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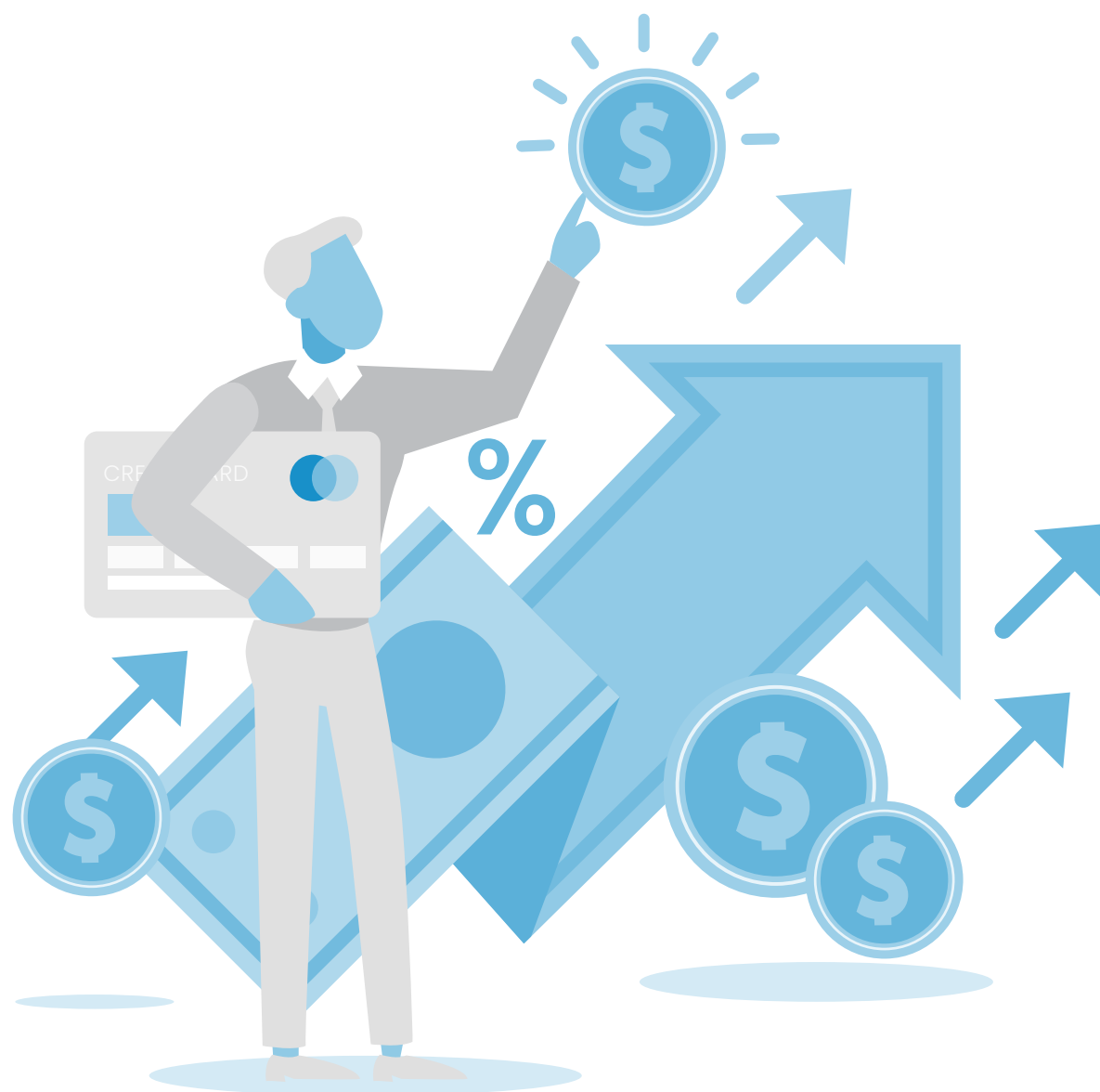
MUCH PROFIT

SHOULD YOU MAKE

ON A RENTAL PROPERTY

INVESTMENT?

Real estate will likely be one of the largest investments in your portfolio. High risk can lead to high reward—but only if you put in the time and research to understand your market and the numbers behind your investment. Good investments require analysis, and you should have a solid understanding going into any real estate deal of what you can expect from your investment's return. Setting unrealistic expectations for your return on investment (ROI) can set you up for failure and hurt your profit. Most real estate investment strategies tie up large chunks of money for quite some time, so you need to weigh the pros and cons between committing for the long haul or finding a property to flip. Setting realistic expectations for property value and cash flow will ensure your investment turns out to be a great deal.



