Apprentice Property Tycoon

Lesson 4

by

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Welcome to the fourth lesson of **Apprentice Property Tycoon.**

Let me congratulate you on taking this next important step on your path to **total financial freedom through property wealth**.

I now have confidence in you.

You are still one of my Apprentice Property Tycoons hanging in there, proving to me you could be made of the 'right stuff'.

I'm beginning to believe you just may be one of the few special people who don't merely dream and drift through life trusting in blind luck.

As you know, property dealing has nothing to do with luck. It's a proven concept. As an Apprentice Tycoon you are being trained in the real inside secrets used by those 'in the know' revealing how you can create a million pound property portfolio for yourself from scratch.

Remember, once you are on the inside and 'walk the talk' you'll have access to an 'inner circle' of deals which the general public never get a sniff of. As a property tycoon you will often buy at 10%, 15% even 30% UNDER market price, thereby locking-in an automatic immediate profit.

You'll have access to almost unlimited money to fund your projects as the banks are never short of money – they are just short of good deals.

They have literally hundreds of millions to lend. You will not have to go 'cap in hand' to some doofus mortgage broker begging for a loan against your salary.

All of this, when I know you have grasped my real estate 'inside' knowledge and stand out as heads above the average Johnny Lunchbucket 'home-buyer'.

Just one of my Apprentices built himself over £1.5million of property portfolio (half a million equity!) in just 12 months. That is quite do-able.

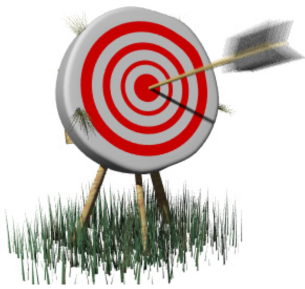
This lesson I continue teaching you my inside secrets – hard won through my years in property. But, before I launch into more property secrets, consider this important question…

Do you know how much money you want to make?
If you don't, then stop and work it out NOW!

This is very important because...

...not knowing will adversely affect the property buying decisions you make and the actions you take.

Before you even *start* property dealing you need an exact target to aim for – this will just be your first target. As you progress other, more ambitious targets will follow.



I'm talking about a <u>financial target</u>. You don't necessarily need one million pounds to set yourself free from the 'rat-race'- in many cases, far from it.

So, how do you set your first financial target?

One simple way is by taking your existing gross annual salary and multiplying it by 20. This is the amount of money that if you put in a building society, you could live off the interest and retire.

Let's take an example: John earns £20,000 before tax and is reasonably comfortable on this. 20 multiplied by £20,000 = £400,000.

If John invested this in a long-term high interest bank account, shares or equivalent fairly safe investment, it should provide him with approximately £25,000.00 income a year, pre-tax.

He could set the figure at £400,000, as his first target, that would be the amount he wanted to make from his first set of property deals. But this is quite high and there's no reason for him to leave his job at this point.

If John made and extra £100,000 from his first deal, I reckon he'd be fairly pleased! That is, after all, five years worth of normal salary.

If he slashed his figure from £400,000 to £100,000, it certainly sounds a lot more achievable than before. So, John's first financial target from property dealing would be £100,000. When that was achieved he would set his next target, which might be, say, £200,000.
Here's what you do NOW…

Set your first financial target from property dealing.

Don't worry about *how* you're going to accomplish your target, that will come once you are up and running.

When a financial target is achieved, you will be ready to reassess your situation and set a new target. As you realise what you can achieve your expectations will probably go higher.

There is no right or wrong figure. You are in charge. You decide how much you want to earn each time you set your next goal. Your financial goals are not the same as mine or anybody else's.

Each goal you set will drive you towards property deals that will create the financial returns you want.

When you are buying like a property tycoon - as an informed buyer – you will find setting explicit financial targets acts as a great incentive towards achieving the financial rewards that give you the lifestyle YOU want.

I want you to be clear about this - this lifestyle is totally UNIQUE to you – it's the life YOU want.

This lesson I am taking you up to the next level – from 'dabbling' to '2-type property dealing'.

I am going to tell you all the inside tips and know-how for buying property to let and what you MUST know about letting before you can create a successful rental portfolio.

So, forget about washing the car, or mowing the lawn and get down to the nitty-gritty of carving out a better tomorrow for yourself – read my words NOW with 100% concentration.

The media would have you believe that it is easy to make money from property. Buying it, renting it, developing it and making a profit from resale. As usual they are hopelessly inaccurate in their quest for a story.

As I write this, the number of people buying a property to let has increased drastically over the last few years because of all the hype - and the result has been many people getting their fingers badly burnt. Even your window cleaner and taxi driver will be boasting about their 'Buy To Let' portfolio! They could get badly burned if they are not careful.

Make no mistake, property alone has created many of the world's wealthy, but it is an area full of traps for the unwary and ill-informed.

It's important you understand how to make money in property - no matter what is happening with the economy.

Financial analysts can and do predict the rate of inflation and vary interest rates to stabilise an economy. But nobody can know with absolute 100% certainty what the economy will do for the next few years.

However property dealers know more than most…

Absolute fortunes are made by cunning entrepreneurs buying run-down property in recessions and then renting them out until the boom times return and then selling them.

Commit that paragraph to memory. It is the KEY to making money even in a recession. Think about it for a minute. You don't think property tycoons wait for a bull market before they do any deals? No, of course they don't. They are in the business of making money – not sitting around for ten years waiting for the 'ideal' moment to clinch the 'perfect' deal.

I'll explain in more depth…

Can you guess what is the main question people buying houses ask?

It's this…

'Can I afford the monthly payments?'

This is **vitally** important to you. The question they ask is not so much about whether the property is worth the money or how the mortgage will be paid off or what the long term growth prospects are (surely the key question with any investment?). Generally, as long as the monthly payment fits their budget they're happy.

And what determines affordability?

Interest rates.

If interest rates go up, the monthly payments get higher so fewer people can afford to buy and people look at renting instead of buying.

