



Episode 917: The Truth About the Real Estate Market, and What Regular People Should Do

Guest: Hunter Thompson

WOODS: Let's start with a question about where the real estate market is right now. Compare it to where it was in 2005 and where it was in 2008 as two guideposts, let's say.

THOMPSON: Yeah, that's a really good question. So looking at it from that perspective, I would say that there's a couple different metrics that we want to look at when determining this. And interest rates are definitely one of them. Interest rates are historically quite low. Occupancy rates are historically quite high. And the cycle – that's really what this is all about. The cycle is, it's hard to make the argument that we're not in the eighth or ninth inning of this entire thing.

So since we're all proponents of the business cycle here, everything is cyclical, so it's important to talk about the market cycle itself. So the current expansion, which is the length of time between the trough, which is the bottom, and the peak of the cycle, which is the high, that current expansion started in June of 2009, which means it's currently in its 96th month since the trough. So since 1857, there has been only two cases when the expansion has lasted longer than 96 months. Again, that's twice out of 33 market cycles since 1857, and that's just how far the data goes back that's available. Something else to consider is that, since World War II, the average expansion has been 58.4 months. So as of right now, this current expansion that we're currently experiencing is more than double the average expansion period in that time frame.

So that's where we are in relation to the market cycle, and this is why so many people are concerned about the upcoming correction. In fact, I was at a Mises event in San Diego that you actually hosted, which was called "How to Be Free In An Unfree World." And I noticed that all of the questions, so many of the questions were really coming from a place of fear in the audience. And I understand why. People are concerned about the recession. But this is exactly the question that made me really motivated to get out and share this information with libertarians, because you don't have to fear the recession. The recession is coming; the government's going to print money; the debt bomb will eventually go off, etc., etc. But asking questions like, What percentage of my portfolio should be in gold?, What percentage of my portfolio should be in cash, and just hoarding those two items, I think those are the wrong questions to ask, and I think the really important question to ask is, Knowing this information, knowing this, how can I benefit from this financially? And that's really what set me on

this path and why I'm super excited to talk about it today with your audience especially.

WOODS: I know that you tend to focus on commercial real estate, but I still want to ask you about a strategy that I've heard, for example, from John [00:04:34], whose argument is that you can build up passive income streams for yourself by buying properties, residential properties today, renting them out, using the rental payments to pay off the mortgage, and then at the end of the term of the mortgage when you own the properties free and clear, now the payments coming to you are just pure profit and that that's the way to go. Now, then the question becomes where to buy and what are the best places to buy, and you have to weigh a lot of factors, but that that's the overall strategy. Is there anything wrong with that?

THOMPSON: Well, no, I wouldn't say there's anything wrong with that at all. I think the key is to actually identify your financial goals and then build your strategy around those goals. So if you talk to people and you really get them down to explain exactly what they're trying to accomplish financially, usually what they'll say, if you help them through it, it's that they want their passive income to be higher than their monthly expenses. If that's the case, they're basically financially free. And this is basically what you get a lot of the times. The problem is almost no one actually sets up their portfolio or their lifestyle to perform this way. So you look at stocks, for example. The average dividend for blue chip stocks is about 2%. So that doesn't even beat the government data, which is about 2.2% or so, if you trust the government data. So for me, real estate is the most effective, fastest way to achieve that goal, because it generates passive cashflow.

And to answer your question directly, that is definitely one strategy, and the timing of that typically works out in people's favor. Like let's say that you're 30 or you're 40. You buy a couple houses with a loan, and they have a 30-year mortgage. By the time the mortgage is paid off, you're at the age where you're not really trying to take on risk anymore, and therefore you're not refinancing, leveraging up, trying to increase that ROI. But to me, leverage is an incredibly important piece of why real estate is so desirable, because you get access to inexpensive loans. So if you think interest rates are staying low, you can take advantage of this as a libertarian, as an investor to generate lucrative cashflow for yourself.

WOODS: Is there a time when people should stay out of real estate, or are there times when they should get in? Are there indicators that tell them which is which? Or should they always be in?

