Ep #89: Don't Miss the Last Train Running with Frank Cava

Full Episode Transcript

With Your Hosts

Dr. David Phelps and Evan Harris

Frank: Many, many, many people that we know, made a fortune in the short sale game, but if we could fast forward 5 years from now. If people have low interest rates and there's not a huge uptick in appreciation, which we may be on that, the real value, like you said, might be in the finance.

You are listening to the Dentist Freedom Blueprint podcast, with David Phelps and Evan Harris. Navigating you through the uncharted waters of a turbulent economy with straightforward advice to transform your practice into a self-sufficient cash machine, compound your net worth assets, and multiply, multiply, multiply your passive cash-flow streams.

David: Well hello everyone, this is Dr. David Phelps of the Dentist Freedom Blueprint podcast, and founder and CEO of the Freedom Founders Mastermind Community, back to you today with a really, what's going to be a very interesting podcast interview. You've heard him before, he's a good friend of mine, also in our mutual mastermind, the Collective Genius, Mr. Frank Cava. Frank, how are you doing today sir?

Frank: I'm doing great David, how about yourself?

David: Doing super, so just by way of introduction, I'll give a short intro, and then Frank, I want you to go back a little bit in time and give people a little bit of your pathway to where you are today, because that's always interesting to people. They want to know where we all came from, we didn't just start where we are today, there's an evolution. Just to let people know a little bit about you Frank, in your past, you were one of the youngest VP's in a more than 60 year history of the nation’s 5th largest home-builder. During your career, you were personally involved in more than a quarter of a billion, actually 3 quarters of a billion dollars, of both home sales and construction. Now, you stepped away from that job in the beginning of 2009 so that you could focus on investing in real estate. Here's the big one, Frank you said you made more money by personally investing in real estate, than you ever did working. That's a key I've been trying show my doctors for a long time.

I'm getting a little bit off track here early, but I wanted to bring that point out. You were very successful in your career path, but you started looking at investing in real estate and found out you could actually make more money doing that. We'll dig in to a little bit about that on this podcast today. You got to a place where you were comfortable, and you stepped aside to do something that today, you really love to do, so with Cava Capital, which was formed in 2007, you're a real estate investment company, specializing in renovations, wholesales, flips, short sales, and rental properties. You've completed in excess of, whenever this was written, it was 250 transactions. How many transactions up to today have you done, would you guess?

Frank: At least 400.

David: Yeah. Now, you focus in a specific market, which makes a lot of sense because we know that real estate is local. We'll talk a little bit about that when we talk about different markets today. You focus in the state of Virginia, you've learned how to adapt to the changing real estate landscape, finding ways to help struggling families, while adding value to distressed properties, and providing exceptional returns to your investors. You've incorporated a lot of years of knowledge about the marketplace, about construction, about development, you've also learned how to study markets. Today's podcast topic is, don't miss the last train running, why this is the perfect real estate investment storm. We'll get into that in a minute, but Frank, go back and talk, fill in some of the gaps, the details about how you evolved from being a VP of the nation’s 5th largest home-builder, and how you evolved into what you're doing today.

Frank: Sure. I'm going to back up a smidge further, this is kind of how I got there, okay? I'm not the worlds smartest guy, but in my family I got 2 other siblings, I'm the 3rd smartest. What I did learn relatively early is, if you're good at something, it usually correlates with you liking it, and I always was gravitated towards and kind of pulled towards things that I liked, and I felt like because of that I got real passion about it and I learned about it. Construction as a young person, I went to the University of Florida, and I know most of the people listening are doctors, so your education levels are so much further advanced than mine. When I went to Florida I found myself initially wanting to become a pediatrician, that was my initial goal.

David: I didn't know that.