Once you grasp this, you view the property market in an entirely different way to most people. You can judge when there is going to be a boom time for letting property (and a boom time for selling).

I wonder if you know which group of people rent more than any other group?

There was a clue in what I told you above about the reason people turn to renting…

It's potential first-time buyers.

These are young singles, or couples (including students) who are just starting out and are faced with 3 main options. They can choose to…

1. Live at home with parent(s)
2. Buy their own first home
3. Rent a home

If they don't have a deposit (many first-time buyers can get a 100% mortgage but obviously this raises the monthly repayments on the mortgage) or have poor credit rating the option is to rent. Both of these considerations directly affect the answer to their main question of "Can I/we afford the monthly repayments?"

Let's take a look at you in the role of buying a house for letting out.

Did you realise that purchasing a house so you can let it gives you the edge over normal buyers who just want the place to live in themselves? **It puts you in a strong position to buy at a lower price.**

This is because every seller's worst nightmare is the house-buying 'chain'. They want to buy another house and move to it, but need a buyer for their property to achieve this. If their buyer also has a house to sell and the sale falls through, they have to drop out and the original seller is left with no buyer. If you've ever bought yourself a house to live in, you'll know the nightmare of finding something suitable. You have to look at dozens of lame houses before you get just the right place. To lose that place due to a problem in the chain can be heartbreaking.

Every house seller's perfect buyer is the first-time-buyer because they do not have to sell anything first! As a buy-to-let purchaser you are like the first time buyer - you do not have to sell a property before you can purchase.

This is important. Remember this…

As a buy-to-let purchaser, you are in the strong bargaining position of being (as far as the seller is concerned) a first-time buyer!

And…there will always be a large number of people that choose to rent rather than buy. There are lots of reasons for this. Many of the people I have let property to are working on a temporary contract (maybe a year) in the area and are not sure if they want to settle down in this area. There are lots of other reasons for preferring letting over buying. Here's another one. Some people really do not like doing *any* maintenance on a property. They want to be able to telephone a landlord if a light bulb needs changing! To them, renting is perfect.

But what can you expect to earn from letting property?

First, it's important to understand that expected yields (income) vary between different types of property.

Don't make the mistake of thinking that the larger the property value, the larger the percentage of that value you can get in rent! It's actually the other way round.

The reason being that there is a higher demand for smaller properties as most of your target audience will be 'first time buyers' looking to rent for a while until they can save a deposit or whatever.

Look at the following table:

Average rental incomes as a percentage of the property value

Furnished Bedsits	19.3%
1-Bedroom Flat	12.5%
2-Bedroom Flat	11.5%
2-Bedroom House	10%
3-Bedroom Semi	8.1%
4-Bedroom Detached	6.3%

Now have a look at this next table to demonstrate the fact that smaller properties are also better for rental in terms of vacant weeks:

Size of Property	**Average number of vacant weeks per year**
1-Bed/Studio	2
2-Beds	3
3-Beds	4
4-Beds	5
5-Beds	6

Vacant weeks are an important consideration for you; all the time the property isn't earning rent and you're paying interest on the mortgage you're losing money. For example, 5 weeks vacant a year means you lose one tenth of your rental income!

Letting has high and low periods. They are:

Month	**Market Activity**	**Details**
Jan	High	High demand after Christmas delay
Feb	Quieter	
Mar	Still quieter	Starts to pick up in late March
April	Very busy	
June	Still very busy	
July	Still very busy	
Aug	Busiest times	
Sep	of the year	Start of academic year
Oct	Falling back	
Nov	Very slow	
Dec	Still very slow	Run up to Christmas

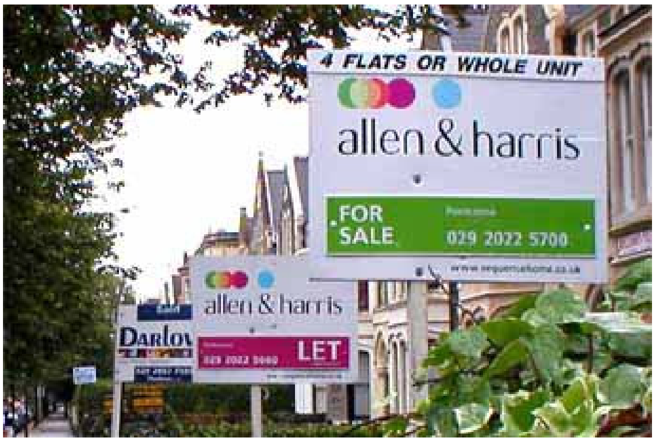
Try to bring your property on to the letting market in January or August/September. This way, with a one year contract, every time a tenant moves out your vacant weeks should be minimal.

A word about January… One reason that the market is busy in January is that couples and families have spent time together over Christmas and realise they can't stand the sight of each other! The highest divorce filings are in January, followed by late summer (after they've been on holiday together!) One

member of these splitting couples usually ends up on the rental market in January whilst they rent a place to try and 'work things out'! Also a lot of young men and women get tossed out of the house by frazzled parents after these holiday periods. They need a place to stay and end up on the rental market.

Everything happens for a reason.

The Right Tenant



You need to decide what type of tenant you want renting your properties.

Here are a few options.

Young professionals…

Very often choose part-furnished accommodation because they are busy and don't want the hassle of buying and moving a load of furniture. Part furnishing gives them the space to add their own favourite objects and even sometimes pieces of furniture, rugs, cushions and suchlike to personalise the place.

In recent years the influx of East Europeans has created a new market place of potential first-time buyers in the young professionals, who usually choose to rent. The number of new Polish immigrants in Reading, Berkshire near where I live for instance, has shot up into the thousands.

Families…

Tend to prefer unfurnished or part furnished accommodation as they usually have their own furniture. If a family is between selling and buying a house (caught up in a broken 'chain' of buyers) they are faced with having to store their own furniture or find accommodation where they can keep it with them.

Seniors…

Occasionally seniors find themselves in a transient stage in their life. For example they may be going through a separation, bereavement or divorce. They are most likely to want part-furnished or unfurnished accommodation, as they will have their own furniture and possessions.

