Breaking Down BRRRR

Your guide to building a rental portfolio quickly and profitably using the BRRRR method

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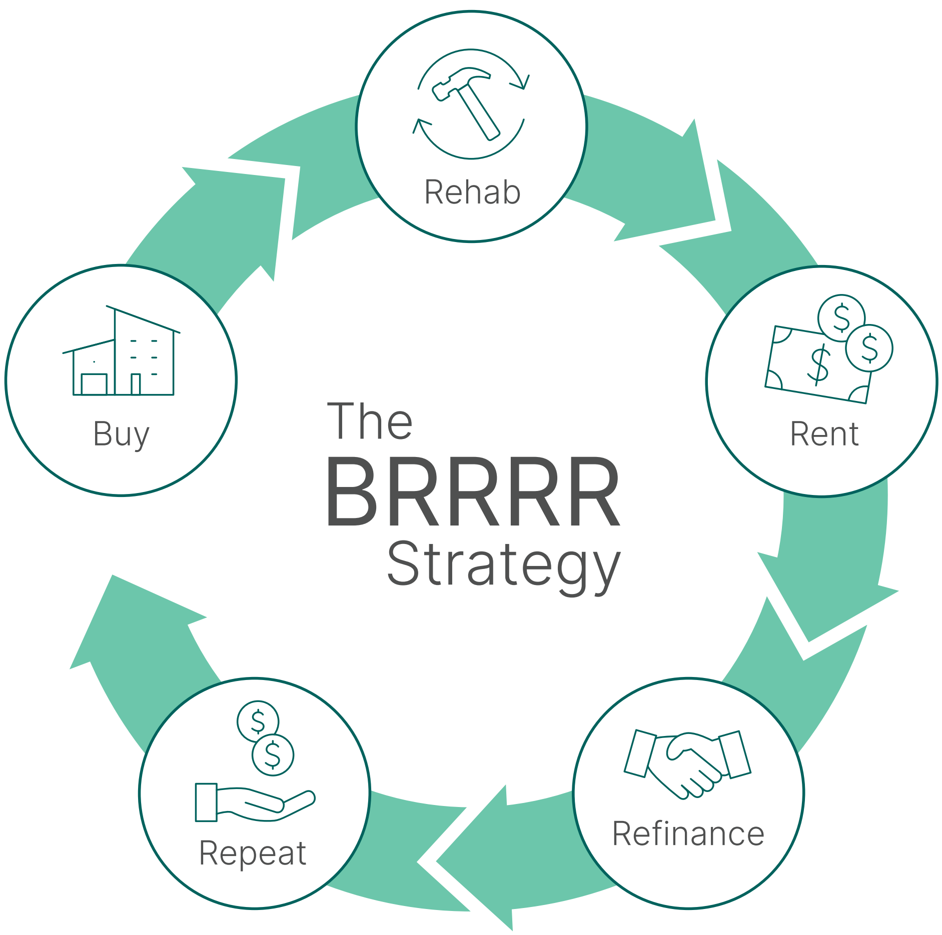
Introduction

The residential real estate community is buzzing about the BRRRR strategy, which has piqued the interest of novice and professional real estate investors alike. After all, who wouldn't be interested in a low cash out-of-pocket and high return opportunity?

So what is BRRRR exactly?

The BRRRR method, which stands for Buy, Rehab, Rent, Refinance, Repeat, is a commonly used real estate investment strategy. Unlike the traditional method of purchasing a turnkey rental, BRRRR involves:

- **Buying and rehabbing a distressed property**
- **Renting it out**
- **Doing a cash-out refinance**
- **Using that cash to do the whole thing again**



Why BRRRR?

When done successfully, the BRRRR strategy can enable real estate investors to earn passive income while increasing their rental portfolio to experience long-term asset appreciation. Here are some reasons why this strategy is so powerful for growing a strong portfolio:

Incredible Wealth-Building Potential
BRRRR has the potential to allow investors to build huge amounts of equity without investing vast amounts of cash.

