



AirburstCapital

AIRBURST CAPITAL'S VIEW OF

**PASSIVE VS ACTIVE
REAL ESTATE INVESTING**



Author: Rudy V Stefanitsis

Introduction:

Real estate investing is an attractive way to build wealth and achieve financial freedom. But for most beginners, it can be a daunting task. With full-time jobs, social lives, hobbies, and personal relationships, it's hard to find the time to learn how to invest in real estate. As a result, many people struggle to achieve the passive income they desire.

This eBook aims to help you escape the time loop of our daily lives and achieve enough education to put you on the path to earning passive income. Whether you're a working professional or not, if you have excess income and aspire to achieve wealth through real estate,

In the next few sections, we'll explore different types of real estate investments, including single-family residential properties, 1-4 family properties, multi-family commercial properties, and passive investing vs. active investing. We'll also cover financing options such as Fannie Mae, Freddie Mac, USDA, FHA, and VA loans. With this information, you'll be able to decide whether you want to be a DIY active investor or a passive investor who lets someone else deal with the headaches of managing property.

As experts in real estate investing, we're excited to share our knowledge and help you get started. And, most importantly, we promise that it will be super fun. So, let's dive in!



Opportunity Zone Investing

For Passive Investing

| Active Investor vs Passive Investor

An active real estate investor is typically someone who is hands-on in the management of their real estate investments. They may personally find and acquire properties, handle all the financing, and manage the property and tenants themselves. Active investors often have a lot of knowledge and experience in real estate and are comfortable taking on the responsibilities and risks of managing their investments.

On the other hand, a passive real estate investor is someone who invests in real estate but does not take an active role in managing the investment. Passive investors may invest in real estate funds or syndications, real estate investment trusts (REITs), crowdfunding platforms, private equity funds, or other passive investment vehicles. They provide capital to the investment, but leave the day-to-day management to others. Passive investors typically have less knowledge and experience in real estate and are looking for a hands-off approach to investing.

Both active and passive real estate investing have their pros and cons, and it ultimately depends on an individual's personal preferences, skills, and goals. Active investing may offer greater control and potentially higher returns, but it also requires a significant amount of time and effort. Passive investing, on the other hand, offers convenience and lower risk, but may have lower returns and less control.



| Determine Whether to choose Active or Passive Investing

Deciding between active and passive investing depends on several factors, including your personal goals, experience, risk tolerance, and the amount of time and effort you're willing to put into your real estate investments. Here are some things to consider when determining whether to choose active or passive investing:

- **Time Commitment:** Active investing requires more time and effort than passive investing. Consider how much time and energy you're willing to dedicate to your real estate investments.
- **Knowledge and Experience:** Active investing requires a higher level of knowledge and experience in real estate. If you don't have much experience in real estate, you may want to start with passive investing to gain knowledge and experience before becoming an active investor.
- **Risk Tolerance:** Active investing can be riskier than passive investing. You may be more comfortable with the risks associated with active investing, or you may prefer the lower risk associated with passive investing.
- **Control:** Active investing gives you more control over your investments, but also more responsibility. Passive investing allows you to leave the management to others, but you'll have less control over the investment.
- **Returns:** Active investing can potentially offer higher returns than passive investing, but it also requires more work. Passive investing may have lower returns, but it can be more convenient and require less effort.

Ultimately, the decision between active and passive investing depends on your individual circumstances and goals. It may be helpful to consult with a financial advisor or real estate professional to determine which approach is right for you.



| Financing

Traditional financing for investment properties typically involves using government-sponsored enterprises (GSEs) such as Fannie Mae and Freddie Mac, or government-backed mortgage programs such as the Federal Housing Administration (FHA) and the Department of Veterans Affairs (VA). Here's how each of these options works:

1. **Fannie Mae and Freddie Mac:** Fannie Mae and Freddie Mac are GSEs that buy and sell mortgage loans from lenders. These entities set standards for the type and amount of loans they will purchase, which means that lenders must meet certain guidelines in order for their loans to be sold to Fannie Mae or Freddie Mac. To qualify for a Fannie Mae or Freddie Mac loan for an investment property, borrowers typically need to have good credit, a low debt-to-income ratio, and a minimum down payment of 15-20%. These loans are typically fixed-rate, with terms ranging from 10 to 30 years.
2. **Federal Housing Administration (FHA):** The FHA is a government-backed mortgage program that is designed to help low and moderate-income borrowers buy homes. FHA loans are available for investment properties, but they typically require a higher down payment (at least 20%) and stricter underwriting guidelines than traditional owner-occupied loans. These loans are also subject to FHA loan limits, which vary by county.
3. **Department of Veterans Affairs (VA):** The VA offers a mortgage program that is specifically designed for active-duty military members, veterans, and their families. VA loans for investment properties are available, but they also typically require a higher down payment and stricter underwriting guidelines than traditional VA loans for owner-occupied homes. VA loans do not require mortgage insurance, but they do charge a funding fee.