Students…

Most students will require fully furnished accommodation. They are unlikely to have their own furnishings. Also, as many students attend colleges and universities away from their home town, they only want to rent for the duration of their studies.

Companies…

When companies relocate they often rent accommodation in the new area for key staff.

Corporate lets are also used extensively by North American and European professionals and business people posted to the UK for a couple of years or more. Company/corporate lets usually prefer fully furnished accommodation to a very high standard. This will often include things like plates, cutlery, electric kettle, toaster and suchlike – even towels and bed linen.

Holidays…

All holiday homes are fully furnished. Self-catering holiday lets don't usually include towels and bed linen. Where a full valeting service is offered, they are.

There are no explicit rules for furnishing, but here is broadly what each term refers to…

Unfurnished

This describes a completely empty dwelling. There is no furniture, appliances, carpets or curtains. There will be a shower or bathroom suite and a fitted kitchen without appliances. There are not many totally unfurnished properties for rental.

Part furnished

This is the most popular of rented accommodation today. Normally part furnished provides just the basic necessities (bed, sofa, tables, cupboards and so on). The tenant has room to add extra furniture, small appliances, ornaments, bed linen etc.

Part furnished accommodation as supplied may be barely adequate to live in but is not usually 'creature comfort' friendly.

In the kitchen/dining room there will possibly be a table and chairs, a cooker, fridge and usually a washing machine with dryer. For rented accommodation at the top end of the market (e.g. corporate lets) a dishwasher and large fridge freezer may also be included along with all plates, glasses, cutlery etc.

In the living area, a table and chairs a sofa and/or armchairs plus a TV table.

In each bedroom a bed and either fitted cupboards for clothes or free-standing wardrobe and dressing table or chest of drawers.

The accommodation will also have curtains, light shades and floor coverings throughout. Heating in each room and instant hot water are fairly standard now.

Furnished

Fully furnished accommodation is ready to move into immediately. It includes a full complement of furniture, carpets, curtains and kitchen appliances. It may also include ornaments, pictures and even blankets and duvets (not bed linen). Think of someone's home minus the clutter and trash – and you have a good picture of fully furnished.

The Right Property

Choose the type of property that there is a rental demand for in your area. Put yourself in the shoes of your potential tenants. Many are likely to be working people possibly without a car and at a transient point in their lives. The following pointers will guide you to getting the right rental property:

- Make sure there are a few large companies around, especially big names - this is good news for relocation tenancies which pay top dollar, on time, and are usually long term. Also it is good for general rentals as large companies generate a booming rental sector in their vicinity.

- <u>Flats produce a higher yield than houses generally</u>. In fact I would advise you against renting houses. Stick to 1 and 2 bed flats. As central as possible location is desirable with good access to rail and bus stations, pubs and shops.

- The town itself should be sustaining growth not declining. Take a look around - are new developments going up everywhere or is the whole place generally deteriorating? What is the town's main source of employment? Is this industry in decline or growth?

- It shouldn't be out of easy reach for you. It doesn't have to be in the same town, but any more than two hours drive would be undesirable from the point of keeping your finger on the pulse.

- Older properties tend to mean more maintenance. Boilers, plumbing etc you just don't want the bother from the letting point of view. Buy newer, up to date places.

- When looking at flats ensure you check on payments to the management company for ground rent and maintenance and don't forget to factor this into your business plan.

Once you have found the right property, you need to make it suitable and attractive to tenants…

- If the place is cosmetically scruffy, all the better as you will increase the value with a lick of paint. If you are going to replace a bathroom make it white, and with a kitchen, use dark coloured durable work surfaces.

- Use neutral or pastel colours when decorating. I find simple 'Magnolia' is very cheap and effective. Carpets should be a medium shade, durable texture preferably with a speckled pattern as this hides dirt, stains and marks. Flats generally have quite small rooms so you can get good carpet from surplus shops if you are tight for cash. Please remember that most people think they have good taste, when they don't. The subtle point I am making here is do not impose your own idea of 'good taste' on your rental units. Keep it clean and simple. White ceilings, magnolia walls, beige carets – that sort of thing. What you're looking for is 'inoffensive – even bland'.

- Part or fully-furnished shouldn't cost much because the 'minimalist' effect is very attractive and makes the place look bigger. Nothing is worse than a small flat cluttered with too much furniture.

- Provide a firm double bed (I never economise on mattresses as this is unfair to the tenant – it is awful sleeping on a cheap mattress). Pick a durable neutral cloth sofa again with a slight speckled pattern, a bedside table and perhaps a coffee table and a TV stand. The bed and sofa need to be compliant with modern fire regulations. Don't pay high-street prices for furniture, use shops that specialise in ex-hotel furniture, a warehouse outlet or a retailer like Ikea.

- Remove net curtains (old fashioned - your tenants will be relatively young usually) and replace with suitable curtains or roller blinds. Use lamp shades and 'soft tone' bulbs but make sure the place isn't too dark - flats generally have few windows so you need to be creative with lighting to make the place look big. Uplighters work very well for dark corners. Have all lights on when showing prospective tenants around – it brightens the place.

- Always use rugs in the bedroom, toilet and lounge. This protects the carpets and adds a 'homely' feel.

- Smoke detectors are a legal requirement and must be serviceable so best to buy these new and put in new alkaline batteries. Don't skimp on this. An approved gas safety engineer must check the place annually and service the boiler (assuming you have gas, of course) - you will need to provide an annual safety certificate to the letting agent.

- You will also need to provide 'white goods' - a washing machine, a kettle, a toaster and a fridge freezer. These can be purchased very cheaply from a second hand or reconditioning shop - but they must be checked electrically for fire hazards. Ensure the washing machine is fitted well to avoid problems down the line. Tip: Drying clothes is a landlord's nightmare. It fills the flat with warm, damp air which causes mould problems. So consider supplying a washer/drier. More expensive but saves a lot of hassle.