Frank: Yeah, David, I hated the classwork, it didn't speak to me and my personality. I had a happenstance meeting when I was a senior in high school with a woman whose husband had gone and graduated with a degree in construction management, and i'd actually known this family since I was in kindergarten. I remember walking to class and being downtrodden thinking that this is not enjoyable, getting to the point of having a practice might be fun, but this part is a slog. I started thinking about what really speaks to me? I remembered being a kid, going to work with my dad, and working in construction, and I remember the joy that that brought. I liked the concrete nature of construction and building. I refocused, I guess 6 quarters in, so about a year and a half into college, and said I want to change my major and I want to get into something that's construction related.

I was very fortunate, at Florida they had a degree program that was built on construction, it was a cross between architecture and civil engineering, and it spoke to all the stuff I was good at. Fast forward about 24 to 36 months, I'm graduating, I'm near the top of my class, I'm having a blast, and I have 18 different job offers so I can pick wherever I want to go work. I chose to go work in residential construction, versus most of my friends who went to work commercial construction. The courses that we were doing were basically designed to get you into commercial construction, but again, I had already learned this lesson several years earlier, it didn't speak to me as well. I thought on the residential side, I'd be able to move to a community or an area, stay there as long as I wanted to, and build communities. Where if you go and build commercial buildings, you build a monument, and then you move to a different area to build something else.

To kind of tell you the reasoning, I thought that spoke to me. I got into the residential side, I thought it was great, and then to fast forward, I learned from a great company, some fundamental steps. This is relating back to making more money. I learned that I could build houses and they taught me how to do it well, but what they really taught me, was how to make money through real estate for them as a business. They were one of those businesses that shared it. What I did was, when I was 24, 26, and 29, I built my own house, 3 different times, and I made a couple of hundred thousand, to a big pile of cash per time I did that.

The beauty was, is that it was basically tax-free money, so it just sat in the account, unlike the money you would make that you would pay your car insurance or buy your groceries with, this money became wealth building money. When I was unhappy with my job in '09, and kind of like slicing through and firing people because the market stunk, I'm like, "why don't I just go out and find a way to acquire property at the right price, hold it, and let that be a wealth building strategy for me." That's how I ended up here.

David: Excellent, excellent, so when you're personally investing in real estate today, you are investing in single family, is that correct?

Frank: We are starting to dabble a little bit into land, and a little bit into commercial, but we're very, very, and we're going to talk about why later, but we're very, very, very cautious there, but almost all single families.

David: Okay, all right, all right. Well that's good, we both know you can make money in any real estate investment class, as a class. I talk to my doctors about being very, very focused, laser focused, and not chasing what we call bright shiny objects, "Oh I got to go do multi-family, I got to do commercial." I think you would agree, you need to start with something and make that your foundation, and as you evolve or as you grow, then maybe yes then move out in some other areas, but trying to be all over the board just doesn't work does it?

Frank: It doesn't David, and I say a very similar sentiment with different words. I say, "Master one thing, or master a few things first before you start pulling yourself thin."

David: Yeah, okay. Frank, I know you, like everybody in Collective Genius and the people that we work with, everybody went through that last massive downturn in the financial crash of 2008 and 9, and we're back up again. I mean again, we talk about the national market being up as a whole, real estate's very localized so I know you're going to talk about that. You learned how to study markets, why do you say that this is like the last train out? Are people being too cautious right now? What are you sensing right now because you work with a lot of investors, what are you sensing, and why do you say this is the last train out? Why is this the perfect storm for getting in now, when it seems like were back in another top level of the market?

Frank: To answer it this way, I look at the real estate market as kind of a 4 quarter game. What I mean by that is, the 1st quarter is kind of coming out of the recession, the 2nd and 3rd quarter are the periods where it's getting strong to boom, and then the 4th quarter you're back into a recession. Usually that cycle takes somewhere between 15 and 20 years to come around. Right now, a lot of the fundamentals are lining up in a way that it says it's still not too late to get in. Let's talk about some of the things that are tangible, okay? The population versus real physical houses, there is a shortage there. Now, there is a millennial ... Without getting into too much detail or getting sidetracked, there's a millennial gap and a philosophical shift there, where that group is more in the rental game than the purchase games, so it may change fundamentally long-term what happens.

