

HOW TO INVEST IN

RENTAL PROPERTY

SO YOU'VE DECIDED YOU WANT TO BUILD A REAL ESTATE EMPIRE...

HI, I'M JENNY.

Historically real estate has been one of the most dependable ways to become wealthy. And many of today's millionaires say it's still a smart investment, for a variety of reasons. Achieving financial security is only possible if you invest your money to let it grow. Your basic savings account won't amount to much, CDs provide mediocre returns, and the stock market is risky. So what's a person to do? Diversifying your investments is the key and investing in real estate is a great way to do it.

"NINETY PERCENT OF ALL MILLIONAIRES BECOME SO THROUGH OWNING REAL ESTATE."

Andrew Carnegie

BUYING YOUR FIRST RENTAL PROPERTY

BUYING A HOUSE TO RENT OUT CAN BE A GREAT WAY TO BRING IN MORE MONTHLY CASH FLOW.

When you buy your first rental property, there is a lot to consider. The type of property, how you'll find tenants, and how you'll manage the property are just the tip of the iceberg.
Lenders look at rental properties differently than your primary residence. They usually want a larger down payment and charge higher interest rates on the mortgage to make up for the risk. You're more likely to default on a home you don't live in than the one you do, especially if you have financial trouble.

Before you buy a second home as a rental property, make sure you have the money saved for a down payment, a contingency plan if you lose your tenants and have to cover the mortgage payment and other housing costs yourself, and a plan to manage the property. Will you hire a property management company or do it yourself?

PROS AND CONS OF BECOMING A LANDLORD

PROS

- You can write off many of the expenses of maintaining and repairing the home as business expenses.
- The net cash flow earned from your rent after expenses can supplement your retirement income or other financial goals.
- The rent collected can offset the mortgage, repair costs, and expenses to run the home while you earn the home’s appreciation.
- You typically don’t have to pay Social Security taxes on your rental income.
- Real estate isn’t as volatile as the stock market and often reacts opposite to the market, helping you diversify.

CONS

- You never know what type of tenant you’re getting, if they’ll be destructive or if they’ll default on their rent.
- You must follow through on a lease even if you need to sell the house fast to liquidate your investment.
- It’s a lot of work maintaining and running a house. Anytime something goes wrong, you are responsible.
- If you invest long distance, you’ll have to pay a property management company which can be expensive.
- There’s no guarantee your investment will appreciate.

CALCULATING RENTAL INCOME

PURCHASE PRICE + NEEDED IMPROVEMENTS + FINANCING & CLOSING COST

= TOTAL COST

MONTHLY RENT — MORTGAGE & FEES — MANAGEMENT COMPANY FEES

= NET PROFIT

“OWNING A HOME IS A KEYSTONE OF WEALTH…BOTH FINANCIAL AFFLUENCE AND EMOTIONAL SECURITY.”

Suze Orman

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STEPS TO BECOMING A LANDLORD

ONE

GET TO KNOW THE AREA

Don't invest in a home without researching the area. When you buy a home, you invest in the neighborhood too. Do your research and find out the average rent in the area, the number of renters in the area, and if the home you're thinking about buying is typical of what the local renter wants.

Just because you love a home and the area doesn't mean renters agree. It doesn't make sense to invest in a rental home in an area where most people buy houses rather than rent. Work with a local real estate agent to find out if it's a good area to invest.

TWO

DECIDE IF YOU WANT A FIXER-UPPER OR A MOVE-IN READY HOME

There’s more than one way to invest. You can buy a home that’s ready for tenants right away or buy an undervalued property that needs some TLC before you rent it out. Before you look at homes, choose your strategy.

If you’re the fixer-upper type, you may save money buying an undervalued property, fixing it up yourself, and renting it out. You will not only earn the rental income, but the home should naturally appreciate the home improvements. If you’d prefer to buy and rent right away, then buying a move-in-ready home is a better choice.

THREE

KNOW RENTAL MARKET RATES

You know what you'd like to charge for rent, but that doesn't mean that's what tenants in the area want to pay. You shouldn't charge more than the average rent for the area, so do your due diligence before buying a home.

A licensed real estate agent or appraiser can help you learn about the area's average rents. Work the numbers to determine if it makes sense to buy the home knowing how much rent you can charge. Is it enough to cover your monthly mortgage payments, 1/12th of the real estate taxes and home insurance, plus any costs to maintain or fix the home?

Leveraging a house-hacking approach? If you rent out rooms but plan to live in the house, you'll also need to determine if the rental income you'll earn is sufficient.

If not, you may want to look for a different home. Investing in a home that doesn't allow high enough rents leaves you upside down from the start.

FOUR
PAY OFF YOUR DEBT FIRST

Buying your first rental property is exciting but expensive too. As the landlord, everything falls on your shoulders. The hot water heater breaks - you're responsible. The roof has issues - you must fix or replace it.

If you have a lot of consumer debt already, you may not have the extra funds to put aside for emergencies your rental home may have. Focus on paying your consumer debt down (or off) before investing in a home for more financial security.

FIVE

FIX YOUR CREDIT

Securing financing for an investment home is a lot different than financing for the home you live in full-time. Lenders view investment financing as riskier, so they usually want borrowers with excellent credit and stable income.