- Remember, don't sink too much time and pride into this - the aim is to keep costs down - you're not going to be living there! Every week spent in renovation is a lost week of rental income. By the same token you want to pride yourself in having better than average rental properties. The agents will soon get to know you and realise you go the extra mile – **they will put the good tenants your way and the junk tenants into the junk property.**

The information provided here must be adhered to **exactly.** You may think it's just my personal opinion or common sense, but believe me, this knowledge has taken years to acquire - the hard way!

So if you have the right property kitted out in the right way, you have gone a long way to ensuring that it is always rented out for top money with few problems.

Hot Tip

<u>When searching for a buy-to-let property find out:</u>

- How many other similar properties are available for rent in that area;
- How much the rent is;
- How quickly they let after they come on the market.

Only buy property that is a good letting investment and which you think you can re-sell when the time comes

Are you risk conscious or risk adverse?

<u>If you don't ever take a risk, you can't make a gain</u>. Risk is part of any venture. However, if you are 'risk conscious' as opposed to 'risk adverse' you significantly reduce risk and increase your successes.

Successful people take controlled risks whilst constantly minimizing their downside. Focus on all the points I make within these modules and you will be fully equipped to take 'risk conscious' decisions and make money like a seasoned professional property tycoon.

Here's a golden risk-reducing rule of thumb for rental properties…

Aim for a minimum 5%+ net annual return on your rental investments (excluding capital growth of the property value). If you follow this rule, you can still make a reasonable return. Many people are rushing into Buy To Let with returns of 1% a year after all costs! Okay, you MAY just be up for that if house prices are booming (say you're making 15% a year capital gain) but this is a recipe for disaster in a stagnant or falling market.

The bottom line in property dealing is <u>the return on your investment</u>. This is the profit you make *after* all of your expenses. In business terms, it's 'net' profit, not 'gross' profit. So, your aim is to make 5% profit after all expenses.

Example:

2-Bed Flat purchase price:	£110,000,000
Decorating, furnishing etc,	£10,000.00
TOTAL	**<u>£120,000.00</u>**

5% of this is £6,000.00 a year or £500 a month. This is the minimum rental you could accept and actually you need more than this as there are ongoing expenses, empty weeks to cover and so on.

The rule of thumb for buying/selling property is that you should aim for 20%+ per transaction.

Example:

Bungalow purchasing price	£150,000.00	
Improvements & legal fees	£ 30,000.00	
Total		**£180,000.00**
Sale price	£216,000.00	
Net profit		**£36,000.00**

If you are unable to buy a property for a price that will give you this 20% return on your investment – walk away. Do NOT buy.

It is no accident that in order to get a buy-to-let mortgage, high street lenders require that you put up 20% of the property's value.

And it's no accident that offering a 20% deposit cuts out (MIG) insurance fee. This is an insurance that lenders make you take out to cover their risk that the market might fall. But if you offer a 20% deposit, mortgage lenders waive this charge, because they consider the loan to be free from risk – which it is, barring total market collapse.

Imprint this on your mind…

Aim for at least a 5% net return on rentals and 20% return on buy/sell and you drastically reduce your risk exposure.

Important point: look, I hope you've sussed this, but there's NO WAY you'd bother with buy-to-let *just* for a 5% net return. Why? Well I'm hoping you know the answer! You could stick the money in the building society and probably get 5% guaranteed without a moment of hassle. So there's no point in going to all the bother of buying a flat, decorting it, furnishing it, kitting it out with white goods, finding reliable tenants and so on – just to get the same as you can get in the Building Society!

So why do we bother?

I hope you know the answer to this as well. It's the capital gain we are after and the rental income is just bunce. And here's the kicker. It's not capital gain on OUR money we want (because we have strictly limited amount of that.) We want to take the capital gains on someone else's money! E.g. the banks or Building Societies.

How does this work? Watch closely. (I'm going to keep this very simple and basic until you get idea.)

You invest £100k of YOUR money into a flat. Wait five years and it's (say) doubled in value. You've made 100% return on your money. Agreed?

Now put £20k of your money and £80k of a bank's money into the deal. Again it doubles. You've made £100k again. But wait! You only had £20k in the deal, so you've made <u>500%</u> on your money (excluding charges etc. as I say, I'm keeping this simple). If you put NONE of your own money into the deal, you have made (quite literally) an infinite return!

So I hope you can see that the name of the game (if you want to get *very* wealthy and not just dabble) is to use the awesome power of OPM – Other People's Money. If you use other people's money you don't care *what* the return rate is because… IT'S NOT YOUR MONEY!!!

To test this, how do you feel about 0.5% return a year, after all costs? Rubbish, right? Wrong! Supposing you get this on (being silly for the moment) £10 million of *borrowed* money??? Hmm? That's £50,000.00 a year to you for ZERO risk (it's not your money, remember? You've got nothing in the pot.)

You've either got this, or you haven't. Let's mush along.

The risk-conscious approach for buy-to-let

How conservative do you want to be? You're in this to make money, remember, so it is wise to plan for the worst – things often turn out like that!

How to calculate potential returns from rental using a 'worst scenario' case.

- Work out mortgage costs on interest rates 2% higher than they are right now.
- Assume rental values hold at the current market rates (although they should rise – we're just being cautious).
- Assume you will only let the property for 11 months of the year.

Look at how these figures add up. If you have used the 20% rule, e.g. you bought the property for at least a 20% discounted price your figures should still be healthy. So whether you make a mistake (e.g. pay too much for repairs) or the rental market goes slack, your investment returns should be safe.

The two key elements all successful property tycoons use are:

- Walk away from any deal that will result in less than a 20% return on your investment when you sell.
- The 20% return on your investment must work whether you plan to sell-on or let the property and then sell on. Meanwhile you should aim to make a minimum 5%+ net on your rentals.

Before buying a property that you intend to let out, ask yourself this question, 'If rental rates collapsed tomorrow, how long would it take to sell the property and still cover my financial costs?'

