Finding the $10 Bill: Applying Howard Marks' Value Investing to Real Estate - by Todd McIndoo

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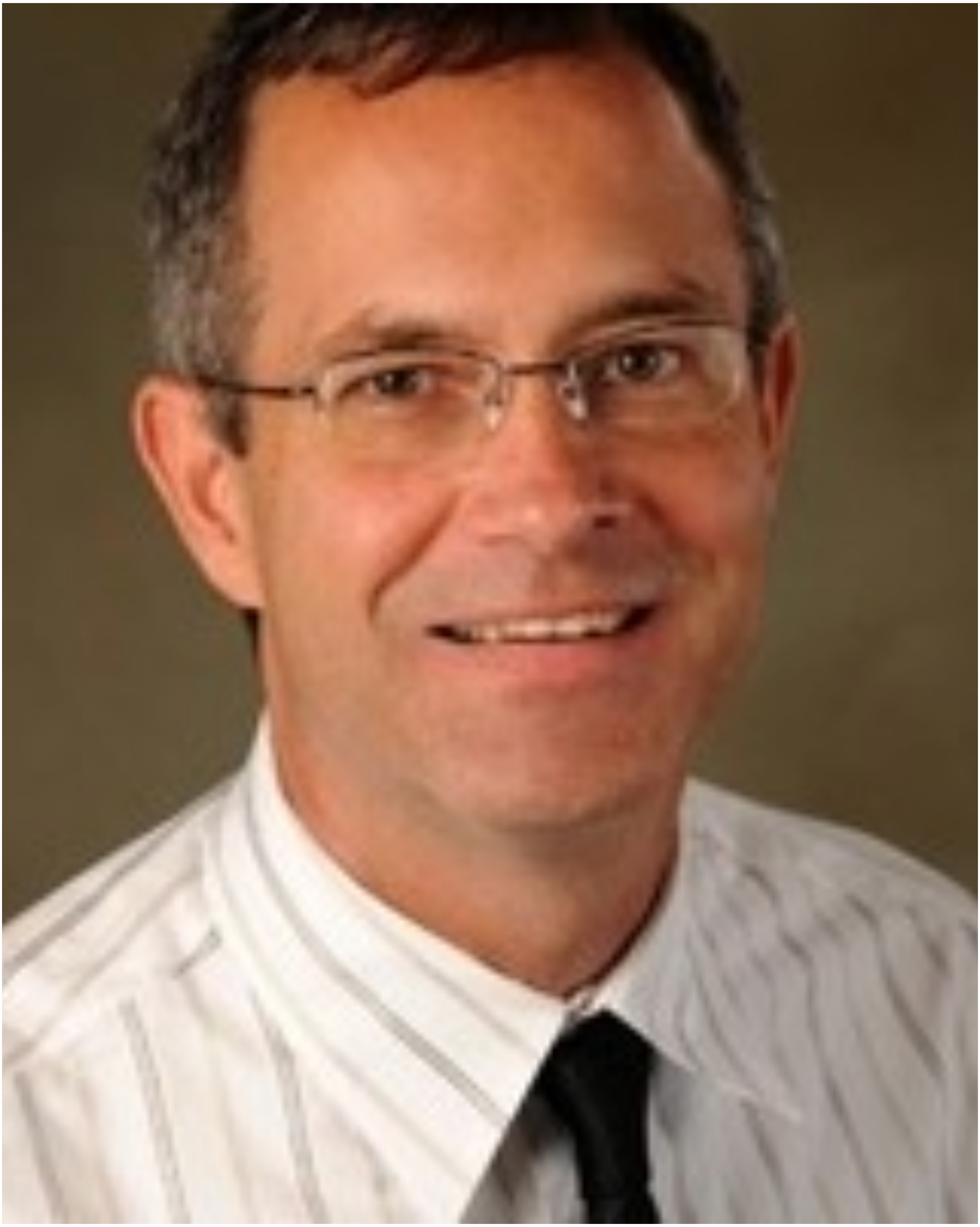

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Imagine finding a $10 bill on the sidewalk. You'd pick it up, right? Howard Marks, co-chairman of Oaktree Capital Management, argues that successful investing is much the same: finding undervalued assets – that $10 bill – and capitalizing on the opportunity. His value investing philosophy, though primarily applied to distressed debt and high-yield bonds, offers powerful insights for real estate investors. With Oaktree managing over $200 billion, the effectiveness of his disciplined approach is undeniable.

Marks' book, The Most Important Thing, distills these principles, emphasizing that successful investing requires second-level thinking, resisting market emotions, and embracing patience. It’s about buying low and selling high, but doing so demands deep insight, rigorous analysis, and the discipline to act when others hesitate.

Marks stresses the importance of intrinsic value. "An asset isn’t an ephemeral concept you invest in because you think it’s attractive… It’s a tangible object that should have an intrinsic value capable of being ascertained.” This means real estate investors must look beyond hype and focus on a property's fundamental worth, not just what someone is willing to pay today.

Finding these "bargains" requires more than just luck. It demands exceptional analytical ability, insight, and foresight. Marks illustrates market inefficiencies with a simple analogy: a professor dismisses a $10 bill on the ground, assuming someone would have picked it up already. The student picks it up. Similarly, astute investors identify opportunities others overlook.

A key principle is understanding the relationship between price and value. "Investment success doesn’t come from ‘buying good things,’ but rather from ‘buying things well.’ No asset is so good that it can’t become a bad investment if bought at too high a price.” Real estate investors must avoid chasing market momentum and understand that even the best property can be a bad investment if overpaid. Leverage, while potentially amplifying gains, magnifies losses, making disciplined investing even more crucial.

Ultimately, successful investing boils down to a simple yet essential principle: "Buying something for less than its value is what it’s all about—the most dependable way to make money.” This translates directly to real estate. Whether considering multi-family properties, distressed assets, or development opportunities, the goal remains the same: buy below intrinsic value. For example, when evaluating a distressed property, investors should analyze its potential cash flow based on realistic rental income and operating expenses, not just its current market price.

As Marks explains, "When you’re buying, it’s important to remember that the value of an asset isn’t what someone will pay for it today, but what it’s worth based on its fundamentals and potential future cash flows.” This means assessing a property's long-term potential, understanding market cycles, and avoiding speculative bets.

Marks' philosophy reinforces the need for patience, discipline, and a commitment to value –

key traits of any successful real estate investor. By focusing on intrinsic worth and resisting market pressures, investors can increase their chances of finding that $10 bill on the sidewalk.

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