving your life savings. I've been there myself and helped hundreds of clients to invest in property.

Like any good mentor, I have some insight into what's going on in your mind when you first start exploring new terrain.

I understand the fears, the trepidation and the false starts. The experience that is putting your money down as a deposit on a property, knowing it's close to your last dollar. The worry that when you first buy a property the tenants are going to move out and you'll lose out. Or what it's like going to a bank and being turned down, with lenders suppressing laughter at your financial statements.

But I also know the good feeling you get when you do get a bank loan, or when a property deal goes well and you make more money in the one deal than you would working a whole year at your day job.

OUR MENTORING PROGRAM

We're going to start our mentoring program slowly and get to know each other first. I'll begin this book with some introductions and talk a little about how I started my journey and what experiences I can share with you.

Then we're going to examine some of the key benefits to choosing residential real estate as your wealth-creation vehicle. Of course, while it's a fairly straightforward investment vehicle, your transformation into a property multi-millionaire is going to be anything but easy, so you might need to consider whether you really have the courage to be rich and ask yourself if you're ready to take action after you receive the insights in this book.

I'll be sharing my 4 Stranded Strategic Approach to investing that has stood the test of time, then we're going to look at some practicalities to getting started and some fundamental investing concepts. We'll begin with a discussion of when, where and what you should consider buying.

With a road map taking shape before us, it will be time to examine some of the challenges you can expect to face. Yes, there are tigers to be tamed out there. You'll have to face some intimidating tactics and learn to hold your own as you try to establish workable relationships with real estate agents, lenders and other market players. There are some handy tricks you can take to the negotiating table and there are some tactics you'll want to watch out for.

Finally, as we get more comfortable with the terrain, we'll start to examine some advanced ideas. We'll look at the attractive tax advantages you can create using some clever investing strategies and ways to speed up capital appreciation by adding value to deals. We'll also look at how you can protect yourself from nasty surprises using a hard-earned methodology I've developed. And we'll visit some of the issues involved in dealing with banks and the secrets to refinancing and revaluing your profitable assets.

Most importantly I will explain the end game; the concept of living off your multi-million dollar property portfolio. This will be the blueprint to your financial freedom.

A WEALTH OF EXPERIENCE

As your mentor I want to share with you as much of my experience as I can, so I have created a special readers-only web page at www.TheBookOnPropertyInvestment.com with a further chapter of this book and useful checklists and reports.

As you read the final pages, hopefully you'll realise that you've actually made it through to the beginning of your own successful investing story. Once you've gleaned the insights from this book, it's important that you take some action if you want to see results. Don't worry – there is a special section I'll leave you with, which will help to point you in the direction of the next steps you will need to take, and some more resources that can help you.

I've made a lot of money for myself, and others, and I've lost money too by making foolish decisions. In the past I've also been caught when economic circumstances changed unexpectedly. I know the terrain only too well, and the purpose of this book is to help point out a safe path and uncover some of the pitfalls for you.

All the techniques you will read about, I have either used myself, or been closely involved with through helping others to employ them – I'm not just spouting forth theory. I will show you the way I operate and share knowledge that can save you real money. But more importantly, I can empower you to start on the path to realising your own financial goals and financial freedom, if you're ready to make the same decision that I made myself many years ago.

After I finished writing this book there was still so much content left over, so I've decided to provide this to you as a bonus. You can access this now at www.TheBookOnPropertyInvestment.com

OK ... are you ready and willing to get started?

CHAPTER THREE

THE FOUR LEVELS OF INVESTING

I would like to introduce you to the concept of the four levels of investing which is a model I've created to explain the progression most investors take in their path to developing financial freedom. This model allows you to know exactly where you are heading financially, at what stage you are at along the way, and what the key focus areas and leverage points are that you can use to fast track your journey.

While some investors will move up this hierarchy and make it to the top, and some people will drift a little from one investor level to the other, unfortunately most will "safely" sit at one level for their entire life. They become stuck because of their mindset (their programming about how they deal with money) and this prevents their financial success.

