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FREE CHAPTER

7 STEPS TO WEALTH

8TH EDITION

THE **VITAL** DIFFERENCE BETWEEN PROPERTY & REAL ESTATE

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CONTENTS

PREFACE

This is not just a book about how to build wealth by investing in real estate. It's a book about how *you* can build wealth by investing in real estate.

There's a big difference. The words 'property investment' probably conjure up visions of serious guys in serious suits talking about things like 'negative gearing', 'leverage' and 'equity positions'. And for most people, that's a major turnoff. Perhaps that's why property investment is one of the best-kept secrets of the financial world.

I'm going to let you in on a few well-kept secrets in this book—and I'm going to try and do it in easy-speak language so that anyone can pick it up and read it. I figure, if Stephen Hawking can write a popular book based on Einstein's theory of relativity, then somebody ought to be able to do the same for real estate investment! I'd like to give you something you can relate to and, more importantly, use without constantly tripping over a load of jargon and statistics.

The books on wealth creation that are full of jargon and statistics (and there are a few of them about) are often written by academics who may have gathered a wealth of theoretical knowledge, but haven't actually—personally—created any wealth. I'd have to say, I'm pretty much the opposite.

However, Einstein himself said, 'Everything should be made as simple as possible, but not any simpler'. Good rule. So you will find numbers, charts and technical terms in this book, but they are there to clarify key concepts—not to prove that I can use statistics and big words. We'll also cover a fair bit of information, but this isn't one of those 'everything you never particularly wanted to know about economics' books. I'm simply going to tell you about the most effective way I know to build wealth.

By the time you finish reading this book, you will have a pretty clear idea of how to maximise your assets, reduce your tax bill, ask the right questions and see through some of the so-called experts in the field. And, perhaps most importantly, you'll know that you can build wealth.

The principles set out in this book aren't new. I've been using them for myself, and for clients, for many years—and they work. They've given us financial freedom, security and a great lifestyle for ourselves and our families. And that's just one part of what building wealth is about. For me, it's also about the potential to make a difference in the world: an opportunity to be all I can be. I think of it as a journey to discover purpose. Welcome to the adventure.

CHAPTER 1

Why build wealth?

Do you want to be wealthy?

Silly question, right? *Everybody* wants to be wealthy. Well, as a matter of fact, when we polled thousands of Australians 98 per cent said they absolutely didn't want to be wealthy but they did want to be comfortable. When we asked what that meant in dollar terms, most said they'd never thought about it. In fact, a July 2017 survey by Australian Unity and Imperica found that 77 per cent of all 45 to 64 year olds had not begun formal planning for their retirement.

Imagine what 'comfortable' should be: the security and the freedom. Imagine retiring with enough money to do all the things you've wanted to do, for as many years as you've got—and not having to rely on the government for a cent!

Let's look at it another way.

How much do you reckon you'd need—per annum—to live comfortably in retirement? I'm not asking you to do budgets and calculations and adjustments for inflation (although at some stage, if you're talking to an investment advisor, it would be a good idea). I'm just talking ballpark figures: what amount per year would you want to retire on, in today's dollars? Most of the people I talk to would say more than $70 000 per annum (even though the median wage in 2018 is closer to $80 000 per annum).

Your own estimate: $ _____________ .

That estimate may be perfectly realistic for your own financial circumstances: you'd have to do a few calculations to find out.

You may be surprised to know that figure 1.1 shows what Australians actually *do* retire on.

Nearly all of us want to be wealthy—and nearly all of us retire below the poverty line! What's going on?

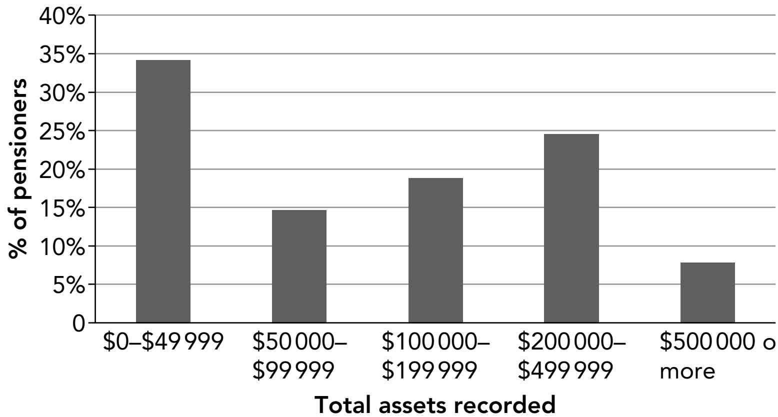

Figure 1.1: total savings and assets that Australians retire on

Source: Department of Social Services Demographics—June 2017 Release https://data.gov.au/dataset/dss-payment-demographic-data/resource/0457422b-f338-4dd8-82b7-35a5d97f798d

Nearly all of us want to be wealthy—and nearly all of us retire below the poverty line! What's going on?