DETERMINING PROFITABILITY OF REAL ESTATE INVESTMENTS

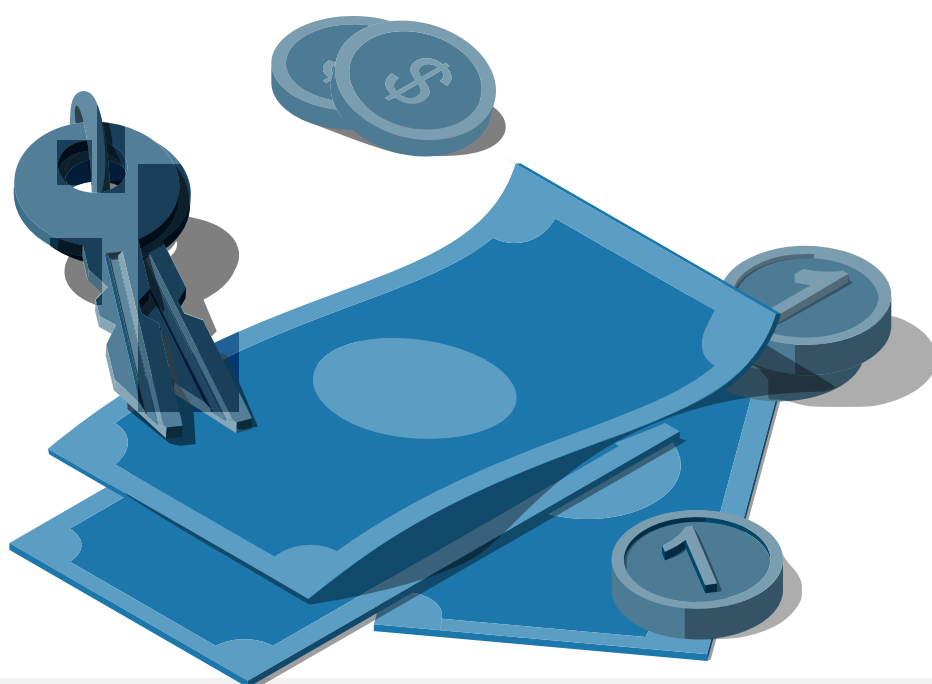
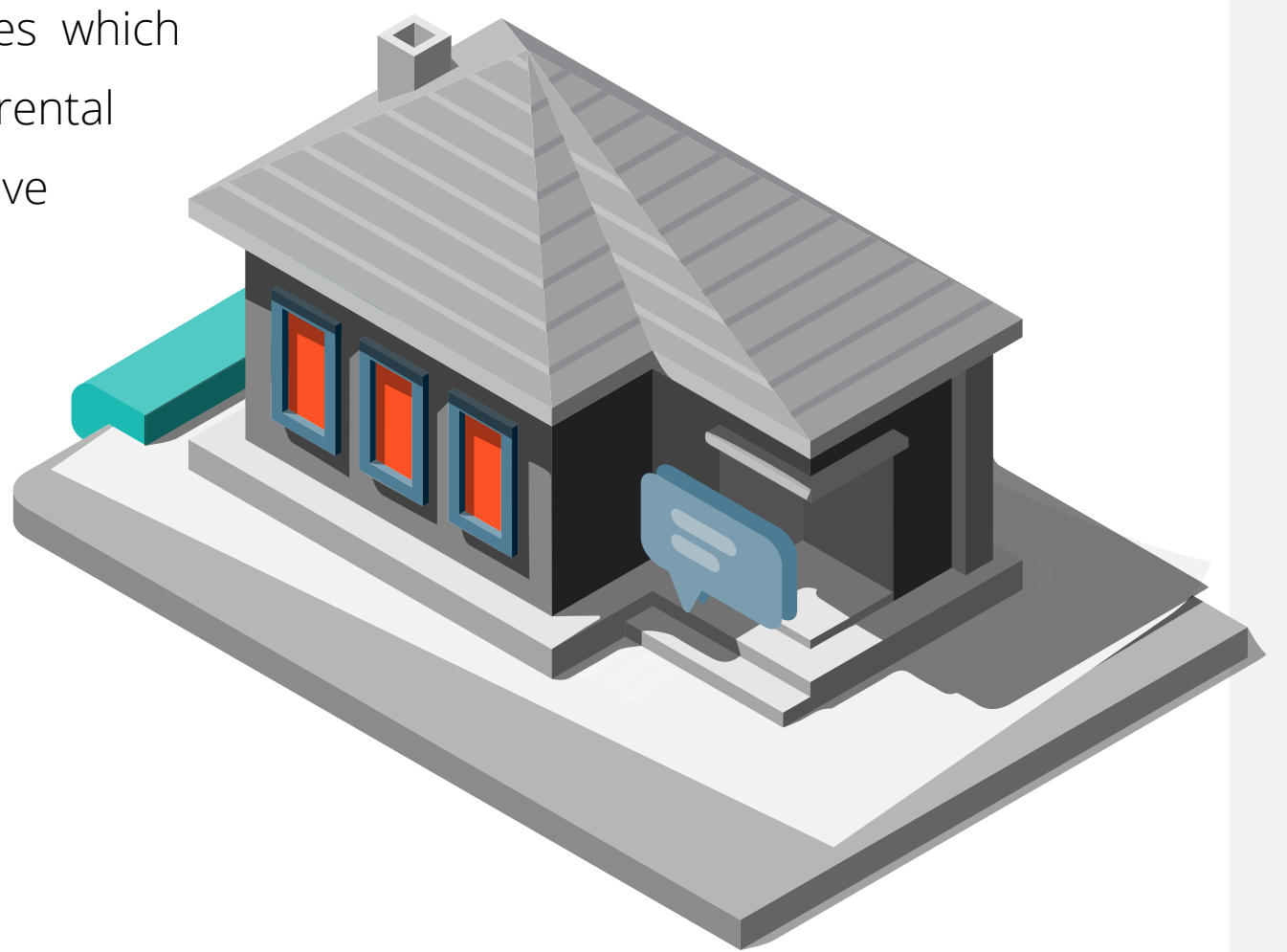
A savvy real estate investor always buys investment properties that yield a good return on investment. After all, the main goal in real estate investing is making money. Thus, what's the point of investing your money in something that brings little or no profits? Beginner property investors often ask themselves "With the thousands of rental properties available in the market, how do I determine which ones make profitable real estate investments?"



