Stepping Stones Letting

Investment Property and Buy to Let

Simply letting!

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1 Introduction

As with all investments a buy to let property can be a great medium to long term investment or it can be a financial disaster. Making the wrong decision can leave landlords with financial difficulties when mortgage payments need to be met even if there is no rent coming in from the property. However, making the right investment can mean extra income and a stable asset for the future. Hopefully the following will help you make the right decisions and enable you to buy the right property for you.

2 First steps

Buying your first investment property can be a complicated and nerve wracking process. However It can be simplified by answering the following questions.

1. Why are you buying? People buy investment property for numerous reasons and these have a bearing on what property is right for them. Is this going to be a long term investment? If so then you need to look closely at the long term sustainability of the neighborhood and town. Is this going to be your only investment or do you intend to build a portfolio? This may well affect what you buy and how you finance. It may also affect the vehicle you use for ownership. Are you looking for a shorter term investment to provide money for your children? This may mean that you look for a property in an area that can provide large short term growth but maybe not long term sustainability.
2. How are you paying for this? You may be fortunate enough to be able to pay for the property outright. This may well work for you but it is worth investigating the benefits of financing part of the cost. As I will explain later, this can provide you with a better percentage return overall.
3. How much do you want to do? As a landlord you can opt to do as much or as little as you want. It is important though that you understand that being a landlord does entail a certain amount of work. You can limit this by ensuring that the property is in good condition to start with and by employing an agent to handle the day to day running of the property.

By knowing the answers to these questions you can be confident in taking the next steps. It means that you will have proper criteria to search for a property that suits your specific requirements. Once you have this you can move on to the next stage.

3 Do your homework

Investing in property to let is not an instant road to riches scheme. Before you dive in, be prepared

1. Finance. The first thing that you need to decide is how much you want to spend? Most initial investors will look at purchasing a one or two bedroom property with a value in the region of 100k to 200k. However don't be put off if you want to spend more or less than this. There is an investment property to suit (almost) all budgets and, as I will show, the important part is how much money the property will make for you. Once you have decided how much you want to

spend then the next decision is whether to finance part or the whole (80% max) of the purchase price. It is best to talk to a specialist Financial Advisor about this. Buy to let mortgages are far easier and normally quicker to agree than normal mortgages although the criteria for approval is very different to a normal residential mortgage. However you may decide that you are able to and wish to pay for the property outright. I discuss all of this in more detail later on.

2. Decide upon the area. Most Landlords tend to buy in their local area as they are familiar with the market. This is not a bad idea for the average Landlord as they can keep an eye on the property, carry out any maintenance work required, and stay local to their agents.

3. Do your research. All towns have good, bad and middling areas and these change over the years with developments and changes in infrastructure and employment within the town. In the first instance talk to Stepping Stones about good and bad areas for letting. You can ask Estate agents but do bear in mind that they will be working to their own criteria and may advise based on what they have for sale at the time. One of the best ways to research an area is to visit! Take a drive around the area that you are thinking of investing in. Look at the local shops, schools and large local employers. This is normally far more informative than looking at the demographics on the internet etc. Another very good rule of thumb is whether you would be willing to have your daughter /wife /husband /dog etc live there. You may smile at this but most tenants (certainly the good ones that you are looking for) will work on the same basis when looking for a house to rent.

4. The real work begins! Now that you have decided upon an area you need to go and make friends with all of the local estate agents. Tell them what you want and make sure that they know that you have funds in place and that you will not be part of a chain. This will make you an attractive proposition to the agent and hopefully they will call you before anybody else when a suitable house comes on to the market. Remember to stay in touch with the agents. Try to call them once a week. If you can't do this then email them regularly so that you remain uppermost in their mind. Register your search with Rightmove, Zoopla, Prime location etc. By doing this you can make sure that you see new properties every day. To get the bargains you need to be able to move quickly so having up to the minute information is essential.

