The Art of Passive Income Podcast
With Mark Podolsky, AKA The Land Geek

Mark and Scott talk with Bob Fraser – AspenFunds.com

Transcript

Mark: Hey it's Mark Podolsky - The Land Geek with your favorite niche-y real estate website TheLandGeek.com and today's guest is a little bit different, very cool but different which I'm supper pumped about because I love learning about new models and new niches in order to build wealth.

However before we talk to our guest I'd be remiss if I didn't properly introduce my cohost you know him, you love him; Scott Todd from ScottTodd.net, LandModo.com. If you're not automating your Craigslist and your Facebook postings PostingsDomination.com/TheLandGeek, learn anything about anything InvestorNinjas.com. Scott Todd, how are you?

Scott: Mark, I'm great. How are you?

Mark: I'm great. Are you ready for this guest?

Scott: I can't wait. I want to learn something new.

Mark: I am too, I love learning something new. So out guest today is Bob Fraser from AspenFunds.us. If you're not familiar with Aspen Funds, Bob started it in 2012 to take advantage of unique opportunity in residential real estate notes.

So after experiencing the volatility of the stock market and seeing investors take large losses with portfolios Bob and his partner Jim were determined to design an investment fund that would provide excellent investor returns and without the volatility of intrusion invest in options. So Jim spent 30+ years career in real estate, in 2010 began looking into the mortgage note space and through all his experience real estate understood that financing was always the key. Scott Todd, does that sound familiar?

Scott: It does yeah.

Mark: And after all the ups and downs of real estate investing it was the banks that always seemed to survive and thrive. Bob Fraser, welcome to the podcast. How are you?

Bob: Awesome to be here with you.

Mark: So Bob let's just rewind the tape a bit and kind of give us your background and why of all the real estate niches you chose residential real estate mortgage-backed notes.

Bob: Sure. Well you know I'm really not a real estate guy. I was a tech guy, I am a computer scientist from Berkeley, was a programmer for many years, ended up starting a dot com back in the 90s, ended up raising $40 million in venture capital, and growing this thing to 300 employees. Then it blew up and I lost everything in the late 90s and really after that did a hedge fund. Started a hedge fund, really got kind of what I call a, you know, a finance degree, a street MBA you know. I say street MBAs they're better than regular MBAs but they're way more expensive and yeah. But again when the crash of 2008 happened I lost everything in this hedge fund.

So really at that point I became a real estate guy I'm like you know, I want something that is a little more predictable, a little more controllable than a fat investment in the stock market. Meanwhile my partner Jim is a real estate guy and he lost everything in the crash. So this is kind of our theme right, you know these massive cycles, economic cycles come and we want something that is far less dependent on the cycle or something that is countercyclical right and so we found it with note investing.

So we buy these notes and partly too I in terms of passive income bought a duplex and it was just such a horrible experience you know. For a computer scientist you know these fingers do magic on a keyboard but boy you know trying to fix a piece of drywall or toilet and I'm just lost. So it was way over my head and it was no fun at all. So that's when I decided to get into this finance arena which is really a lot more suitable to me and real estate based finance is just so much cleaner, so much more scalable, so much more upside, so much more controllable in so many ways than any other thing I've ever touched.

Mark: Scott Todd I think all these benefits sound very familiar to you in our land investing model, but I just want to get your thoughts Scott on all of this.

Scott: You know I agree. I think that the thing is you know to me our business is not necessarily about owning the land it's really about putting that land onto a note and converting that into paper. The paper is worth much more than the real estate itself because the paper, the land payments it's what sustains us you know every month. Like every month I don't have to wake up and worry about like oh man I've got to flip two properties or three properties this month. It takes a lot of stress off even though you do get addicted to seeing the growth in your paper portfolio or the paper that you're generating ultimately I was told long time paper is gold. That's what I was taught.

Bob: Yeah. So you turned your asset into cashflow.

Scott: Yeah.

Bob: So we buy real estate based cash flows primarily owner occupied residential real estate, we buy that at a discount almost entirely. So we buy, you know, we don't do our own originations. So what you guys are doing with seller financing or originating a piece of paper we don't. We buy distressed paper and we typically buy at a discount. So what that has is that we get enhanced deals because of the discount plus in a refinance or sale event we have a Cap gain in addition. So we get cash flow plus Cap gain.

