



# **The Passive Income Manifesto**

**WORKBOOK**

**(part 1)**

**A SPECIAL GIFT TO  
NOTEWORTHY MEMBERS**

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## Loan Constant Exercises

Complete the exercises below. Multiple correct answers may apply.

*NOTE: We recommend you watch the webinar replay for help with any questions you're unsure of. Check your email for the webinar replay link.*

1. Loan constant is used as a...
  - a. Measure of risk of a loan
  - b. Measure of how much more interest I can get
  - c. Measure of how good looking I am
  - d. How low the interest rate is
  - e. Measure of how much principal and interest is in a payment
  
2. When trying to maximize cash flow from an investment, I would...
  - a. Maximize the spread between what the asset pays and interest rate
  - b. Maximize the spread between price of an asset and loan amount
  - c. Maximize the spread between what the asset pays and loan constant
  - d. Maximize the spread between the person sitting next to me and myself
  - e. Maximize the spread between an asset price and interest rate
  
3. You decide to buy a fixer-upper, fix it and sell it within 6 months. You calculate your profit could be as much as \$25,000. You're excited, and you get the property under contract. You have 2 weeks to finance this and close the deal. You have access to the following financing options. Which would you pick?
  - a. A hard money lender charging 12% and 5%, with a loan constant of 12%. (we don't use loan constants for such deals. We use them for passive income)
  - b. "Bank of X" has a 6% interest for 30 years, and a loan constant 7.2%.
  - c. Dude, where's my car?
  
4. Which of the following is correct:
  - a. The LOWER the loan constant, the more cash flow
  - b. The HIGHER the loan constant, the safer the loan



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WORKBOOK

- c. The LOWER the loan constant, the more attractive the loan for deals.  
(this assumes CASH FLOW deals)

### **Exercise 5:**

You find a income-producing asset listed for \$1,000,000  
You calculate the asset pays you 8.5% if you were to buy it all cash  
You decide to borrow the whole \$1,000,000.  
You find 4 sources to lend you the whole amount  
Which of those 4 loans would choose for this loan?

- 1) Calculate the loan constants below  
(use spreadsheet from [www.NoteworthyUSA.com/george](http://www.NoteworthyUSA.com/george)).
- 2) Which loan generates the most cash flow?

#### **Loan 2**

<b>Loan 1</b>	<b>Loan 2</b>	<b>Loan 3</b>	<b>Loan 4</b>
4.50%	6.7%	8.0%	6.2%
5 year fixed (amortized)	30-yr fixed (amortized)	Interest-only (10 years)	15-yr fixed (amortized)
<b>22.37%</b>	<b>7.74%</b>	<b>8.00%</b>	<b>10.26%</b>



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WORKBOOK

**Exercise 6:**

You decide to buy a rental property. You have the down payment. Your loan agent gives you the following 4 loans to purchase the property.

a. Calculate the following loan constants:

Loan 1	Loan 2	Loan 3	Loan 4
4.90%	6.6%	7.8%	6.0%
5 year fixed (amortized)	30-yr fixed (amortized)	Interest-only (10 years)	15-yr fixed (amortized)
<b>22.59%</b>	<b>7.66%</b>	<b>7.8%</b>	<b>10.13%</b>

b. Which loan is BEST for cash flow and why?

**Loan 2 because it has the lowest loan constant**

c. Which loan is the RISKIEST and why?

**Loan 1 because it has the highest loan constant. Notice, it has the lowest interest rate also, which is what many people choose.**

d. Which loan is the LEAST RISKY and why?

**Loan 2 because it has the lowest loan constant, which happens to be the BEST for cash flow!**



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WORKBOOK

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## **Financial Leverage & Arbitrage**

*Complete the exercises below. Multiple correct answers may apply.*

*NOTE: We recommend you watch the webinar replay for help with any questions you're unsure of. Check your email for the webinar replay link.*

1. "Financial Leverage" is...
  - a. Being nice to people
  - b. The use of borrowed money
  - c. The use of "good debt" only
  - d. The use of other people's efforts
  
2. To calculate a "spread," it is simply...
  - a. Cash Inflow (\$) – Cash Outflow (\$)
  - b. Cap Rate (%) – Loan Constant (%)
  - c. Cap Rate (%) – Cash Outflow (\$)
  - d. Cash Inflow (\$) – Interest Rate (%)
  - e. Cap Rate (%) – Interest Rate (%)
  
3. I lend \$200,000 to Bob at 12%. I borrow that same money from Jane at 7%. My spread is...
  - a. 5%
  - b. 7%
  - c. 12%
  - d. -5%
  
4. I buy a building for \$3M. The cap rate on it is 7.5%. My mortgage's interest rate is 5%. The spread there is...
  - a. 2.5%
  - b. 3.5%
  - c. 5%
  - d. Cannot tell (we need to loan constant, not the interest rate)
  - e. 0%
  
5. I find an asset that has a cap rate of 7%. I find a loan with a loan



## THE PASSIVE INCOME MANIFESTO

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### WORKBOOK

- constant of 7.5%. This is called...
- Neutral Leverage
  - Negative Leverage
  - Positive Leverage
  - No Leverage
  - “I can't believe it's not butter” Leverage
6. For the same asset with a cap rate of 7%, I find another loan with a loan constant of 5.5%. This is called...
- Neutral Leverage
  - Negative Leverage
  - Positive Leverage
  - No Leverage
  - “I wish I knew about this 4 years ago” Leverage
7. For the same asset with a cap rate of 7%, I find yet another loan with a loan constant of 7%. This is called...
- Neutral Leverage
  - Negative Leverage
  - Positive Leverage
  - No Leverage
  - “The cost of not knowing this information has cost me A LOT” Leverage
8. The cash flow generated from a spread can be used to...
- Buy other assets
  - Buy my toys (cars, homes, vacations)
  - Invest into other businesses & real estate
  - Help my favorite charity
9. When trying to maximize cash flow from an investment, I would...
- Maximize the spread between cap rate and interest rate
  - Maximize the spread between price and loan amount
  - Maximize the spread between cap rate and loan constant
  - Maximize the spread between the person sitting next to me and



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myself

- e. Maximize the spread between price and interest rate



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**Exercise 1A:**

You find a cash flow asset listed for \$1,200,000  
You calculate the cap rate to be 8.5%  
You realize you need to raise \$250,000 in OPM  
You agree to give the investors 50% of the deal  
You call your mortgage broker to get financing. She submits 4 possible loans (shown below).

