

Avoid these pitfalls when buying rental property

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While investing in rental property can offer excellent rental returns, there are some pitfalls that you should be aware of.

So, you quite like the idea of owning a rental property and think you might be able to earn good rental returns. Yes, that might well be the case, but Samuel Seeff, chairman of the Seeff Property Group says, you need to take care as there are pitfalls.

Property is one of the most exciting investments for just about anyone. Often, in addition to owning a first home, buyers will aspire to own additional property, sometimes a holiday home, but generally with some form of rental income in mind.

Seeff says that during boom times, it can be very tempting to invest in additional property as there is usually plenty of money and finance available and financial pressures are low. It can also be relatively easy, as you could take out a housing loan to help you finance your purchase and use the potential rental income to help off-set the monthly bond costs.

When the market turns and the economy declines, properties come under pressure and owners, especially those of secondary properties such as rentals will quickly find that the cost might now outweigh the benefits, says Seeff. Household budgets are now under pressure and being able to fund additional monthly utility bills and maintenance can be a stressful burden.

At the same time, Seeff says that the rental market will also come under pressure during an economic decline. Fewer people will be making holiday bookings and you may need to lower your rental rates. Residential tenants will also feel the economic decline as their disposable income and household budgets come under pressure. They will battle to keep up with high rental rates. Most will look to scale down to a cheaper rental. Rental arrears might start creeping in and tenants will also not have the extra funds to maintain the garden and swimming pool for example.

It is important to understand that the economy always moves through cycles. Boom times seldom last beyond a few short years, then the inevitable decline sets in for one reason or another and the market dips before a recovery phase comes along to again take the market up.

It is important to understand this and if you are looking at investing in a rental, that you do so with a long-term view, not just in terms of the property value to be had, but also how you could hold out during an economic downturn.

Be aware too, continues Seeff, that not all properties or areas offer good rental investments and it is therefore vital that you do your homework before leaping into such a vast financial commitment. The non-negotiable rules for investing in property:

Location

The location is vital. Properties in areas with good schools, amenities and convenient access to business and commercial nodes tend to be the most in demand, regardless of the state of the economy. Sometimes, specific areas undergo an economic or development boom and this can lead to strong rental demand and in turn boost buy-to-let investments. Bear in mind though, that once the boom comes to an end, the demand for rentals might also subside.

Affordability

Generally, the more affordable property ranges tend to be most in demand regardless of the economic cycle. For example, in general, anything in the R4 000-R12 000/month range is highly sought-after. When it comes to holiday accommodation, anything close to beaches or tourist attractions or with great views would command higher rates.

Property configurations

Together with location, security has become a vital requirement for tenants. That means security complexes and secure neighbourhoods tend to be most in demand. When it comes to investing in a rental property, it is best to take emotion out of the transaction, think with a business hat on. Don't make a sentimental purchase. Rather, speak to a local area expert to assess what kind of accommodation is most sought-after and at what rental rates.

Holiday versus residential versus student rentals

Each type of rental is unique. Student accommodation for example might be most popular in two or three bedroomed configurations because it allows for sharing. The most popular holiday flats on the other hand might be one and two bedroomed units. For residential rentals, three bedroomed townhouses or houses might be most popular in one area while two bedroomed flats might be popular in another. It is therefore advisable to research the requirements of each area very carefully.

Supply and demand

Just because an area has a very busy rental market, does not necessarily mean that it requires more rental stock, especially under weaker market conditions. It is therefore important to assess whether you are investing in an area where there is a shortage of stock in real terms that is matched by an equally high demand. Be sure to check how sustainable the demand will be in future.

Holding costs

Property is a costly investment. In addition to the acquisition costs, there are ongoing expenses such as the monthly utilities and services as well as property tax, insurances and maintenance and upkeep.

Maintenance of rental property can be costly. Remember, your tenants are unlikely to look after your property in the same way that you would.

Tenant management

Ensuring that you have good tenants who will look after your property and pay their rent on time, is critical. Even just one to three months without a tenant can quickly become very costly to a landlord. The laws around property and tenancy is complex and it can be onerous and costly should you need to evict tenants. Unless you are in the business of property rentals, it is best to work with a credible rental agency who can ensure that your tenants are properly vetted.

If you are financially able and stable, then investing in additional property could be an excellent option. You might want to invest in a coastal property for future retirement and can in the meantime, rent it out to help you pay for the asset. While there are many positive reasons for investing in rental property, Seeff cautions that it should always be done with thorough research and a long-term view, not just in terms of the asset value and growth, but also the potential for the market to take a turn for the worst.