



## **6 Mistakes to Avoid When Buying Investment Property**

*As you're aware, investment opportunities present themselves in all property types: residential (single family and multi-tenant) and commercial (retail, industrial/manufacturing and professional). Much of what follows addresses the general subject of investment and touches on all property types, but focuses on residential investments. Certainly, if your interests lie in any other category of investment, we're available to offer more insight on other possible pitfalls to avoid.*

- 1. Never use the seller's agent to represent your interests.** Seller's agents (listing agents) are contractually and morally obligated to represent the best interests of the seller, not the buyer. In a large, complex transaction like a real estate purchase, you should have representation that is not compromised by any conflicts of interest. Having an exclusive buyer's agent (one who never takes listings) is the only way to insure uncompromised representation of your interests alone.

Trust is the key issue. Never do business with someone you do not or cannot (by virtue of who they are contractually obligated to represent) trust completely to represent your best interests. Likewise, you'll benefit by not having to wonder (or suffer the consequences) if the agent representing you is not showing you each and every property that might satisfy your investment objectives, instead of just the listings on which they can earn commissions on both sides of the transaction.

With commercial properties, this issue can be even more pronounced, as many agents like to sell their own listings rather than market them widely through the MLS to and through the real estate community. Of course, this does not necessarily benefit the seller, as it limits the potential customers who become aware of the property. And, it clearly does not benefit the buyer to be represented by the same agent committed to getting the seller the highest price for the listed property. Quite simply, the listing agent is the only likely beneficiary of this scenario.



An aside here is that an agent who takes listings must pursue listings. This requires an entirely different set of activities from pure representation of buyers. This represents another conflict in terms of the time and attention this agent must devote to that effort instead of spending *all their time* investigating and vigorously pursuing each and every property that might fit your investment criteria.

- 2. Avoid properties with limited appeal or those that do not stand up to the competition in the immediate vicinity.** They will be harder to sell when the time comes. It is always a good practice, when buying any property, to think about who will rent the property today, and who will buy that property from you when you're ready to sell. If you're buying a residential rental, you'll have fewer tenant prospects wanting to live on a busy street. Or wanting to rent a unit with few amenities when directly across the street or around the corner is a complex of units with many features. When vacancy rates are near zero, this will not be as much a factor as when they start creeping upwards of 5-8-15% at the more appointed units; if yours are lesser units, you might then be suffering a 25% or higher vacancy rate.

When buying a commercial investment property, keep in mind the prospective tenant's desire for easy access, availability of parking, traffic density and demographics of potential customers in the immediate vicinity.

No matter what type, if a property appeals to a narrower market, the demand for it will be lower and the time needed to market it will often be longer. In a seller's market, most properties will sell and relatively quickly, usually at and often above asking price. In a balanced market or a buyer's market, less appealing properties may require deep discounts and/or long marketing periods to sell.

- 3. Avoid being swayed by cosmetics.** Put the greatest weight on characteristics you cannot change. Smart sellers will freshen their paint, clean up the landscaping and make other cosmetic improvements to enhance the appeal of their property to potential buyers. These kinds of improvements are usually inexpensive, but they can have a powerful



appeal, especially on an emotional level. Try to look beyond what can be easily and inexpensively changed. Location is obviously the aspect that is least changeable -- and most important in selecting any type of investment property. Floor plans and space utilization are often changeable, but usually at somewhat more significant expense. Updating, especially with kitchens and bathrooms, usually carries a high price tag.

4. **Avoid having a short-term perspective.** Unless your strategy is geared around buying, fixing and turning your investments, buying any form of real estate with the anticipation of selling in a year or two can be risky. Real estate transaction costs are relatively high to both buy and sell a property. Markets change, although the long-term trend has always been upward. Buying an investment that will satisfy your needs for longer than a year or two insulates you even if the market turns downward: you won't be stuck with the wrong investment and unable to sell, or able to sell for the price you paid.

This thought may seem absurd in the present 1031 Exchange market, but all markets are cyclical, including the real estate market. There have been times in the past when prices did not increase, and even decreased, and that will happen again.

Another facet of a short-term perspective that can keep one from their investment objectives is trying to buy at *under the market price*. By definition, in the mainstream of real estate transactions, this is impossible. The market determines the market price. In a rare instance, where the seller is under intense pressure to sell immediately, or even less likely, where both seller and seller's agent are oblivious to market values, a bargain can be had. But if this were the only circumstance under which you'd be prepared to buy, be prepared to wait a long time or possibly forever to make your next purchase. And, of course, while time is ticking, prices are usually rising. So tomorrow's 'bargain' price might even be higher than today's market price.

5. **Avoid losing focus of your investment objectives.** Good decisions are hard to make when external pressures overrule reason. The very nature of 1031 Exchanges, with the rigid time lines involved, can tend to undermine objectivity. You need to have a clear set of goals. And your goals cannot be



in conflict with one another. For example, you cannot usually maximize cash flow and leverage at the same time. Cash flow is certainly important. Especially in the short run. But longer term, appreciation is where you're likely to derive the greatest return on any type of real estate investment. Your near-term tolerance for negative cash flow will determine the amount of leverage you can apply. The more leverage, the more you can expand your portfolio of holdings with a given amount of capital to invest. In the long run, this will yield the greatest appreciation potential -- more assets appreciating = more total appreciation. For younger, longer-term investors, this is usually the best approach. For those approaching or already at their retirement, positive cash flow, not leverage, may be more important.

Emotions can also quickly cloud a real estate purchase picture. Clearly this is less problematic with investment properties than with your personal residence. Yet, there are many facets to one's emotional quotient that can hinder sound decisions. When the market is as competitive as it currently is for investment buyers, buying a desirable property can be more frustrating than normal. If you recognize the normal sources of frustrations and pressures that can come into play, you will be better prepared to respond in a positive way and thereby, keep your longer-term goals in focus.

6. **Do not overlook appropriate property inspections.** When the investment market is as competitive for buyers as it has recently been, there may be a tendency to want to overlook prudent investigation prior to buying. It's difficult to see how that can ever be a smart move.

An investment property purchase is a major financial commitment. Sellers who are confident of the condition of their property should not object to a buyer wanting a reasonable period for expert inspections. If you're buying a residential property (1-4 units), you'll receive disclosures from the seller. With 5+ residential and commercial investments, you won't even have that statutorily required information to work from. Certainly you should be seeking, and your lender will be interested in seeing toxic hazard and waste disclosures from the seller with commercial properties.

If a seller objects to your reasonable request for disclosures and thorough inspections, it may be a red flag indicating there may be problems the seller



either knows about or suspects. Don't let the urge to do the deal overpower your good common sense.

***Your For Buyers Only Realty representative would be pleased to expand upon any of the subjects contained in this report, or any other area you'd like to explore, in a no-obligation personal consultation, either on the phone or in person. Why not call Gene Berman at (707) 794-9789 (or toll-free, 866 ONLY BUY) today to make an appointment and take a major step toward ensuring a positive outcome with your next real estate investment.***