# Ep #298: Eddie Speed - Owning Debt as an Asset - Be the Bank

## Full Episode Transcript

### With Your Host

### Dr. David Phelps

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David Phelps: Hi, David here. In this podcast, I have the privilege of having a conversation with my good friend, Mr. Eddie Speed of Colonial Funding Group in Dallas, Texas site. Eddie and I go back many, many years, and we had a discussion about owning debt as an asset. I'll say it again. Owning debt as an asset. Eddie has been for decades, since 1980 in the real estate space, particularly on the note side or the paper side, financing secured by real estate and how we as small investors, as individual investors can have a participation in this space of real estate or alternative investing.

In this first half, this first session that we did, we talk about notes and debt as an asset, as well as how the 2008 marketplace, the great recession, unfolded and what makes this time, what we're going through right now, and the potential for more of a reset recession on the back end of COVID, to also provide new but different opportunities. It's all about your placement, your positioning in a marketplace, your relationships, your network, that allows us to do what we do. This two series

podcast will help you identify that. Part one today, enjoy it. And then we'll have part two, the second half next week.

Good day, everyone. This is Dr. David Phelps of the Freedom Founders Mastermind community and the Dentist Freedom Blueprint podcast. Today, I've got the privilege and really, the opportunity to take some knowledge that goes back well, about four decades. Mr speed, and I, Mr. Eddie Speed and I, we started in real estate in kind of different areas, but over time, I met Eddie and I learned his trade and I'm going to bring a lot of his experience to our discussion today because I know all of our listeners are thinking about where we are in the marketplace today.

In terms their investments, particularly in the alternative investments, which is what we do at freedom founders, is how does that look today? Where are we going in the marketplace? What can we learn from history? Let me give you a bit of background about my friend, Eddie Speed. He started out really in 1980, in what we call the note side or the debt side of real estate. It's an area that most people that are hobbyists, you really don't understand until you do a deeper dive.

In fact, it's not where I started either. I started with rental houses, typically, where people start, let's go buy some rental houses. Let's get in the game here and figure it out. And what I learned about the debt side or the note side, meaning owning the debt like a bank, owning the debt, a great way to elicit passive income streams, which is what we'll talk about today.

There's really a dance between the two, debt and equity. Eddie is just, he's been in the trenches for four decades.

He is the founder and CEO of Colonial Funding Group, which has been forever, like one of the biggest aggregators, if you will, of people nationwide that have carried back notes, carried back the financing from real estate that they have sold and then they want to sell that income stream. Eddie has been at the forefront of that forever.

In the last couple of decades, Eddie has been on the forefront of teaching people who want to enter the real estate arena, either as a business or as passive investors, either one and how to enter through the note space, which Eddie, I will dive into this. But with our group, with the Freedom Founders, when we have people first coming to Freedom Founders, and they're just learning about real estate, whether they've had any experience with the equity side, owning some rental houses, good or bad, good, bad, or ugly, whatever it is, I say the easiest place for you to start with some direct ownership is own some notes.

Own some notes because you're a step removed from the ownership liabilities, the moving parts. Your collateral position is much safer in the marketplace if you design it correctly, which is obviously what you teach. It's a great place to start, but most people have no idea what that looks like. Your retail brokers out on the street that are trying to help investors buy their investment product, they have no clue what that looks like. It's a niche that's for the most part, very undiscovered, but you bring it out in a big way. Eddie thanks for being here today with us, and I'm going to prompt you for some good insights into where we are and what you see going forward.

Eddie Speed: Thank you, David. I can't say enough about our relationship. David and I have done many, many, many projects and relationships together over a long period of time. He has truly, I consider him to have been a mentor of mine. I may have gotten to teach you something about the note business, but you got to teach me a lot of things about life.

David Phelps: Well, my friend, this is ... Without getting too deep here, but relationships are everything. I talk about circles of relationships and there's your family and nuclear circles. And then you might go out to maybe some tight friends you went to school with, and then you've got some business people. I just find that those tight circles, that you're in those inner rings, you and Martha, just because of the time we spent together. Knowing who you are, what makes you tick, your character, your integrity, your values, knowing that that side of you is what I think, accrues a lot of people tell you because yeah, you're a genius when it comes to all things financing and real estate.

I mean, that's a proven fact. But what people really like is, who's the person behind the genius of all this and who are the people around you? I always was not amazed, but I just found incredible, the incredible credibility that you have with so many people, past and present, people you've done business with over the years who maybe you're not currently doing business with, but you still have these great relationships and that's life. Life is relationships and that's what's allowed you to be so successful because you make great connections.