THOMPSON: Yeah, that's an interesting question. So as market cycles change, as the price changes for these different asset classes, it's important to adjust your strategy. And of course this is my personal opinion; this is not anything that anyone should just go and implement, but you want to go and talk to your own financial advisor, etc., etc. But for my personal strategy, I was able to find lucrative investments in typical real estate opportunities — in multifamily, retail, etc. — until about 2013 or so. And it became challenging for me to get the type of returns that I looked for until that period.

And this is when I started becoming more concerned with the recession, because I understood the reason prices were high – they have somewhere to correct now – and I started focusing on what I consider recession-resistant assets. And that is something that I think is really important to consider, especially late in the economic cycle. So these are investment vehicles where the demand for the product increases during recessions. And the most notable examples of this are mobile home parks and self-storage facilities.

So the first one is kind of obvious from a big-picture perspective. When recessions happen, people lose high-paying jobs. If they're lucky enough to get rehired, they usually are hired into lower paying jobs, so you have this massive shift downward in income, which increases the demand for affordable housing. But you also have demographic issues perpetuating this further. So there's 10,000 baby boomers retiring every single day. When I say "retiring," I mean they're turning 65, because many of them have zero savings and they're relying on social security. The problem is the average social security check is about \$1,300 a month, but the average two-bedroom apartment rents for like \$1,200 a month. So it's mathematically impossible for you to implement that strategy, yet we have hundreds of thousands of people that are doing it every single year.

And you compound this with the fact that it's pretty much impossible to build new mobile home parks. Cities just simply don't give the permits for their construction. And the reason that they all exist, basically, just so you know, is this was built as part of a veterans' housing program in the '60s and '70s. So since then pretty much, every single year the number of mobile home parks has actually decreased due to the negative connotation that takes place.

So you've got this unbelievable situation from an investor's perspective. There's all this increasing demand, pent-up demand for affordable housing and literally a decrease in supply. So to answer your question directly, it is a great time to look at those type of asset classes and cycle out with the more traditional asset classes like single-family houses or even apartments.

WOODS: Now, why would somebody want to focus on commercial rather than residential real estate? Didn't we, by the way, hear for a long time that there was going to be a glut of commercial real estate because we were seeing so many companies going out of business and there's all this retail space that's going to be available? Wouldn't that seem to be a depressed market?

THOMPSON: Yeah, no, that's an interesting point; it's a good point. One thing to consider is that this is an incredibly localized investment vehicle. So there are certain markets that are extremely high that I wouldn't touch at all under any circumstance, under any asset class. And then there are some markets that are completely undersupplied still in particular asset classes. So you have to be very cautious.

With retail in particular, there are some concerns about retail from a broad perspective. The Amazon threat is unbelievably serious, and you've got these big boxes closing left and right. JC Penny, Blockbuster, companies like this. No one is really stoked to be shopping at Sears these days, and you're not really happy if you're running

to Sears either. But there are certain markets in the right tenant base that you can actually – I'll give you a great example. From a recession-resistant component, grocer-anchored retail shopping centers, people need to eat during all stages of the economic cycle, and it's very challenging to do groceries online. People have been trying it for decades and the margins are just very, very thin. So we think that grocer-anchored shopping centers is a great way to do that just because of the lack of cyclicalness of that particular asset class.

WOODS: So then I guess what I want to know is, let's say we're talking to, as indeed we no doubt are, a lot of people who will be completely new to all this – this is a brand new world to them – and they don't want to lose their shirts. What would you recommend?

THOMPSON: Education, firstly. There is just no reason to rush it. And I think that this is kind of what I was mentioning at the beginning. There's always opportunities out there, but if you rush it, things are not going to go well, because these are long-term investments that are not liquid. You can't just buy in and buy out. So there's a couple of different companies out there. FIBI is a great one, For Investors By Investors, that has free educational content. I have a blog that I can send you as well, the *CashFlow Connections Real Estate Podcast*, which is free. And when you start to have conversations with people and start to learn, you realize that there's a ton of opportunities out there, but if anyone's trying to rush you into a real estate transaction, just stay away from them. That's been something that's helped me for quite some time.

WOODS: Okay, so there's that. Are there – well, let's see. What resources would you direct people to? Of course you have your own website and your own work that you do.