Investing for Financial Freedom
Earn a passive income while holding rental properties that will continue to appreciate in value over time.

Potential Tax Benefits
Building a rental portfolio can come with tax benefits. Consult a CPA for more information*.

Earn High-End Rents
Under the BRRRR model, the end product is a beautiful, newly-renovated home that is attractive to renters. Thus, decreasing the chance of vacancies and increasing the opportunity to charge top dollar.

Higher Cash-on-Cash Return
One of the main benefits of BRRRR is earning cash-on-cash returns that are much higher than when using the traditional method of buying a turnkey rental (see figure below). The final "R" is added to BRRRR because investors can continue repeating the process.

Hypothetical Example of a Cash-on-Cash Return of BRRRR vs. Turnkey

BRRRR

Cash-on-Cash Return BRRRR

Annual Cash Flow Estimate	$3,600
Cash Out of Pocket	$20,750
Cash-on-Cash Return	**17.35%**

VS

Cash-on-Cash Return Turnkey

Annual Cash Flow Estimate	$3,600
Cash Out of Pocket	$41,000
Cash-on-Cash Return	**8.78%**

97%+ Increase Over Cash-on-Cash Return Turnkey!

In this eBook, you'll receive a step-by-step breakdown of the BRRRR method, insights into how it works, and a detailed example of how quickly it can help investors scale attractive returns using this strategy.

*A professional tax advisor should be consulted before implementing any of the options presented. Content should not be construed as legal or tax advice. Always consult an attorney or tax professional regarding your specific legal or tax situation.

Buy

The BRRRR strategy starts with purchasing a distressed property, and accurately determining the after repair value (ARV) is vital. The ARV will reveal the home's estimated value after the rehab is complete, help the investor know how much to offer on the home, and determine how much money will be needed to spend on renovations.

With the property likely needing updates and repairs, the value can be challenging to assess on appraisal. Additionally, given specific qualifying guidelines, a traditional mortgage may not be an option. Many investors utilize bridge (or fix-and-flip) loans to secure the property and cover the rehab costs.

A major key to success in a BRRRR is buying at the right price. Many investors start their offer at a purchase price that is equivalent to 75% of the ARV minus the renovation cost estimate. However, in such a competitive market, investors may need to go to 80-85% ARV minus renovation cost in order to secure the deal. Investors should keep in mind that the better deal they find, the less their own cash will have to be left in the property once they refinance. The purchase price will greatly influence the cash-on-cash return.

Did You Know?

ARV = The value of your home once renovations are completed.

To determine value, appraisers typically won't look at the gross monthly rents, so you'll want to ensure you are using comparable sold properties to determine your ARV.

Rehab

A distressed property requires more than just a few well-placed nails and a fresh coat of paint. The first improvements made should ensure the home is up to code, safe to live in, and will pass inspection.

Next, the investor should make improvements aimed at increasing the property's value. Making updates to the kitchen, bathrooms, and flooring, as well as adding new features, installing new fixtures, and improving curb appeal are just a few items to consider.

Hottest New Home Rehab Trends

When a property is designed and staged well, potential buyers or renters can picture themselves living there, so staying on-trend is essential. Below are some hot trends from Architectural Digest[1] to keep in mind for your next rehab:

Enhanced Outdoor Spaces

Homeowners are investing in the outdoors. Awnings, water features such as an outdoor kitchen, fire pits, extensive seating, and dining areas are high on wish lists!

Texture is Hot

Flat finish drywall is out, and textured surfaces are in. Consider a faux finish – think exposed brick or Venetian plaster.

Tech Savvy

The smart home is not just a trend – it's becoming a necessity. Consider adding specialized outlets with USB-C ports that allow for faster charging and no adapters.

[1]Zoë Sessums, "10 Renovation Trends You'll Be Seeing a Lot of in 2022," Architectural Digest, December 24, 2021, https://www.architecturaldigest.com/story/home-renovation-trends-2022.