5. What to look for. Location, location, location! This is one of the most important factors a tenant will look for. Desirable properties are conveniently located for public transport, local amenities, restaurants and bars and have parking facilities nearby. A well maintained and attractive property will be much more in demand than a rundown property. If you decide to let the property furnished, it is worthwhile taking some time to find out what features make a property desirable to tenants. When you are buying the property, try to remember that it is not you who is going to be living there. Look at it with an objective eye. Think about

the property from a tenant's point of view. Talk to Stepping Stones who will be able to advise you on this.

6. To renovate or not to renovate? If you have the money, time and inclination, you may consider investing in a property that needs some work. You'll be able to customise it to the needs of your tenants. If you do not have the time or interest to buy a property that needs a lot of work, a newer property may be more suitable. However, it is worth remembering that even new properties will need maintenance and this will increase as the property ages. Stepping Stones have access to a wide range of tradesmen who we are happy to provide details of and references for.

4 Letting Agencies

The lettings industry is still unregulated and as such there are an awful lot of poor quality letting agents out there. As a first time landlord it is very difficult for you to tell who is good and who isn't!

Here are some pointers that you should be looking for when choosing an agent.

1. Are they members of ARLA or another regulated body? It is always best to find a company that has voluntarily joined a redress scheme as it shows that they are willing to be bound by their complaints procedure and that they have met certain levels of service standard. The main body for the lettings industry is ARLA (the Association of Residential Letting Agents) and you can check on their website if the company is a member.

2. Are your monies protected? ALL agents should hold their deposit and rent monies in a specific client account and this should be protected with Client Money Protection Insurance. This means that if the company goes bankrupt or worse your monies are safe and protected. Ask to see their certificate or ask if they are a "safe Agent". This is an organisation that ensures that their members have such protection in place.

3. Are they qualified? I cannot stress enough how complex the lettings and management business is. There is a whole raft of legislation that needs to be navigated and all managers should be properly trained. Don't forget that these people will be looking after what could be your most valuable investment. You would not trust an untrained lawyer so don't trust an unqualified agent!

4. Who is managing your property? This is a really important one that most people forget when looking at agents. Most agents are very interested in letting the property as they see this as the money maker for them but then pass the boring day to day management to either another office or to the least experienced, youngest member of staff. You need to ensure that you know exactly who is doing what with your house and that they are dedicated to that job. You should have an experienced and trained property manager looking after your house who you can discuss all aspects of the management with.

5. Who does the accounts? Another big one. Do they have dedicated accounts staff who know exactly what is going on with your property? If they use a centralised accounts team they will not know the details of your tenants and rent collection will simply be a process and loses the human intelligence side which is so important.

6. Are they Landlords? Just as you would not trust a driving instructor who can't drive you need a letting agent who has experience of being a landlord themselves. This means that they see the industry from both sides. Someone who is not a landlord can still be a good agent but to get the

best you want someone at management level who has done it themselves!

Until the industry is fully regulated all agents are definitely not equal! I hope that this gives you some idea on what to look for when looking through your options.

Working with Stepping Stones is a great way of entering the letting market. There are a number of benefits in using us:

- We are a specialist residential letting agency.
- You will receive international marketing exposure for your property
- We will handle all of the management from move ins to move outs!
- Agents usually charge between 15-20% of the rental income as their fee. We charge a straightforward 10% with no hidden extras!
- Talk to Stepping Stones to get completely impartial advice on the best place to buy and the best property to buy. We are independent and so all of our advice is 100% impartial.

5 BUY TO LET MORTGAGES

There are increasing numbers of lenders who have loans and mortgages tailored specifically for the buy to let market. These mortgages (also referred to as Residential Investment Loans) …

- will lend up to 15-80% of the purchase price of the property
- are usually about 0.5 % higher than a normal, standard variable rate mortgage
- are available in Long, Short, Fixed and Capped options

Before committing to an investment loan like this, it is advisable to review your current and long-term situation and make sure that you know exactly what you are getting yourself into. You should ask yourself:

- Will I be able to cover my mortgage repayments and insure the property if I have no money coming in from rent?
- Can I afford to lose money/take a loss if the housing market slumps?
- Will taking out a mortgage on this property affect my chances of getting a mortgage if I decide to move house at a later date?

Buying an investment property may be the largest single investment you will make. Below are some hints and tips that can help you understand the process a bit better.