If you always check these elements and ask the vital question above, you will eventually develop an instinct for which properties you can purchase and develop without risk.

Tip: Always check there are no mortgage redemption charges for paying off a mortgage early, otherwise you can pay a hefty cost if you decide to sell the property at short notice.

I'm not going to go into much detail on the financial side, at this point, because as you know, you won't have to deal with high street lenders if you complete your Apprenticeship.

However, to give you an idea of what you should look for, always consider reducing your risk. Look for flexibility in your finance contract. Consider the possibility of the odd non-rental income months between tenants. Maybe you would need extra top-up if major repair work became necessary.

Fixed interest rates help you to budget but you have to check the conditions and redemption charges. For example, let's say you purchased a flat so you could rent it out. The interest rate of your mortgage was fixed for 2 years.

A year later you decide to stop renting out the property and sell it with vacant possession. You could find that the penalty costs for paying back the mortgage before the 2 yrs fixed interest rate expires would knock a significant dent in your profits.

If every time you purchase a property (whether to let or resell) you aim for these two key points you won't go wrong.

They are:

- **Buy at the right price.**
- **Finance at the right rate.**

Study prices and know your market. Don't rush in just because you want to keep up with your window-cleaner! (They are going to be hit hard by the first slight downturn in property prices or the first slight rise in interest rates.) Combine this knowledge with how much you feel you can trust the agent and set a price that will pull tenants in.

Now this next point is very important.

As I've explained, when you buy a property make certain it is suitable for both letting and re-selling. However, you need to know there is an inverse relationship between properties for capital appreciation and properties for rental income.

That is to say, a one bedroom apartment will give you a higher rental yield, but at the other end of the scale, a luxury four bedroom house may give a lower rental yield, but the actual property will usually appreciate more in value each year.

So it depends what you want. The two ways to make money from property are:

1. Buying and selling for profit - larger properties do best.

2. Renting properties. Smaller properties do best.

There's no reason why you can't do both of course, but don't ever confuse the two!

How to set a rental price

- Ask 3 letting agents in the area for an estimate of the rental value and their costs for tenant finding and suchlike.
- Take the mid price, marketing your property at that level.
- Expect to receive 90% of the market price.

Rental yield is how much your return is on an investment. Aim for 8 to 10% gross yield, 5% net.

This is not the same figure of 20% return on investment used when assessing the development potential of a property, or the profit margin on the re-sale of a property.

It may be that after emergency repair insurance and improvement costs etc. your rental yield is small. However, as rents and property values climb each year, your capital gain will increase and be substantial.

TIP: I always use a letting agent to find and vet tenants for me. It's a REAL hassle doing this yourself. You don't want to spend your time interviewing a bunch of no-hoper tenants who can't really afford the rent.

How to work out gross yield

This is simply the yearly rental income divided by the capital value of the property x 100.

So that's the amount of rental per week x number of weeks it will be let (between 46 – 50 – although a 12 month tenancy contract will give you a 52 week run).

DIVIDED BY:

The total cost of buying the property (purchase price, stamp duty, solicitor's and surveyor's costs, improvement and furnishing costs).
ALL MULTIPLIED BY 100.

That's called the GROSS YIELD.

Example:

£250 per week for 50 weeks per year =	£12,500.00

DIVIDED BY:

Total purchase & costs =	£172,000.00

X 100

GROSS YIELD = 7.3%

You have a go. What’s the gross yield on a £150,000.00 flat with rental income of £7,500.00?

Answer: 5%. Too low by the way. (Remember, this is GROSS yield, not net yield.)

How to work out net yield

This is easy as we just need to add in our expenses.

So it’s the total income less all costs of renting (e.g. letting agent fees) and maintenance costs

DIVIDED BY:

Total purchase and improvement costs

x 100

Example:

Total rental income <u>less all costs</u> = £6,250.00

DIVIDED BY:

Total purchase & refurb cost = £172,500.00

x 100

NET YIELD = 3.6% (A little on the low side, depending what capital gain you can expect.)

Another safety check…

Rental income should be a minimum of 130% of any mortgage payments you may be making.

Between 8 – 10% gross yield is what you can aim for in a healthy property market.

What drives rental returns down?

- A boom in house prices can mean that property prices increase faster than rental prices and so the returns are diminished (the yield is lower). Example. A flat was £150k with £15,000.00 a year rent (10% gross yield). But a recent surge in prices has put it up to £200k – but rents have not caught up. So the return is now 15/200 x 100 = 7.5%.

- An increase in rental properties can cause a glut and demand is outstripped by supply.

What drives rental returns up?

- If property prices go too high, first-time buyers are often forced to rent rather than buy, so more people flood onto the rental market, forcing prices higher.

- Fewer buyers puts the brakes on property prices but drives up demand for rental accommodation.

Before moving on, I wonder if you're a little puzzled by my worked example above? I mean, you may be thinking who cares if the yield has dropped from 10% to 7.5%? You're still getting exactly the same amount of money in rental each year (£15k). That hasn't dropped, so it doesn't matter, right?

Wrong.

If you think that, you are NOT thinking like a property tycoon. Let me put it this way. You have £150k to invest, let's say in my bank. I say to you: "If you deposit that with us, we'll give you £15k a year interest." You're fairly happy with that, but you say: "That's good. I'm thinking of depositing more than that, let's say £200k. What would you give me on that?" You are somewhat stunned to hear me say: "Our bank will also give you £15k on that amount."

In other words, yields matter. If your flat has gone up from £150 to £200k, that's REAL money, not some fairy money you've got for free and so you think it 'doesn't count'! It's *real* because you could choose to sell that flat, take the £200k and invest it elsewhere. Just because you own a property, that shouldn't stop you constantly thinking: "If I *didn't* own this property, would I buy it at the current price and the current yield?"

If the answer is 'No' you should sell it immediately.

I hope you have understood this last very important section. I would strongly suggest you do not proceed until you have 'got' what I've just said. You may have found it obvious of course.

