

Five Ways to Minimize Risk in Real Estate Investing

By Mark Loeffler

These days, minimizing risk in your real estate investments is vital to long-term success. But do not confuse "minimizing risk" with "limiting risk". Limiting risk means investing conservatively. Minimizing your risk involves a few steps one must take to ensure their maximum-return investment will have the best possible chance of turning a great profit.

Risk minimization consists of strategies one can implement to keep risk low as your investment works for you. Minimizing risk in real estate investing need not be a confusing topic. In fact, keeping a few things in mind as you invest will help to minimize your risk without moving you into a conservative investing strategy. Of course, with each investment your risk minimization strategies will vary, but here are a few that are mostly universal.

1. Determine the Seller's Motivation

Ask questions to find out the reason behind a seller's actions. Are they trying to get out of a bad property investment, or simply trying to sell the property to finalize an estate? Is their current property too big or small for their current family, or are they aware of a plumbing issue and trying to rid themselves of a problem? Asking questions of the sellers and judging both the things they say and the way they say them will go a long way to determining the seller's motivation, and could perhaps keep you from taking over someone else's problem.

2. Determine your Renter's Motivation

Are they new to the city? Going through a divorce? Perhaps downsizing to deal with the current economic down swing? Or have they been evicted from their previous rental property for hosting a grow-op in their unit? Just as you were able to determine the seller's motivation by asking questions, you can do the same with your tenant. Judge not only what they say, but also how they say it and always, ALWAYS check references.

3. Lower the Chance your Tenant will Default on their Payments

To a certain extent, you have control over whether your tenants will default on their rental payment. Using a TDS/GDS calculation of 40% will ensure your tenants do not have too high of a debt ratio, and can actually afford to rent your property. Failing to do this could set your tenants up for disaster - no one wittingly rents a property with the intention of not paying their rent, and everyone's intentions are good at the beginning.

Juggling the numbers properly could prevent a sticky financial situation for your tenant and save yourself a lot of hassle in the future.

4. Look for Medium Term Investments Over Short Term Investments

Flipping a house in a bad market is not as good an investment as it is in a good economy. In fact, many people who bought at the wrong time are now scrambling to find ways of recouping their investments. If you have a property you purchased at the height of the real estate influx, selling in a low market is a bad investment decision, especially if you've fixed it up with the intention of flipping it. Instead, consider a rent to own strategy, and when the economy springs back up, look again at selling.

In this market there are some great real estate deals to be had. Purchase low and hold that property on a rental basis for two to three years while renting the property with a high monthly cash flow, and then sell when the market is back up. The monthly cash flow will ensure you have cash coming in when the market is low, and your profit when you sell will line your bank account, ready for your next purchase.

5. Use a Tried and True Strategy

Why make all of the mistakes others have already made if you don't have to? Find a good investment strategy that works with your goals and stick to it. After all, why would you walk through a mine field alone if there was someone else familiar with the route who could lead you safely through?

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