REAL ESTATE INVESTMENTS

Location is an important factor that property investors should take into account before making any investment decision if they want to succeed in the business. Location determines many aspects related to real estate investments, mainly supply and demand – which is the first thing that affects the profitability of rental properties.

The best locations to buy an investment property are where demand for real estate investing is higher than the available supply of properties. In such locations, a real estate investor enjoys high occupancy rates which further lead to a high rental income. Therefore, if you live in a real estate market with these characteristics, chances are you'll find profitable real estate investments that are worth investing in.



TYPE OF REAL ESTATE INVESTMENTS

The real estate investing business offers numerous types of investment properties, some of which are more profitable than others. There are residential real estate investments, commercial real estate investments, fixer-uppers, etc. However, what determines the profitability of a certain type is also closely related to its location. For example, a real estate investor investing in a market increasing in population might find residential rental properties (like multi-family rentals) more profitable than commercial rental properties.

Return on Investment:

Since profitable real estate investments are those that yield a high return on investment, property investors need to know how to calculate the ROI to make smart investment decisions. There are a number of calculations needed to determine the ROI, most importantly are:

Cash-on-Cash Return

Cash-on-cash return (CoC) is a widely used metric for calculating real estate investment profitability. It measures the yearly return on an investment based on cash invested and net operating income. CoC will vary greatly depending on your financing method, such as whether you bought a property with cash instead of using a loan. According to most experts, aim for a CoC that yields between 8% and 12%.

TYPE OF REAL ESTATE INVESTMENTS

Capitalization Rate

In real estate, capitalization rate (aka cap rate) is the ratio of net income to the purchase price of the property. For example, a \$200,000 property that you rent for \$1,500 per month would lead to a net operating income of \$12,000 each year. This equates to a capitalization rate of 6%. A successful cap rate depends on a variety of factors. In a less desirable neighborhood with risks or safety concerns, 6% might not be worthwhile. But in a high-demand neighborhood with reliable tenants, 6% might be a great return.

Cash Flow:

The difference between monthly rental income and monthly expenses of an investment property. It comes in the form of monthly rent collected from tenants and it could be positive or negative. Obviously, as a real estate investor, you always want to invest in positive cash flow investment properties. Negative cash flow means you can't keep up with your expenses to make profits.



ANALYZING WHETHER A RENTAL PROPERTY IS A GOOD INVESTMENT

While real estate investment has significant benefits, that doesn't mean you don't face hardships and challenges along the way. Having a solid understanding of your financial situation and the potential of the property you're interested in is crucial, but you'll also need to consider the unexpected expenses that are likely to arise.

Will you take care of the property yourself and manage any tenants? How will you prepare for an emergency repair like a burst pipe or leaky roof? What are your long-term financial goals? All of these questions will ultimately impact the profitability of your real estate investment.



ANALYZING WHETHER A RENTAL PROPERTY IS A GOOD INVESTMENT

Here are a few other factors to keep in mind when evaluating an investment opportunity:

Initial investment: How much money will you be putting up and for how long? An amazing ROI might not be worth it if you're spending every penny of your savings to purchase the home, leaving no room for error.

Property condition: If the property is going to need significant repairs or updates in the near future, calculate these costs into the purchase price of the home.

Rent-to-mortgage ratio: If you're investing in a rental property, do the math to make sure the numbers have you coming out on top. If the expected rent payment is not going to cover your mortgage, insurance, taxes, and association dues, then it's not a good investment.

Property location: You can change a lot of things about a property, but you can't change the neighborhood it's located in. Even the nicest house in the worst neighborhood might not turn out to be a profitable investment.



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