Rent

After the rehab is complete and before refinancing, the investor should select a tenant for their rental. Finding a quality renter who will help maintain the home and pay on time each month requires a screening process to be put into place. To properly screen potential tenants and be compliant with Fair Housing regulations, many investors hire a third-party management company or use an online screening service.

If the investor chooses to screen tenants independently, they must follow local and federal Fair Housing Laws. They need to be fully educated on what information is allowed to be used when determining a renter[2]. While not intended as legal advice, and you should seek legal counsel to assist you in determining legal requirements, here are some common items often examined when screening potential renters:

- **Sufficient, verifiable income**
- **Stable work history**
- **Credit score**
- **Criminal background**
- **Prior rental history**

When determining the monthly rent, the investor must calculate an amount that is fair to the renter and provides a positive monthly cash flow. An excellent place to start is researching comparable properties in the area to understand the average home prices and rental rates of similar properties. Also, subtracting the total expenses of owning, maintaining, and renting the home from the total monthly rent amount helps determine what the cash flow will look like per month.

Did You Know?

The average growth rate of the U.S. rental market **increased 10.1% nationally in 2021[3]**

The median rent in the 50 largest metro areas was **$1,781 at the close of 2021[4]**

[2]Sarnen Steinbarth, "Council Post: How to Screen Potential Tenants and Save Thousands," Forbes (Forbes Magazine, March 8, 2018), https://www.forbes.com/sites/forbesrealestatecouncil/2018/03/08/how-to-screen-potential-tenants-and-save-thousands/?sh=728f6cd8332c. [3, 4]Jiayi Xu, Author, and Danielle Hale, "December Rental Data: Rents Surged by 10.1% in 2021," Realtor.com Economic Research, January 26, 2022, https://www.realtor.com/research/december-2021-rent/.

Refinance

Under the BRRRR method, investors often replace their existing bridge loan on the property using a cash-out refinance at a lower, long-term rental loan rate.

A cash-out refinance will replace the existing loan with a new home loan that exceeds the amount owed on the property. The investor can tap into the difference in the value of the home and the amount owed, receiving a cash payout. Lenders usually restrict the allowable amount borrowed to a percentage of the property's equity[5]. An appraisal is required, and additional fees, including closing costs, are also assessed in the process.

What to Expect

To qualify for a cash-out refinance, traditional lenders typically look at:

- **Debt-to-Income Ratio (DTI)**
- **Minimum Credit Score**
- **Home Equity**
- **Seasoning (the amount of time the home has been owned)**

Did You Know?

One of the benefits of working with a lender like Kiavi, as opposed to a traditional bank, on your rental loan is they focus on debt-service-coverage-ratio (DSCR) as opposed to DTI.

