Building Wealth and Teaching Financial Wisdom to the Next Generation (Part 1) - Anna Kelley: Ep #475

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Dr. David Phelps

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Welcome to the Dentist Freedom Blueprint, a podcast about freedom—freedom from expectations of society and the traditional path to success that has been ingrained in us from our early years, I'm joined by mavericks, renegades, and non-conformers to discuss an anti-traditional path to financial freedom, freedom of time, relationships, health, and ultimately freedom of purpose. My name is Dr. David Phelps. Let's get started.

David Phelps: Hi, David here. This week, actually for the next two weeks, I'm having a conversation with a good friend of mine in the real estate space. That is Anna Kelley. Anna is going to give you a little bit more of her bio background in our actual conversation coming up here in just a moment. But what I want you to focus on for this first session this week is on what I call the mindset and the discipline of wealth building.

Anna pays the story of where she came from in the corporate world and a husband who was in the health professions. And how they together, along with raising their family, started with the tangible assets of real estate and over a decade or so built that into their financial freedom, where they are both essentially retired from their day jobs or their career jobs and now enjoy life on their own terms. This is what I believe it's all about, and I think you'll really appreciate this conversation with Anna Kelley.

Well, Anna, it's great to have you on today. I've been looking forward to this conversation for quite some time. Anna Kelly, you have quite a backdrop in history in the real estate industry overall. I think it'd be helpful for all of our listeners to know a little bit more about where you came from, how you entered the arena, and take us through a little bit of history timeline and to where you are today. Then we'll jump into metrics in the market today.

Anna Kelley: Sure. Wonderful. Thanks so much for having me. I'm so excited to be here and to be your guest. Feel free to stop me because my story is about 25 years in the making, but I'll tell you just a basic backdrop that I think would be helpful for your listeners to know is I didn't grow up knowing anything about money. I grew up very poor. My parents were divorced and I grew up in Section 8 housing.

And all I knew was go to school, get a degree, work hard, make as much money as you can so that you'll be okay one day. And so I was very driven to succeed in the corporate world and to do well, and I landed myself after college working for Bank of America, which is the first time I really started to learn anything about banking, money, finance as I went through and got my management degree.

And I went through their financial advisory training program to be a private banker. And so that was the first time I really knew anything about investments other than put money in your 401k and maybe someday it'll be worth something. And they really pounded that in my head over and over again.

But I had basically a book of the top 10%, David, of the clients, the wealth in our bank in Houston, Texas. And so my job was to talk to them about their finances, find out what they had and where, and get them to bring more of it to Bank of America through all of our different investment options.

And through that, I had a lot of conversations with investors who, one of them said to me, I remember this was back in ‘97, ‘98, and we were offering a CD in the 8% range and he laughed at me and he said, “Oh, sweetie, I make way more than that in my real estate investments.” And that stuck with me. I thought I'm learning all this stuff about investments, but I've been taught nothing about real estate.

And I started noticing a thing, David, that my wealthy clients, most of them have real estate. So that was enough to get me to start thinking about real estate as an option. And I bought a little condo instead of renting, tried to make good financial decisions. But what really got me really interested in real estate was I had a baby.

And so back in 2000, I had a child and all of these flip-this-house shows just started coming on TV. And I was convinced that I could replace my six-figure income by flipping a few houses. And I wanted desperately to be home with my kiddo, but I couldn't because my husband had just come out of chiropractic college with six figures in school loans, not unlike many of your dentists, and so he was an associate making very little money. And at that time, I made about three times what he did. And it just wasn't possible for me to stay home. So I started flipping houses when I had a three-month-old baby, made lots of mistakes there, didn't know what we were doing, but you know, I had a determination that I would figure out how to replace my income.

So at that time, David, I had left Bank of America and I worked at AIG, and I worked at AIG for 20 years before I retired five years ago. On my own, I went through the GFC with AIG, thought I was losing my job many, many times because of what happened there. And essentially, what I did before the GFC is in 2007, we sold everything in Houston.

I moved to Hershey, Pennsylvania for my husband to start his practice. We were told the economy's booming. It's a great time to start a business. It's fine to go into business debt. And we did. We went into a lot of debt to start a business in Pennsylvania, with his mom watching then my two kids. And I worked full-time.