THOMPSON: Yeah, absolutely. I mean, there's a tremendous amount of books. I'd say *There's No Free Lunch In Real Estate* is a great book if you're looking for the math behind why commercial real estate makes sense. And that's why it makes sense to me. It's a numbers game. It's very easy to establish the value of a property because it's based on income. And this is why – you look at the cycles of real estate, you see that things go up and down similarly to stocks. It's not as volatile as stocks, but at the end of the day, you experience corrections. But if you're investing based on cashflow, then it's very easy to anticipate the value of the property, to hold if you have the correct tenant base, and just to hold with reasonable financing and just receive the benefits of passive cashflow directly to your bank account, essentially.

WOODS: Yeah, now, people hear "passive," and if you're like me, you start salivating because we all love that idea of passive income. But not all real estate investment can be characterized that way, right?

THOMPSON: Definitely, definitely. So there's two distinctions that are really important, and part of this is structural and part of this is from a personality perspective, what type of structure fits your personality. So when people think of active investments, these are investments where the investor is playing an active role in the day-to-day operations of the investment. So for example, if you buy a home, fix it up, rent it out, that would be an active investment. Even if you have a property

manager, this would be considered active for the purposes of this conversation, because you are actually interfacing with that property manager.

But I prefer what's called passive investments. In this conversation, it's referred to when there are — when there's a fund manager, this is when you buy into an LLC, passive shares in an LLC, and there's someone who's called a sponsor, who's usually hyper specialized in one asset class. So I let's say, for example, self-storage. All this company does is purchase self-storage. They know how to find the deals, they know how to rehab the property, they know how to sell the property for lucrative gains. And that's the sponsor, and they take a split of the proceeds for putting this deal together. When you're a passive investor, you invest into an LLC and take a percentage of the gains as well. But the key here is that if something goes wrong with the property — let's say termites infest the property — the property manager may call the sponsor, but the sponsor doesn't call the passive investor and say, Hey, we have a termite problem. They just never do. It's a silent partnership.

So to be honest with you, it sounds like an infomercial maybe, but all of the work should be front-loaded, meaning that all of your due diligence will be upfront. After you fund, you should just be simply reading quarterly reports if you want to, but literally cashing checks. And I know that sounds silly, but that's the way that these investments are structured to perform.

WOODS: So real estate, in other words, is an avenue people have for investing. They've got money; they'd rather not just keep it in the bank; they can do that. They can put their money in stocks; they can put it in gold and silver if they want; they can put it in bitcoin. There are all kinds of possible outlets for it. But each one of these has its ups and downs. What are the downs to real estate?

THOMPSON: Yeah, that's definitely a good question. So first of all, I'd say that 99% of all the horror stories you hear on real estate, especially those to do with loss of principal, they have something to do with people taking inappropriately aggressive leverage. And there's many different ways — I have a short eBook that kind of goes over this, but I'd say the main thing that people do is take too much leverage — meaning loan. The loan is too large compared to the value of the property. And then the loan term is too short for them to implement some kind of value-add strategy.

So self-storage. We haven't talked much about self-storage yet. Self-storage is a great recession-resistant asset class, because there's tremendous value-add strategies that you can implement, because it's a complicated business to run. So one of these strategies is U-Haul. When you purchase a property, you can get U-Haul to park trucks on your facility and rent out those trucks for a commission, essentially. So it takes a while to implement, though, but it can add hundreds of thousands of dollars to the property's value. If you purchase a property with a short loan term and you don't have the time to implement this value-add strategy and you have to refinance prior to the loan coming due, this can put you in an incredibly bad situation, which can result in foreclosure. So I'd say that the number one mistake that people make is taking too-aggressive loans, and that's the major risk with all of real estate.

So that's one of the main things we want to look out for, as well as investing in assets that are extremely speculative. If you're investing in development at the wrong time,

things can go really wrong. So this is why I focus on value-add, recession-resistant real estate with appropriate loans.

WOODS: What about an event like 2008? Is there any way you could have protected yourself against that or shielded yourself from the effects of that?

THOMPSON: The entire point is to protect yourself from those types of situations, and the way you do that has a lot to do with investing in the right asset classes where there's demand for the product when those situations take place. So I mentioned self-storage earlier. People need that product when they're going through some kind of transitional period, and a lot of those transitional periods can be brought on by recessions. So you think about people getting their house foreclosed, people having kids move home from college unexpectedly, losing jobs, foreclosures, etc. All of those things take place more frequently during recessions, and all of them make people more likely to use that product. So we have a ton of data to back this up. That's the theory, but the data backs it up very credibly, and both 2001 and 2008, the income produced by those self-storage facilities was either about equal or even increasing on a national basis.