Rental yield on holiday homes

Short let returns are typically 50% better than long lets. Despite the weeks that holiday property is not being let (out of season) you should expect to see a gross yield return in excess of 10%, plus you should be looking to get decent capital growth on the property.

On the downside, short lets and holiday lets require a lot more management than a traditional let. The property needs to be cleaned between lets (typically weekly) which are traditionally the time between one set of holidaymakers vacating by 10am on Saturdays with the next set of visitors allowed entry from 2pm on the same day. This leaves just four hours for the property to be cleaned! So if you purchase holiday property don't forget to factor cleaning into your net rental yield.

Current legislation works in favour of the landlord. The reason is simple. When they tried to change the law to make tenants supreme and landlords completely vulnerable and disadvantaged, guess what? The rental sector collapsed and there was virtually no rental property available!

However, to avoid any problems, aim with every let to secure tenants who can pay the rent and do so willingly. That's why I like to use a letting agency to find decent tenants.

Before I explain the different types of tenancies, here's what you should know about **sub-letting and lodgers…**

Most tenancy agreements contain the condition that your tenant may not sub-let the property to a sub-tenant. A tenant cannot appeal against a landlord's refusal to allow sub-letting.

The principle aim of the condition is to prevent a sub-tenant gaining any security of tenure. That would mean the landlord could not get his/her property back.

Tenants can however, take in lodgers if they so wish. Landlords sometimes allow this on the condition they are notified.

These are the reasons…

- Having a lodger can make it possible for the tenant to afford a higher rent than if he/she lived in the property alone.

- In a district of lower income, it can make it easier to let higher value properties.

As you can appreciate, both situations can make it easier to let higher value properties.

A Lodger

As far as the law is concerned, a lodger is someone who lives with the person who occupies the accommodation. They are provided with meals and services which may include cleaning and provisions of linen.

The lodger is also someone who may not have any separate accommodation of their own.

A Sub-tenant

The difference is that a sub-tenant has their own separate accommodation of at least one room, usually with a separate lock and/or access. And they will not normally be provided with meals and services.

Single Tenancy

Single occupancy means your tenancy agreement is with one person alone. However, single tenancy does not necessarily mean that only one person occupies the accommodation.

A single tenant may live with members of their family, or friends or ‘significant others’. But, it means they alone are responsible for the tenancy. In other words they pay the full rent to you and how they collect portions of the rent from their lodgers (if at all) is entirely their responsibility.

A landlord may also have single tenants within a shared house or a house sectioned off into bedsits.

Shared tenancy

Shared tenancy means the tenancy agreement is made jointly with several other people.

This is common practice for property let to students, friends or a group of people. They share a house because they know each other.

With shared tenancy each occupant has a share of responsibility for the tenancy.

Shared tenancies can be on a joint and several basis. This means that each tenant is responsible for the full rent and actions of the other tenants. If anyone of the tenants defaults, the remaining tenants must pay up the full rent.

If a tenant damages furnishings and absconds without replacing or paying for the item, the other tenants must do so. Up to four people may be granted a joint tenancy.

Shared accommodation

The following conditions could be officially classified as overcrowding:

- Children over the age of ten, of the opposite sex sharing a bedroom.
- Two people of the opposite sex who are not living together as a couple sleeping in the same room.
- There are more people living in the accommodation than it was designed for.

In either of these circumstances tenants can complain to the local authority who can prosecute both the landlord and the occupier of overcrowded accommodation.

Types of Tenancy

It's important you have an understanding of the different types of tenancy agreements. Then you can make an informed choice of whether you want to buy-to-let and if so, what 'type' of letting you want to do.

There are six different types of tenancy:

- An Assured Shorthold Tenancy
- An Assured Longhold Tenancy
- A Periodic Tenancy
- A Licence
- A Company Let
- A Holiday Let

Let's have a brief look at each in turn.

An Assured Shorthold Tenancy

With the shorthold tenancy a landlord does not have to give any reason to end the tenant's occupation of the property. A typical reason, by the way, would be that the landlord wishes to sell. But the landlord must give the tenant at least two months notice. For example, if the shorthold tenancy is for a six month period, at the end of month four, the landlord can legally notify the tenant that they must vacate the property at the end of the contract term.

In most cases, a landlord grants a tenant further tenancy. If they do so, the tenancy becomes a **periodic tenancy** (unless the landlord agrees to a brand new tenancy agreement).

An Assured Longhold Tenancy

The longhold tenancy is also referred to as an 'ordinary' tenancy.

At the end of the agreed renting term, the tenant does not have to leave. They have the legal right to remain in the property for as long as they want.

A landlord has to take legal action to regain possession of their property (this is why the assured shorthold tenancy was introduced).

Since 28th February 1997, unless stated otherwise in the agreement, all new domestic dwelling tenancies are taken as assured shorthold.

Two further points to know about are:

- It is extremely difficult to repossess a property during the first six months of an assured shorthold tenancy.
- If a tenant deems the rent to be excessive, they have the right of referral to the Rent Assessment Committee.

A Periodic Tenancy

This agreement runs either from week to week or month to month. It carries on until either party give notice. The minimum period of notice required will be stated in the agreement and is usually one month or two.

Periodic tenancies can be contractual or statutory.

Contractual Periodic Tenancies

When an assured or assured shorthold tenancy is created with no initial fixed term, the tenancy continues indefinitely until either the tenant or landlord gives notice.

Statutory Periodic Tenancies

If the fixed term of assured or assured shorthold tenancy comes to an end, the tenant remains in the property (holds over) with the landlord's consent.

In this case the terms of the tenancy do not change, except that the tenant and landlord have the right to give notice (within term agreed) which will end the tenancy.

A Licence

This permits the licensee to occupy the property but does not offer the licensee security of tenure.

If the property is sold, the licensee has no security of occupation, however, they may not be evicted without a court order.

Licenses are usually only used for short term lets, e.g. students during term-time.

However, there is risk attached to this for both the licensee and the licensor.

For the licensor:

- The courts could decide that the license is a tenancy agreement and grant the occupant security of tenure.

