

A Landlord Seeks a Solid Foundation

This cash-poor investor needs to diversify.

By Jeffrey R. Kosnett

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Chicagoan Yan Searcy exudes entrepreneurial zeal. Yan, who is 37 and single, has invested in a carwash and aspires to own an ice-cream franchise on the city's South Side, where he resides. In 1998, Yan bought a three-flat apartment building, which he still owns. After buying and selling other nearby properties, he acquired a two-unit condo a year ago. Despite living in one of the five units he owns, he breaks even on cash flow. "I'm trying to own the whole block," quips Yan, who estimates that the real estate is worth \$850,000, or \$300,000 more than he owes on the mortgages.



Yan Searcy

Although real estate is his passion, Yan has no thoughts of giving up his day job. He's a professor of social work at Chicago State University, which provides a 403(b) retirement plan, a pension and other benefits. Yan has about \$40,000 in a few stocks and mutual funds, held mostly in retirement accounts.

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Two problems

With little debt except the mortgages, which have favorable fixed rates, Yan's finances should

improve as long as he maintains the properties and keeps the units occupied. But he has two major problems. First, he knows he needs a sizable cash reserve, which he lacks. "In two years or less, I'd like to have \$100,000," he says. Second, with the overwhelming majority of his assets in real estate, Yan's portfolio is extremely unbalanced.

Real estate investors need liquidity. Vacancies, repair bills and unexpectedly high tax assessments can strike without warning. Yan has enough in the bank to cover a couple of months of personal expenses. But if he needed, say, \$20,000 on short notice, he would have to borrow against the properties, get another kind of loan or sell his stake in the carwash.

One option is to refinance the mortgages, take out cash and hold the money in safe investments, such as bank accounts or short-term bonds. Dave DeWolf, a Los Angeles adviser to real estate investors, figures that Yan could refinance for as much as 80% of his properties' value, or \$680,000. But then Yan would need to raise the rents to cover his higher mortgage payments. The risk is that tenants would balk and move.

Jorie Johnson, a real estate adviser and financial planner in Manasquan, N.J., agrees that Yan should hold more cash. But she advises him to save as much as he can from his salary, despite the many years it will take to reach his \$100,000 goal. Meanwhile, she says, Yan can establish an equity line of credit at a bank to cover unexpected operating expenses.

With about 85% of his net worth standing on one street, Yan's investments need to be more diversified. The carwash, from which Yan receives a modest amount of income, is a start, albeit an untraditional one. So are his funds and stocks. DeWolf observes that over periods of 10 to 20 years, most amateurs earn less by holding real estate directly than by investing in the stock market. So Yan should continue his program of channeling \$550 a month into his 403(b) and into funds outside of the retirement account. That money should go into a diversified mix of stock funds, which should go a long way toward creating a more balanced investment program.

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