

SOME LESSONS TO LEARN BEFORE INVESTING IN RENTAL PROPERTY

by: Tim Sullivan, CFP®, EA

Investing in rental property can be a great way to build wealth, diversify an investment portfolio, and create a significant passive income flow. It can also be an excellent way to lose money, concentrate net worth in an illiquid asset, and cause an otherwise normal person to question their own sanity.

Before jumping into the world of investment property, would-be-landlords should consider the following "lessons learned" before taking the plunge.

A bit of personal background here is probably appropriate. I have owned and actively managed various types of rental property over the last 20+ years in Columbia. This includes single-family, multi-family, and commercial investment property. I say this not to boast, but to point out that any wisdom shared was often learned through the school of hard knocks. If you can do something dumb, I have probably done it.

Lesson #1: Your personality is more important than your credit score or down payment amount when determining if you should purchase your first rental property. Whenever a client or friend inquires about purchasing rental property for the first time, I ask them a simple question. "If it is a Sunday afternoon and you sit down to watch a football game or binge watch your favorite TV show, will your day be ruined if you get a call that requires you to go fix a broken toilet at your rental property?" If the answer is "Yes," then owning rental property may not be for you.

Lesson#2: Do not purchase rental property with a partner to whom you are not married. OK, this might be a slight exaggeration, but only moderately. Debt maven Dave Ramsey has a well-known quote that says, "The only ship that won't sail is a partnership." Of course, there are countless examples of partnerships that have successfully navigated the treacherous waters of a partnership, but what Mr. Ramsey captures accurately is that partnerships are HARD and therefore more likely to sink to the bottom than to deliver a pleasant voyage.

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Lesson #3: Your most important job as a landlord is to find great tenants (how to do this is another article entirely). My emphasis on this skillset sometimes surprises would-be investment property owners. However, I would contend that nearly every other aspect of being a landlord can be learned over time. But, if you are unable to sign good quality tenants regularly, your experience will be so terrible that you will never have the time to gain all the other knowledge required because you will quit long before that point.

Lesson #4: Do not overpay for an investment property. If you are buying a personal home and the plan is to be there 10 years or more, overpaying is not necessarily a critical mistake. However, savvy investors fall in love with the deal, not the property. As such, the numbers must make sense. This column will address these “numbers” - calculations such as cap rate and return on investment - next month.

Lesson #5: Treat your tenants as if you might someday be their neighbor. Consider this the “golden rule” of property management. Like most investors, I was a tenant well before I was a landlord. If life were to take an unexpected turn, I could be a tenant yet again. If you treat people fairly and recognize that while you look at the property as an investment, for them it is their home, you will have respect for their space and empathy if a problem were to arise. It is my contention that landlords who view tenants as just an ATM lose out over time.

It is unreasonable to think that a new rental property owner will not make mistakes. The key is to limit mistakes and when they occur, make sure a lesson is learned that is not repeated in the future. While it may have taken me years to learn some of these lessons, hopefully others can learn from my mistakes and enjoy a smooth and prosperous path to investment property ownership.

Lastly, my property manager would add that hiring a great property manager will make all the difference and make your life a whole lot easier...her words.

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