The ultimate goal is to become a Level 4 investor; this is the top rung of the investment ladder and means you have become financially free and the good news is that with some insight and education and by building a multi-million dollar property portfolio you too can become financially free.

My model allows you to know exactly where you are heading financially. The first step is to understand what type of investor you are now, then you decide what you want to achieve – how far you want to progress – and then start learning the things that the next level of investor already knows. In order to reach that next level you will have to understand what they understand and behave like they behave. It's not enough to just have the knowledge; you also need to take the actions the next level of investor has taken if you want to climb your way to the top.

Just to clarify things, moving up this investment ladder has nothing to do with your income. I've seen many people earn hundreds of thousands of dollars a year, but by spending most of it on a flashy lifestyle, they fail to graduate up the investment ladder.

Having said that, I've also seen successful investors who work at what some would call menial day jobs, earning relatively little in their pay packet, yet who have over time built a multi-million dollar property portfolio. In other words, their job becomes something they choose to do, not something they have to do for their primary source of income.

As you read through these four levels of investors, I want you to know that at various points in my life I've been at every stage. It's only as you develop more knowledge and understanding, step up and take further action that you will also have the opportunity to move up this investment hierarchy.

Let's now look at the four levels of investors:

LEVEL 0 – THE SPENDER

Level 0 investors are really not investors – they tend to be spenders and borrowers and as a result, end up with a high level of debt. They spend everything they earn and often more. Their money runs out before the month does. They usually survive from pay packet to pay packet, using credit cards and store credit where they can.

The Level 0 investor lives for today. If they have some money they spend it, if they don't have money they borrow it. These are the people who, when they need some cash, go to the ATM and pay a fee to collect an advance on their own money and then pay interest on it. Their solution to financial issues that arise is to spend their way out of it or to take on more debt. They'll often get a new credit card or refinance their home in order to buy more things on credit. Their idea of financial planning is robbing Peter to pay Paul.

The biggest problem for spenders is their money habits, and this has nothing to do with how much they earn. It's what they do with the money they earn. As they move on in their lives and earn more, they just spend more. Today, they can't survive on the type of income they would have only dreamed they could achieve five years ago. They are consumers who spend their money as soon as, or even before, it comes in rather than conserving it for the future.

There are many high income earners who fall into this category because they spend as much, or more, than they make. Sure some spenders can look rich – they may even have big homes or fancy cars, but they also have huge loans that they have difficulty repaying.

For the most part, spenders are not overly conscious about money or their spending habits. Shopping is one of their favourite pastimes, they buy things they don't need and they spread their debt over a long period of time, kidding themselves that they'll work harder and pay off their bills someday.

When asked what their problem is they will tell you that they don't make enough money. They think more money will solve their problems. Yet no matter how much money they make, they go deeper into debt. They fail to see that the real problem is not their level of income, but their bad money habits.

Do you know any level 0 investors? A large part of our adult population falls into this category.

These people haven't learned the fundamental rules of financial freedom I shared with you in the previous chapter. They don't spend less than they earn, they don't invest the difference and they don't take advantage of compounding capital growth.

LEVEL 1 – THE SAVER

The vast majority of Australians who are not spenders will generally be Level 1 investors or what I call savers. Their main investment is their house, which they aim to pay off over time. Sometimes they also save a little, putting a small amount of money aside on a regular basis.

In general they save to consume, not to invest. Level 1 investors tend to be afraid of financial matters and are generally unwilling to take risks. They're following the plan their parents and grandparents followed – get a steady job, buy a house, pay it off and save a nest egg for retirement. The problem is savings, or even owning your home outright, doesn't make you rich.

What usually happens is they work hard over their lifetime, diligently save or pay off their home and at the end, are left with what will be a modest, most likely old and tired house.

The problem is that saving doesn't make your rich. Three things tend to get in the way ...

