LeadDeveloper

13 Golden Rules Of Investing In Commercial Real Estate

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Commercial Real Estate Investment 101

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Commercial Real Estate Investing For Beginners

Investing in real estate, whether residential or commercial, offers ample opportunities to investors. They can build wealth, save for retirement, achieve financial freedom and what not.

There are several ways to invest in real estate; you can flip houses, buy real estate stocks, rent out properties, REITs, etc. I have already shared a detailed blog on **different types of** real estate investment strategies in an earlier post.

Among all the options, the most attractive are residential and commercial real estate investment. I must say, CRE or Commercial Real Estate Investment is worth eyeing for every property developer. A high-risk, high-reward asset class that includes a variety of property types you've probably never considered investing in before.

What Is Commercial Real Estate?

In simple words, Commercial real estate is a property where people do business.

You can also think of commercial real estate as a property having at least five or more units utilised only for commercial or income-generating purposes. Based on this simple concept, you can quickly identify commercial properties. Commercial real estate includes retail premises, workplaces, assembly plants, warehouses, hotels, motels, theme parks, quarries, hospitals, airports.

On the contrary, residential real estate include properties where people live. It includes houses, individual apartments, duplexes, triplexes, etc.

Tenants are typically families or individuals in a residential property, whereas businesses and corporations lease commercial properties. Commercial properties may be subject to more complicated zoning rules than residential ones, depending on their location.

It is critical to prepare yourself before investing in real estate. You should be familiar with all of the fundamentals, hazards, and, most significantly, the techniques employed by seasoned property developers. All you have to do is enrol in the most popular and well-structured property development courses, and you'll be on your way to success.

Why Invest In Commercial Real Estate?

Commercial real estate has a long history of compelling financial play during both up and down market cycles. It plays a vital role in a diversification strategy for property developers and investors. Domestic and international investors are looking to the United States as a haven to park their money to protect their original investment while generating a profit.

CRE or Commercial Real Estate can be a decent place to put your money whether you've had a long and successful career in residential real estate or you've never invested in real estate before.

Because of its stability, CRE remains a viable investment even when market cycles shift for various reasons. Commercial real estate is a beautiful method to diversify a portfolio because of its steady nature. Furthermore, direct Commercial real estate investment provides offers properties that can appreciate and deliver cash flow.

If this isn't sufficient for you, I can give you some convincing reasons for investing in commercial real estate. Before that, you should understand how to get started with property development and investment.

Here's a quick-start property development course that you should not miss at any cost (especially when it is FREE😉). This Free online course will provide you with a comprehensive overview of the property development process and the secrets to quickly becoming a property developer.

Learn the tips, prepare your strategies, and choose your own path to becoming a successful real estate investor.

Top Reasons To Invest In Commercial Real Estate

Consider the below reasons as an overview of why commercial real estate attracts a broader investor audience to the sector.

Attractive Returns Over Time

Most investors recognise that it is best to hold an asset for an extended period rather than trade in and out in search of profits. Commercial Real Estate can deliver substantial, predictable returns in this regard.

Commercial real estate investors frequently enjoy consistent cash flow from their investments, with income paid out annually, quarterly, or even monthly. This is because high occupancies and predictable rents often provide the consistent cash flow that most investors seek. Annual returns range from 6% to 12%, compared to 1% to 4% for residential properties.

This is also the stage where most real estate developers and investors fail. It is the time to learn from the mistakes of others. Consider the following five significant reasons why buy-and-hold investors fail to develop a property.

Lease Duration

A residential lease is usually month-to-month, or in rare cases, it may last for six months, a year, or even two years. On the other hand, commercial leases are not often month-to-month, occurring only at the end of a longer lease when the parties have not agreed to sign a new lease. A commercial lease is usually for two years, three years, five years, or longer.

The result for your property development portfolio should be clear. Longer lease terms mean fewer lease renewals and less time spent looking for new tenants. If you have a renter who has four years left on a fifteen-year lease, you know that you will have an unbroken stream of rental money for the next four years (barring the tenant's bankruptcy). This instils a strong sense of assurance. It allows you to confidently estimate your finances into the future, calculate margins, and build your strong portfolio property development.

Tax Advantages

Commercial real estate is subject to tax credits that can cut the tax burden on the property significantly.

There are several options for reducing or eliminating capital gains. If you buy properties in good locations, they should increase in value over time. However, you can depreciate the value of the structures over time for tax reasons, lowering your annual taxable income. In the end, you're depreciating what should be an appreciating asset for investment purposes for tax considerations. This benefit is not available in many asset classes.

