

# Dispelling the Myths of Leveraged Investing

Copyright Talbot Stevens, 1999

---

Lack of awareness and understanding prevents millions of investors from taking advantage of one of the best long-term wealth-building strategies that exists.

Leveraging, or borrowing to invest, is a strategy that the wealthy have used to make themselves richer since capitalism began.

Unfortunately, there are several misconceptions or myths that prevent people from openly exploring whether *conservative* leverage makes sense as an integrated part of their financial plan.

**Myth #1 is that leverage is only for the “wealthy”.** Generally the wealthy do act on more powerful wealth-creation strategies like leverage. The fastest way for middle-income investors to become richer is to act on the same strategies that the wealthy benefit from.

**Myth #2 is that all debts are bad and should be avoided.** Expensive, non-deductible debts used to purchase things that depreciate by 20 to 50% per year obviously should be avoided or paid off quickly.

But there is also “good” debt with low interest rates that buys assets that appreciate 10 to 13% per year, and the interest expense is tax deductible to further reduce the cost.

**Myth #3 is that leverage is “too risky for me”.** The reality is that most people who could qualify for an investment loan have probably already leveraged in a much worse way without even realizing it.

Anyone who has taken out a mortgage has already borrowed to purchase an equity investment that has zero diversification, poor liquidity, with low future growth expectations, and the interest expense isn't even tax deductible. Borrowing to

purchase equity investments expected to grow 10 to 13%, with better diversification and liquidity, and where the interest expense is deductible is obviously less risky.

**Myth #4** is that for leverage to be profitable, **investment returns must exceed the cost of borrowing**. Most people rationally think that if your interest expense is 9%, then your investment returns must be higher than 9% or you won't make any money.

The only problem with this rational and reasonable view is that it's wrong. When borrowing to invest in equity investments which are mostly capital gains that are taxed less and, more importantly, tax deferred, the real breakeven point is much lower than most people think. Not only that, but the breakeven point, which defines the risk of the strategy, decreases over time.

Someone in a 40% tax bracket that borrows at 9% interest only needs to earn 5.1% equity returns to breakeven after a 10-year period. This is a little more than half of the cost of borrowing. After a 30-year period, the breakeven point drops to only 3.6% relative to the 9% interest expense.

Until the myths are dispelled, people will not be able to understand and implement conservative leverage as a complement or alternative to RRSPs, to significantly increase *their* retirement fund.

---

Talbot Stevens is a financial educator, speaker and author. For more information, visit [www.TalbotStevens.com](http://www.TalbotStevens.com).