I helped my husband start his practice and handled the billing and the hiring and the marketing and all of that. And then I started doing real estate on the side. So we bought his building instead of leasing space. And it had tenants and so we said, hey, the tenants will help kind of offset the cost. This could be a good thing. Then that wasn't so bad. So we bought a 4 unit. So I kind of fought the urge to buy a big house again and said, “We need to live below our means. So that we can get his practice up and running.” And it was the best decision we ever made was to take a step back and live in that little 4 unit and during the GFC, everything was basically failing within a week and I found out I was pregnant the week that AIG was going under. I lost almost all of my 401k because it was heavily in financial stocks.

That's what I knew and understood. I thought. And all I knew was that my tenants were still paying rent and I needed to find a way to get more rental income. So I bought another 4-unit. Fast forward, it took me 10 years of what I thought would be very quick, husband's practice would boom, I'd be home with my kids in a year.

It took 10 years to dig ourselves out of about $700,000 in business startup debt to start his practice in ‘07, but I created financial freedom. I've now retired my husband. I've retired myself from AIG and I moved from basically the portfolio of about 100 units when I retired, so it took 10 years to get 100 units.

And then from there in the last five years, I've done about 400 million in multifamily real estate. I've been very focused in commercial over the last five years.

David Phelps: Well, that's a great recap. And I did not know the connection that our audience has to the medical health profession through your husband's chiropractic.

So there's a lot of connection there. We all understand the startup costs and what it takes and particularly, but not so much when you started in 2007 and just hitting the skids there with the great financial crisis that we had there, which was a real battle for anybody in any kind of business, real estate, or otherwise it was, if you could battle through it or many people lost, as you said, assets.

And just had to get back down to the bare bones and drive back a bit. Those are the stories that I think we all appreciate. We both know many people, everybody had some struggle during that period of time, some level of struggle, and those who stayed strong and made some disciplined changes, whatever their model was and resurrected and came back.

Those are the people I like to stay connected with and continue to do business with because I know that their character and their strength is inner and that's what we like to fight in our inner circle. So I think there's a lot.

Anna Kelley: Absolutely. That grit and determination, I think, more than anything. I mean, yes, I thought I knew a lot, but what I didn't know is what kind of made things really hard, but just being willing to say no matter what it takes, I'm going to get home with my kids and it may take longer than I think it will, but I'm just going to keep growing that extra income until I have enough.

And so the grit and the determination I think more than knowledge or experience is really what I came out with that served me well.

David Phelps: So we opened one little loop. Well, I guess you did. It's about your husband. So I'm not going to make him the star of the show. But I have to know, you said you retired yourself, but you also retired him. What's he doing? Or what did he do?

Anna Kelley: He's really enjoying financial freedom. I mean, he's been retired now for two years and it was like pulling teeth to get him to retire because it was his identity for so long. He loves being a doctor. He loves seeing patients, but he didn't like marketing. He didn't like all of the insurance stuff and all the business side that doctors are not taught very much in college. Just didn't enjoy that at all. So it took me begging him to finally say, “We're making so much more money. Why are you doing this?” And he retired two years ago. We have in our own portfolio locally about 300 units between our own and some that we own with two partners. And so he helps manage some of those, the ones that are in our own portfolio because he enjoys it.

He always liked working with his hands and even though I'm the one that kind of gets the talk time or whatnot, I could never have done it without him and vice versa. He's the one that learned how to flip houses and replace windows and deal with tenant maintenance issues while I did kind of the buying the underwriting, the finance side of things.

And so he's enjoying doing more of that. He's taken up new hobbies. He's playing hockey with my son and ice skating and going to the gym and really just enjoying the fruit of all the hard years of work.

David Phelps: That's so great. There's several things that came out of that that I know to be so true. and first thing you said, you both work together in consorts in what, you know, your family, your origins back at Houston and then you left your position to go back to Hershey, Pennsylvania to help him start his practice and resettled there.