First there's **inflation**. What you save today won't be worth the same in 15 or 20 years' time. Then there's **income tax**. The average Australian loses 30 per cent of their income on taxes over their lifetime. And finally there is **spending**. We're a nation of consumers. The cold, hard fact is that the majority of Australians will spend a large chunk of their income on consumables: another car, a bigger TV, a holiday, a caravan, etc, all the while eating up much of the money they should have put away for retirement.

Level 1 investors are what I would call financially illiterate and need to focus their efforts on building a solid base of financial and investment skills, upon which they can grow their financial future. They will get the most leverage by investing in themselves and getting a quality financial education (one that is relevant for this new financial era) and begin to build a network of peers they can make the journey with.

LEVEL 2 – THE PASSIVE INVESTOR

Level 2 investors have become aware of the need to invest. They realise that their superannuation won't get them through retirement, so they start learning about investment and begin accumulating assets.

While they are generally intelligent people, Level 2 investors are still what I would call financially illiterate – they don't really understand the rules of money. But remember it's not their fault – nobody taught them. If anything their parents taught them old-fashioned, outdated ideas about money.

They have very little idea of how or where to invest their money; so many blindly follow the advice of financial planners or sometimes their accountant who works closely with a financial planner (who just happens to be sitting in the next office). These investors are usually taught to save and put their money into managed funds or a group of blue chip shares because they are "safe', and to spread risk by diversifying. Interestingly, most really successful investors don't diversify. They find a niche that they specialise in.

> Level 2 investors need to start refining their financial and investing education and focus their efforts on choosing a specific wealth vehicle that they are going to master.

Unfortunately many Level 2 investors have watched the value of their investment portfolio decrease dramatically during the turbulent economic times over the past few years. As much as this has devastated some people and is a terrible situation, there's an important take home message in this experience – diversification doesn't necessarily protect your portfolio. My strategy is to find your own niche, one in which you can specialise. I invest in high growth, income producing, capital city residential properties to which I can add value through renovations or refurbishment, and I would strongly suggest this becomes your niche too.

The point I'm trying to make is that rather than taking responsibility for their financial education (their financial literacy) themselves, Level 2 investors tend to look for answers to their investment needs from outside sources or "experts". This makes them easy prey for financial planners or brokers, or worse still the newest "get rich quick scheme" advertised in magazines or the latest flash-in-the-pan investment schemes spruiked by telemarketers.

Level 2 investors need to start refining their financial and investing education and focus their efforts on choosing a specific wealth vehicle that they are going to master. This could be residential property (my preferred suggestion) or shares or a business. The key is not trying to master every wealth vehicle, but rather to specialise in one. They are also going to have to unlearn the flawed, incorrect and mistaken lessons they have learned about money and wealth from unqualified teachers. I describe these and the golden rules of money for the new financial era in my book *What Every Property Investor Needs to Know about Finance, Tax and the Law.*

LEVEL 3 -THE ACTIVE INVESTOR

Level 3 investors realise they must take responsibility for their financial education and become actively involved in their investment decisions. They become financially literate by building a knowledge base of investment strategies and techniques. They grow to understand and use the three marvels of wealth accumulation: compound interest, leverage (using other people's money) and tax-effective investments. They are starting to get their money working for them.

These investors actively participate in the management of their investments and concentrate on building their net worth and their main focus is on growing their asset base and as they do, their cash flow increases.

As this is the asset accumulation stage of their investment life, these investors have in general moved to high growth, low yield investments and take advantage of the opportunities of compounding and leverage to grow their wealth. This is where residential real estate really shines – it's the best asset class I know for growing your wealth safely.

Level 3 investors usually leverage the time and expertise of a network of industry professionals as they realise that they can't do it all themselves. They also upgrade their network of advisors and peers, often joining a Mastermind group of like minded people.

They must focus on actively doing something to make their assets more valuable before, during, or after they acquire them. This includes things like buying a property below market price, or renovating a property they have purchased, or actively building a business to increase its value.

LEVEL 4 – THE PROFESSIONAL INVESTOR

A very small group of investors move on to the top rung of the ladder and become a Level 4 “professional” investor who has built and now manages a true investment business.