What you look at is the supply versus demand of physical roofs and people, there are not enough roofs for people. At it's simplest core, if the millennial gap continues, and what I mean by that is they continue to want to rent and not own, for those of us that are savvy enough to be owners of multiple real estate properties, we then can help satisfy a segment of the market. Long term David, what you and I have talked about before is my rental strategy might be a little different than someone who's remote, but I'm right here in Richmond and I own everything right here in Richmond. What I focus on, on an acquisition side of real estate, is we focus on shelter, we go blue collar, and the reason is, is people like me can be a pain in the butt to rent to.

I'm very needy, I want, I have discretion with my purchase and my rent, I want people who want shelter because that becomes almost like a commodity that you can measure. That is what we chase on the rental side of the business, but to fill in the gap with this. There's still a lot of green chutes in real estate, but there's a few things that are starting to come in, there's a lot of price appreciation, I don't think it's yet unhealthy, but I think it's something you should look for. Why this is the time to jump on the last train out of the station is, some of those things are starting to come in, and the really good buys are starting to go away, and the market is getting flooded, so that's why we say that.

David: You were talking about the millennials, you think a lot of the issues with millennials are probably a lot of them have a lot of debt today, coming out of school, right? Maybe some of them saw their parents go through the last downturn and they're thinking, "Well, ownership in a home is not really where I want to be because I don't want to get caught in the same kind of down-slide, and lose my property, and lose my credit." Then also that generation seems to be a lot more mobile, and they're a lot more quality of life centered whereas our generation or my generation was more about get out there and be drivers and someday down the road we'll live our life. Do you see some of that, that millennial generation versus the older generations?

Frank: I do quite a bit, and the point you brought up at the end, the mobile piece is one that I haven't given a lot of credence to, but it's a very good one. Nowadays, anyone's job basically is transportable with a laptop, and that group has embraced that more than anyone, so yeah, there's definitely that component to it.

David: Yeah. Then we have the baby boomers that are right now moving in mass towards retirement. Typically, they're going to, when the kids are out of college or out of the home, they're going to start downsizing, so that's why I think you focus on that blue collar segment, right? Because that's that market area where they're good houses, we're talking about good neighborhoods, and good people, but a you said, they're very appreciative of having a good home. They're not going to be, as you said, like yourself, where they're very needy. By the way, I guess I shouldn't rent to you, right? Well you own your own home anyway Frank, so I don't have to worry about renting to you. You're right, people that appreciate having a good home in a good neighborhood, good schools, that's what they want. That's what you focus on, single family, that's your bread and butter, and you stay away from the higher end, correct?

Frank: That is correct, and what we focus on David is, I've had the good fortune of having many friends and mentors who have owned many more properties than me, and through the Collective Genius, you and I have both seen that with some others. The first influencer that I had as someone who owned residential was ... He told me point blank, he goes, "Frank, I have 300 rentals. My goal is to under rent to market, find a really, really good tenant, and then retain them." If your market rent is 1000 bucks, if you mark it down by 50 dollars, now 50 dollars is an inexpensive number for us, but for someone renting, that is 5%, that's a big number.

What you do is if you knock it down a little bit, you can be really selective on who you get in, and then if you only have to rent that house every 5 or 6 years, you make up so much more money over time if you just slowly raise the rent, and you keep your occupancy rate near 100. That has been our focus is provide a really good product, now it's not necessarily really good product that I want to live in, but it's a really good product for the price point and for the market. Then what we do is we find a good tenant, and we keep that tenant in place.

David: Frank, with the way the economy is today, and I think we have to talk about affordability. You mentioned price appreciation, rents have certainly gone up substantially since 2010, 11, I mean across the board we've seen rents go up. There's got to be a point where in this affordability arena, things top out, and I'm thinking today right now, the big buzz out there is this darn Obama Care, it is literally going to hammer the middle class. It's hammering everybody, but the middle class, which typically lives almost paycheck to paycheck, and these could be our very good renters. What's going to happen as the government, because of the debt, because of Obama Care, because of other factors that you and I can't control starts to squeeze our best renters more and more? What effect could that have on the affordability index for tenants, and price points of properties that have been going up quite a bit, what do you see there?

