Investments:

For Growth Potential, Look for Growing Markets Part 1 of 2

When advising clients, or while shopping for my own account, I look for investment properties with good growth potential. Rising property values come from rising income – which in turn comes from higher demand. Even if I'm more concerned with current income on my properties – that rising demand can help my rents stay high. How can I focus on properties with good appreciation potential? I look in areas with good population growth. In this month's first part of a 2-part series, I'll discuss the growth that we are looking for, and explore a few different geographic areas.

While researching this article, I found that historical population data is hard to come by. Fortunately, I have population research spreadsheets from articles I have written over the last 10 years and, by combining new data with what I have already collected, we can take a look at longer term trends.

According to the US Census Bureau, a new American is born every 8 seconds, while one dies every 11 seconds, and a new international migrant arrives every 29 seconds. The combined effect of these 3 influences yields us a net gain of one person every 12 seconds, or over 2.5 million per year. This means that we are building the equivalent of the San Antonio, TX region every year to give these people places to live work and shop. These new residents are not all spreading all over the country equally – where are they going? To answer this question, we need to look at the growth of individual areas – called Metropolitan Statistical Areas, or MSAs.

Where are more people moving? What areas of the country are growing faster than the U.S. population as a whole? Let's look at a few states, and examine their fastest-growing MSAs:

California – Still the Golden State?

California is continuing to grow, but that growth is slowing. Those of us who have lived in the state for a few decades, (Southern California, in my case), have seen the explosive growth that the region expe-

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rienced – the Los Angeles suburbs in the 1950s and 1960s and Orange County during the last 30 years. Many of us believe, however, that we have seen all the explosive growth that we are going to get. How would it be possible to add 30% to the population over the next 20 years? Where will they all live? The Los Angeles-Long Beach-Santa Ana MSA added 944,000 residents between 2000 and 2016: a 7.6% increase. That may look like a large number, but remember: this is a large area we're talking about. This MSA goes from Malibu in the west to Gorman in the northwest, (on I-5 North: almost out of the Grapevine if you're heading north), to the town of Hi Vista (east of Lancaster), south all the way down to the Orange County line with the Camp Pendleton Marine Base. That is a large area to put all those new residents, and it illustrates why I prefer to focus on % increases.

The San Francisco-Oakland-Fremont MSA added 555,000 residents between 2000 and 2016; a 13.47% increase. I was expecting to see a higher number here, with all the press that the "second tech boom" is getting. (We all need to remember how that first one ended.) These growth numbers may seem healthy at first; but not after we look at competing MSAs in other states.

Aside from slowing population growth, the largest factor that's steering my investors away from California is price. If you've shopped investment properties in California recently, you see what I mean. Extra low CAP Rates equaling extra high prices which lead to lower returns. Fortunately, there can be "greener pastures' out of state.