Mark: So let's unpack that a little bit for the listener because you've really said a few things that our listeners may not be familiar with number one is origination you're not doing that. So you're taking somebody let's take Scott for example who lives in his house and the bank has the first mortgage on his house. You are not buying that first mortgage, correct?

Bob: You know we are buying that first mortgage.

Mark: You are buying that first mortgage.

Bob: We don't originate, we don't create the paper we simply purchase the paper.

Mark: So the bank already has the paper, they already have... so Scott is paying the bank.

Bob: Yes.

Mark: However, now let's define distress. So what does that look like? Why do you get this sought of discount?

Bob: Typically these are notes that were not being paid for a period of time and they maybe they were modified. So if you don’t pay your mortgage sometimes you can talk to your bank and they will modify the loan and once modified it’s called a Troubled Debt Restructure from the bank and once a Troubled Debt Restructure always a Troubled Debt Restructure. It doesn't matter if that borrower is FICO credit score goes back up to 800, it doesn’t matter if they’re making a million dollars a year, it doesn't matter if they're paying on time it is still a garbage loan, it’s a Trouble Debt Restructure, it’s a black eye. So these things get sold. So the banks end up selling them off to clean their books.

A lot of times they sell bad loans; these are loans that are not performing because banks don't know what to do with them. They are bought by specialty funds and hedge funds and other investors who reperform the loans or take possession of the property and create seller financing. Once they do those things they have a piece of paper that they no longer want, it's simply cash flowing boring paper and they to get their money out - so they sell it. So we buy the secondary market performing notes basically.

Mark: But they are performing once you get to them, but because they've been troubled you get them at discount and your yield is way higher. Can we define when we say higher yield what would a traditional note look like compared to your note?

Bob: All right here is an example it’s a little New York - upstate New York house - little tiny house, it's $100,000 house, he has a $100,000 loan on this, he gets a 6% interest rate on this loan he's paying $579 a month. We bought that loan for $50,000 so really he owes us $100,000; his house is worth $100,000. He doesn’t know that we paid 50,000 for that note.

So instead of a 6% yield; so the note is a 6%, he's paying 6% per year but because we paid $0.50 for that we're getting a 12% yield because we only paid $0.50 on the dollar. Then what's more so he's paying us every month $566 or whatever it is and when he refinances or sells that house, he pays us off. He pays our note off and the new buyer will satisfy the previous debt. So we'll get how much? We're not going to get 50 we're going to get a 100.

So we end up making a 12% yield on that paper until we earn a 100% cap gain.

Mark: I like this. Scott Todd, your thoughts?

Bob: Exactly we do too.

Scott: I mean I think it's great. Anything that drives your yield higher is definitely a good deal.

Mark: So Bob I would assume it's a due diligence model where you're looking at this tranche of distress notes from your bank let's say. Do you get a chance to pick and choose which notes you want and which notes you don't?

Bob: It depends on the seller. We have tons of sources but we generally underwrite every note individually. You have to do that and generally we do have a right to put back loans or exclude them from the pool since it doesn't meet our criteria but yeah it's definitely an underwriting process. We're very sophisticated underwriters using discounted cash flow models we look at every possible scenario, every possible outcome for this note including default scenarios and we build a cash flow for each one and based on our experience we assign a probability to each one. I mean that becomes the cap of the price that we pay for that note and you know there's really no such thing as a bad note to us it's just a bad price.

Mark: There's no such thing as a bad note it's just a bad price and you are very comfortable with the asset being a residential home. Because what's the worst case scenario for you?

Bob: And the worst case scenario we probably had it right where property prices declined by 35% across the nation you know. So you definitely want equity in these things, we look at a key metric we call Investment To Value meaning our cost basis relative to the value of the home and we include we buy a lot of second mortgages. We actually prefer second mortgages yes you heard that right and I'll tell you why but we look at total investment, total debt on this property measure by our cost basis on a single note relative to the price of property. We like to keep that 65% or less so that we can weather a downturn and you know borrower may watch their equity decrease but we're safe as a lender.