For the licensee:

- They could be asked to leave at any time, unless notice time has been agreed. If it has, it will be short, days or maybe a week.

A Company Let

This is the only type of tenancy without the condition that the property must be occupied by a tenant in person.

When a company rents a property for an employee it is the employee who occupies the property, not the company. Neither the company or the employee have security of tenure. This means the company and employee can be asked to leave on request.

A company tenancy let cannot be ended unless the landlord agrees.

A Holiday Let

For a holiday, the normal rules of tenancy don't apply. This means:

- The holiday-maker tenant has no security of tenure.

- They cannot occupy the property longer than the agreed period of their holiday.

It is absolutely essential this is made clear in your tenancy or rental agreement. Otherwise a holiday-maker could gain security of tenure and have the right to remain in the property after their holiday period. It has to be said this is an unlikely scenario!

Resident Landlord Let

You can earn money from the property you live in by choosing to be a resident landlord. The following situations come under residential landlord:

- You live in a large house and let part of it.

- You convert your house into several flats, live in one and rent the others out.

There is a major difference in the agreement for resident landlords – the tenants do not have security of tenure. This means they can be asked to leave at any time.

However, the tenants' right to security of tenure DOES apply for the following situations:

- Purpose built blocks of flats (even if the landlord lives in one).

- If the landlord moved into their property after the tenancy began.

Trouble-Free Letting

We're now going to look at what makes the actual tenancy successful and free of aggravation.

Let's talk about 'problems'.

I wonder if your mind is filled with the potential problems of letting? What if they don't pay the rent? What if they damage the place? What if they move out?

Although problems can occur it's important that you don't put yourself off the potentially lucrative business of letting just because your mind can envision a string of problems. You have to be bold to make money! In fact some wise

person has said that ALL money is made by solving some else's problems. I think that is very true.

A *real* problem is having to be a wage slave for the rest of your life constantly depending on other people for the next pay cheque!
Sure, you're going to get things crop up occasionally even with all the advice I will be giving you here. Deal with it - it only becomes a mega problem when you make it one by inattention to detail.

Don't start cursing and blaming yourself for it - "I knew this was a bad idea!" That's the loser mind set.

One thing I can promise you is that you will get problems if you set out on the path of wealth. But hey, in case you haven't noticed, you've got problems already by not being wealthy!

Okay let's push on...

Better to have an agent or not?

If you employ an agent to find tenants for you, you should allow for a letting agent's management fees which are usually 10% of the annual rent. If you want 'full service' (there's a joke there but I'm not touching it...) then that will set you back 15%. With a full service agreement, the agent will do everything – even change a light bulb. You need never even visit the property. They will charge you for any works undertaken (e.g. a new boiler) at cost on top of their fees of course.

Regarding tenant-finding (which is pretty much all you get for your 10%), please don't bother trying to do this for yourself - believe me, the fees are worth it as long as you find a good agent – which is not so easy I'm afraid.

The agent's job is to find you a quality tenant asap and keep them there as long as possible. They will check the tenant's credit and stability of employment, write an inventory, document the condition of the property and move the tenant in (and check them out) for you.

Use a letting agent that has an agreement whereby as one tenancy comes to an end, you have the right to have the agent show new prospective tenants around the property before the existing tenants have moved out. Used successfully, this technique could reduce your vacant weeks to zero! The last thing you want is a tenant leaving, and then several weeks of viewings!

But make no mistake, all they are interested in, quite rightly, is their cut. If your property is vacant for a few months, they don't lose out - you do. If the tenant misses a month's rent, they don't lose out - you do because they get their fees in advance- they will collect one month's rent in advance and one month's rent as deposit from the tenant and deduct their annual fee from it.

With this in mind, it's important that you vet your agent very carefully indeed. I cannot recommend one because you must use an agent local to the property, for obvious reasons (doing viewings and so on). Usually the agent will between a few hundred yards and a mile or two away at most.

Here are some tips on what to look for:

- A prominent high street location that will attract potential tenants and regular advertisements in the local paper. If someone is offering low fees it's because they can afford to by not having these things in place - don't be tempted!

- Conduct a 'mystery shop' on them. Phone up pretending to be a potential tenant and judge their customer service skills. Ask yourself if you would be comfortable renting something from them.

- Ask them what they specialise in. If it's DSS tenants, forget it. This isn't about snobbery it's about business. Wear and tear tends to be higher and there is always the risk of them conducting benefit fraud - if this is the case the government are entitled to reclaim all of the rent they have paid to you (via the claimant) back from YOU! Ouch.

- It's a good sign if many of their clients are companies. Companies use rental agents for relocating staff and this is very good news indeed. You can charge more and the rent is always paid on time.

- Make sure the rental side of the business isn't just 'bolted on' as a sideline for an estate agent. Many of the best ones are affiliated with estate agents but be sure that it is a totally separate and dedicated department within the estate agent. The one I use regularly is a husband and wife team. He does the property sales, she does the letting side.

- Ask them outright why you should use them as opposed to their competitors.

Your aim is to find a good agent and build a relationship with them that will last a long time. Explain to them that you plan to expand over the years and want someone to count on. This relationship is so important, I can't begin to tell you. The truth is that agents get a variety of tenants from 'gold chip' through to so-so. They all pass the credit ratings of course, but at the bottom end it's a close call. The agent will put the gold-plated tenants with their top customers (you) and the so-so tenants with their casual customers who are unlikely to do repeat business. It's just a fact of life I'm afraid. All business comes down to relationship in the end (including any job you're holding down, by the way).
They may also offer you 'full management' for an additional 5% a year. As I've mentioned, for this, you can basically leave everything down to them - they arrange all repairs and maintenance as and when it happens. This is the level of service needed by people who (say) have rental property but they are abroad and cannot attend to tenant problems.

Which service you go for depends on you and your situation but I advise against full service unless you have special circumstances. I'll be showing you how to do a much better job yourself for little effort and it's a great way to learn more about this business anyway. That extra 5% will eat into your profits and I hope you're clear that you also pay for any workmen and materials the agent arranges for you. That's not included in their fee!

