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7 Fatal Mistakes to Avoid as a Property Investor

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Chapters

1

You Do Not Have a Clear Strategy & Get Easily Distracted

Fatal Mistake 1: You Do Not Have a Clear Strategy and Get Easily Distracted

Too many investors buy because someone tells them the property will go up in value or they will be given a perceived discount, and not because it will help them achieve their goals.

Are you buying for yield?

Speculation on cap growth?

Or to add value?

Too many investors buy without having a clear strategy, or buy the wrong type of investment for them i.e. they want income but buy an off plan property that requires a 30% deposit and 10% buying costs, tying up all of their savings - and do not realise until further down the line. Or buy a buy to let and then realise do not like the idea of being a landlord!

They can also have a perfectly reasonable strategy, which is working for them i.e. buying buy to lets for around £60,000 in their local area, and suddenly get distracted by a sexy new deal, buying a very expensive villa in Dubai, or a discounted apartment in Spain which does not fit into their overall strategy.

Or buying a renovation project without the skills or adequate funds to complete.

It is vital that you plan out your strategy before start buying. I.e. how much time do you want to put into this, how much in terms of funds, what skills do you have, what timescales are you working to?

Too many people go with too wide an investing strategy, for example I know investors who have bought individual properties in 5-6 countries which I would think is too many. They may be good deals, but can be difficult to manage all the legal/tax and finance issues - **I would aim to go with 2 or a maximum of 3 types of investments at a time**, as it is easier to keep an eye on the overall market this way. It is better to become an expert in 2 or 3 markets than spread yourself too thin over 5-6 markets, whether it is buy to let/buy to sell/overseas.

Part of your strategy should also include looking at exit strategies i.e. when do you plan on holding on until - what triggers will make you want to hold or sell?

How soon will / may you want out, and how easy will it be to realize your profits?

For example what may seem an excellent purchase when you buy may be difficult to sell on, which would mean it is difficult to realize your profits. For example purpose built hotels or student accommodation, where you can buy a room may give a good rental yield but not have a strong re-sale value. If you suddenly need to sell up - will there be buyers ready to snap your property/room up?

Or many apartment blocks in UK and overseas are sold purely to investors. This means all may have similar investment strategies i.e. buy to rent or sell, and could be a large number trying to sell at once. This again will affect the re-sale value, purely down to supply and demand.

It is often best to target an area where is a good mix of local owner occupiers and investors - so there will be a good mix of strategies and you will not be competing with many others all with the same strategy.

For this reason it can be better to target smaller developments, as are less likely to attract the large numbers of investors, or investment clubs that look for 30-50 apartments at a time.

Some areas will see an immediate increase in capital growth, whereas some will be more of a case of hold for 3-10 years to see the best levels of growth. You need to be aware of this before buy and also be sure about how desperate you may be for the money you have tied up. If you think there is a chance you may need to call on this money sooner rather than later, **you need to ensure there is a strong exit strategy** or you will become desperate to sell, and therefore not be able to sell at such an attractive price. So considering your strategy at the start is very important – you should consider:

How much do you want to invest?

What are your goals? Over what time period?

How much time do you want to put into this?

What will your exit strategy be?

This should help you get off to an excellent start!

2

Forget Importance of Location, Location, Location

Fatal Mistake 2: Forget Importance of Location, Location, Location

Yes prices may be rising in the latest hotspot at an average of 15% p.a. but remember that is an average.

Within streets you will see huge price differences. I.e. there may be terraced 2 bedroom houses at an average price of £50k going up 10% per annum, and 2 bed new build apartments at an average price of £120k going up 3% per annum within 2-5 minutes walk. So in that area the average across the 2 types of property would be 6.5% - but is significant difference - which is magnified when you have leveraged your investment.

I.e. if borrow 75% on a buy to let mortgage on both:

On terraced property, deposit is £12500, and borrowing is £37500. If house prices go up 10% in year 1, is now worth £55000. So you have made £5000 in equity – therefore your initial £12500 is now worth £17500 – this is a 40% increase.

On the new build apartment, deposit is £30,000, and borrowing is £90,000. If house prices go up 3% in year 1, is now worth £123600. So you have made £3600 in equity – therefore your initial £30,000 is now worth £33,600 – this is a 12% increase. (Clearly we have not taken any other costs in - and for simplicity have not taken yields in to this example).