In order to retire on $70 000 per annum, you actually need around $1.5 million in assets *and* to own your own home.

And that's in today's dollars. In 20 years' time, with inflation at 3 per cent, the equivalent sum would be $150 000 per year, requiring $3 million in assets.

How many of us have a plan in place to build up those kinds of assets by the time we retire? Apparently, only one in 100 of us! As you can see from figure 1.1, more than 99 per cent will retire on less than one-third of what we need to be self-sufficient in retirement! If you are part of the other 1 per cent, please accept my congratulations—best wishes, and feel free to stop reading (although there may be a few things in this book that will surprise even you). If you are *not* one of those, it's *your* responsibility to change this for yourself! (Think about it. Who do you want to be financially dependent on when you retire? The government? Your kids? Read on …)

Why aren't more Australians wealthy?

There are a number of answers to this question, as you'll see below. (I haven't included 'waiting to win the lottery'—although, with $75 billion 'invested' in gambling in Australia each year, you'd think we were pretty serious about this as a retirement plan!)

'We don't have enough money to build wealth'

Wrong. The structure I'll show you in this book allows you—even encourages you—to start small. You only need a combined annual gross income of $100 000 and a small amount of cash, or equity in your own home or other property, to get started. Wealth is accessible to most Australians. Mostly, it's about using the resources you have and restructuring your cash flow. And all that takes is (a) knowing how and (b) choosing to give it a go.

'Our parents never taught us to build wealth'

Most people my age were taught that we would grow up, get a trade or a university degree and then get a job: we'd save up enough money for a deposit on a house, and we'd use our work income to pay off the loan on that house over 25 years—and *then* maybe we could consider another investment. Sound familiar? Well, that's exactly what most Australians do.

I call this 'income thinking'. We need to replace it with 'capital thinking'.

'There's always a safety net'

I think this is part of the same concept. Our grandparents seemed to live fairly happily on the pension in the post-war years, and in the 1950s and 1960s, Australia enjoyed a relatively high standard of living compared to other nations. Of course, that was when there were about 18 taxpayers for every pensioner. Today, there are fewer than five taxpayers per pensioner, and if demographic trends continue, within 20 years there will be fewer than one taxpayer per pensioner. Meanwhile, because we're living longer, the average Australian will have to fund at least 20 years of retirement.

It won't be long before the government simply won't be able to afford the age pension—even at its current meagre levels. By 2020, welfare will cost Australia more than $190 billion per annum, up from $160 billion in 2017. That is staggering, and I'm sorry to say that unless you have a credible strategy, you are part of the problem. The government is fully aware of this—that's why in 2017 it stripped 320 000 Australians of some of their pension payments ($9000 per annum for singles and $15 000 per annum for couples). So we might like to think about making our own arrangements.

'We don't like debt'

This is something else our parents taught us. There are some sound values behind this view—self-reliance; pay your own way—and it's true that escalating debt is a concern. But we need to distinguish between debt on consumer items that depreciate in value (like a car, a dining suite or a stereo system) and borrowing on an asset that *appreciates in value* and *generates income* (like property). The latter kind of debt:

- supports the borrower's ability to make the necessary repayments
- offers a profit on sale of the asset.

On the other hand, you could buy a new BMW Cabriolet (say) for \$100 000, and by the time you drive it out of the showroom, it's only worth \$85 000. If you borrowed \$100 000 on it, you're already facing a deficit of \$15 000, which you have to pay off. Each year, more of the same: you could end up making payments of \$12 000 for four years and still face a balloon payment of about \$70 000 (which may, or may not, equal the capital value of the car by that time). Now, *that's* debt.

Ironically, people routinely run up thousands of dollars in 'small' debts on consumer items but baulk at taking on a mortgage.

Let's get debt into perspective. You can't build wealth without acquiring substantial assets for capital growth—and you can't, realistically, do that without borrowing the money to invest—that is, without *gearing*.

'It's an income world'

What does 'being wealthy' mean to you? Some people might say 'a big salary, with a lifestyle to match'. But that's not how wealth works. Income by itself doesn't make you wealthy. You spend some. You save some (maybe), and inflation gradually wears its value away. Capital, on the other hand, is material wealth that can be used to produce more wealth by investment. Capital grows, income flows (mostly, through your fingers).

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Unfortunately, most people don't get past income: they don't get their money growing and working for them. The system is there, but only capital-focused people use it to build wealth.

You can't *save* your way to wealth.

You can't *save* your way to wealth.

'Wealth-building is strictly for whizz-kids'

Some investment advisors would like you to think so. But the good news is that property investment need not be the sole preserve of financial experts. By the end of this book, you'll know enough about 'leveraging' and 'negative gearing' to get by. You'll have a simple investment structure and clear principles to work with. And if the whole business seems like too much of a hassle, remember: you don't have to do it all yourself! You can get advice and help with everything from working out an initial budget to managing a whole portfolio of investment properties.