Frank: David, I am not nearly smart enough to understand all of the nuances that factor into that. What I'll tell you I do is this, I use a little bit of blind faith, and the reason I say it that way is strategic. I feel like even though if you turn on the news, it doesn't always seem like, or feel like, or sound like, we have an amazing country, but we do. I think our fiscal policy is better than anyone else's, I think governance is hard. I will tell you that I think our policy and the way that it's set, is the world leader, and although we're dealing with some speed bumps now, I feel like we're going to work those things out.

What I focus on in my business is the other side of it, I put faith in the US government to appoint a ... We're going to have a functional system. Because if we didn't, because I've had fears of that and I've thought about it very hard, and I'm like, "Well it could cause you to have absolutely no action," and I don't want to have that mentality. I look at it from the macro of, we're going to have a functioning system to work in. Then it comes back to the fundamentals that I can control. I pick communities where people want to live, and then I give them what I said earlier, which is a home that they want to live in.

Every one needs a home, unless we're going to go back to tents as a society, everyone needs a roof. We give them a roof, we give them ... I'll get specific, we re-do or make sure that a roof is less than 10 years old, we re-do the electric, we re-do the plumbing, and we give them above-average finishes for the price point. The reason for that is 1000 dollar rent here, it can give you different things, so we want to give them the most we possibly can for that money so they stay. That's what we do is we take ourselves and divorce some of the variables we can't control, and force the variables we can.

David: Good, good Frank. Back to the last train running. Here we are with probably still some room to go, you said we're in the 4th quarter, so are you seeing a lot of people that are holding back because they think the market has appreciated too much? Is that your sense, is a lot of people saying, "Well wait a minute, I don't want to get in now because I might be getting in too late and the market could take a downturn, we could have another reset." Is that what you're sensing a little bit?

Frank: I actually sense something different David. I think very savvy people, probably the people that you interact with your group, they may feel that, but I think the masses are still coming in. That's why I think there's still runway, is because if you turn on cable television in 2016, every channel you go to has a house flipping program, when in 2006 there were none. The masses I think are still arriving, so for those of us that run full service real estate businesses, we wholesale a lot of our houses because there are people coming to the market who are willing to pay more than we think a house is worth, and we take that profit.

From someone who's more of a ... Maybe isn't an operator in the market but is instead a participant, and kind of trying to be someone who is building long-term wealth through real estate, I still think it's a good time to buy, but I think you have to be mindful of what is your exit strategy and pick the right deals. You don't want to over-pay, you don't want to let the euphoria of the market push you out. I think you have to be a little it more selective in what it is that you purchase, but as we've all said, you make money when you buy, you realize profits when you sell, that's been the adage for years, you just have to be a little bit more selective on the entry. If you do that right, I still think it's a very, very good time to be in real estate and to get in.

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David: Frank, my experience has been that people who have looked at real estate as an arena where historically a lot of wealth has been achieved, and right now, where there is a lot of euphoria. People from the outside that are novices kind of jump in, they jump in their own backyard, they maybe know a realtor through the rotary club or the chamber of commerce, and that realtor, not knowing what they don't know but, "Yeah Frank, I'll hook you up with a good rental house," and they jump into a market probably paying retail, probably close to, at best, a break even on a rental, and those are the people that typically will come back a year or 2 later and go, "This real estate stuff doesn't work."

You and I both know because of Collective Genius, people like yourself, to acquire really good wholesale deals, there's a lot that goes into that. We call it lead generation, or it's marketing for the opportunity. I don't think a lot of people understand what goes into that, could you just give our listeners a little bit of an idea what you at your company does in order to lead generate, and out of all the perspective leads that come in, how many do you close? What do the numbers look like a little bit there?