So there are **big differences in the returns on your money**, in an area where average house price growth is 6.5% and big differences in how much money you have tied up in each deal. You could be getting 3 times greater a return just by investing in a better investment within the same area.

The other area where people get caught out in average price rises, is forgetting that this is not always the most relevant figure. I.e. if you are buying a buy to let, the rental yield in that location is the most important. Is no point buying a very cheap property, where is no rental demand, if want the rent to pay for the mortgage.

There are areas of Scotland for example where prices may be similar for similar types of property - but one will have strong rental demand and one will not.

There are areas of certain countries I will buy in and some I won't - just as there are towns with area that are good for investing in and areas not so good - always look at the specifics and not just the generalisation of an area.

You must either know your areas very well, or have someone you can rely on to check them out for you before committing to a specific location.

3

Do Not Factor in Buying / Selling / Management Costs

Fatal Mistake 3: Do Not Factor in Buying/Selling/Management Costs

I.e. do you know the average buying costs to buy in different countries?

You may expect capital growth to be 15-20% in country X but if buying costs are 12% and selling costs are 7% it will take at least 2 years before you make any money - are there quicker ways to make money? And may have to spend a few thousand on furniture - all this must be taken into account.

If prices are flat for 2-4 years then this would not be a good investment - as would be far easier ways to make money. I am reluctant to recommend any deal where buying costs are this high. For example, it may be better buying where buying costs are around 3%, and selling costs are around the same even if capital growth is expected to be half what it is predicted to be in country X.

Do you know the different buying costs in UK, Spain, France, Cyprus, Bulgaria, Estonia, USA?

In Spain is around 10-13%

UK is around 3%

Cyprus is around 6%

USA is around 5%

Estonia is around 3%

Bulgaria is around 4%

And management costs will vary significantly depending on the type of investment i.e. holiday lets, corporate lets, student lets.

For instance in UK - can negotiate in some areas of the country a 10% flat rate for management of standard tenant. However management for some e.g. student tenants can be as high as 20-25%. Clearly this makes a huge difference to your net yield. The gross yield is less relevant when comparing across different rental sectors.

For example: I have seen student buy to lets advertised as higher gross yields than normal buy to lets eg 8% gross yield - but if management costs are 25% this takes this yield down to around 6% net.

While a normal buy to let with 7% gross yield and 10% management costs, would still give you a net yield of 6.3% ie higher.

It would also often have lower maintenance costs.

It can be the same overseas - short term lets will invariably give higher gross yields, but will have higher ongoing costs – must always factor this in.

So do not get distracted by headline figures giving potential capital growth or gross yield.

And make sure you are aware of the total buying costs and management costs before commit to buying.

4

Buy Buy-to-Lets with Negative Yields Hoping for Capital Growth

Fatal Mistake 4: Buy Buy-to-Lets with Negative Yields, Hoping for Capital Growth

I still can't believe people do this but all over the country I see people marketing and selling unattractive BTL deals.

If your objective is to make a passive income do not buy an asset that will cost you money each month! If you have a good healthy salary, earning a net income may not be as crucial - but I would still be hesitant to buy a rental property with a net deficit unless was very confident on the economic situation and future capital growth of the area i.e. new EU country or regeneration area.

You must also factor in management/maintenance costs, and any potential interest rate rises i.e. in the UK interest rates are very low just now, so will go up at some point - I would always suggest aiming for a minimum of a 7% yield in the UK.

Do not just take the selling agents word for this - and if buying off plan try to see exactly what else is being built around it i.e. right now rental demand may be high but within a year may be oversupplied e.g. many city centres in UK.

Too many buy to lets are marketed on supposed discounts, and potential capital growth with little mention of the rental expected, or inflated rental figures quoted. But **the most important figure in any rental investment should be the rent expected** - as if there is no rental market, this will be a very unattractive investment, and therefore little chance of capital growth unless owner occupier demand.

If figures are not attractive - hold off and wait until improve, or look to other property markets.

5

Do Not Understand the Importance of Opportunity Cost

Fatal Mistake 5: Do not Understand the Importance of Opportunity Cost

Understanding the Opportunity Cost of any decision you make is critical - to ensure you make the best choices to maximise your profits, and ultimately your long term earnings.