You have connections to the people that you help in the real estate business, the note business. Anyway, I think that's always important to say. And so, thanks for letting me open the door to say that. We have had some great, great times together and no doubt we'll have many more going forward, as we're both trying to help people figure out a game plan to invest in capital that they otherwise would go to the default mode, which is Wall Street. It's the 401k, is that so many people come to us and they've been doing that game and they realize they have no control.

They're at the whim of the marketplace. When the market's great, it's all good. It's all great. And then the market takes a tumble and bam, they're back to square one and they got to make up lost time over the next six, eight, 10 years, to catch back up and even. And they're like, well, how many more of these decades do you have? Real estate, like for you, Eddie, has been for four decades for me, the way to go. I started boots on the ground, very active investing. But today, I love to be on the other side. I love to be passive. I love to be in the deals, but not running the deal. I think that's a good way to say it.

Anyway, let's go back to 2008, what we now call The Great Recession. Let's talk a little bit about that because people are always interested in knowing, what's kind of set the stage for a lot of that's happening today, and then we'll bring them up with current. Take us back in time. In 2008, what came down? What came out of that, that you watched and actually facilitated a lot of opportunity in?

Eddie Speed: Well, 2008 was one of the few recessions that was started by real estate. It really was started as simple as two aggressive lending practices, right? Wall Street got too clever at doing mortgage-backed securities. In the early days, they kind of replaced selling loans to insurance companies and banks, and they would sell them to investors on Wall Street. Where just a small investor could buy a piece of a loan portfolio, a mortgage-back security. Right? They worked through the first piece of inventory and it did good. The second piece did good. And then next thing you know, they ran out of real loans to make, and then they started baking.

David Phelps: Now, what you're saying is they had a little inventory problem.

Eddie Speed: David, these were fake loans.

David Phelps: Okay. Yeah. I'm surprised that they would actually think of doing such a thing. The Greek lands kind of opened up and it's like, well, wait, this thing's running well, we got all this money, in fact, people are throwing money at us. We got to create something out of thin air because we don't have the inventory or any more of the good loans as you said.

Eddie Speed: David, when they did a billion dollar securitization, they probably made about 80 to a hundred million dollars. It's not real hard to figure out why they would do such a thing, right? People that want to make bad choices and can be easily tempted, that would easily tip somebody on Wall Street. That's what started it. We got down to it and they made a bunch of loans they shouldn't have made. By 2005, and you knew me in that era, I was telling people this doesn't make any sense. It is crazy. It won't work.

And of course they're like, no, this is new way of old lending. It's modern day stuff. You old school dog. They're telling me that in 2005. Right? So-

David Phelps: Is that kind of like the new math that they teach kids in school today? Is it something like that?

Eddie Speed: Yeah.

David Phelps: All right. Got you. Okay.

Eddie Speed: The bottom line is, it was fake lending, right? It came home to roost. So then after that, David, there were some very interesting things though, that first of all, data entered the market, right? Because Wall Street came into buying distressed assets and Wall Street doesn't invest in anything they don't have measurable data of. And so, for the first time ever, we had all these data sources, CoreLogic and Black Knight and Realty Trac, and just you name it. Right? David, you remember I was gathering all kinds of charts and data. We'd never seen all of this stuff. Right? And so, it was because Wall Street really entered the market.

So the one thing that we started learning about after 2008, was what was called shadow inventory. It wasn't just the loans that were presently foreclosed and properties that were being resold as REO, right? Real Estate Owned, bank foreclosed properties. But it was also the properties that were in the queue, right? There were assets yet to come. And so, that became a big conversation of shadow inventory. Right? We saw at one time about 12 million loans that became delinquent. About five million of those loans went to foreclosure and were resold as bank foreclosed properties.

David Phelps: Who is buying those properties? Were people that wanted to have new homes or move up or change, were they buying these or where did these properties primarily go?

Eddie Speed: Well, the highest percentage of them went to small investors. The highest percent.

David Phelps: Small investors meaning would buy typically how many? Give us a range.

Eddie Speed: The number was one to five. When you see these stats, one to five units. They are about 80, I believe it's 82 or 84% of the market. I don't have the number right, specifically today. But that's still a ... But here's what really happened, David. About 2010, for the first time ever, Wall Street decided to enter the single family, residential space. Of course, they've been in commercial and multifamily and all those businesses for years. Right? Because they could scale it. It's hard to scale buying single family houses. David, about that same era, you and I were kind of new members of a couple of hot shot, real estate investor clubs, basically masterminds. Right? We're the biggest, most aggressive house buyers in the business. The hundred house a year club. Right? Not a club, but that we call it that. Right?