Frank: Sure. I'm going to pull up on my screen while I'm talking some specifics and make it real-time for you guys. This month, so it's October currently, and there's a little bit of overlap between October and November but if we just condensed it, we sent out 55,000 direct mail postcards. For us, in our marketplace, Richmond is not an enormous metro-plex or market center, so that's a lot. We have generated, this month alone, we've almost generated I think 800 calls to date. If you do the math on that, yep, we're at actually 979 phone calls this month, so that's about a 25 response rate. If you look at that 50,000, 1000 phone calls, a 2% response rate in our business is actually pretty darn good. What we will then do with those 979 leads, this month, behind me you can see the war room I'm sitting in, we have 18 deals currently on the board. That means 18 deals that we have under contract for the month, so out of 979, it's a bout a 2% response rate, yeah.

To make this a little bit easier, we get about a 1 to 2% response rate from our direct mail postcards, then we get, for every 50 to 100 calls we get in the door, we usually get 1 deal. In our business David, over the past 5 years, it's about 50 phone calls to 1 deal. If we're generating 900, we have literally 18 deals on the board, we're exactly that 1 to 50. Of those calls is people who, "Please take me off your list, to I want retail, to I can sell my house at a bit of a discount." You have to sort through a ton to get to those 15 to 20 deals that you're going to buy, but that's how we do it. From a lead gen standpoint, we do direct mail, we do PPC which is pay-per-click, we do a little bit of SEO, and then we also buy leads from other internet lead aggregators, and we funnel all those in, and that's how we pick out our deals.

David: We know that marketing is the key for any business, whatever industry you're in. I mean, a dentist, I have to do the same thing, I just wanted them to understand from your perspective, and typically everybody else in CG, this is what it takes to dominate a market, to be able to buy wholesale deals, make good buys, those are your numbers. In so doing, you're able to turn around and still give very good deals to your investors, because you've got the margin there, you've built the margin because of your lead generation, your ability to buy wholesale, the investors that work with you, invest their money or buy your houses, or people who buy the wholesale properties from you.

You've left enough meat on the bone because of your ability to buy, and that's what most people don't understand from the outside. They look at real estate and go, "Well I'll just call up my local realtor," well the local realtor isn't lead generating like you, the local realtor has access to 1 group of properties and that's on MLS, and today MLS is retail all the way. That's high, high retail, those are for homeowners, for people who want to buy pretty houses that are ready to go. That's not where the investment is, correct?

Frank: Absolutely. Now, there are outliers, I don't want to say there's none, because we buy some off the MLS, but by and large it's not ... it doesn't sustain a business of my size buying things off the MLS. We can cherry pick a few here and there and that's it.

David: Okay. The other part of the perfect storm today Frank, is for those who understand the use of leverage, financial leverage, the ability to lock in long -term interest rates at, what are right now, historically the lowest rates we'll ever see the rest of our lifetime. I mean I've been doing this since 1980, I started out when prime rate was about 17.5% back in '80, and today we're down, for homeowners, well under 4%, I mean it's unbelievable but people who haven't lived through those other times don't get it. Locking in low interest rates, that's ... I tell other investors, "In lots of ways, that is your discount."

You can literally buy, in the right market, the right price point, you could pay retail for a totally rehabbed, the way you do it, fully rehabbed property, you could pay retail for it in the right market, and the rents would cover your debt service and all of their expenses, maintenance, turnover, taxes, insurance, and still have a very hefty cash-flow profit margin at the end of every month, correct? I mean that's part of the beauty of this market, right? Because we have those low interest rates, so leverage allows people to take what money they have, what capital they have to invest, and allocate that over the acquisition of more properties, that's wealth building on steroids, yes?

Frank: Completely. In my office I use the term pretty frequently of, "Interest rates are the lowest they've ever been since the advent of overhead." I mean they might be able to go a little bit lower, but I don't know how, and you're exactly right. If you do the math on 100,000 dollar house at 4% interest, versus you do the math on 100,000 dollar house at 12% interest, I mean it's almost 2 and a half times more expensive. It's almost like price appreciation of 250%, and that's ... I'm going to launch into this David. One of the main reasons I chose to go to work where I did out of college was this, they taught us how to build houses, and they gave us the ability to own o home ourselves if we were willing to build it.