While most investors have got involved in property investing because they understand the opportunities to make money – through leverage and capital growth or high yields - I still see and hear of many who do not fully understand opportunity cost and therefore do not maximize their profits.

Remember anyone that gets into property is usually in it to generate money or income - how many deals/properties you own is insignificant - but I meet some investors who feel it is all about buying as many properties as they can and never selling, irrespective of performance or other opportunities.

So what does opportunity cost mean?

Well according to the encyclopedia, "Opportunity cost is a term used in economics, to mean the cost of something in terms of an opportunity foregone (and the benefits that could be received from that opportunity), or the most valuable foregone alternative. For example, if a city decides to build a hospital on vacant land that it owns, the opportunity cost is some other thing that might have been done with the land and construction funds instead. In building the hospital, the city has forgone the opportunity to build a sporting center on that land, or a parking lot, or the ability to sell the land to reduce the city's debt, and so on."

So in property investing terms, if an investor decides to invest £50k in a property in for example Wales, the opportunity cost would be what he could have made by investing in Spain, Ireland or Dubai. Or similarly if an investor decides to keep equity of 50k in a property, the opportunity cost is what he/she could alternatively have invested this money in and the resultant value.

Now again this will depend on your specific strategy - and many people are not too concerned about opportunity cost, they are just keen to buy 1-2 properties that they can hold onto for 15-25 years to use as a pension. That is fine if that is your strategy – but for me that is too broad a strategy, carries risks and is not maximising the opportunities available.

I have always had a philosophy, rightly or wrongly, that I should always be working my money hard. What does this mean? Well as soon as I feel my money has made a significant return and the returns are likely to drop off, compared to other possibilities, then I will look at realising my profits and investing elsewhere i.e. when I feel the opportunity elsewhere is greater than the current opportunity, after costs are taken into account.

The great thing with property is this does not necessarily mean selling, as you can refinance, and invest money elsewhere.

This is no different to any other type of investing, such as buying stocks and shares - you make/lose your money depending on what price you paid, and what price you sold at - although clearly with property there is a good opportunity to earn a regular income as well. If you hold onto a property for 15-25 years you will make money, but most likely there will be a few scares along the way, as the market passes through several cycles!

To be a successful investor, you must know when to enter the market, and leave the market. And the people that do best buy low, and sell high!

I'll give you an example. By doing all my due diligence I bought a property at the right price in the right location, but then sold on within a year of completion as I felt that was the period I would see the maximum returns in - and more importantly, the opportunities would be greater elsewhere over the next 3 years.

So to go through the numbers, I have just sold a property 6 months after completion, that I had bought off plan last year 12 months before completion. I bought at a price that was already £15k below market value based on my research in an area that had little buy to let competition - and no it was not in any city centre in the UK! This was secured with only a £5k deposit. On completion, I put another £28k into the deposit - so tied up £33k of my own money.

There was no stamp duty in this area.

I then put the property on the market on completion - now even with the market slowing down slightly in the area, I sold it for a £23k profit. So I tied up £5k for 18 months, and a further £28k for 6 months, to get back £56k 6 months later.

Why did I sell? Did I consider refinancing?

My first choice would have been to refinance and let out, but the rental would not have stacked up at the new valuation. So while the rental would have stacked up at the price I paid for the property, I felt that I would have had 56k in equity sat not doing very much for me for the next 3 years in this property investment. And I felt that there were better opportunities for my money both here in the UK, in different regions, and in several overseas markets, which would give stronger returns.

How can I tell this?

Clearly when we are looking into the future there is an element of risk and speculation and there are no definite answers - so you are having to forecast as well as you can with the data currently available i.e. how you forecast interest rates, buying/selling costs, supply and demand, employment, the overall economy and market sentiment over the next time period in the markets/regions you are investing/looking to invest in.

I do not forecast huge capital growth in the area over the next 3-5 years, for a range of reasons - the main reason being that the prices are now pretty high compared to the average salary, and the rentals are not as attractive for an investor at the price I sold up at - around 5% gross yield.

As the yield was not attractive enough for me it was best for me to release this equity and find another investment - ie I felt there were better opportunities for me to spend my £56,000 on, to generate more money.