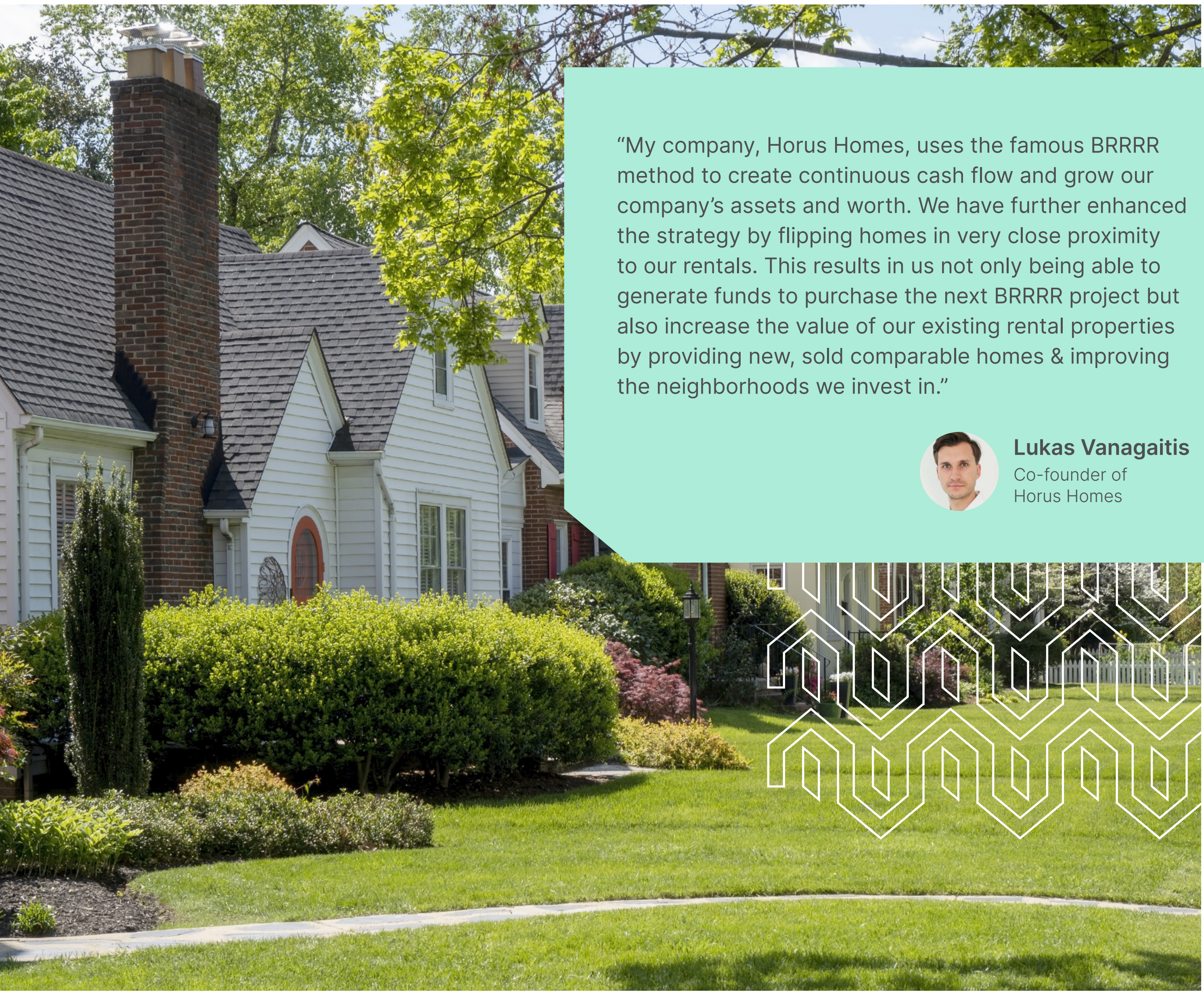
What is DSCR?
To determine value, appraisers typically won't look at the gross monthly rents, so you'll want to ensure you are using comparable sold properties to determine your ARV.

DSCR vs. DTI Qualification
Real estate investors can have trouble qualifying for loans through conventional lenders who underwrite for DTI, which isn't an issue with DSCR loans.

[5] Egan, J. (2021, October 8). What can you use a cash-out refinance for? Experian. Retrieved February 2, 2022, from https://www.experian.com/blogs/ask-experian/what-can-you-use-a-cash-out-refinance-for/.

Repeat

The last "R" of the BRRRR method is the simplest. Use the cash-out from refinancing to repeat the process over again. Once the BRRRR method is complete and repeated, the investor has tapped into the ability to earn passive income, increase their rental portfolio, and realize long-term property appreciation.



"My company, Horus Homes, uses the famous BRRRR method to create continuous cash flow and grow our company's assets and worth. We have further enhanced the strategy by flipping homes in very close proximity to our rentals. This results in us not only being able to generate funds to purchase the next BRRRR project but also increase the value of our existing rental properties by providing new, sold comparable homes & improving the neighborhoods we invest in."

Lukas Vanagaitis
Co-founder of
Horus Homes

BRRRR Pros and Cons

The BRRRR method is one of the most popular and exciting strategies for real estate investors for a reason: it works. But that doesn't mean it's without its drawbacks. Here are some pros and cons of working with the BRRRR method investors should consider.

