

This is the prime reason so many investors have been able to start from scratch and build a fortune; also the reason they have been able to go on from there to build even larger fortunes.

Better yet, despite the interest you pay on the money you borrow, you actually increase the rate of return. (The next page shows how it pays off in dollars-and-cents.)

HOW LEVERAGE INCREASES YIELD AND PROFITS

It pays to borrow money on investment real estate property. That's because any income property really worth buying gives you a bigger yield (on a cash basis) than the interest you must pay on a mortgage. In effect you're earning money on other people's money. That, in a nutshell is "leverage."

Example: You buy an office building for \$125,000 cash; \$25,000 for the land, \$100,000 for the building. Its net income is \$10,000 a year—a return of 8%.

Using leverage.—You buy the office building with \$25,000 downpayment and a mortgage for \$100,000 at 6% interest. The mortgage interest is \$6,000 a year which reduces your net income to \$4,000. But since you have only \$25,000 cash invested, your yield has increased to a booming 16%.

That's how a good deal becomes a lot better. And of course, when you put up only \$25,000, you have \$100,000 that you can use to pick up other top real estate deals.

Using all-out leverage.—Let's assume that you can pick up four more buildings with the same cost and yield. We'll also assume that you can get the same kind of mortgage on each building. *New result:* Now your net return—after interest payments—is \$20,000 on a \$125,000 cash investment.

Now let's go back to the one building and see what happens if the property increases in value and you decide to sell it.

How it works.—Suppose in 10 years the same property doubles in value to \$250,000. If you've put all cash into it, you have doubled your money. But if you've only put in \$25,000 you can come away with \$150,000 (\$250,000 less the \$100,000 mortgage). That's six times your cash investment.

Now let's see what the story would be if you owned the five buildings.

Idea in action.—You sell the five buildings for \$250,000 each. After paying off the mortgages, you come out with \$750,000 cash on your \$125,000 cash investment.

That's what leverage can do for you and that—in brief—is what leverage is all about. It's simply a technique of using somebody else's money to send your net profits soaring. The examples also graphically show why astute real estate investors use borrowed money instead of laying out their own cash.

While leverage is an effective technique for investors, there is a darker side. In a falling market, it works against the investor, reducing the rate of return and increasing the percentage of loss. However, over the long run, real estate values generally go up, and even over the short run—in normal times—the trend in values is up rather than down. So if you've chosen your property wisely following the guidelines we've set throughout this Report, you can use the leverage principles to start you on the road to fortune.

HOW LEVERAGE PRODUCES TAX-FREE REAL ESTATE INCOME

The tax law gives you a big break when you borrow money to buy property for investment or for the production of income. In addition to a deduction for interest, you get the same depreciation allowance, whether you pay all cash or part cash-part mortgage, or no cash-all mortgage.

If you are the first user of a new building, you can take accelerated depreciation and your depreciation allowance may be high enough to more than meet the annual principal payments on the mortgage. In other words, you get a chance to build up your equity in the property with tax-free funds. Watch this: You can't depreciate the cost of land.

Example.—You buy a new office building; you'll write it off over a 40-year period, using the 200%-declining-balance method of depreciation. *Cost:* \$125,000—\$25,000 for land, \$100,000 for the building. *Net rental income before taxes:* \$10,000 a year.