Although opportunity cost can be hard to quantify, its effect is universal and very real on the individual level. The principle behind the economic concept of opportunity cost applies to all decisions, not just economic ones, for example when Steven Gerrard decided to stay with Liverpool, his home club and where he is captain, the opportunity cost was what he could have achieved if he had moved to Chelsea or Real Madrid. In the end he felt the rewards he could achieve at Liverpool would be greater than he could achieve at Chelsea - but clearly this is an individual decision depending on individual goals.

So, in conclusion, what does this mean for a property investor?

Well, I would say always be looking at your equity/investments and looking at how well they are performing. If you have money tied up in a property that you think will go up in value over 15 years - but may not go up for the next 5 years, is this the best place for your money?

It is no different to the stock market, you must keep an eye on market movements and other opportunities.

By working your money hard, and maximizing potential leverage, you can maximize the opportunities out there.

6

Get Distracted by Supposed Discounts Offered by Developers or put off by Surveyors Valuations

Fatal Mistake 6: Get Distracted by Supposed Discounts Offered by Developers, or put off by Surveyors' Valuations.

I was checking over some properties last week, and the first thing the agent I met said was, "How much discount would you be looking for?"

Now what does this mean?

Discount from what?

An already inflated price?

A surveyor's value?

Or current market value?

All 3 will generally be different.

When you see off plans being marketed at 15-20% discounts, remember this is marketing. All this generally means is the prices were too high in the first place, and have had to reduce to sell, or are trying to attract business with a promotion. No different to a shop that cannot shift its stock, and has to have 20% off sales, or even half price sales. Because the Brits love a bargain they often buy at these "discounted" prices - but just because you have got a discount, this does not mean you have bought below market value!

Even the large supermarkets have been accused of putting the prices up one week, and then discounting them the following - is simply a marketing method.

You have bought at market value, as that is what investors were willing to pay.

However, having said this, if you can get a more aggressive discount eg 30-40% discount on off plan due to the developer needing to either prove themselves to the bank, or keen to get their Sales off to a flyer, then this can be an attractive proposition.

The key as always is not worrying too much on the discount offered from the headline figure, but how this new figure compares with comparable developments in the neighbourhood. This will tell you how good a deal you have managed to negotiate.

If can see the development going up in asking price through the development, this can be an attractive proposal.

If someone offers me a discount of 15-20% but the property still only offers a 5% yield this is not attractive, I'd rather buy a property at 5% discount offering a 10% rental yield!

The properties only offering a 5% yield, for me are still too expensive for their local area ie the local population cannot afford to buy here currently, so hard to see much room for any capital growth.

Remember the value a surveyor gives a property will often be different to the value a buy to let investor, who is more interested in yield, gives a property.

I'll give another example of the differences in different markets. Over the years I have targeted areas in the UK where yields are strong and capital growth is still strong – although is getting very competitive. Around the mid 2000s, properties that were being valued by a surveyor at £40,000 were selling on the open market for nearer £50,000 in these areas. Why was this? Well because yields were so strong, and demand was higher than supply, and the local population could comfortably afford these prices.

So again, you have not paid above market value, you have paid market valuation. This is often the case in a fast growing market, where surveyors look at historic data and do not grasp fully the value to buy to let investors, in this country and overseas.

I know I'd rather be buying in a market where market valuation is 10-15% above the surveyed valuation, rather than 10-15% below it, as this is a very good indicator of future prices and values.

These discounts should not be confused with genuine distress sales, where one offs will come up, where the seller is desperate for a quick sale and will sell for below the market value, or as discussed where you can get an aggressive discount by buying for cash, or buying at the off plan stage – here I would want a minimum of 30% discount.

So I would say take any discount with a pinch of salt - always look at the actual figures paid, the yields, and the comparable prices in the area when making a decision.

7

Forget Importance of Cashflow

Fatal Mistake 7: Forget Importance of Cashflow

"Cash is the oxygen that enables a business to survive and prosper, and is the primary indicator of business health. While a business can survive for a short time without sales or profits, without cash it will die."

I spoke to an investor 6 months ago who told me he was asset rich but cash poor.

What did he mean? He had bought several investments off plan, and several low yielding deals which he hoped would have good capital growth. Therefore while he had several good assets on paper, these assets were actually costing him money each month, meaning he had a negative cashflow.

