



CIG Trend Talk™

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CIG Realty & Loans

1755 Creekside Oaks Dr.
Suite 110
Sacramento, CA 95833

O 916-570-1180
F 916.570.1181
C 530-848-4312

10% - 12% on Private Money

- \$250K Residential 1st Deed of Trust, 70% LTV, 12% interest, Los Angeles
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- \$325K Residential 2nd Deed of Trust, 12% interest, 70% LTV, Pasadena

Payment vs. Interest: What's More Important?

by Mitch Kossar, CFO, CIG Realty and Loans

When looking for a home loan, many borrowers focus almost exclusively on the interest rate. More sophisticated borrowers realize interest rate is not the only relevant component of a loan. But is it the most important component? I would argue that monthly payment is what most borrowers are really concerned about and the two are not related. Take, for example, a 500,000 loan with a 6% interest rate. Which of the following do you think is the monthly payment?

- a) \$2,998 d) \$1,726
- b) \$4,219 e) \$1,386
- c) \$2,500
- (f) Any of the above

Those of you who can calculate an amortized 30 year mortgage would likely have guessed a). But you only be partially correct. A 30 year, fully amortized mortgage does indeed have a \$2,998 payment. However, amortized over 15 years, the payment is b) \$4,219. An "Interest Only" mortgage has a payment of c) most Option Arms (adjustable rate mortgages) have a payment of d) and yes, an Option Arm, amortized over 40 years has a \$1,386 payment on a \$500,000 loan or (e). The correct answer is (f).

So is interest rate the key factor? I think, given the above example, most would say not. What *IS* important is the payment structure. And, which structure to pick depends on one's needs and ability to handle certain types of risks depending on the situation. Such a discussion is too lengthy to discuss in this forum, but speak to your loan consultant to truly understand how to pick the right loan. If your loan consultant does not understand this concept, find another one! All CIG Corp loan consultants go through extensive training to understand how to find the perfect loan for a borrower. It's not just the interest rate!



Real Estate Matters: Investment Cash Flow!

by Jeff Tung, VP Real Estate, CIG Realty and Loans

Cash flow is king for many real estate investors. Finding positive cash flow requires achieving enough rent to cover debt and operating expenses – tough to find in California. To increase cash flow, investors have six levers at their disposal for a given property:

1. **Increase rent.** If possible, it's the most obvious solution. How often is it possible?
2. **Lower operating expenses.** Lowering operating expenses clearly increases cash flow, but taxes and insurance are the biggest components of operating expenses and are not easy to change.
3. **Increase down payment.** The

smaller the loan, the lower the debt expense, which is often the biggest real estate expense. This is fine if cash is available and there is nothing else to do with it.

4. **Lower tax bill.** If possible, most of the basic tricks are usually already utilized.
5. **Lower the interest rate.** As explained above, this can help cash flow, but its not as big a lever as most people think.
6. **Change the terms of the loan.** We showed in the above article how important loan terms can be. Switching to an I/O or an Option Arm loan is the easiest way to dramatically reduce debt servicing and turning a cash flow negative property

around.

Example. Property has a \$500,000 mortgage, 6.5% conventional mortgage with \$3,000 mo in rent and \$600/mo operating expenses.

Cash flow = \$3,000 rent - \$2,998 in mortgage - \$600 in operating expenses = -\$598/mo cash flow.

Changing to an Option Arm:

Cash flow = \$3,000 rent - \$1,726 mortgage - \$600 expenses = +\$674/mo cash flow

That is a dramatic \$1,272 swing in cash flow; the difference between losing and making money.