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Investment Property Guide

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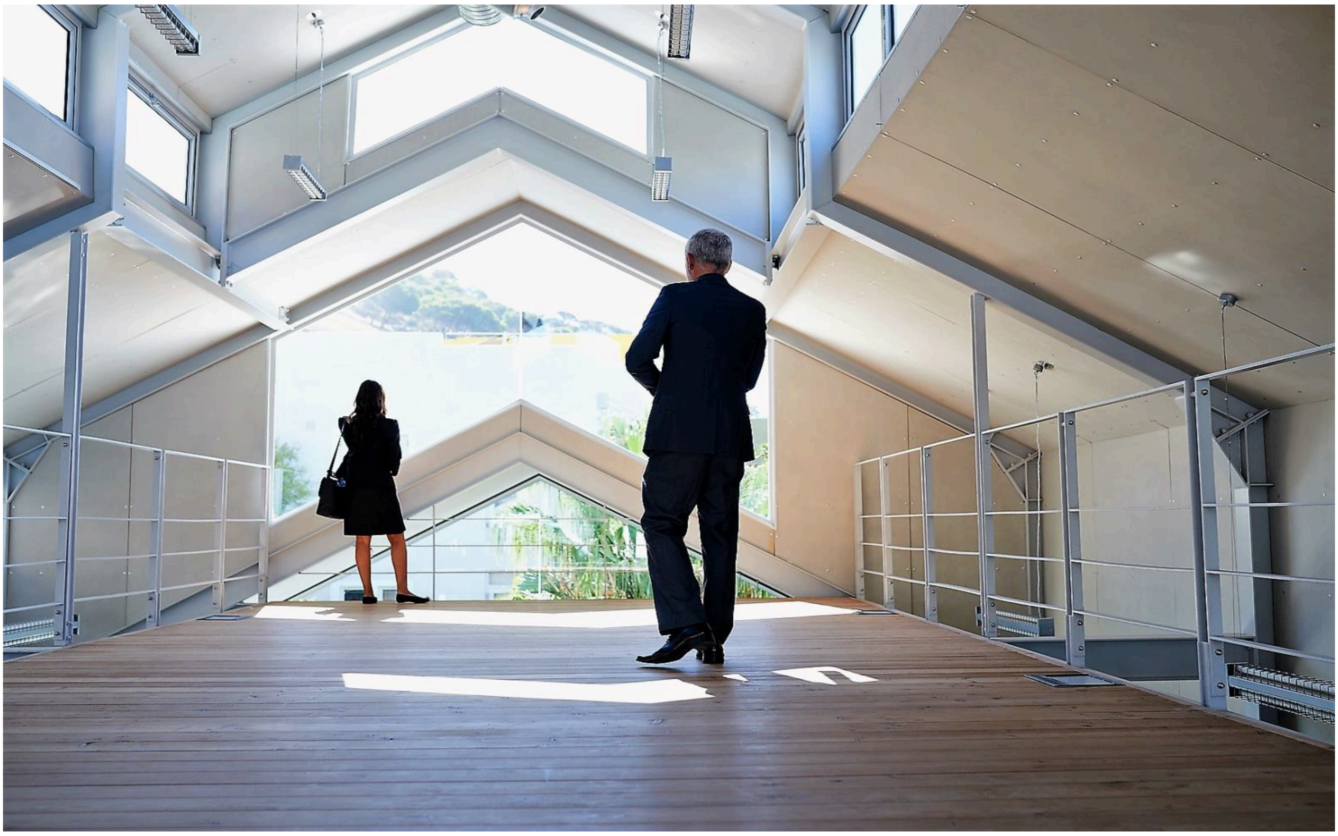

Ready to invest in property?

Owning an investment property with rental income coming in each month is a clever way to create a consistent, yet passive, income flow.

While this concept is no secret, the details in relation to this investment option can be confusing. Some lenders require you to have a certain amount of cash available to contribute towards the purchase, while others accept a deposit in the form of equity accumulated in another property.

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GUIDE TO FINANCING AN INVESTMENT PROPERTY

Investment property loans are available in several different structures. Despite the many investment property mortgage options that exist, choosing the wrong loan type can be just as detrimental as choosing the wrong investment property.

A great mortgage Broker will guide you through every option available to you before you approach a lender, making it easier for you to make the right choice.

An important point to make is that if you are using your own home as a deposit for your investment property purchase, you must understand the risks associated.

Alternative number one - a conventional bank mortgage

If you have previously purchased a property and it is your primary residence, it's likely you are already familiar with the conventional home loan process. With a traditional mortgage, the expectation for a deposit can vary between 5% - 30% of the property value. This variation is determined by a particular lenders credit policy. This deposit may come from personal savings, or perhaps they are gifted funds. Either way, most lenders require a form of documentation to prove the origin.