Level 4 investors have a substantial asset base that generates sufficient recurring passive income to pay for their lifestyle costs, plus keep growing their investment portfolio whether they work in a real job or not. In other words they have built their own *Cash Machine*.

Level 4 investors are well educated in the world of investing. They are comfortable with the language of money and fully understand how the game is played.

These investors tend to concentrate on optimising the performance of their investments, while at the same time minimising their risks. While they are still accumulating assets, they are now more interested in cash flow that will allow them to gain the most out of life. Rather than investing what is left over after they have spent their money, they have the correct tax structures in place that enable them to spend what is left over after their money making investment machine ploughs more cash back into further investments.

Professional investors realise the value of outsourcing much of the work for their investment business to give themselves more time freedom. They have a team that consists of accountants, property managers, solicitors and property strategists to assist them in managing and growing their investment portfolio. The professional investor doesn’t hand over control of his investments to others; he still remains in control whilst employing a proficient team who have great systems that achieve repeated and consistent results which are reliable and predictable.

This gives Level 4 investors the freedom to choose whether they get up in the morning and go to work or not. Many still continue working because they enjoy it (as I do), but now they go to work because they choose to, not because they have to.

Others find th time to contribute more to their community or to charities. I know that over the years Pam and I have contributed more and more to charities and the community. We get great satisfaction in helping a number of charities that assist sick children, street kids and others in need. Metropole conducts a Charity Ball and Pam is in the habit of travelling to Cambodia and building houses for underprivileged families.

It's not surprising that the professional investor knows that bad economic times provide some of the best opportunities for success, which means they get into the market when others are getting out. They heed the advice of Warren Buffet, one of the world's richest share investors who said: "Be fearful when others are greedy and be greedy when others are fearful". They will thrive in difficult times, not just survive.

While Level 4 investors are financially fluent, they rarely stop educating themselves. They read, they subscribe to investment newsletters and they still attend seminars and surround themselves with a great team of advisors and mentors and are prepared to pay for solid advice – not only to increase their wealth, but also to protect their assets from opportunistic family members, lawsuits and the government.

You will find that Level 4 investors own very little in their own names personally. But even though they "own nothing", they control everything through companies and trusts. By controlling the legal entities that own their assets, these investors gain considerable legal tax benefits and asset protection.

A final point about these professional investors is that they tend to teach their financial knowledge to their children and pass on their family fortune to future generations as their companies and trusts endure after they have departed this life.

While Level 4 investors are financially fluent, they rarely stop educating themselves.

INCOME IS THE WORST PREDICTOR OF WEALTH

I've come across many clients who earn substantial amounts of money, well over six figures, yet still don't "have" anything. I know Bob, my doctor, has earned hundreds of thousands of dollars a year for the last 35 years. He's just over 60 now, but still lives in a rented house, drives an old car and continues to feel like he's on a treadmill. Every day he goes to his medical practice to see patients and at the end of the month, he just manages to pay the bills.

I have spoken to him about this a number of times. The trouble is, every time he earns money, he seems to spend it. He has never managed to put anything aside in the way of savings or investments, or even as an emergency fund. He said to me a while ago that his car broke down and needed major repairs and even that created some degree of financial hardship for him.

The story of someone like Bob, who probably earns over $500,000 a year, may sound strange to you. But if you're like most Australians, you're going to earn well over $2 million in your lifetime.

Think about it – you will probably earn more than $50,000 a year for over forty years. That equates to well over $2 million in total working income. And that's in today's dollars, not taking into account how your wages will rise with inflation.

So the question isn't really can you make one or two million dollars. My question to you is: are you able to keep a million dollars? If you're like Bob, in fact if you're like many people, you're going to find it difficult to save and easy to spend.

I asked Bob why he still rents; why despite his income he hasn't managed to save up a deposit for his own home and he told me the following story: each new year he makes a resolution and says to his wife, "This year we're going to take $1,000 out of every week's pay and put it aside for the future". (Maybe $1,000 each week is so much you couldn't imagine having that amount to save from your wages but that's okay, just follow the story and you'll soon see my point.)