But you're both doing things to complement each other. And I think that's so important. It's a divide-and-conquer world. And each of us in our partnership or marriage bring different assets and unique capabilities to the table. We learn to align those in the right way. I think it brings people together. I think it really does. And I think the fact that you have your expertise in your area, but your husband's finding some new areas that he enjoys that freedom. I know when I finally broke the shackles to my practice, it is so freeing. And it's not that I never want to stop doing anything. I want to still do things, but there's more and that freedom to have that flexibility.

Well, I was at the gym this morning before we jumped on here because I can now I can do that. And I don't have that schedule, having patients schedule out. It's a blessing and also a curse.

Anna Kelley: Absolutely. For us too, when we started out, my son was 3 months old, so we flipped quite a few houses before we did the whole moving toward the rental kind of thing, but he's almost 21 this summer. And so we've got kids that are well, 15, 17, and 20, and this time with so many of their early years were spent with us, David, while we spent lots of quantity time, it wasn't so quality. I mean, they slept on dirty floors while we renovated apartments at night between tenant turns.

And it was a lot of blood, sweat, and tears in those early years. But once we were able to really pull back and say, “We've really developed enough income and wealth that we really can shut it down every day at 3 o'clock.” When they get home we're totally focused on being parents and just loving on our kids and enjoying lots of time to travel and do things.

And so having that practice kind of tied us down to having to be there because it's really tough to bring in temporary doctors if you want to travel to see your kids play or different things. So the hard work in those early, early years was so worth it for what we have today. But we're really truly living to enjoy our kids and enjoy our family and not chasing more necessarily just for the sake of more–if it's going to take away the time freedom, it's so important to us with them today.

David Phelps: Yes, I so agree. Well, let's think about it. Your kids got to see how their parents put in the hard work, the discipline. They got to see that and feel that, even at the young age when maybe they thought that's just the way life is, but you know that they've built character and probably also built discipline and resolve along the way. And, well, several generations back, going back maybe a hundred years, a lot of kids grew up with parents like on the farm and there's always work to be done.

Today, people say, “Well, I don't want to have more kids because they're a liability.” But if you had got houses and the kids, at a certain age, you put them to work, right? I'm kind of thinking there's an added benefit to that along with the character building that I'm sure that they have seen.

Anna Kelley: Absolutely. Yeah. And it's really important for us. There's a phrase and I'm going to butcher it, but it's something like, “Hard times produce tough men, tough men produce easy times, easy times produce weak men.” And so we're constantly telling our kids, “We're able to start you out in so much of a better position than what we did, but you cannot take for granted what you have. You have to work hard to make it continue. You have to work hard to do something for yourself.”

Life is not the easy button and as we've seen with economies and many things since the GFC between pandemic shutting business down and just the economy we've had over the last few years, nothing is guaranteed forever.

And so I tell my kids, “There's no guarantee that you're going to have wealth and so you've got to learn how to harness your skills and your passions and your abilities and make good financial decisions on your own. And you're going to have to go through some hard things where we're just not going to throw money at it and make it easy for you. You've got to learn and do the hard work yourself.” So hopefully that sticks with them as they grow as well.

David Phelps: Well, I'm going to stay on this line just a little bit. I wasn't going to go down this rabbit hole, but I think it's important. We'll get to the economy. I've got a bunch of questions about the economy and the market. I know people are dying to hear that, but I think this is some importance here. So the ages of your kids right now are?

Anna Kelley: 15, 17, and 20.

David Phelps: All right. So a lot of people believe because they're hardworking and most of the time today, as in your family and my family, growing up, it was a two-income earning family. Not always out of necessity, but there's just a drive that everybody wants their career, right? And you certainly did it and it sounds like you've done it well, but a lot of back and forth and give and take to do that. What I'm asking you is a lot of the people who have kids have grown up in the last 20, 25, 30 years.

There's some guilt on the parents. I'm not saying that you have it, but I'm saying there's guilt. And we always want our kids to have a maybe at least as good a life or better life than we had. How do we do that? And I think there's a lot of people think, “Well, I'm just gonna make sure my kids get the best education ever,” right?

“Whatever school they want to go to, if they can get into it, then we'll give that to them. We'll give them graduate school or medical school or whatever it is.” Just curious, what is your philosophy about how much you provide for your children in this regard and helping them launch versus how much is on them? I'm just curious.