Now here's the most important thing to remember with letting agents. **They want you to charge as little as possible in monthly rent!** The reason?

Well let's say you could get £600 a month in rent. If they can knock you down to £550 a month they'll be able to let it very easily and make their money quicker- they'll only be £5 down a month (10% of £550 as opposed to 10% of £600) but you'll be £50 down a month! They'll also look good in your eyes as they will have found a tenant quickly.

At the same time, and to be fair to them, if your property is too expensive, it may remain vacant for a while and this is something you definitely don't want. If you push for too high a rental and lose a month each year waiting for a tenant who will pay that amount, then you have lost nearly 10% anyway, so you'd be better reducing your rent by 10%.]

Reducing Risk

Now let's look at some basic procedures for ensuring things run smoothly, whilst building in a little more 'safety margin' for ourselves in the process:

- It is well worth making the effort to actually meet tenants at the beginning of the tenancy. I used to do this during 'check in' (that's the time you meet the new tenants at the property and show them around, give them the keys etc.) Be pleasant and subtly let them think that you've sunk every penny into the place. Tell them you hope they'll have a pleasant time there. If the tenant sees you as an actual, honest working person rather than a fat-cat landlord, they are less likely to abuse the property and get behind on rent. Don't get over-friendly though - this is a business relationship and in the future you need not feel guilty about raising rents in line with the market!

- Try to catch small problems before they build into big costly ones. Each time the tenancy is renewed, take an hour to give the place a thorough check over.

- If maintenance is required don't get the letting agent to sort it out for you - they won't care how much other people charge you they will just use their 'tame' contractors! And don't bother hiring out specialists such as plumbers etc. - far better to get acquainted with a general handyman for much cheaper rates. Better still, learn a few basic DIY skills yourself. This is rather important. When starting out you can save yourself a fortune if you can wield a screwdriver. If you have to call in a tradesman for every tap washer and lose screw, this will really eat into your profits.

- From time to time, walk past and have a look at the outside of the property. Do not enter though. **Once a tenancy has started you are under no circumstances to enter the place without permission from the tenant.**

- Take photos of the property inside and all the furniture as a record. This is in addition to a well-prepared inventory listing all items and their condition.

If you follow all my instructions, you should find tenants quickly and have little problems. If the property is not let out within a week or two approach the agent. You then need either to find another agent or reduce the price based on

your gut feeling, always remembering that the agent wants you to knock the rent down as low as possible.

Finally the area of non-payment of rent. If you've taken all my advice and especially if you have company lets, I would be surprised to find you in this situation. Most rent problems come when budding entrepreneurs decide to save the 10% and find their own tenants. Bad idea. Nevertheless, here's what you should do if you get some problems:

- Don't jump to conclusions if the rent doesn't appear on time. Banks make mistakes and so do individuals and there could be a perfectly simple explanation. A stroppy attitude will lose you respect from the tenant. Make a simple enquiry through the letting agent, failing that, approach the actual tenant directly.

- Your next step depends on what the outcome of the last one was. Remember all rent is paid in advance, not arrears and rent day cannot be allowed to pass - the tenant asking you to use the deposit or pay in arrears is not acceptable.

- If an immediate solution is not forthcoming, you must write a letter giving a deadline by which the outstanding rent must be paid before legal action is taken. Deliver this letter personally at 8:00 am on a Sunday Morning. This is not harassment, just a polite way of letting the tenant know that this will have an impact on their life and privacy.

- The second letter should repeat the message of the first with the addition of stating that within one week you will start action to terminate the rental and refer the incident to a credit agency. If they don't pay up after all this it was a lousy job of vetting them in the first place!

Above all (and this is SO important) do not, repeat do NOT get involved in 'leniency games' no matter how hard hearted this seems.

By leniency games I mean buying in to their sob stories about unexpected expenditure and a cheque on the way from an aged aunt. It starts with "Can I pay you £400 now and the final £100 on Tuesday?" The answer is 'No!' At the outside they can have until Tuesday (or whenever) to make the FULL payment. If they give you £400 they will consider they have 'paid' you and find another use for the £100 if/when it ever materializes. Trust me, I've seen

every variation of this. Everyone is well-meaning, but it ends in tears. You are not a credit agency or loan company.

Their part of the deal is to pay the rent in full and on time; your part is to give them a top class, well maintained property to live in.

The equivalent of what they are trying on would be if you said to them: "Could you please just repair that boiler at your expense and I'll try and get the money to you installments over the next few months as I'm a bit broke at the moment?" How do you think that would go down with the average tenant?

Don't be put off by all this talk of non-payment of rent. **In all the time I've been doing this I've had a serious problem** so don't take it out of perspective. Like I say, if you do all your homework in the first place it shouldn't be a problem.

The Ultimate Letting Risk Buster

Still worried?

Okay, I'll tell you about a secret weapon that gives you the ultimate safety guarantee for even the most nervous landlord!

It's called Letting Insurance. This guarantees against non-payment of rent but it costs around 3% of the monthly rental. Go to www.homelet.co.uk or www.letsure.co.uk for details. If you have quality company lets though, I wouldn't bother.

Well that wraps it up for this month. I want to congratulate you because you are doing really well. A lot of this can seem a bit 'dry' but I hope it's also common sense to you and not too difficult.

If you are seriously interested in becoming wealthy through property there is simply no substitute for what you are doing right now – learning your craft. It would be amazing, don't you feel, if an ignorant hack-amateur could just wander in off the street and start pulling down huge money from property dealing. It's only the mistaken belief that people 'know a bit about property;' because they've bought their own house, which makes them blunder into this field. They wouldn't start dealing in fine wines, paintings, antiques or horse racing on the basis that they'd drunk a bottle or two of red plonk, had a picture of a 'Crying Boy' on their wall, had Gran's 100 year old table in the dining room and once taken a bet on Aardvark in the 2.30 at Epson!

I'll see you next lesson.