- 1) Calculate the loan constants below  
(use spreadsheet from [www.NoteworthyUSA.com/george](http://www.NoteworthyUSA.com/george)).
- 2) Which loan generates the most cash flow?

**Loan 2**

Loan 1	Loan 2	Loan 3	Loan 4
4.50%	6.7%	8.0%	6.2%
5 year fixed (amortized)	30-yr fixed (amortized)	Interest-only (10 years)	15-yr fixed (amortized)
<b>22.37%</b>	<b>7.74%</b>	<b>8.00%</b>	<b>10.26%</b>



## THE PASSIVE INCOME MANIFESTO

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### **Exercise 2A:**

You decide to buy an income-producing property for some passive income.

You find a 4-plex listed for \$1,000,000 in San Francisco Bay Area. The listing agent laughs when you ask about the cap rate. He tells you *“4-plexes do not have cap rates! Only commercial buildings use them!”* He also tells you the property is below market.

You realize he is ignorant! You calculate the cap rate to be 2.8%. You contact your mortgage broker. She sends you a “great” loan with a loan constant of 5.4%.

You then decide to use a HELOC you have for the down payment. The HELOC costs 4.25% interest only.

Would you do this deal? Would you use a HELOC as a down payment?

**NO! We would not do this for cash flow.**

**The Cap Rate < Loan Constant, which gives us Negative Leverage on both loans (mortgage and down payment, which is a loan as well).**

**Would not use a HELOC as down payment since the LOAN CONSTANT on the HELOC adjusts, and the maximum interest on the line would be my LOAN CONSTANT, which is probably higher than the 2.8% cap rate.**



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**Exercise 3A:**

Calculate the following. In 12 months, I buy \$2,000,000 worth of cash flow assets. I generate a 3% spread. Assume 100% LTV loan for this example. My ANNUAL and MONTHLY cash flow are:

Description	Calculation	Note	
Asset Value	\$2,000,000		(a)
Spread	3%		(b)
Annual C/F	<b>\$60,000</b>	Multiply (a) * (b)	(c)
Monthly C/F	<b>\$5,000</b>	Divide (c)/12	



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**Exercise 4A:**

18 individuals borrowed \$3,000,000 from me last year at 14%.  
At the time, I only had \$1 so I decided not to use it for this deal since I had planned on using it for to buy off of McDonalds' \$1 menu.  
\$300,000 of that came from individual private investors at 7%.  
I was able to leverage that \$300,000 9 times to get the additional \$2,700,000 at 8%. All interest is interest-only.

Calculate how much cash flow I am making:

Description	Calculation	Cash Flow	
Incoming Cash Flow	\$3,000,000 At 14%	<b>\$420,000</b>	(a)
Outgoing Cash Flow	\$300,000 At 7%	<b>\$21,000</b>	(b)
Outgoing Cash Flow	\$2,700,000 At 8%	<b>\$216,000</b>	(c)
Annual C/F	$a - (b + c)$	<b>\$183,000</b>	(d)
Monthly C/F	$d / 12$	<b>\$15,250</b>	
My cash-on-cash return	$d / (\text{my principal})$	<b>infinite</b>	



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**Exercise 5A:**

After the deal above, I had some money to use.  
24 individuals borrowed \$4,000,000 from me this year at 14%.  
I used \$400,000 of my own money. All interest is interest-only.  
An additional \$400,000 came from individual private investors at 7%.  
I was able to borrow the additional \$3,200,000 at 8%.

Calculate how much cash flow I am making:

Description	Calculation	Cash Flow	
Incoming Cash Flow	\$4,000,000 At 14%	<b>\$560,000</b>	(a)
Outgoing Cash Flow	\$400,000 At 7%	<b>\$28,000</b>	(b)
Outgoing Cash Flow	\$3,200,000 At 8%	<b>\$256,000</b>	(c)
Annual C/F	$a - (b + c)$	<b>\$276,000</b>	(d)
Monthly C/F	$d / 12$	<b>\$23,000</b>	
My cash-on-cash return	$d / (\text{my principal})$	<b>69%</b>	



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WORKBOOK

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**Exercise 6A:**

You find a good apartment building listed on Loopnet.com (website for commercial real estate). It is listed for \$2.4Million. The cap rate is listed for 8%. Upon further due diligence, you realize it really is a 7.8% cap rate. You call your mortgage broker. He gives you the loan with the lowest loan constant of 5.8% fixed. This loan requires a 20% down payment.

So far, does this sound like a deal you would continue pursuing? Why/ Why not?

**Yes, positive leverage (cap rate > loan constant). Nice spread between cap rate and loan constant.**

The spread of 2% is against what dollar amount?

**The spread is against 80% of the \$2.4 Million, which is \$1.920.000.**

Calculate the cash flow from the 2% spread on the amount you calculated above?

**2% spread x \$1.920.000 = \$38,400 of spread on the mortgage alone.**



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