Anna Kelley: Yeah, I think there's a couple of things you said there, very astute. One is, yes, there's always guilt. There's always things that we can look back and say, “If I had known better, I would have done better.” For us, it was that despite my why I’m being so compelling, I wanted to be home with them, I mean, we worked 70, 80 hours a week, David, for a decade. So there is that, “You missed my birthday that year because you were painting an apartment in the middle of the night.” They never forget those kind of things and you want to make sure that you're leaving good for your kids.

There's a, I think it's in Proverbs, the scripture that says, “A good person leaves an inheritance for their children and their children's children.” And so I don't want my kids to just have money and be spoiled for that, but I want to leave a legacy, mostly of character for them, but how to be a good person, honor God, love other people, and be a good steward of their time, their skills and their money. That's what we really focus on.

So I'll tell you like when my oldest decided to go to college, he's a senior getting a finance degree at Pensacola Christian, and what he said to me when he graduated was, “Mom, I don't want to go to college. There's no need for college anymore. You can teach me everything I need to know about money and finances.”

And he wanted to syndicate multifamily like I do. He said, “I don't want to do the hard physical labor like we did early on. I want to use my brain and run funds.” Right. But I said to him, “One, college may not teach you everything you need to know. And, yes, I can teach you a lot, but two, you need some time to grow and mature away from us. You need some time to be around people that aren't like you, that don't think like you, that aren't the same religion necessarily, there may not be on the same political wavelength, because you need to have the maturity to have really difficult conversations with people that completely disagree with you.”

And number two, I wanted him to get that finance degree, David, because I believe as someone who's also an accredited investor and I invested a lot of other things other than just being an operator, I said, “No one's going to give a check to a young kid who rode their parents' coattails just because they had money. They need to understand that you've worked hard, you've gotten a degree, and you at least understand finance to some extent.” So I encouraged him to go to college. But then we were left with these choices. One, where do you go? And college is so expensive today. And as we learned the lesson of all the debt from school that took us seven years of Dave Ramsey rice and beans, beets and rice before we even went into debt to start a practice.

I didn't want him having a lot of college debt. And so I said, “I will pay for your college like my parents worked two jobs to pay for mine, but I think you need to make one of two choices." He wanted to go to a public school or even some private schools. David, at that time, even three years ago, were 25 to $40,000 a year.

And I said, "Is that degree going to be worth a hundred to $160,000?" Probably not knowing that he was going to go into something I could teach him. However, I gave him the option. And I said, "If you go to Pensacola Christian–" It's a college who, they own a book company called Abeka, that does publishing of books and curriculum for a lot of Christian schools and homeschools, and all the profits go back into the college to keep the cost affordable for families.

So I said, "If you choose to go there and get your finance degree, it's an accredited school. They have three years, get the fourth for free," David. So I will pay less than $50,000 for four years, tuition, room, and board for a finance degree. And I said, "If you decide to go there, I will gift you your down payment on your 1st rental property when you come out. So that one, you have your degree, two, you have an apartment, probably a 4-unit that you can move into, live in, be on your own, keep your costs down, and learn to live below your means while you explore where do you want to go work. Do you want to work for yourself? Do you want to work for a fund or whatnot?"

And so he chose, I was very thankful, He chose to take the less expensive college degree so that he could get started with the down payment on our rental property. And so that's our gift to them. We've told them, "There's no guarantee we'll ever give you any more money, but get your degree. And if you finish, we'll gift you the down payment to get you started to living below your means while you work to expand your means."

And hopefully, we live to a hundred and they don't inherit anything until they've made money on their own and done well on their own. So that's kind of the guidance we gave him.

David Phelps: I think that's very, very thoughtful. A lot of insights there. The thing I think back on today is we're talking about our kids. And what I try to give to other generations that are coming up as well today, not necessarily do this, but like you, I was always one who kept my cost of living, my lifestyle relatively low. And so you did the same thing today. I tell kids, "If you'll learn the basics of finance and you'll learn how to be an investor in whatever asset you want to invest in, pick something you can be an investor in, whether you're active or passive. And if you'll wait and not allow your lifestyle to expand, that will pay for that, you'll never be on the treadmill that so many get on." Do you agree?