When considering traditional financing for investment properties, it's important to shop around for lenders and compare rates and fees. Work with a mortgage professional to determine which loan program best fits your needs and financial situation.

There are several advantages to financing investment properties with debt instead of paying cash, including:

1. **Leverage:** By using debt to finance your investment property, you can leverage your money and potentially increase your returns. For example, if you put down a 20% down payment on a property and finance the rest with a loan, you're effectively using someone else's money to invest. If the property appreciates in value, your return on investment will be based on the full value of the property, not just the amount of cash you put down.

2. **Cash Flow:** Financing an investment property can also improve your cash flow by reducing the amount of cash you need to invest upfront. By spreading the cost of the property over time, you can free up cash for other investments or expenses.
3. **Tax Benefits:** Mortgage interest and property taxes are tax-deductible expenses that can help reduce your tax bill. By financing your investment property, you may be able to take advantage of these tax benefits and lower your overall tax burden.
4. **Diversification:** By financing your investment property, you can diversify your investments and reduce your overall risk. Instead of tying up all your cash in one property, you can use debt to invest in multiple properties or other types of investments.

However, there are also risks associated with using debt to finance investment properties. If the property does not appreciate in value or if rental income does not cover the mortgage payments, you may end up losing money. Additionally, taking on too much debt can increase your financial risk and potentially harm your credit score.

Ultimately, whether to finance an investment property with debt or pay cash depends on your personal financial situation and investment goals. Consult with a financial advisor or real estate professional to determine which approach is best for you.



| Know the lingo

When investing in real estate, it's important to understand several key financial metrics that can help you assess the potential return on your investment. Here are explanations of some of the most important financial metrics for real estate investors:

1. **Capitalization Rate (Cap Rate):** The cap rate is a metric that measures the expected annual return on an investment property. It's calculated by dividing the property's net operating income (NOI) by its current market value or purchase price. The higher the cap rate, the more attractive the investment opportunity.
2. **Return on Investment (ROI):** ROI is a measure of the profitability of an investment. It's calculated by dividing the investment's net profit by the investment cost. A higher ROI indicates a more profitable investment.
3. **Internal Rate of Return (IRR):** IRR is a metric that measures the total return on an investment over its entire lifespan. It takes into account the time value of money and calculates the rate at which the investment will earn a positive return. The higher the IRR, the more attractive the investment opportunity.
4. **Cash-on-Cash Return (CCR):** CCR is a measure of the cash income generated by an investment property relative to the amount of cash invested. It's calculated by dividing the property's annual pre-tax cash flow by the total cash invested. A higher CCR indicates a more attractive investment opportunity.
5. **Net Operating Income (NOI):** NOI is a metric that measures the income generated by an investment property after deducting all operating expenses but before deducting mortgage payments and taxes. It's calculated by subtracting all operating expenses from the property's gross income.
6. **Debt Service Coverage Ratio (DSCR):** DSCR is a metric that measures the property's ability to cover its debt service payments. It's calculated by dividing the property's NOI by its annual debt service payments. A higher DSCR indicates a lower risk of default on the property's debt.

Understanding these financial metrics can help you assess the potential profitability of real estate investments and make more informed investment decisions.

| Where to start

Real estate investors may choose to begin as active, hands-on investors, particularly if they lack experience in the field. Managing and owning a smaller number of units, such as 1-4 properties, can provide valuable experience for beginners. One of my acquaintances, for example, is a Union electrician who has amassed a portfolio of 10 single-family homes over the past 13 years. He started purchasing one property per year following the real estate collapse in 2008 and 2009, recognizing that it was an opportune time to acquire properties at a lower price point. As a result of his shrewd investments, he has accumulated significant equity.

Recently, during a coffee chat, he mentioned his expectation of acquiring some excellent deals on apartments by the fourth quarter of 2023. Although he does not wish misfortune upon anyone, he is positioning himself to take advantage of any potential market downturns. If he can find a suitable 20-50 unit apartment complex, he intends to sell his single-family homes in the first quarter of 2024, anticipating a decrease in mortgage interest rates by then. His story is a testament to the value of a patient, long-term approach to real estate investing. Additionally, he acknowledged that managing a larger apartment complex can be challenging and plans to employ a management company if his acquisition plan succeeds.

| The Busy Professional

In my experience, busy professionals tend to prefer investing in other people's projects rather than managing their own real estate investments. By identifying skilled operators who focus on multiple deals, busy professionals can participate in ownership of large real estate projects that may have otherwise been out of reach for a new investor. Real Estate Investment Trusts (REITs), real estate funds, and syndications are all options that provide opportunities for accredited investors, qualified purchasers, and qualified investors to invest in large real estate projects when subscription is open, with a minimum investment of typically \$100,000 or more. Passive investors who invest \$500,000-\$1,000,000 or more tend to receive more significant benefits, and depending on how early they get in on an investment, they can earn higher preferred returns or receive larger shares.

Many of these large pool capital investments offer different investment strategies, such as Core, Core Plus, Value-Add, and Opportunistic Investments, with the potential to yield returns of 10-20% or more annually. The typical split for these investments is 80% for the investors, known as Limited Partners (LPs), and the remaining 20% going to the operators, known as General Partners (GPs), who handle the day-to-day operations.