Pros

High ROIs

This strategy works with very little cash out of pocket, especially compared to traditional investing methods. Lower out-of-pocket costs mean higher ROIs. For example, if the investor ends up having only $10,000 in the deal, but the cash flow is $2,500 per year, that's a 25 percent cash-on-cash return[6]. Plus, equity is built during the rehab.

Get Cash Back

Under the BRRRR model, the investor refinances the property based on the ARV after renovations, not what was initially paid. Because of this, they are not only able to pull out the cash that was put in when purchased – they can sometimes pull out more, which can make buying the next property that much easier.

Property Appreciation & Equity

Because the investor is starting with a renovation project, they can buy at a lower cost and do the renovation. The improvements to the property build equity and allow for long-term property appreciation.

Higher Rent Potential

After the Rehab phase of the BRRRR is complete, the investor has a home that is in pristine condition. The property is more attractive, and renters could be more willing to pay a higher rate.

[6]Brandon Turner, "Is a BRRRR Right for You? Check out the Pros and Cons," The BiggerPockets Blog | Real Estate Investing & Personal Finance Advice, September 24, 2021, https://www.biggerpockets.com/blog/brrrr-pros-and-cons.

Cons

Potentially Two Closing Costs

The BRRRR strategy includes two separate loan transactions before the model is complete, the purchase and refinance of the property. Each loan has closing costs and lender's fees involved. Investors must be diligent in finding the right lending partner, who they can trust, to work with on the project.

Possible Low Appraisal

When refinancing, an appraisal on the property is required. There is always the possibility of the property not appraising well. That's why proper planning, doing the correct math, and developing a solid budget when going into the deal are essential.

Bad or No Tenants

In the BRRRR strategy, the pressure is on to have tenants in the home before refinancing, as they want their costs covered and having the property rented is often required by lenders. This added pressure can cause hasty investors to skip imperative parts of the screening process to get renters, not considering that quality returns depend on quality tenants[7]. Investors need to resist the urge to rush through this process and properly screen for quality renters – their income relies on it.

A Rehab is Still a Rehab

Large rehab projects often come with complications. There are many moving parts to the rehab process. Investors must deal with contractors, tackle unknown problems when they arise, work through unexpected expenses, and be able to pivot on a dime. Let's face it, extensive renovation projects are not easy, and investors need to be ready for anything when going in.

[7]G. Brian Davis, "The BRRRR Model: Pros, Cons & What Rental Investors Should Know," Investment Property Tips | Mashvisor Real Estate Blog, February 11, 2019, https://www.mashvisor.com/blog/brrrr-model-pros-cons/.

BRRRR in Action

A Success Story

This chapter is a hypothetical example of the BRRRR strategy in action.

Matt Smith is a real estate investor who has invested in rental properties using the traditional method of buying turnkey rentals. He wants to scale his rental portfolio and is using the BRRRR strategy for the first time.

Matt is looking to invest in the rental-friendly market of Central Texas and has identified a median property to buy. The purchase price is $100,000, the renovation cost is $40,000, and the ARV is $175,000. The property will rent for $1,600 per month.

Property Assessment

Purchase Price	$100,000
Renovation Cost	$40,000
After Repair Value	$175,000
Monthly Rent	$1,600

Matt uses a hard money lender to do a short-term Bridge Loan on the acquisition. The lender will allow him to put only 10% down. With this down payment, plus the closing costs, plus the lender's costs – Matt is out-of-pocket $16,000 at the closing of the purchase.

Buy

Down Payment	$10,000
Closing Costs	$3,000
Lender Costs	$3,000
Cash Out of Pocket at Closing	**$16,000**

$16,000
Cash Out of Pocket at Closing

The breakdown of Matt's loan includes the purchase of the property, renovation cost, and monthly interest on the loan, which, in the case of this example, is $975.

Matt goes on to renovate the property and lease to a tenant. He wants to make sure he is ready for anything and doesn't want to set himself up for failure. Matt decides that to determine his monthly cash flow from the rental, he will account for property management fees, maintenance and capital expenditures, the mortgage payment, taxes, insurance, and a vacancy allowance – subtracting those accounted expenses from the monthly rent. He finds that his net monthly cash flow is about $300 a month.