Anna Kelley: Absolutely. And in fact, my kid's favorite game, it took me a couple of times to get them to love it. I had to pay him to stay in it, but we play cashflow all the time, the rich dad, poor dad, cashflow game.

And so they understand a balance sheet and they understand a profit and loss statement, and they understand that if they can get their passive income higher than their expenses then that's really the name of the game that'll allow them then to take money to really invest in other things more passively and so.

You know, it's funny, those that come out with the highest paying jobs have the highest expenses, and therefore they usually lose versus, you know, I could pull the school teacher card and keep my expenses low, and end up exiting the rat race really quickly. So we have hammered into them not going into debt, not having to have the big house right away, not going in and getting a car payment and a school loan and all those things. And so they understand that quite well and, hopefully, continue to live that path where, you know, I tell them a sign of maturity is the ability to delay gratification. And if we hadn't been able to delay gratification for years and years, we never would have had enough extra cash flow at the end of the month to be able to invest, to grow our wealth and our income to where we truly have financial freedom today.

David Phelps: Exactly. So good. So good. All right. I love that. Let's jump into a little bit about today. You said you retired yourself and your husband out about five years ago. So that's 2019-ish, right? Pretty good time. You didn't know it. Who knew it. In terms of what happened in the markets, and we can talk a little bit about that, but there's been quite a tailwind. It could go back to coming out of the GFC, going 12 on, you know, quite a tailwind that many of us have had because we've had the ability or we've been disciplined to be able to invest in assets.

And so that's worked really well, but we're seeing some shakeout happening now, as an operator, but define what you do as an operator today. I know, I mean, you've been an operator for well over 20 years, going back to when you first flipping houses, that's an operator. You're on the ground, you're operating and you've got quite a few units that you may call them single family, one to four units in your area, but I know you also have other syndication operations. What does that look like today?

Anna Kelley: Yeah, I'd say the first three years from 2019 to 2022 was pretty good other than a blip of fears with COVID. Right as I left AIG and I said, "Okay, I'm financially free. What am I going to do with the rest of my time while my kids are in school?"

I was like, well, let's just keep doing apartments, but let's finally scale it. And so started doing some syndications of class A to B apartment complexes, A minus areas, trying to turn a C to plus B minus asset into something nicer. So we basically went down the value add path because the economy continued to grow, rents continued to go up even despite COVID.

So COVID was a real challenge in that the news told everybody you don't need to pay rent. The government gave everybody more money, but they knew that they didn't have to pay rent and couldn't get evicted. And so that was a challenge where I realized, wow, handling investors money on assets where things happen outside of your control is much, much more stressful than handling your own money, and it was a burden that I quite frankly wasn't quite ready for even though I had worked with investors for many years saying,you know, what happens when something happens outside of your control that you never anticipate like a national pandemic. And that got me becoming even more conservative in my investments in the assets I chose to do.

So I pretty much, David, have been a value add investor, but only of properties in really strong major markets. So like Atlanta, Georgia, Houston, Texas, Raleigh, North Carolina, markets that had really strong jobs, really strong economies. Generally speaking, undersupplied, although that changed over the last couple of years, and very conservative areas where the pro-growth, pro-business, pro-employee, low taxes, so I started value add operating, basically flipping apartment buildings for those that don't know what value add is.

You're going in and you're renovating most of the units. You're increasing the rents, lowering the expenses, and therefore increasing the value. And in an economy, what I did learn, and maybe we can touch on this a little bit, but I learned through the GFC that no matter how good I was at what I did for a living, and I was in the financial world, I worked at AIG, no matter how smart I thought I was from what I had learned, if something in the economy happens that I can't foresee, everything can be lost.

And so I became a real student of the economy. I started studying macroeconomics and microeconomics and the fed. I have volumes on fed history and how they react to different things. So I started believing we're probably reaching a peak of the economy and potentially a peak in the economic cycle.

And then once the pandemic happened, I was really afraid of mass inflation, even before we started going. And so I bought properties that I thought, okay, we can value add them, but I wanted to make sure I got debt on those properties that was longer-term debt. So I didn't do any of the bridge financing, which is where most of the pain is today in multifamily.