So as long as you had an appropriate loan in place that wasn't coming due right in the middle of that crisis, you were just holding for cashflow and it was relatively stabilized. Some of the operators, some of the top operators in the world were even able to increase occupancy and raise rents during that time period. So that's the way that I try to mitigate that problem, is by focusing on those types of assets.

WOODS: You must in your dealings, though, nevertheless run into people who are caught up in more traditional kinds of real estate, and I'm just curious about how – they must have been shell-shocked in 2008, what the reaction was from people.

THOMPSON: Yeah. I actually live in California, which was one of the hardest-hit markets in the country, and so I was going to meetings and networking events, and first of all, they were very small at the time. A lot of people lost their shirt. But the people that were able to go through the cycle and keep their business above water were the people that were being conservative in their underwriting assumptions, not taking on too much risk, and implementing a strategy which added significant value to the property. Because if you can add value to the property relatively quickly, then in the event of a correction, especially in the capital markets, you're still able to keep the property up and running and keep the value high in the event that there's some kind of liquidity taking place, meaning a sale or a refinance. So that's what I have learned, learning from some of the great people that were able to weather the storm of California, which was no joke. I mean, it was insane. So that's pretty much my answer there.

I actually don't invest in California very frequently, or any of those other states. There's five states that were responsible for half of all of the foreclosures in the entire country, which is just unbelievable. Unsurprisingly, it's the states that the government was doing most of the loans in and the most amount of loans in. But there's plenty of markets out there that are in the middle of America, maybe not the sexiest places to go on vacation, but they're just slow and steady-type of markets. You know, Kansas

City, Memphis, Tennessee, etc., where the property values are based on income, which is much less volatile than speculative appreciation.

WOODS: Are there any regulations that people who are going to engage in this kind of investment need to be aware of and struggle with?

THOMPSON: Yeah, absolutely, and so I say that one of the benefits of both of those that I mentioned earlier, mobile home parks and self-storage facilities, both of them, it's the industry standard to work on 30-day leases. So you don't have to extend leases beyond the 30 days. This is particularly the case in self-storage. Unlike single-family houses and multifamily apartments, the laws in the court system are much more favorable for the owners of self-storage facilities compared to typical real estate. Laws – I mean, everyone's kind of seen the shows. The self-storage owners can literally lock, keep, and sell your possessions after just 30 days of failing to pay, sometimes even faster.

And then as far as the other side, the investment side, that distinction between passive and active is also really important. So if you are a passive investor – you don't have decision-making skills, you don't have decision-making control of the investment – then you are really limiting if not eliminating your liability and credit risk. It would be very, very uncommon or almost unheard of to be the receiving end of some litigation due to something going wrong with the property if you're a passive investor.

WOODS: All right, now a few minutes ago, I mentioned a few other things people might do with their money that are common, that a lot of people do with their money. A lot of people just leave it in the bank, don't do anything. Give me the pros and cons of these as compared to real estate, which is obviously your preferred outlet.

THOMPSON: Yes. So I would say that, first of all, cash, obviously you're getting really taxed by inflation. And I'm sure some of your listeners are probably familiar with ShadowStats.com. That's a company that kind of tries to estimate what their real, anticipated inflation rate is, and it's much higher than the government data. Government data is around 2% or so. So if you're in cash, yes, the risk is off, but the risk is definitely on for – you're actually losing value every single year. So if you're not going to use that cash to purchase cashflow, it doesn't help you achieve your goals, as far as I'm concerned in terms of that cashflow-being-greater-than-expenses model that I was discussing earlier.

WOODS: All right, what about gold and silver? Which, by the way, I have some gold and silver, but I do not now believe and never have believed that gold and silver is simply where it's at. Just get gold and silver and that – I think that's a ridiculous strategy. That makes no sense, and it's not going to – It's nice to have, but I don't think it's a wise – If you want to get rich or you want to be prosperous, I just don't think just basically treading water, which is usually what you wind up doing, is the best approach. But what are your thoughts about gold and silver?