Texas

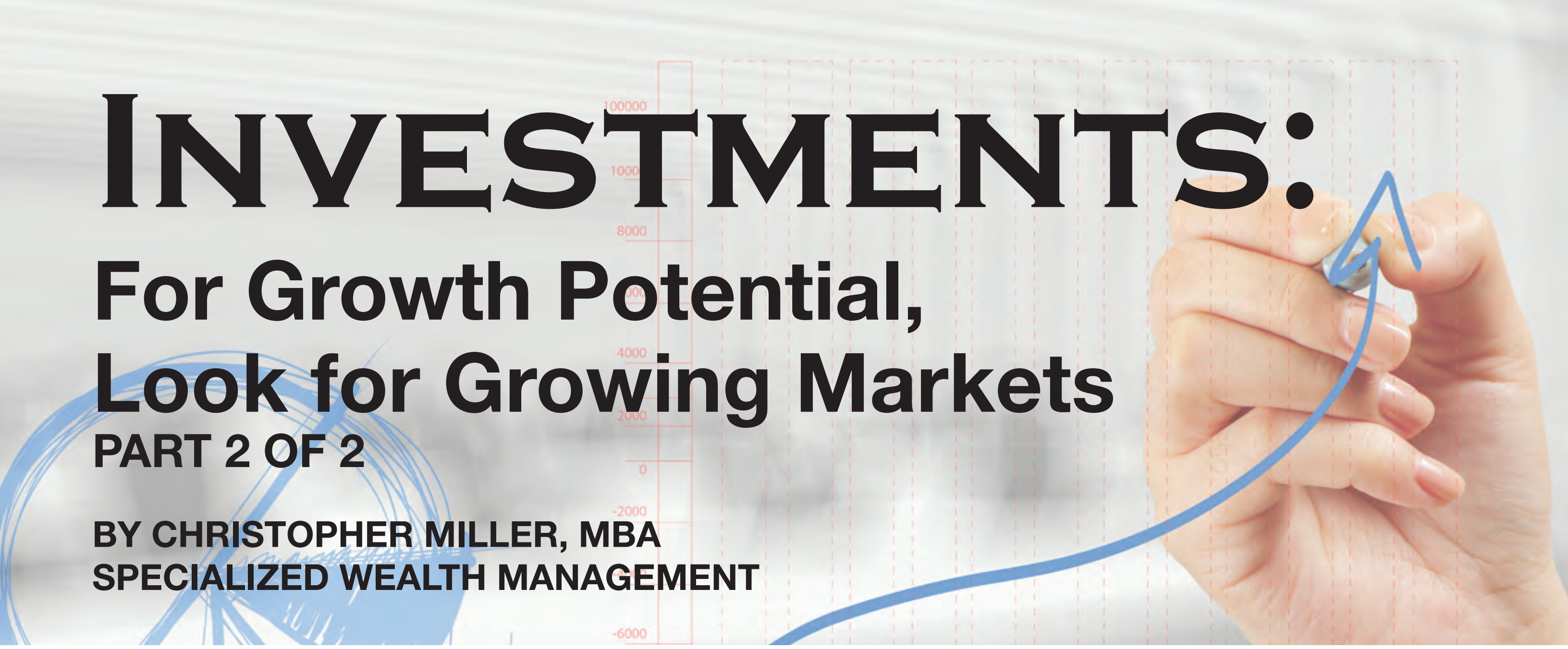
Many of us are familiar with the Texas story: companies are fleeing high regulation and taxes in other states for the lower property, wage and tax costs of Texas. (Recall the 3 automakers that fled the Torrance, CA area in the last decade for the Lone Star State.) As a bonus, Texas charges no state income tax – so an employee can keep the same California salary, buy much more house, and pay no state taxes after he moves to Texas. His employer has just raised his standard of living and given him a 9.3% (the most common California state income tax bracket) raise.

The population growth numbers are truly astounding: between 2000 and 2016, population in the Dallas-Fort Worth-Arlington MSA rose 40%, while Houston is up 43% and San Antonio grew by 42%. I've been talking about the growth in Texas for almost 20 years, and these numbers even shocked me.

Georgia

Along with Texas, the Atlanta suburbs have also been a favorite of mine for at least the last 10 years. Atlanta grew 9.5% between 2010 and 2016 for a total of 36% growth since 2000. The smaller city of Savannah deserves some consideration, too – it's MSA's 31% population growth since 2000 means an addition of over 100,000 residents.

Sometimes I'll develop a concept for an article and my research will yield so much material that it becomes a two part series. That certainly has become the case this month. I prefer to buy properties in growing metropolitan areas so that population growth can drive demand for my apartments or for the stores that lease space. Since owning rental property that is an hours-long plane ride away can be problematic, I find that partial interest properties are appealing investments when buying out of state. We'll discuss this in more depth, along with a few more of my favorite MSAs, next month.



INVESTMENTS:

For Growth Potential, Look for Growing Markets

PART 2 OF 2

BY CHRISTOPHER MILLER, MBA
SPECIALIZED WEALTH MANAGEMENT

This month's article is the sequel to my composition from February. We'll continue our discussion of why I believe growing markets can help encourage growing rents, growing occupancy, and therefore growing value.

DEMOGRAPHIC TRENDS - WHAT ARE WE LOOKING FOR?

Between 1940 and 1950, the US metropolitan population (Those living in metropolitan statistical areas) passed the non-metropolitan one. (Before 1940, more people lived "in the country" than in the city.) By 2010, the non-metropolitan population was 19% of the entire country – and had only grown 0.7% since 2000. This migration effect made things easier on us real estate investors: populations concentrated around cities, (metropolitan statistical areas), giving us more potential properties to buy around larger population groups. While this rural to suburban movement isn't as pronounced today, this gives us an idea of the type of population movement we are looking for: Those folks who left their farms during WWII for jobs in the city on the east and west coasts didn't ever move back. We are looking for signs of permanent population movements – where is everyone going? What areas of the country are growing faster than the U.S. population as a whole?

WHAT WE ARE NOT LOOKING FOR

What we are not looking for are population shifts that could be temporary. North Dakota is an excellent example of such a shift that I would rather avoid. You may recall seeing petroleum production from North Dakota's Bakken Formation in the news quite a bit ten years ago. Back in 2006, interest in this formation increased significantly, and the state's population surged as workers flooded in to the state, and as daily oil production surged from about 175,000 barrels per day to over 1.2 million barrels daily. [1]

1 "Bakken Region – Drilling Productivity Report," United States Energy Information Administration, February, 2018.