With a traditional mortgage, the lender uses multiple forms of information to determine whether they will grant an approval or not. This includes your credit rating, credit score and your credit history. Lenders will also require evidence of your income, your expenses, and your assets to demonstrate your capacity to service the mortgage.

This is also the case with an investment property loan, however, in addition, your lender will seek to determine the rent that you will be charging to establish whether the debt to income calculations fit within their credit policy. Many lenders will also expect the borrower to have additional funds set aside to cover the first 3 months of repayments.

Alternative number two - a line of credit or short term finance

It is not uncommon for a property investor to implement a strategy to only hold their investment property for a short period. An example of this may be when an investor purchases a property, spends 3 to 6 months renovating the property, and puts it back on the market. In this case, an investor can secure a line of credit against their existing property provided the property meets the
lender's guidelines, and the property has sufficient equity available.

Alternative number three - using the equity in your home

If you intend to purchase an investment property as a long-term rental, using the equity you have accumulated in your home is a popular way to achieve this. In many cases, lenders allow borrowings of between 70% - 80% of the
investment property value.

Depending on the economic climate and a lenders credit policy, you have multiple options available in terms of how you structure your loan. For example, you may select an interest only repayment period, or prefer paying off the principal and interest. The option between having a fixed rate loan, a variable rate loan, or a floating rate loan are also popular considerations.

Investors may choose to structure their loan as an interest only loan. This will mean the repayments are very low. An investor may choose this strategy with the view that if there has been capital growth, the investor can sell it at a profit while only ever absorbing with borrowing costs, for example home loan interest repayments.

Determining your investment budget

Prior to making the decision to invest in residential real estate, it's important to review your budget to determine what level of debt you're able to comfortably manage. This will also give you the opportunity to determine whether you can afford the repayments during period where rental income is not received.

Investing in residential real estate is generally viewed as a long-term commitment. By considering any anticipated income or lifestyle changes that may be on the horizon, you can avoid any scenario that could trigger a premature sale of your investment property due to cash flow issues.

You will find many valuable online resources including online calculators featured on most Bank and lender websites.

Cost-effective mortgages on investment properties

As the value of your property and the rental income you receive increases, the nature of your borrowings become more cost-effective. The growth in the value of the property is referred to as capital growth. In the immediate short term, you may see considerable value in the investment property of your choice, but this does not negate the need to establish a correctly structured
mortgage loan to suits your needs.

As economic conditions and interest rates can change quickly, and at times, personal circumstances fall out of your control, many people prefer to lock in a fixed rate loan to reduce the risk.

Investment property cash flow analysis

When it comes to potential real estate investment, it is a sound and prudent step to conduct a cash flow analysis on your potential investment choice. You should look at the costs involved in purchasing the property, the anticipated loan repayments, the costs of ongoing maintenance in comparison to the rental income you expect to receive. Once considered, you will be able to
determine how much money you need to outlay each week, or by contrast, the profit you will receive as a result of positive cash flow.

Your weekly cash flow is determined by subtracting your total weekly ongoing costs from your gross rental income. Remember, it's important to consider periods of time where you may not receive any rental income. This may occur when the property is between tenants, or while you're completing renovations. You'll also need to take into consideration any legal fees payable, real estate fees payable, and the costs associated with building inspections.

Appropriate insurance for your investment property

Insuring an investment property is one of the most important purchases a property investor can make. Protecting you in a similar way to your own home, investment property insurance will provide you with peace of mind by reducing the risks associated with owning an investment property.

You will need to include the cost of investment property insurance into your final budgets analysis. Whilst each insurer has a unique policy offering,

Investment property insurance, otherwise known as landlord insurance, generally covers the cost of any damage that may occur to your property as a result of an unforeseen accidents such as fire, theft and storm. The policy is likely to include a component relating to your tenants. This may include cover if tenants deliberately damaging your property, default on their rental
payments, or theft by your tenant.

Mortgage protection insurance is a form of insurance which can cover you in the event you're unable to make your home loan repayments. Mortgage protection insurance may cover your home loan repayments in the event of death, terminal illness or loss of employment. If you claim on an insured event, the funds may be paid directly to your home loan, or paid to you personally.

Lenders mortgage insurance is an insurance policy to cover the lender in the event you default on your home loan. Lenders mortgage insurance will not cover you in this instance. It is often a mandatory requirement that is enforced by the lender if you're unable to provide a large enough deposit in comparison to the value of your investment property purchase.

Important note - Prior to arranging any insurance cover, it is important to ensure sure you read the fine print to confirm you're confident and comfortable with the level of cover provided by the insurance policy.

Summary:

Historically, property growth is far less volatile and certainly more predictable than many other investments options. For many, the purchase of an investment property has meant an additional income stream, often continuing well into retirement. Buying the right property in the right area can usually influence the success of this investment strategy.

I specialise in helping clients secure the best available investment property loan that is suitable for their circumstances.

If you would like to receive detailed information that is suitable to your circumstances, please don't hesitate to contact me either by phone, email or skype.

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