What I learned was this. If I had a dollar, and I invested that dollar in the stock market, I got 1 dollars' worth of stock, but the beauty of home-ownership is that with 1 dollar, I could basically get five dollars' worth of home. Most loans are 20% down, so you had leverage. The other thing is you have a term period that's defined for you with the mortgage, so you have leverage getting in, and you have a defined term of where that loan is going to go, or what's going to happen to it over a period of time so you can really plan, and not as humongous.

Then once you really get good at this business, and you own 50, 100 houses like I do, it starts giving you real leverage points where then you can take pools and use that pool to buy a bigger pool, or to re-leverage a pool so you can get more cash-flow. It gives you a ton, a ton, a ton of options, which is a lot of fun. When you sit back and look at it every once in a while, and you're like, "Ooh, this is a pretty cool place to be in," because it gives you not only the leverage, but the options to do different things with them.

David: Yeah, good. Okay, last question. Frank, we don't know when interest rates may go back up again, I mean the Federal Reserve has been talking about it for the last 12 months, and they barely bumped them up a quarter of a point I think what, 4 or 5 months ago. With the economy, they're still shaky, I think they want to raise them back up a little bit over time because they want more of a cushion to be able to work with the economy by dropping them again. Let's just talk about what happens when interest rates go up? Let's say between now and the next 5 years, what if interest rates go up by 2, 2 and a half points, what does that do to the marketplace in your experience?

Frank: It's going to put a bit of a squeeze on ... You asked me a question earlier about Obama Care, and basically the raise of expenditure to just basically afford normal life. What ends up happening with an uptick in interest rates, before the economic system can catch up, it's going to really stress people that don't have discretionary earnings or income. In its simplest form, what that means is that people who ... It just costs more to live, and with costing more to live, if you have rentals and you have something that people can migrate to, they're going to be there longer.

I think on the retail side of business, you have to be ... For someone like me who buys and flips houses, you have to buy and flip a house and provide just absolute value, and be in the best possible areas, so you constantly don't have impact of outside forces. For someone who's a passive investor, what I would say you really have is the ability to keep people longer-term into your rental units. There's a flip-side to this David. Many, Many, Many people that we know made a fortune in the short sale game, but if we could fast forward 5 years from now, if people have low interest rates and there's not a huge uptick in appreciation, which we may be on that, the real value like you said, might be in the finance.

You may be able to buy through someone like me who knows how to market. We're buying lots of houses now that are 2 years old, that are basically market value, but they're funded at 3.75%, so they got 27 left at basically for free money, so you look at that and that can become another lead source. If interest rates do uptick and there's not a huge appreciation, the lead sources that you're going to be chasing, you may have to migrate a little bit to find value. The upside is, is we've got tons of options.

David: That's the key. I think Frank, you know, and other people that we run with, being adaptable, being flexible, being nimble, because the market is always going to change, it's always going to evolve, and if you get locked into 1 model that works in 1 particular marketplace or economy, that can change. You've got to keep your finger on the pulse and ride those changes, and that's what you do so well, that's why I love being in a group like we're in. We've got so much talent, so much of a thought leader tank in Collective Genius that it really helps us all so much. I also want our members to know that you are, Frank, you're going to be at our next Freedom Founders Mastermind in Dallas coming up.

You're going to do a special presentation and have agreed to be with us all weekend long so people can get to know you a little bit more and understand some of the talents, and experience, and expertise that you bring to the table. It's what we do at Freedom Founders, and Frank I'm grateful to you for what you've done just to help me and my investing mindset. We all push each other to the next level, that's what makes it such a strong group. The accountability, we never let ourselves take our eye off the ball, it's pure focus and moving forward. Just want to thank you for your time today and look forward to seeing you next month at Freedom Founders.

Frank: It was my pleasure and I'm looking forward to being there very much.

David: Excellent, talk to you soon Frank.

Frank: Sounds great David, thank you.

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