This surge, however, slowed significantly as commodity prices for oil and natural gas dropped. Production plateaued at that 1.2 million BBLs level before declining 15%. Production has since recovered, but the outlook for oil demand has changed in the decade since this boom began. Will the United States be consuming still growing amounts of petroleum 20 years from now? As electric automobiles are becoming more feasible methods of transportation, many people are unsure. This doubt has caused investment, and therefore growth, to slow.

The North Dakota story highlights the danger of what I call "single industry booms." Las Vegas is a good example of this, too. "Sin City" is heavily dependent on revenue from the tourism industry; and rises in good economic times but contracts sharply during recessions. We saw this both before and after the September, 2001 terrorist attacks and the more recent "great recession."[2]

To avoid exposure to such single industry booms (and busts), I like to seek growing markets with diverse job markets.

2 "Strip Left Reeling: Picking Up the Pieces After the Great Recession," Jan Hogan, Las Vegas Review Journal. March 27, 2016.

GROWING MARKETS – FLORIDA

Florida is a state that, similar to Texas, is enjoying great growth due to warm weather, a business-friendly climate and a favorable tax environment boasting no state income taxes. Florida's diverse economy lists Tourism, Agriculture, Aerospace and Aviation, Healthcare and Financial Services as the state's top 6 industries.[3] This broad base can help to insulate against economic shocks to 1 or 2 industries.

DOESN'T FLORIDA HAVE HURRICANES? WHAT ABOUT THAT RISK?

Florida does have, as you may have seen in the news, hurricanes occasionally that can cause major property damage. The risks from natural disasters come in two forms: 1. Property damage – which can be mitigated with insurance that covers both damage and loss of income and 2.

3 https://www.investopedia.com/articles/investing/011316/floridas-economy-6-industries-driving-gdp-growth.asp . Accessed March 2, 2018.

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Local economic damage – let's say that the town is destroyed and nobody moves back. If this happened, the property would be rebuilt, but property value growth could be limited.

To address risk #2, we'll need to look at the surrounding areas. If a natural disaster caused major damage, would the area bounce back? Remember Hurricane Katrina's devastation in New Orleans, and note that the city has been in decline ever since. This decline was nothing new, however; the Crescent City was already in the middle of a long decline: According to the US Census, The Big Easy's population declined substantially during every decade since peaking in 1960, and was down 22% to 484,000 by the beginning of the 21st Century. After the Hurricane Katrina disaster, New Orleans' population dropped 29% - to 343,000 by 2010. The city's population is estimated to have since grown to close to 400,000 – but that is still 20% below pre-Katrina levels. The Big Easy declined after this disaster because it wasn't growing beforehand.

In contrast, if a large disaster were to wipe out part of a vibrant metropolitan area, development would likely flood into the affected area. Imagine what would happen if, for example, a great earthquake and fire wiped out a few square miles of the Los Angeles suburbs. Large tracts of developable land in the Los Angeles area? That's almost unheard of – local developers would be busy re-building in no time. This could lead to even higher property values in the future as new, master-planned, communities spring up around our hypothetical rebuilt property. Are the properties we are considering in thriving metropolitan areas, or in smaller "tertiary markets?" The answer to this can provide some clues as to how they will bounce back from disaster.

IS THERE AN EASIER WAY TO INVEST OUT OF STATE?

Owning investment property can be tough when it is several hours of traveling away. When investing your real estate dollars out of state, partial interest properties could be an excellent alternative. For my out of state investments, I prefer to buy part of a larger property and let a professional management company run things. After all, my local properties take up enough of my time as it is.

This month's article was the conclusion of my two part "Growing Markets for Growth Potential" series. If you have any questions, please call my office at (877) 313-1868.

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What Is.. Your Investment Property's *Cash on Cash Return*?

Would you put your money in a bank account at a low interest rate? Probably not, but many investors are doing just that with their investment properties. Although property values have increased dramatically, income has not for many investors.

Try This- Calculate your Cash on Cash return.

Yearly Income - _______(subtract) Expenses ______(subtract) loan payments _______

= Annual Cash Flow ______________

Now, estimate your property's value___________ (subtract) Loan Balance__________

= Your Equity Value ______________

Now, divide your Annual Cash Flow by your equity value, and you get your

Cash on Cash Return % _____________ .

Want to increase your properties' income potential? Call Chris Miller at **877-313-1868** today!