All of a sudden Wall Street boys show up and they say, Hey guys, you built the marketing machine. We got the money. What if you just flipped your contract to us and we'll go take it from there and then you could go find the next deal. We'll help scale how many houses you can buy because you've built a house acquisition machine that they didn't have. And Wall Street had plenty of money. And so, that was the first of the really most aggressive, first ... This wasn't something they did occasionally, this

became their business. Today, the modern day, real estate investor calls that wholesaling. You remember the pre days, prior to 2008, there were a few people at wholesale, but there was a very short list that made a living doing it.

David Phelps: It was few and far between. Most people were buying the houses either for a rental portfolio, hold onto them or they were fixing and flipping to a consumer. Right?

Eddie Speed: Yeah. Wall Street runs and they really are aggressive out buying the market. Now, let me say that a lot of individuals were buying rental houses in that period. Right? People were buying rentals. Some very few of them were buying them, fixing them, and doing all that. Most of them were buying them from promoters. Real estate investors that would go package them and even get them rented for them and they called them turnkey rentals. Right? Yes. This became a market era. Right?

And then around 2015, there was a turn in the market. That turn in the market was specific, that Wall Street really tapped the brakes on what they were buying. Right? I don't know whether they felt like the lift was gone out of the market, David, or they just found something else that they could invest in, or maybe they found that they couldn't scale it, like they thought they could. I don't know that they've ever been totally clear with us as to why they backed out. But around 2015, they clearly backed out some. And then all of a sudden, there was this gang TV network, that just made house buying in whole, and fixing up a house, rehabbing made it look exciting.

Automated voice: Very, very glamorous. Quite a lifestyle. I mean, who wouldn't want to go do a Chip and Joanna Gaines, right

just down the road in Waco? I mean, it really looks like the thing to be doing.

Eddie Speed: If you and I laugh, because if you've ever rehabbed houses, it's a grind. It's a real grind.

David Phelps: Well, yeah. There's no way to scale that. You talk about scaling up an operation, but yeah. That's just a meat grinder, every time you go out to try to do it. Yeah. Talk about burnout pretty quickly. I mean, unless you have a TV show, you're probably not going to stay in that game very long. I think that's the key.

Eddie Speed: Well, you and I know several of those people have TV shows.

David Phelps: Yes, we do. Yes, we do.

Eddie Speed: So around then, the wholesaling business had really become a business. These half volume guys really had developed buyers list and really developed it. And then the HGTV buyer kind of came in that room, and he's not really Wall Street money. He's probably borrowing money, higher percent time than not. He's definitely not Wall Street sophistication. Now, he's probably very sophisticated in what he does in his day job. But the truth be told, he was definitely a rookie on the scene of a real estate investor.

So the middle guy became the dominant. He's the one that dictated the terms. And that's the guy who was finding the house, putting it under contract, and then he flipped it off to this HGTV buyer. This drove a whole another chapter, of what now everybody's heard of, is house flipping or wholesaling houses or that kind of thing.

Their end result is David, we have 18 million more rental doors, residential rental doors. That could be a duplex, but we have 18 million more doors than we had in 2010.

David Phelps: 80 million more. We've got 18 more typically now, smaller investors, the one to five, on one to five thereabouts. We've both been in that game. I'm not putting down owning rentals. If you run it as real business, which very few hobbyists do, but if you run it as a real business, I mean, you can do well, but we're talking about much bigger portfolio. The small investor who's got into the HTV realm or has some rental houses, 18 million more of those, the propensity for them to hang in there, particularly when there's a volatility in the marketplace, or like with COVID, which has created a lot of impasse in collecting rents, evicting, foreclosing, just because of the various jurisdictions and national edicts that have put a halt on that. What's your sense of the marketplace with all of these smaller investors, these landlords, that are out there, do they have the wherewithal to buck up and maintain? Because then again, it's not Wall Street money. It's a lower bar here.

Eddie Speed: There's a guy that used to do some emceeing, I was with him yesterday and he is saying, how do I get out of my rental portfolio? There was another call that I had this morning with a guy that you would know who was in a Mastermind with us. And he says, how do I get out of my rentals? Unfortunately, David, there's a percentage of people that own rentals that found out that owning rentals was a business. Right? Unless you were set up in the right network and your guys are in the right network, you've got a network like that.