This can be ok, if some areas of your life, or investments, are making a positive cashflow to balance this. However this investor did not have this, and he ended up being forced to go back to work, and selling a couple of these low yielding assets for a loss – as he was put in the position of being a desperate seller - that is, desperate for cash.

It is crucial to always be aware of how important cash is when running a business - which property investing is!

The reality is that without cash, you won't last very long. This may seem obvious, however it is very easy to buy assets, and then realize you do not have enough money coming in each month – which can leave you in a very difficult position.

Property investors must try and plan and prepare for all potential future events and market changes. This can include interest rate changes, economic changes or market sentiment changing, as well as changes in your personal life which you may not immediately associate with your property investing - such as promotion at work, or worse, being made redundant, or having children which can all make big changes to your cashflow as a whole.

So I would suggest, **the most important aspect of planning, for a property investor, is not expected capital growth, historic data, cost of borrowing, or yields but is effective cash flow management.**

Failure to properly plan cash flow is one of the leading causes for failure. I know how tempting it can be to overstretch yourself and put all your liquid cash into assets - and then due to an unexpected, or more likely unplanned for, poorly performing asset, find yourself over budget and desperate for cash short term. You then are looking to borrow cash, either through loans, or overdrafts at less acceptable interest rates.

However if this runs out you can be left with difficult decisions that are forced onto you by poor planning. This usually involves selling an asset, at a price below its value, as you are desperate for cash short term to support your property investing business overall.

Cash flow serves several purposes.

Firstly it is used for meeting normal cash obligations such as paying mortgages, buying costs, development costs and covering voids.

Secondly, it is held as a precautionary measure for unanticipated problems. This is the area that usually is forgotten by investors. A cash reserve should be available for these unforeseen problems - this can be actual cash, or a flexible mortgage or overdraft, but must be available.

Thirdly it is held for potential investment purposes. The term "cash" refers to those assets that are liquid and have immediate cash redemption value.

There is not a problem with buying a property or land that costs money in the short term ie a plot of land to develop on, or a property off plan, indeed this can be very profitable - but it is clear that this will not generate cash in the short term – and therefore you must make sure this is properly planned into your overall strategy.

I always think it is important to have a good level of cash generating assets - ie generating more money than the costs involved with borrowing and maintaining the asset.

This gives you a positive cashflow which can help balance out less well performing assets, or can be held in reserve for emergencies or future investments.

The other attraction of holding cash positive assets is that if you are ever forced to sell an asset due to an unexpected change in your professional or personal life, there should always be demand for cash positive assets, and therefore you should be able to sell this on relatively easily.

For example, if a property development you are carrying out goes wrong or over budget, and you need extra cash - if you own a buy to let in the UK which is generating a gross yield of over 8% - or a net yield, ie after all costs, in any country of at least 2% - then this should be attractive to other investors and you should find a buyer relatively easily or be able to refinance this asset, which should generate cash quickly.

It is no surprise that when you go to the banks requesting more money, they want to know your monthly cashflow - they need to see from your projected monthly cash flow if you will have the capacity to repay the loans or mortgages.

So when you are forming your property investing strategy – ask yourself the following questions,

How much cash will my assets generate? How much cash is required each month? How much cash do other areas of my life require? And how much do they generate?

I.e. if you have a high paid job which you enjoy, which generates a high positive cash flow, or you already have assets generating extra cash on a monthly basis - you may be able to buy assets that will not generate money in the short term, as you can cover any short term costs, or unforeseen circumstances. You may therefore want to look at a longer timescale, and may go into property development, buy into a property fund, buy a plot of land – where you are comfortable tying up this money for a period of time, confident that it will rise in value, and you will have no short term need for this asset which could compromise the value.

If on the other hand you are pretty stretched already for cash on a monthly basis i.e. say cashflow neutral, you may well want to buy an asset that immediately will generate cash, or at least as soon as the mortgage, borrowing costs start i.e. a more traditional buy to let.

There are many ways to make money as a property investor – but financial planning is always key to ensure your cashflow stays positive to allow you to grow your property investment business.

Well that was the last part of your free course - well done for getting this far! I hope you have found it useful.

Good luck with all your future investing!