David Phelps: How do you do that? Because most banks, most lenders, do they not want a property with what we call stabilized and you're doing value out and renovations and you're going to–so just give us a little tutoring on that.

Anna Kelley: Sure. So, value add can have anything from a minor value add to a major reposition. A major reposition is not the business that I'm in. So, major repositions is when someone buys a property that, I mean, it needs significant work. It's getting dilapidated, plus C minus kind of stuff, and they're trying to completely, sometimes down to the stud, gutting units and redoing everything, electric, plumbing, et cetera.

Those, you unstabilize. So, you buy a property stabilize. Meaning it's got 90% occupancy in order to get Fannie and Freddie financing, which is the government back holy grail of financing for multifamily, you had to have at least 90% occupancy, continually, and most properties during this last 5 years have been 90% occupied because there was a lack of supply in a lot of different areas, which kept apartments full.

When you buy something that isn't stabilized, you can't get Fannie and Freddie debt, so you have no option but to generally go bridge debt. I didn't want something that was unstable already. I wanted something where I could lock in good debt and that if the economy turned and didn't allow me to value add and see continued compression in cap rates, meaning, the returns demanded by the market go down therefore, my value that they'll pay is going to be higher. Just in case, because I'm a long term hold investor and I learned lessons through '08, I said, "I want an asset that I can hold longer if anything else crazy happens like a pandemic." And so I put on all but one property and I've done seven large dedications and five smaller ones here in Pennsylvania in this last five years.

But other than one property, we did do a Freddie loader. So it was a fixed loan for 10 years, but the rate flow and we bought rate cap insurance just in case rates went up and there are still challenges with that as well that I'm learning that have never happened before. But generally, I bought value add deals where they're already in good shape and good locations. We're just making them a little nicer. We might tear out cabinets and put it, new, nice cabinets and Formica countertops and put in granite. So we're doing some nice cosmetic updates to the property, which creates higher rents, which creates higher value, and then you're exiting. And we've been able to exit several deals and did really well.

Part of that, I'd like to say, is because we're experienced operators, so we knew what we were doing, but part of it, to your point, was just the economy, the tailwinds, really pushing all values up, all assets up, post-COVID free money, and helped us to do really well. So I did learn that where you are in the market cycle can have tremendous impact on you as an investor and your success.

And so I chose to learn, “Hey, if we're nearing the peak, even though I'm going to keep doing these deals and writing these deals as long as I can, and I'm going to try to mitigate risk by being able to hold a long term with some longer-term debt, if we hit a peak and we start to have a recession, I want to be able to prepare with an asset that I can afford to hold long through that.”

And I'm thankful that I had that mindset where many of my friends were like, “Anna, you're being too conservative, you're too worried about a recession.” And quite frankly, I thought a recession would be here much sooner than it is. And I've learned that sometimes, you start seeing the warning signs, but with financial manipulation and the fed and what they do, it can really create big lags and when things naturally would fall out.

But essentially I was a value add investor. I have a couple of deals still today where we are positioned to hold them longer term if we need to. But I'm really back towards more right now, David, long-term buy and hold type properties, like what I started with because I think that in an economy that I really believe is pretty unprecedented in many ways, you can't always do stuff that forces appreciation. That only really works in the expansion period of a market cycle as you reach the peak.

And then as things start to come down, you really start to need to think about moving from huge growth investing to asset preservation and to income. And so I've moved from these big value at growth deals too. Hey, now I'm in preservation mode. I'm only going to do amazing deals that I think are going to preserve my capital.

And then the appreciation may be the gravy on top or the cherry on top. And then the income is what I'm really looking for right now. So I'm back to buying some smaller properties again, David. I never thought I would, but I think that some smaller properties are a better position right now to be in than continuing to do the large multifamily deals.

David Phelps: All right. Hope you enjoyed the conversation with Anna today. Next week, I'll pick back up with Anna and we'll talk about where we are in the economy and the real estate markets today. I know you'll have a lot of interest in that, so stay tuned, pick this back up and I'll see you next week.

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