6 HOW MUCH CAN YOU AFFORD?

The price of your new house or flat is just the beginning of the costs involved in purchasing a new property. If you take out a mortgage, then you must add interest into the equation, which can be a significant sum. On top of that, you have the following fees that need to be paid:

Solicitor's fees	£1,200
Searches	£25-150
Land Registry	£80
Solicitor's disbursements	£35
Lending source's solicitor's fees	£300
Mortgage Indemnity Guarantee	£1,400
Lender's valuations	£160
Survey fee	£300
Buildings insurance	£300
Carpeting?	
Decorating expenses?	
Furnishing?	

7 CALCULATING YOUR RETURN.

When buying rental property it is important to know how to calculate the return your investment will make. Below we will discuss and demonstrate some of the most common calculations and figures you'll need to know. You should always do a quick appraisal of any investment before you go ahead to make sure it's worth your while.

When calculating rental yield values you can also examine the effect that borrowing has on your potential returns, e.g. between buying a property for cash or using a buy to let mortgage to fund the purchase.

How much you decide to borrow also depends on your attitude towards risk as we all know that interest rates can go up as well as down. It's really a matter of personal preference and how you see the local economy and cost of borrowing for the future that should influence your investment decisions.

Let's look at a simple rental yield calculation.

Say that you purchase a property for £150,000 and you receive rental income of £700 per month from your tenant.

The yield calculation would be as follows:

£700 x 12 = £8400 per annum rental income.

(8,400 ÷ 150,000) x 100 = 5.6% Annual Yield

So simply put, Yield is the return on your investment expressed as a percentage of what you put in (i.e. If you invest £150,000 and you receive £8400 in profit/income per year, then £8400 is 5.6% of £150,000.)

The above example has been put very simply without factoring in any property maintenance costs insurance and doesn't include any mortgage payments.

So let's look at calculating yield with a mortgage & associated costs.

Let's say you purchase a property for £150,000 but this time you use a buy-to-let mortgage and have to pay for the property insurance and some maintenance costs.

The following are the figures we use to calculate the yield value;

Purchase costs: £1000 (including solicitors fees and insurances etc)
Deposit at 20%: £30,000

Mortgage costs are calculated as follows:

A £150,000 property (purchase price) with a 80% LTV (loan to value) interest only mortgage at an interest rate of 5.5%.

£150,000 – £30,000 = £120,000 mortgage

Monthly repayments are: £120,000 x 5.5% = £6,600 per annum. £6,600/12 = £550 per month.

The gross profit would be;

£700 rent – £550 Mortgage = £150 gross profit per month

£150 x 12 = £1800 per annum.

Now we have these figures we can now calculate the yield value as follows;

Amount invested so far is: £31,000 (deposit + costs)

Annual gross profit is: £1800

(£1,800 ÷ £31,000) x 100 = 5.8% Yield Value on cash amount invested

Looking at these figures you could have bought 5 properties secured on a buy to let mortgages with a £150,000 investment and receive £9,000 in gross rental profits compared to £6,600 using the cash to purchase one rental property.

Because you can now buy 5 properties you will own a larger amount of assets (£750,000) so you will also get greater capital gains if the house price was to rise in the future. If the property rises in value by 10% over the first five years then your five properties will have given you a "value" increase of £75,000 when the one property will have increased by only £15,000.

If you factor in the capital gain then your percentage return is significantly increased. For example if your return against rent is as above but you then factor in a 5% annual property price increase (£150,000 x 5%) this gives a value increase of £7,500 per annum. This is then added to the rental income so annual rent after costs (£1800) plus value increase (£7,500) gives an annual income of £9,300. Take this against the value of the investment (£31,000) gives a percentage return of 30%!

8 SUMMARY

I hope that this all makes sense and that you will find that renting out property is far easier and cheaper than you expect. We pride ourselves on giving a personal, professional service to help you every step of the way. We can visit you in the comfort of your home and talk through the procedures of renting and answer any questions you have regarding our services and how we can help you. You will find that we can tailor our service to your needs and being a family run company we are far more flexible and approachable than our corporate competition.