You pick relationships that can do it pretty much all done for them. I'm not saying all of them don't work, but you and I know, I got this term from you, you call it real estate promotions, right? They acquired rental property by promoters. Now, they weren't real estate brokers. They may have been a broker, but they were really promoters. And those promoters sometimes didn't have all the systems and all the processes that would be consistent and last over time. Now they have become what I refer to as the burnt out landlord. I believe that's a big number.

David Phelps: This is really a good discussion because not to make it my story at all, but having been in the rental business, if you will, as an investor for many, many years and the note side as well, I was just balancing it. But Candace and I, we made a decision, gosh, even five years ago, that we wanted to go ahead and start harvesting the equity out of our rental portfolio. You could say, we were getting a bit on the burnout side, even though we had people managing. But even if you have managers, you've got to manage the managers. There's a point in time when either it's time to pivot out and find something that gives equally, actually even better sustainable returns. That's what I want, sustainable returns without all the brain damage.

And so, we started harvesting that equity. And I think that's what you're going to talk about a little bit here. So when you have people asking you, well, how do I exit my rental properties? Again, most people think, well, there's one way. You list it with a realtor and they're going to put it up for sale. In some markets right now, it could be a good time to get a cash sale. But then we have a problem, don't we? Because I don't think most people that

still appreciate the benefits of real estate, not withstanding the fact that they may be a burnt out landlord, they just don't know the other options. They still want to be in real estate. They still want to be in the alternative space, alternative to Wall Street. And that's what brought them there in the first place. If you get a cash out on a property, on your equity, now what do you do?

Eddie Speed: Well, and that's the problem, is where would you reinvest your money? I manage my mother-in-law ... My father-in-law got me started in the business and I manage my mother-in-law's, essentially her business. It's an independent business. And we sold a piece of land that had been for sale a long time. We sold it and it generated a fairly large amount of capital. I had the same problem, David, where would I go invest it? Right? If I did want to go put it back in real estate and stuff.

One of the options that you can do, let's talk a little bit about where the market's going and why I say certain things. There a couple of variables here, I want to add to it. Okay? Generally David, I think in 2021, we are going to see a reset in real estate. Now, I can't tell you what month, right? I'm going on the record here that I could be wrong. I will say that I think most real estate economists, residential real estate economists, I don't think I'm in conflict with most of them.

David Phelps: No, you're not.

Eddie Speed: Maybe I'm just copying what everybody else is saying, but there's two or three reasons for it. This month, David, seven million people didn't make a mortgage payment. Right? That's a giant.

David Phelps: That's a big number. Yeah.

Eddie Speed: Half of those were in the forbearance, that we've all heard about. And half of them is what you haven't heard about a lot, which is they are 90 plus days delinquent on their mortgage. That's a gigantic number. And at the worst, I'm just reminding you, at the worst of around 2000 and post 2008, it was only about 12 million assets. I'm not saying we're at 12 million, but we're not ... I mean, that's a pretty shocking number. That in combination with burnout landlords, because burnout landlords have some equity.

One of the things that, like you and I have friends and they're like, Oh, they're all short sale guys. Right? And they're like, short sales are back. I don't see it because short sales were all driven by people that were seriously underwater. They owed way more than the property was worth. These people are going to have choices to sell, last time the bank made the choice to sell.

David Phelps: Correct.

Eddie Speed: Is that a fair statement?

David Phelps: Yeah. No, no. You're a hundred percent right. Yeah. The position of the majority of equity owners today is far different than it was back in 2008, where again, super leverage and a downfall in the market, put them under water. So they had no choice. The short sales were the game back then, but I think you're right. I think there's other opportunities. And so therefore, there's different motivations and approaching that opportunity then becomes really a positioning of solving a new problem in the market. Not exactly the same at all, as what we saw in 2008. That's what you do well. That's why we're part of

mastermind groups, is because we get our chance to get our fingers on the pulse of the markets, different markets, all across the country.

You certainly have your finger on the pulse and seeing what's coming up pipeline. So therefore, we can position how we want to go forward with our current investment assets, the equities we have, where's the best place to move. If we're going to move some of them, where do we move to get in the line of where the best inventory is coming. That means solving a certain amount of problems. I like where you're headed with this. Let's take it to the next step.

Eddie Speed: All right. Enter a new variable. Okay? The mortgage industry has already reacted in a way that real estate hasn't reacted yet. Okay? Mortgage Bankers Association puts out a chart and they basically put it out every quarter, I guess it's the end of every month too, but called Mortgage Credit Availability. It's a graft. And so, David, if you looked at it around the 1st of March, right? And you looked at it, it's not going straight down, but it'd be a double black diamond ski slope. Let's just call it that.