Overall, investing in other people's real estate projects can be an attractive option for busy professionals who lack the time or expertise to manage their own investments, but still want to participate in potentially lucrative real estate projects. By partnering with experienced operators and investing in large projects through REITs, real estate funds, or syndications, investors can gain access to opportunities that would otherwise be out of reach.

| Opportunity Zones for Passive Investments

In addition to the long-term holds and potential returns, passive investing in an Opportunity Zone offers several tax benefits.

One of the most significant benefits is the potential for capital gains deferral. When investors realize capital gains from the sale of an asset, they can reinvest those gains in an Opportunity Zone fund and defer paying taxes on the gains until the investment is sold or until December 31, 2026, whichever comes first. This allows investors to reinvest their gains and potentially earn additional returns without the immediate tax burden.

Furthermore, investors can benefit from tax credits through their investment in an Opportunity Zone. For example, investors who invest in a Qualified Opportunity Fund (QOF) that invests in a Qualified Opportunity Zone Business (QOZB) may be eligible for a 10% or 15% tax credit, depending on the holding period of the investment.

Finally, perhaps the most significant benefit of investing in an Opportunity Zone is the potential to eliminate capital gains taxes entirely. If an investor holds their investment in an Opportunity Zone for at least ten years, any appreciation on the investment is tax-free. This means that investors can potentially earn significant returns without having to pay any capital gains taxes on the investment.

Overall, passive investing in an Opportunity Zone can offer investors a unique combination of potential returns, long-term holds, and tax benefits, including capital gains deferral, tax credits, and the potential to eliminate capital gains taxes entirely.

One way to identify Opportunity Zones in the United States is to use the map provided by the United States Department of Housing and Urban Development (HUD) on their website.

The map can be accessed at <https://opportunityzones.hud.gov/resources/map>

The map allows investors to search for Opportunity Zones by state, county, or census tract. Once an investor identifies an Opportunity Zone they are interested in, they can then begin researching potential investments in the area.

Using the HUD map is a convenient and reliable way for investors to identify Opportunity Zones in the United States. The map is provided by a government agency and is regularly updated to reflect any changes to the designated Opportunity Zones. By using this tool, investors can quickly and easily identify potential investment opportunities in Opportunity Zones across the country.

| Depreciation

Standard depreciation outside of Opportunity Zones can result in a recapture tax of 25% in most cases

Depreciation is a tax deduction that allows real estate investors to deduct the cost of an asset over its useful life. However, when an investor sells the asset, the IRS requires them to pay back some of the depreciation deductions they claimed over the years. This repayment is known as recapture, and it can result in a tax rate of up to 25% of the amount recaptured. In contrast, investing in Opportunity Zones allows investors to benefit from depreciation and cost segregation without worrying about recapture. This is a significant advantage for investors, as it allows them to retain more of their profits and potentially earn higher returns on their investment. Overall, the Opportunity Zone tax incentives offer a unique combination of tax benefits, including no recapture on depreciation, capital gains deferral, and the potential to eliminate capital gains taxes entirely. By taking advantage of these incentives and working with knowledgeable professionals, investors can maximize their returns and contribute to the revitalization of underserved communities across the United States.

| Conclusion

In conclusion, both active and passive real estate investing strategies offer unique advantages and disadvantages, depending on an investor's personal goals, experience, and available resources. Active investing requires more time and effort but can potentially yield higher returns, while passive investing allows investors to benefit from others' expertise and potentially earn strong returns with less effort.

Regardless of the investment approach, it is crucial for investors to conduct thorough due diligence and work with knowledgeable professionals who can provide guidance and support. At Airburst Capital, LLC, we are here to help investors understand their current accreditation and develop an investment strategy that aligns with their goals and objectives. Please feel free to reach out to us at info@AirburstCapital.com for more information or to schedule a one-on-one consultation.

Please note that the information provided in this guideline is for educational purposes only and should not be construed as investment advice. We are not seeking any capital investments, and investors should always conduct their own due diligence and consult with their own legal and financial advisors before making any investment decisions





AirburstCapital

Are you looking for a low-stress, low-maintenance way to invest in real estate? Passive investing in real estate may be the answer. In this eBook, you'll learn why passive real estate investments are a smart choice for many investors, including the potential for stable cash flow, diversification, and low fees.

But that's not all – we'll also explore the many benefits of investing in opportunity zones, designated areas across the United States that offer tax incentives for real estate investment. With this comprehensive guide, you'll be able to confidently navigate the world of passive investing in real estate and make informed decisions about your portfolio.

Inside this eBook, you'll find:

An overview of passive investing in real estate and why it's a smart choice for investors

Different types of passive real estate investments, including REITs, crowdfunding platforms, and private equity funds

The benefits of investing in opportunity zones and how to take advantage of tax incentives

Strategies for diversifying your portfolio and managing risk

And much more!



RUDY V STEFANITSIS