THOMPSON: Yeah, so this is something that frequently comes up in libertarian circles, and I'm definitely sympathetic to it, because it's really acting as a hedge against inflation. So that makes sense. My concern, again, is that it isn't a vehicle which is going to directly help me achieve my financial goals. Now, part of my financial goal is

to sleep at night knowing I'm protected, and for a lot of people, that's what gold and silver does. But the main thing that I'm looking for is cashflow. Gold itself does not provide any cashflow. It's a 0% cashflow model. And the appreciation historically just hasn't been that successful, so over the last 100 years or so, the average is close to 4.25% on gold and it's about 2.91% on silver. So you're not having a lot of price appreciation and the cashflow is zero.

So something that I have thought to share with – again, this is just my personal opinion, but if you're really concerned that there's going to be a collapse in the dollar, then ask yourself how long you think entrepreneurs will be able to solve that problem in the United States. Despite the years of government regulation, there is still a spirit of entrepreneurship in this country. And so what I mean by that is, if there was a banking collapse and the dollar became useless, how long do you think it's going to take before that problem will be solved? I can't see it going much longer than three months. I mean, that would be unfathomable. So for me, if you wanted to have gold and silver, let's say that you keep three months of expenses in your possession in bullion, but other than that, I think you're being a little bit too cautious because it's not directly helping you achieve your goals.

Now, your goal may be very different than mine. You may be at a different period in your investment career than me and protection is all that you really care about. But I think that the combination of cash-flowing real estate and potentially cash-flowing businesses are directly going to help you achieve your goals, especially when you consider what I was talking about earlier with the recession-resistant component. I sleep like a baby, and that's really what I wanted to share with your listeners today.

WOODS: Yeah, yeah, yeah, exactly, exactly. And I'm sure they would all like to do the same and not be driving themselves crazy with worry and stress.

THOMPSON: Exactly.

WOODS: So tell me about your company and what it is you do.

THOMPSON: Yeah, sure, so I'm the founder of a company called CashFlow Connections, and I think that the key part about this whole conversation is a lot of this stuff makes a lot of sense from a big picture perspective. Like you can read a 30-minute eBook that'll explain kind of what I talked about today, but really the entire point is the execution of these strategies. And so what we do is we help link investors with sponsors that can execute these strategies and have been executing these strategies successfully over multiple different properties, and that's really what I think the key is. It's something that's really changed over the last few years, but that's what we do and that's how we do it.

WOODS: All right, so how do people find out about that?

THOMPSON: So you can go to my website at CashFlowConnections.com, and also there's a podcast that we host. That is *CashFlow Connections – Real Estate Podcast*. It is located in iTunes, SoundCloud, and Stitcher.

WOODS: Okay, so I'm going to link to those things at TomWoods.com/917. Now, am I allowed to mention another one of your associations, if I may put it that way?

THOMPSON: [laughing] Yes, definitely for your listeners.

WOODS: Do you know the one I'm driving at?

THOMPSON: Yes, I do. I have —

WOODS: Okay, so Hunter — Yeah, go ahead. Why don't you tell?

THOMPSON: Yeah, so I did do a podcast series that was really, the attempt was to take people who are just interested in libertarian all the way to full-blown anarchocapitalism, and that is on SoundCloud at AnarchoTopics. And I think a lot of listeners — it's going to be a lot of stuff that you guys have heard before, but I have a nice, ginger tone and some interesting concepts which I'd love to appreciate you guys to take a listen to.

WOODS: Okay, so it's funny; I just like hearing somebody like you who can speak so intelligently about a regular, mainstream topic, and then you can also talk about our crazy topics too [laughing]. It's really great.

THOMPSON: Right. It makes a lot of sense too, I think.

WOODS: I mean, usually it's just one or the other, that somebody does something professionally very well, doesn't even know about us, or all they do all day is think about anarchism. So anyway, it's great stuff. So I'm going to make sure and link to that at TomWoods.com/917. Definitely check out CashFlowConnections.com — did I get that right? I have a bad short-term memory.

THOMPSON: Yeah, that's correct.

WOODS: Okay, good. All right, thanks so much, Hunter. I appreciate the guidance here, and I hope people will follow up with you and get some more information.

THOMPSON: Awesome, I can't thank you enough, Tom. Thanks a lot.