He hoped that putting this money into a savings account would give him $50,000 by the end of the year and, combined with the small return he'd get on his investment, it would give them a deposit to finally purchase their own home. When I asked him why that didn't happen he told me, "Life keeps getting in the way".

Somebody got sick, or he needed a new plasma TV, or his car broke down. You know what it's like – there are always unexpected expenses.

So he asked me, "How do I do it? How can I do it? What am I doing wrong?"

I explained to him that if he wanted to save but didn't make a firm commitment to pay himself first, it wouldn't work. I suggested he do exactly what the Government does.

"What do you mean?" he said.

I explained that every time we get paid, the Government automatically takes out small amounts of money in the form of taxes. I guess they do it that way because they know that if they didn't take it then, it would be really hard to get it out of us any other time. Therefore, he should similarly set aside a small, pre-determined portion of his wage each and every time he got paid. He should take at least 10 per cent of his wage and put it into a form of savings account before doing anything else with a cent of his money.

Remember I've already discussed this concept and Bob had heard this before, but had just left it very late to change old habits and make a start. You can probably guess what Bob probably thought when he heard this theory many years ago – "How much difference could 10 per cent of my pay packet really make? How much could I really gain from that?"

Don't underestimate the power of this wealth building rule. Consider this – if you started investing $100 a month at age 25 and managed to achieve a 15 per cent return over the next forty years, when you retired at age 65, you would have over $3 million in your savings account.

Conversely, if you waited until 35 years of age to get started, while you might have enjoyed spending that extra $12,000 during those first ten years, you'd only end up with around $700,000 in the bank. In other words, that extra $100 a month spending money for those first ten years, which in total adds up to $12,000, meant you lost out on close to $2.5 million worth of investment savings on retirement. That's the power of compounding.

We've all heard of the power of putting a small amount of money aside to secure our future, so why doesn't everybody do it? We've all heard of the idea that we should pay ourselves first, yet most of us don't. Although many of us make an attempt, we want to put some money aside to save for a rainy day or we want to invest, why doesn't it seem to happen as we plan?

I've spoken to so many people who've told me the same thing; no matter how hard they try, they just never manage to get ahead. They run out of money before the month is over and regardless of how much they earn, they only ever seem to have enough just to pay the bills and scrape by.

The scary thing is, I hear the same story from people making $25,000 a year as I do from people making over $200,000 a year. Just think of my friend Dr. Bob, who earns over to $500,000 a year and is still constantly broke.

"That can't be possible," you might think. "If I made that kind of money I'd be rich by now." But would you? Or would you find more to spend it on? The simple fact is that because Dr. Bob does what most people do, spending all the money he makes and then some, and he has no investments and nothing set aside for a rainy day, the fight to get ahead has never worked for him.

Like I said, the basis of success in moving up the investment ladder is to:

1. Live below your means so that you have money left over and invest the difference

2. Convert your earned income into assets that will generate passive income.

Since there is no amount of money you cannot outspend, managing your money is essential to building wealth.

WHAT LEVEL OF INVESTOR ARE YOU?

Now it's time for some home truths ... How far up the investment ladder are you? Where do you currently sit in this hierarchy of investors?

Remember, this assessment of your current investment level has *nothing to do with your income.* You can be a "low income" earner when it comes to your day job, but still be a Level 2 or 3 investor. Likewise, you can be considered "rich" by working income standards yet still be a Level 0 investor, spending every dollar you earn.

What I want you to understand is that the "active" income you make (the pay packet you work for every day) has nothing to do with what level of investor you are and in fact is one of the worst predictors of wealth.

IN SHORT

- While there are 4 Levels of investing, most Australians "safely" sit at one level for their entire life, being held back by their mindset.
- Income is a very poor predictor of wealth.
- To become financially independent and a Level 4 professional investor, you need to build a substantial asset base. Many successful Level 3 investors build their asset base using residential real estate.