Rehab

Purchase Funds	$90,000
Renovation	$40,000
Total Loan Amount	$130,000
Monthly Interest	$975

Rent (Monthly Cash Flow)

Rent	$1,600
Property Management (8%)	$128
Maintenance/CapEx (10%)	$160
Mortgage Payment @ 5.00%	$700
Taxes and Insurance	$200
Vacancy (3 Weeks/Yr)	$112
Net Monthly Cash Flow	**$300**

$300
Net Monthly Cash Flow

Matt is now a successful landlord of a rental property. Everything went smoothly, and he hit his ARV at $175,000. He is now ready to move forward with his BRRRR.

He returns to his lender to refinance out of the short-term bridge debt and into a long-term rental loan six months later. With a 75% loan-to-value (LTV) ratio, his new loan amount is $131,250. Once again, Matt pays closing and lender costs and pays off his original short-term bridge loan of $130,000. He also pays $4,750 additional cash at closing.

Refinance

After Repair Value	$175,000
75% LTV	$131,250
Closing Costs	$3,000
Lender Costs	$3,000
Bridge Loan Payoff	$130,000
Additional Cash at Closing	**$4,750**

$4,750
Additional Cash at Closing

Since obtaining his first loan, Matt is now at $20,750 cash out of pocket. With a monthly net cash flow of $300 from his rental property, he is earning a $3,600 annual net cash flow. His stabilized property cash-on-cash return is 17.35%, and he also has an appreciating asset – he's feeling pretty good! Matt is excited and ready to continue scaling his portfolio and repeat the process with another property.

Repeat (Cash-on-Cash Return)

Annual Cash Flow Estimate	$3,600
Cash Out-of-Pocket	$20,750
Cash-on-Cash Return	**17.35%**

Don't Forget!
You also now have an appreciating asset!

When all is said and done, Matt reflects on his first purchase using the BRRRR method and considers what his deal would have looked like had he used the traditional method as he'd done in the past. If he had bought that same property turnkey, his loan would have been at the total $175,000, and with 20% down plus closing costs, his cash-on-cash return would have only been 8.78% – that's about half of what he got using the BRRRR strategy.

Cash-on-Cash Return BRRRR

Annual Cash Flow Estimate	$3,600
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VS

Cash-on-Cash Return Turnkey

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Cash-on-Cash Return	**8.78%**

97%+ Increase Over Cash-on-Cash Return Turnkey!

Conclusion

The BRRRR method is one of today's real estate investors' most popular and exciting strategies. The strategy involves buying, rehabbing, renting, and refinancing an investment property—before repeating the process over again. BRRRR is a proven method for building equity through the rehab process, leveraging the ARV to improve cash flow, and investing in more properties through refinancing.

Although this strategy is not without its risks, potential failures can be avoided by proper planning, research, crunching numbers, and due diligence. With higher percentages of cash-on-cash return, this method is perfect for real estate investors ready to double down on their planning to scale a successful portfolio profitably.

Ready to get started with the BRRRR strategy?

Kiavi provides the intelligence to act, the timely capital to fund opportunities, and the confidence real estate investors need to scale their businesses and unlock the value of America's aged homes.

Kiavi's advanced tech platform removes many traditional barriers, automates time-consuming manual steps, provides quick approvals and true transparency throughout the entire process. We provide robust backing with expert guidance for both new investors as well as seasoned professionals:

Bridge / Fix & Flip Loans

- Competitive rates
- Up to 90% of the purchase price
- Up to 75% of after-repair value
- 100% rehab costs
- 12, 18 & 24 month terms w/ interest-only options

Rental Loans

- Competitive rates
- 5/1 & 7/1 ARMS or 30-year fixed rates
- Interest-only and cash-out options
- No prepayment penalty after year 3

Our team's expertise, paired with a true understanding of today's real estate investors' unique needs and challenges, allow us to play a pivotal role in their investment journey.

Learn More

KIAVI

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