# Ready to Rent?

When you're preparing to rent out a home, there are many boxes to check to ensure you're well protected and capitalizing on all the benefits of owning rental property. Here are some items to begin researching and considering well in advance of closing on a new rental property or converting a primary residence to a rental.

Financing

- Determine available cash for the down payment and closing costs.
  - Savings/cash on hand
  - Available equity in current properties
    - Maintaining 60-75% loan-to-value ratios in rental properties is a good rule of thumb.
    - In the initial phases of building a rental portfolio, one option is to leverage your primary residence a bit further, with a loan-to-value ratio of up to 80%
  - If purchasing a new primary residence, you can put down as little as 3%
  - If purchasing an investment property, you must put down at least 20%; if you're able to put down 25%, you'll benefit from a lower interest rate.
  - Average closing costs range from 1-2% of the purchase price.
- If you're pulling equity from an existing property, consult with a lender to determine the optimal timeline for your refinance.
- When considering cash requirements for purchase, it's recommended that you also reserve approximately 6 months of the total mortgage payment (Principal + Interest + Taxes + Insurance) in a bank account for an additional layer of protection.

Property Selection

- Consider reasons why renters live or rent in a given area:
  - Proximity to universities, military bases, large corporate campuses, etc.
  - Proximity to urban areas or neighborhood hotspots (dining, entertainment, shopping, green space)
  - Resort towns
  - Sought-after school districts
- Along with location considerations, consider the physical characteristics of strong rental properties:
  - Single-family homes
  - Multi-family residences (e.g., duplexes) – you can purchase up to a 4-plex as a primary residence if you live in one unit and rent the others.
  - 3-4 bedrooms and at least 2 bathrooms
  - Low or no HOA fees
  - Brick exterior
  - Hardwood or durable laminate floors
  - Minimal updating is immediately required (unless you have cash available to renovate)
  - A small number of mature trees and low-maintenance landscaping

- Focus on cash flow:
    - Base purchase decisions on the ability to achieve cash flow: are you earning a monthly rate of return you can measure?
    - Calculate estimated cash flow using:
        - Estimated rental amount less:
            - Mortgage payment
            - Vacancy rate
            - The dollar amount for risk factor – at a minimum, this should cover the amount of your insurance deductible on the property.
            - Property manager – hire a property manager as soon as you can afford it to minimize risk and potential time investment.
                - If you don't have specific numbers yet, consider using 10% per month as the estimated cost of property management.
            - A good litmus test is that monthly rent should be 0.55-0.7% of the purchase price.
                - Purchase price X 0.0055 = minimum rent amount needed
                - Purchase price x 0.007 = very strong cash flow potential

Property Management

- Begin discussions/interviews with property managers approximately 60 days in advance.
- Questions to ask:
    - Length of time in business
    - Number of properties managed
    - Service area(s)
    - Fee structure for tenant payment, monthly maintenance, and service coordination
    - Vacancy rate
    - Contract length and termination specifications
    - Process for tenant identification and screening
    - Process for property turnover
    - Process for required maintenance
    - Process for repairs
    - Recommendations and rent estimates for specific properties under consideration

Property Insurance

- Compare quotes for property insurance to determine the best combination of coverage and price.
- Ensure that insurance companies quote the policy as a home to be rented to others.
- Determine the deductible amount that you are comfortable with as part of your potential risk in the event of an accident or issue.