

Three Questions to Ask Before Investing in Real Estate

It's important to ask these three questions when you invest in real estate:

How can I increase my rate of return? The cornerstone of any smart investment strategy is to calculate your rate of return. With real estate this is done by running the numbers using an internal rate of return (IRR) formula that takes into account:

- Present Value (PV) - what am I paying out of pocket to get into this investment?
- Term (N) - what's my timeline and how long am I going to hold this investment?
- Periodic Cash Flow (PMT) - what's my monthly cash flow?
- Future Value (FV) - what are my net proceeds (after expenses) when I sell the investment?

How does my rate of return with real estate compare with other investment opportunities that may have less headaches?

When calculating your rate of return, make sure to account for:

- Carrying costs (mortgage, taxes, insurance, maintenance, etc.)
- Your time spent managing the property
- Vacancy loss if you don't find a tenant

How can I reduce my risk? You may want to consider these strategies to reduce your investment risk:

- Increase your liability insurance in case something goes wrong and someone sues you
- Consider a rent-to-own strategy where you find a tenant before you find a property
- Consider mortgage strategies that result in more cash flow and/or better liquidity

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