

Big Investments in Small Houses by Craig A. Lane, C.C.I.M.

One of the biggest stories that we keep seeing in the newspapers and television news is the rapid increase in home values. The increases in some areas have been incredible. Some homes have increased \$100,000 in a year.

Over the past twenty years, many real estate investors have specialized in investing exclusively in homes. If you might think of this as a small investment, think of some investors who own 100 or more homes in the \$250,000 value range. How about the owner of 100 houses that increased in value by \$100,000 each? Don't reach for your calculator – the answer is \$10 million!

Now might be the time to look into an investment in houses! Buy several scattered rental houses and you have the equivalent of, as one owner calls them, "horizontal apartments".

This owner does not have to sell to get at the money. He can refinance and pull out most of this money, tax free!

An owner with 100 or 200 homes can't manage them alone. The houses are like apartments that are in scattered locations, and are managed the same way but without an on-site manager.

Now might be the time to look into an investment in houses! Buy an extra one for a rental – buy several scattered rental houses and you have the equivalent of scattered apartment units, or as one owner calls them, "horizontal apartments".

Easy To Get Started

The potential for higher returns is better in real estate than in some other investments, such as the stock markets. Investing in single family homes can be particularly attractive, since they will have little chance of taking any huge drop in value at one time. Instead, over the years, the values have had a sure steady increase. Compared to the stock market, the amount of capital required can be remarkably small. The leverage is better, with down payments still as low as 10% of the value. You may be able to make an investment in a significant property with just a down payment in the \$25,000 to \$30,000 range (or much less). Someone else, either a lender or maybe the seller of the property will put up the rest of the investment capital. Real estate, particularly houses, is always the perfect place for the use of OPM (other people's money).

After you have made the purchase, you must plan for some monthly expense. Even if the tenant pays all of the utilities and upkeep, you still can face a negative cash flow situation. The monthly "eat" may be offset at the end of the year by the tax shelter from the "residential income" property.

You could set up a cash reserve to cover any problems on the investment, such as in a money market account. It might be smarter to obtain a line of credit to cover this. Since the idea is to have a "leveraged" investment, why not borrow as much of the needed cash as possible?

The Profits

If we have anywhere near the increase in value in real estate that we had a few years ago, the potential for capital gains on a leveraged (OPM) investment can be significant. Remember, an increase in value affects the whole value of the property, not just your equity.

Where Should You Invest?

Remember the old saying about the most important thing in value when searching for any kind of real estate. It is still **location, always location**. This will remain the same in homes as in any other real estate investment. What should you look for?

A neighborhood where most homes are occupied by the owners. You will probably be able to get higher rates in an area where the other houses are owner-occupied. Owner-occupied houses will usually be better maintained and the neighborhood will be more stable. We can check the neighborhood by looking at the property-tax register. Since the name and address of the owner is provided, simply see if the address of the owner is the same as the property address.

Since the objective in this investment is “increase in value”, we are looking for the possibility of the resale. We will always have greater appreciation in a neighborhood where people maintain their property with pride.

Be aware of the location of schools, churches, shopping – just as you would if you were purchasing the property for your own residence. Your ultimate buyer of the property will be doing the same. Make sure of the zoning of the neighborhood and any adjoining areas. This will insure that you will not have any sudden surprises after you make your purchase.

Craig A. Lane, CCIM is an investment consultant with AOA Commercial Brokerage and has over 25 years experience in Investment Real Estate. He specializes in facilitating the acquisition, sale and exchange of multi-family and commercial properties in Southern California. For questions or more information, please call (818) 235-1142 or email laneca@aoausa.com.