David Phelps: Got you. That's a good-

Eddie Speed: You can relate to that. Right?

David Phelps: That's the visual I couldn't understand.

Eddie Speed: It's basically about 35% of the people that could get a mortgage in February, can't get one today.

David Phelps: All right. Why? Because we have all this money, the feds have just been pumping in the market, pumping in the

market, trying to keep liquidity in the marketplace, where's the constraint?Why is this happening right now? I see, as you do, things can get worse and more constrained, but why are we seeing it right now at this point?

Eddie Speed: Well, basically, I mean, if you look at Fannie Mae, Freddie Mac, FHA, National Association of Realtors, National Home Builders, they're all saying that we're going to have a decline in real estate values. They're not in disagreement about where the market's going. And the lenders specifically have cut back their own criteria, even though FHA cut their criteria back or Fannie Mae or Freddie Mac cut the criteria back, the lenders then went in and they would put their own enforcement.

In fact, they developed a term for it called COVID Overlay. And so, here's an easy example somebody can relate to. About two months ago, Fannie and Freddie said, if you're self employed, they really want you to have audited financials, right? They really want you to have audit ... Now, there's a little bit of an exclusion to that. Now, David, you're self employed and I'm self employed. I'm going to be perfectly honest with you, it'd probably cost me about 200 grand to go out and get audited on financials and everything I got.

David Phelps: Yeah. It would be a serious barrier to want to go and go down that path. No doubt.

Eddie Speed: Basically, those are the kinds of things. Now, I'm not saying that's exclusively, there are some provisions around that, but I'll be perfectly honest with you. I'm just going to be transparent. I own about eight different entities. I am financially qualified and my wife and I have an 800 credit score. And we owe 40% of what our house

is worth. Right? We live in a desirable neighborhood, all that good stuff. We sent our loan out and about eight days later, they called us, just we still don't think we can get ... They won't even start to try to figure it out. You know why?

Because the mortgage company that they worked for were scared to make that loan and somehow Fannie Mae or Freddie Mac comes back and discovers that they didn't put all the in stuff in there, they needed to. And it would be called an agency buyback. Right? Being deeply involved in the business. I told my wife when we did it, I said, they're never going to make this loan. I said, because somebody in the underwriting department is going to panic because we got too many entities, too much stuff. It's too hard to sort through when they're that busy. They just don't think they can-

David Phelps: Yeah. It just doesn't fit their box. They're trying to be like any business, they're trying to have a flow of business that provides them the transactional income. And if you come along, well-qualified, but it doesn't fit the box and there's any risk of the buyback, which means that the lender has to buy back the loan from the agency, from Freddie or Fannie, they got to buy it back. Now, all the risk is on them. Yeah, I mean, if you're a prudent business operator, whatever is, you're going to have a certain filter of who you take on. Let me just take it to my dentist and doctors, you've got to filter on what patients you would take in your practice to do any number of procedures. You've got filters in place, whether they're written or they're just in your head.

You know this is a case, this is a person, this is a personality, that has an expectation up here. And you know if you jump into that case, you're probably not going to satisfy. With experience, you know that. Same thing here, the underwriters look at this and they go, we could do this, but number one, it's going to take a lot of time, a lot of effort, there is a higher risk. Why don't we just do three or four of these other loans, that we can just move through and make our quick transaction fee and call it a day. Right?

Eddie Speed: I'm 60 years old. I have better credit than I've ever had. I have more net worth than I've ever had. I'm trying to refine my personal home where I owe about 35 or 40% of what it's worth and the mortgage industry says you can't get a loan Eddie.

David Phelps: Yeah. All right. We have this COVID overlay in place, which depending, again, you can look ahead and decide what you think is going to happen in the future. But we know that the economy has been for a long time affected. We have to see what recovers but a lot of industries aren't going to recover. We can't list those here. We don't need to, people know what's not going to recover. It just means the economy is not, even though things have bounced back in a lot of areas. I think the the stimulus, that they may have another roll out of stimulus, it kind of keeps things pumped up the air pumped up, but being prepared for some kind of reset in 2021, that's where the cards are.

What you're seeing on the front facing with the lenders, is seeing that they're in a protective mode right now, if you want to call that. A protective mode, which means they're forecasting that they don't want to get in a position where

things do get more dicey. That concludes my discussion of part one with Mr. Eddie Speed on owning debt as an asset. Next week, we'll pick up and talk about where the opportunities are in the marketplace going forward from here.

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