So you know we love seconds. People are terrified of seconds and I'm so glad they are because it creates huge efficiencies in the market. So second mortgage; so a typical first mortgage maybe around 4% coupon rate you know interest rate. Second mortgage is typically double that so maybe a 4% rate. But are they any riskier? It's really not it really depends on the property and the debt stats. So if it's a $300,000 property there's a $100,000 first at 4% and $100,000 second at 8%. Which one would you rather have? I'll take the second all day long especially since the first I probably can't get a discount on the first mortgage and the second I need to get a 50% discount. So I'll buy a $100,000 loan which is at 8% and I'll get it 50-60-70 cents on the dollar. So I love seconds.

Then what happens when there's a sale or a refinancing we get a capital gain. So we far prefer seconds but we do have in our portfolios we typically have quite a bit of first just for the safety factor of you know, having firsts where there is really nothing that can happen to these loans.

Mark: Though Scott and I are what you would call ambitiously lazy and we certainly aren't going to go outside of our own niche even though we might love this model. So what can we expect as investors investing in Aspen Funds as far as a return?

Bob: Got you. Well it's a pretty cool fund. We made a passive income fund because you know most people want the passive income and you know it is difficult to do you know. Our industries heavily regulated we're lenders so you do have to know what you doing with laws and license etc. So we manage all that, we do all of the due diligence, we have of course lots of sources and we typically pay $8^1/_2$% cash returned on an annual basis paid monthly basis so it's really nice.

You know it's mailbox money and here's the other really cool thing it's a huge differentiator from us versus most of the real estate funds which you have a lot of. Typically real estate fund you've got I'm actually on a 10 year lock up so you really cannot get your money for 10 years. Well who wants that? We have 100% liquidity at any quarter. We actually price our notes on our portfolio every quarter we come up with a net asset value price of the fund, it's a per share price and you can put in more money at that price, you can take money out at that price.

And how do we do it? We've been operating for seven years now and never failed to meet a liquidity need for an investor. How do we do that? We have 350 loans on our portfolio right now. 8% of them we'll refinance or sell every year and when that happens we get cash coming in, because we've so many notes there is always liquidity enough. So every quarter if people want to get their money back they just send me a note saying, " I want X bucks back in the quarter." I just reserve that much cash as it comes in and we're able to pay our investors. So it's kind of you can have your cake and eat it too. So we give pretty much unlimited liquidity, quarterly liquidity. We do require one year lock up as well but then after that it's unlimited liquidity and $8^1/_2$ percent return, a 100% passive. So it’s honestly this asset class really lends itself to a really attractive income path.

Mark: Scott Todd, what are your thoughts?

Scott: Okay here's my question Mark and I invest in raw land, just the land, no house, nothing.

Bob: Scary, scary, scary.

Scott: Like raw land. I take this land and I put on a note okay. Like I don't run credit on my buyer okay, it's a low down payment to the total purchase price, I've got this note. Will you buy it?

Bob: I probably wouldn't buy it because there's no underlying cashflow on that property. So there's nothing to support the value, there's no cashflow to support the value if you will.

Scott: You see like my point behind that is this like it's really funny. Look I'm not dissing you I just want the audience to listen to this piece therein lays the opportunity. Like Bob talked about the second mortgages being an inefficient market right, like how's he's benefiting from an inefficient market. Mark and I and the other land investors in this community we're beneficiating from the inefficient market and if Bob won't buy your paper I will buy your paper because I understand it. Like Bob understands his world and that's cool. I understand our world you need money come talk to me I'll do it, I know Mark will buy that paper too.

So like you see you've got to find people. There's value in the assets as I said and you've got to find the people that understand that component of it. A lot of times I know when I started I went to people like Bob like will you do this and the response I got like I kid you a hundred times was exactly what Bob said and I argued. Not disrespectful but I would say like, "Bob there is cashflow coming from these because I sold it once on the note, it's there, the cashflow is there and the yield is there to support." And the Bobs were like no, because you see they are accustomed to their niche and that's cool and I really think...

Bob: And you're right. I mean traditional lenders you know you look at in real estate you want to have income to pay the debt service and so on land there really isn't that. So you’re creating paper but it doesn't have an underlying income on it. You know it doesn't fit our model but not to say that I wouldn't start an income fund to do that because we like all cash flows. But in our fund we will not buy those but you know we have five different funds so they have different metrics. There's certainly a model that will work on that I totally agree.

Scott: That's right. But see like you know...

Mark: Yeah. Go ahead Scott.

