Great reasons to invest in real estate

According to recent statistics published by the U.S. Census Bureau, 75% of multifamily investors are over the age of 45. Over half of these (51.6%) own less than five units, and they earned approximately 31% of their income from ownership of rental properties.

These statistics may surprise you, but some logical reasons explain these numbers. Most real estate investors come to the market later in life because they are concerned about their retirement and are at their highest potential earning power, or some have inherited money or real estate; the U.S. Census Bureau reports that 48% have inherited a home.

There are four major reasons that an investor might choose real estate for investment.

1. Cash flow: Yes, it is still possible in some parts of the country to have a cash flow return. In other words after all expenses have been covered: mortgage, vacancy factor, repairs, property management etc., there still can be some money left on the table. Most banks will not lend money to buy a property if there is no hope of a cash flow.

2. Appreciation: As a result of our growing population - a net gain of one American every 14 seconds, according to the U.S. Census population clock - we could expect to have a population in excess of 400,000,000 in 2050 compared to today's population of 286,401,757. Loosely applying the rules of supply and demand, we can rest assured that with our current immigration patterns as well as our population growth, there will be a continued need for housing over the next 50 years. You can safely assume a 4% appreciation level. Of course, some years will better than others depending upon supply and demand and the escalation of costs and the increased costs of construction and land/infrastructures. As long as governments keep up major increases in impact fees for developers, your real estate investments will continue to appreciate.

The average single family home sold for $23,400 in 1970; in 2000, a similar average home sold for $169,000. That is an approximate 8% annual increase. Of course, appreciation will vary with the location and condition of the property as well as the condition of the local economy.

3. Equity build-up: You reduce your mortgage and increase your equity with every mortgage payment made on underlying debt. A portion of your payment goes toward reducing the principal. The shorter the loan period, the faster the equity builds.

4. Tax savings: Uncle Sam allows everyone but dealers in real estate to depreciate their investment properties on schedule E when filing annual tax returns. Residential properties depreciate over 27.5 years and commercial over 39 years.

You probably like all of these opportunities to make money. Bear in mind, though, that the government needs to pay its bills and they get their share when you sell one of your investments. When you sell a property, you will be faced with a 20% capital gains tax on the increase in value of the property and the recapture of the depreciation. This cost could be deferred if you complete a 1031 tax deferred exchange to trade up from property to property.

Think through the following example: With $500,000 you can buy a $1,500,000 investment that may give you an 8% cash flow, an annual 4% appreciation, an annual equity build and a depreciation of $43,000 a year *(1,500,000 X .8 = 1,200,000 (minus the land value); 1,200,000/27.5 = 43,000)*. This comes in at over a 20% annual return and should make you feel like you have made the right investment decision.

Regardless the size of real estate investment, you can make a return and build up your retirement. It is important to not buy the first investment that comes along; rather you should buy the best investment. Pick an investment that you are the most comfortable with, maybe your grandmother's duplex. This will give you a chance to make some small mistakes and plan a long-term future investing in real estate. Choose a real estate agent that has some of his or her own investments to help you and a property management company with good references.

(Note: Not all real estate investments have a fairy tale ending. It takes time, experience and a good eye for location and detail to achieve these kinds of results. On the other hand they are achievable results.)

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