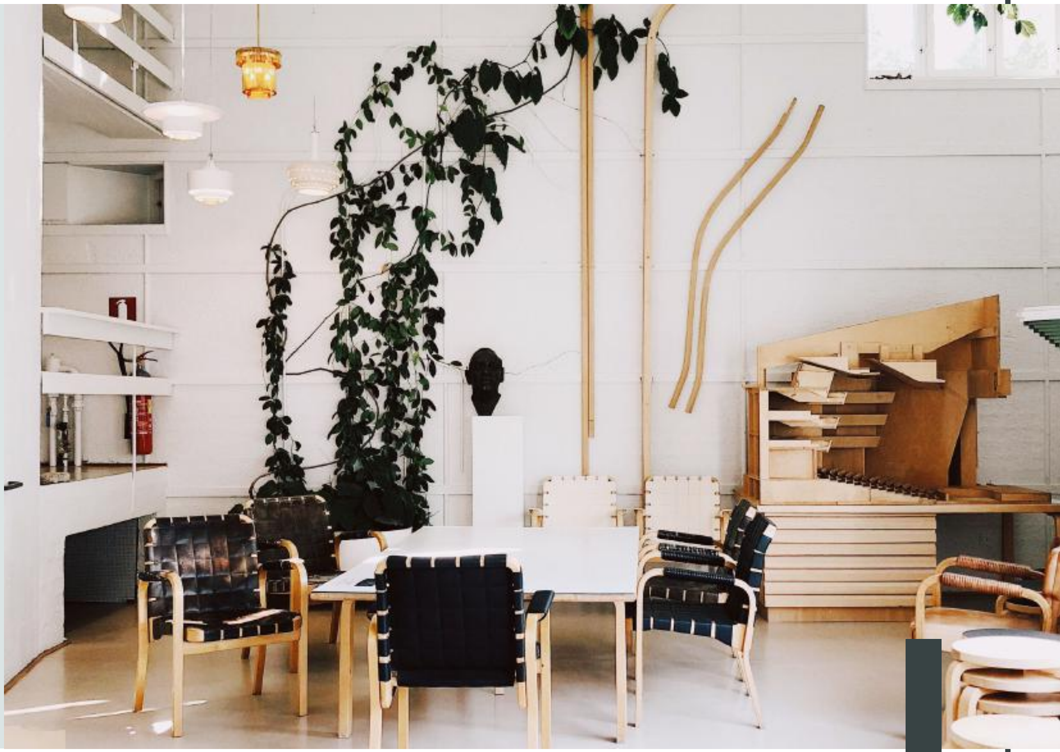
At least a few months before you think about buying a house to rent out, pull your credit and make sure there's nothing to fix. Look for things like:

- ☑ Late payments that you can bring current
- ☑ High credit lines you can pay down
- ☑ Collections you can settle
- ☑ Mistakes you can dispute with the credit bureau

SIX

GET LEGAL HELP

There's a lot that rests on your shoulders as the landlord. Know your obligations and rights before buying your first rental property. Having a lawyer review your purchase, the rental agreement, and your strategy can help you determine if what you're doing is worth it, legal, and beneficial for everyone involved.



SEVEN

FINDING A HELPFUL AGENT

An increasing number of real estate agents are assisting investors with finding their investment property. However, it is necessary to look for a real estate agent that's familiar with investing. They can help you make a much more informed decision.

Real Estate Agents know the local real estate market and have their pulse on new listings. However, there are far more listings than those that are easily uncovered by Internet searches. Agents have access to listings included in the multiple listing service (MLS) AND the agents that deal in income properties can have the scoop about properties coming on the market.

RECAP

Historically real estate has been one of the most dependable ways to become wealthy. And many of today's millionaires say it's still a smart investment, for a variety of reasons.

For one thing, investing in real estate gives you a way to diversify your investments. "Don't put all your eggs in one basket" is tried-and-true advice for a reason. There are a lot of moving parts to the economy, and there's always the chance that one can crash while the others thrive. Having exposure in several different markets helps insulate you from risk.

Secondly, real estate gives you ownership of a tangible asset that can appreciate. While I enjoy logging into my portfolio and seeing my stock values increase, it's all very abstract. There's something appealing about having a physical investment that you can actually see, visit, and improve.

And since people will always need a place to live, real estate tends to hold its value as long as the property is maintained well and the area is appealing.

There's also a decent amount of flexibility when you own real estate. You can decide whether to rent out your property, sell it, subdivide it, rezone it for a different purpose, and so on. This way, you can respond to changes in the economy in a way that still makes your investment useful.

All of that said, there's also a big note of caution here. Real estate can be a large and expensive undertaking, and as the housing market crash of 2008 illustrated, it's never a sure thing. Especially when it comes to real estate investing for beginners, it's wise to proceed with caution. You don't want to stretch your finances too far before you're ready and end up with debt that you struggle to repay.

STAY IN TOUCH

Jenny Post Burton

26062 Highway 17 Suite A
Waynesville, MO 65583
573-586-7711
573-774-2183

www.Post-Realty.com