Scott: I was just going to wrap up. See like look I'm not trying to like argue it one way I just want to everybody to see like it's all about perspective. Like Bob knows this piece and like what Bob said was there's no underlying income from the land and for me I could easily say that look when that house is empty there's no underlying income from that house either until it gets resold again.

Bob: True, true.

Scott: That's the piece. So all I'm saying is like everybody you've got to understand like there are investments that we all make and once you understand. You see Bob is not saying no because he doesn't like land. Bob is saying no because he doesn't understand what we do; that's really the [00:21:17] [indiscernible].

Bob: It's totally right and it goes to really what you guys do and what we do is taking advantage of inefficient markets and finding niches that are very profitable niches in what we do. We have another business, another strategy where we buy non-performing debt and that just terrifies the heck out of people but we so understand that market. Our margins are incredibly high and we make a lot of money on those things but again it's one of those things that people do not know how to go after this and we're buying debt for as little as 10 cents to 15 cents on the dollar and it has a lot of value but may not have cashflow but it has value. So we totally understand that there's so much money to be made in so many different models.

Mark: Yeah absolutely. But that reminds me that today's podcast is sponsored by TLFolio, TLFolio.com. If you have a performing note and you need cash you can sell 12 to 18 months of that cash flow, take that money, redeploy it, put on a new note and really get exponential returns for yourself and then you get another bite of the apple after the note in 12 to 18 months you get that passive income reverts back to you. So you get the cash and then you get the passive over there and we can walk you through the numbers so TLFolio.com for your land notes.

All right Bob Fraser we're at that point now in the podcast where your mentorship has been phenomenal and thank you so much for educating us and our audience on your model and your fund. But now we're going to ask you for one more tip: a website, a resource, a book something actionable for the Art Of Passive Income listeners to go improve their businesses, improve their lives. What have you got?

Bob: Okay, are you ready to have your live completely changed for 2020?

Mark: Absolutely.

Bob: There is a tool I use its called Microsoft Power BI - Power Business Intelligence and I just can't recommend this tool highly enough. It's basically lets you create data dashboards for any data including: finance data, spreadsheet data and it lets you slice and dice this data in a live way. We do analytics on every one of our portfolios. I can tell you everything about my portfolios and I can slice that data nicely in seconds and minutes. It is one of the coolest tools and it's free to get started.

Mark: Very cool. Scott Todd this is a super geeky.

Scott: Yeah that's cool.

Bob: That's pretty geeky exactly.

Mark: I love it, I love it PowerBI.Microsoft.com very cool. We'll have a link to that in the notes. Scott Todd, what's your tip of the week?

Scott: Mark, my tip is just for you and other but really I thought of you when I really found this one. Check out the book *The Daily Stoic: 366 Meditation on Wisdom, Perseverance and the Art of Living* on Amazon.

Mark: I love stoicism and I attribute that to Ryan Holiday *Ego Is The Enemy* yeah. Okay done I'm going to get it that's how I'm going to start 2020 with my stoic practice. Thank you so much and now my tip of the week this one is going to be one that's going to actually get you wealthy slowly and increase your passive income go to AspenFunds.us and I'll have a link to it AspenFunds.us and learn more about how you can just invest your money and make $8^1/_2$% on real estate backed mortgage investments. The risk: reward ratio seems very, very appealing and if you have qualified retirement money, you're subject to IRA money and it is just sitting there this is a great place to start getting that larger yield with it sounds like very, very little risk. Is that right Bob?

Bob: I would say.

Mark: All right well Bob Fraser are we good?

Bob: Yeah. It's a pleasure to be here with you guys.

Mark: Thank you so much. Scott Todd, are we good?

Scott: Yeah Mark we're good.

Mark: All right. I want to thank the listeners and just remind you the only way, the only way we're going to get the quality of guests like a Bob Fraser from AspenFunds.us is if you do three little things you've got to subscribe, you've got to rate and you've got to review the podcast. Send us a screenshot of that review to support@TheLandGeek.com we're going to send you for free the $97 *Passive Income Launch Kit* as well as the new wholesaling course *How To Double Your Money in 30 Days or Less*. All right Scott, are we ready to do this?

Scott: We are Mark.

Mark: One, two, three.

Mark & Scott: Let freedom ring.

Mark: Bob is like if I knew you guys were going to end like that I don't know if I would have been on the podcast. All right thanks everybody.

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