Custodian is just one example of an organisation that offers a whole range of services in the property investment field, or you could get advice from other sources. Look behind the veil. Try to find someone who has actually done what they are advising you to do! There's only truth in numbers: ask the person who is advising you to give you a copy of their land tax bill for the past 10 years. You want to follow somebody who pays a lot of land tax because clearly they own a lot of real estate. This goes for accountants, financial advisers and real estate agents. There are some good ones who have built wealth—and that's the first credential I'd look for.

'Wealth-building is strictly for sharks'

It's easy to get that impression—and not everybody relates to the idea that 'greed is good' the way we seemed to when Michael Douglas said it in the movie *Wall Street* in the early 1980s.

Sharing in the custodianship of our society's future is one way of being all you can be.

I think we need to challenge the way we think about what wealth is for. Sure, it's about quality of lifestyle, providing for family, a financially secure retirement, control over your future and all that good stuff. But it is also about *responsibility*.

As I outlined in my personal story, the Custodian philosophy is that the few of us who are fortunate and informed enough to build wealth can—and must—choose to use it responsibly. Wealth puts us in a position to help those in trouble and need, and to shape the kind of fair and hopeful society we would want our children to inherit. It's also our responsibility to educate the next generation to manage and preserve capital for our nation's financial and social wellbeing.

Custodian believes that this is what true investment in the future means—and we find that it yields the most valuable and satisfying returns. We encourage all fellow wealth-builders to adopt this philosophy. This book is about what's possible in all sorts of ways. Sharing in the custodianship of our society's future is one way of being all you can be.

What's the solution?

At the risk of sounding like a sportswear advertisement, the solution is quite simple:

Just think differently: capital, not income

When we talk about 'wealth-building', we are talking about:

- establishing a *structure*, or system, to manage your *cash flow*
- acquiring *assets* (in this case, residential real estate)
- creating *capital growth*—that is, increasing the value of your investment over time.

Your investment may, of course, also offer you income and tax advantages. But it's the capital growth that counts. It's the capital growth—combined with compound growth—that makes millionaires.

And as it happens, most millionaires achieve capital growth by investing in real estate. This book will take you step by step through how it all works and what you have to do.

I'm essentially going to teach you how to turn $100 000, which could be the equity you've already built in your own home, into $2 million and be cash flow positive. On top of all that, you'll get a tax deduction. I hear you: it's too good to be true, or if it is true, why isn't everyone doing it? Yes, I hear that a lot. People who have been following me for 20 years say they wish they had started 10 years earlier and also ask why all Australians aren't doing it—and that's what stumps me as well.

> *Cash flow positive* is where you have income exceeding all costs of holding an asset.

We hope you enjoyed this sample from

7 Steps to Wealth

by John L. Fitzgerald

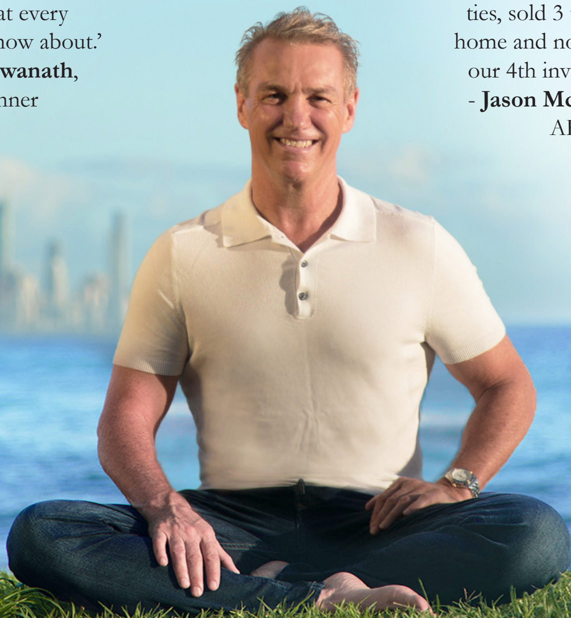
'I congratulate John on his compelling insights into how to make real estate work for you.'
- **Maha Sinnathamby**, Top 100 BRW Billionaire

'John is not just an author; he has been in property for 35 years and built his own fortnue. Every Australian must read this book.'
- **Bob Ell**, Top 100 BRW Billionaire

'This is the best book for property investors. John's book should be taught in every single high school.'
- **Nev Pask**, Top 100 BRW Billionaire

'John Presents an honest, time-tested strategy to wealth accumulation that every Australian should know about.'
- **Michael Baragwanath**, Financial Planner

'I followed 7 Steps since 1998. My wife and I acquired 6 properties, sold 3 to fund our family home and now we've purchased our 4th investment property.'
- **Jason McCartney**, Former AFL Player



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