You can also avoid capital gains taxes when you eventually sell your property, thanks to 1031 exchanges. You'll need to "swap" those gains for another property or item when doing so.

Deductions for mortgage interest, depreciation, and non-mortgage expenses, including upkeep, repairs, and association fees, are all conceivable when investing in commercial real estate.

Not good in math? Are you concerned about your tax and financial calculations? Not anymore with the advanced property development feasibility software.

Inflation Hedge

Commercial real estate has the advantage of being able to offset the long-term impact of inflation. The fact that property rentals can be adjusted with inflation, which is frequently the outcome of robust economic growth, is a crucial influence. This is different from assets such as stocks and bonds, which might experience decreased returns due to inflation.

Government Interference

There is not much interference by the government in CRE as compared to residential real estate. In comparison to residential real estate, government influence in CRE is minimal. If a commercial tenant fails to pay his rent, the landlord has the same recourse ability as a car leasing firm dealing with non-payment. This is one of the main reasons why many property developers opt for commercial real estate investment.

Let's understand this with a fantastic example. Consider a pleasant entrepreneur who rents both his home and his place of business, whether it's retail space, offices, or whatever. Assume he doesn't have enough money to pay both his residential and commercial rents. I believe he will pay the commercial rent long before he considers paying the residential rent, simply because the consequences of failing to pay the commercial rent are significantly harsher.

Whether you are investing in residential, commercial, or another form of real estate, understanding property options are necessary. Start reading the ultimate guide to property options if you're unfamiliar with the terminology or want to learn more about the various types of property options.

Management Overhead

When compared to residential real estate, the management overhead of commercial real estate is negligible. To be sure, commercial real estate ownership necessitates some management. Keep track of when leases are up for renewal and when rent reviews are due. You'll need mechanisms in place to keep the properties in good repair, deal with unforeseen events, verify rentals are paid and pay your own costs, such as property taxes.

More Off-Hours

Don't get confused with my words - Commercial Real Estate requires a lot of work. By more off-hours refers to the number of hours spent talking to tenants. In comparison to residential real estate, these hours are minimal in commercial real estate.

In commercial real estate, most of your tenants will be following the typical 9-5 schedule. It usually entails extra "time off," this way; you will be away from your phone and enjoy more personal time.

Want to start your property development career? I have already answered all the significant questions regarding property developers, their work and their career. Check out Property Developer FAQs and clear all your doubts.

Benefits Of Investing In Commercial Real Estate

As you saw, there are many good reasons to invest in commercial real estate. Commercial real estate investing can be both personally and financially rewarding. Many people engage in commercial real estate for future prosperity and stability, while others do so for tax benefits and to diversify their investment portfolios.

Commercial redevelopers can also benefit from the following advantages:

Higher Income

The primary benefit of investing in commercial real estate is the higher potential income. In general, CRE can provide better ROI, on an average of 6-12%. Second, because properties tend to have more units, commercial real estate has a more negligible vacancy risk. Also, as explained above, Commercial leases are often lengthier than those seen in residential real estate. This means that commercial property owners will experience significantly less tenant turnover

Professional Relationships

Many small business owners are proud of their businesses and want to protect their livelihood. Commercial property owners are usually limited liability companies (LLCs) who manage the property as a company. This allows landlords and renters to have more business-to-business connections, which helps in maintaining professional and friendly contacts.

Less Competition

Another benefit of commercial real estate is that there is less competition. The business space is less saturated with other investors due to the perceived difficulties of commercial investing.

Public Eye On The Property

The general public is watching the property. Retail tenants have a vested interest in keeping their store and storefront in good repair because it will harm their business if they don't. As a result, the interests of commercial tenants and property owners are aligned, allowing the owner to maintain and increase the property's quality, and hence the value of their investment.

13 Golden Rules Of Commercial Real Estate Investment

Rule 1 - Not Every Form Of Property Is The Same

There are several different asset kinds in commercial real estate. While commercial real estate is traditionally divided into five categories: industrial, office, retail, multifamily, and particular purpose, there are numerous other property types to consider, including self-storage, medical, elder care, land, and hotels. Each sector's market forces, return, and net profits are all different.

Based on availability and demand in the asset's specific area, some properties do better than others. Even on a macro level, though, some industries outperform others. In today's environment, it's critical to understand how to pick the asset types that are most profitable or offer the best potential.

No matter which asset type you are selecting, get yourself acquainted with property developer FAQs if you want to achieve ultimate success in each of your property investment and development projects. You will find answers to all your questions.

As per the current trend, we can say that industrial CRE asset is one of the best performing classes while retail space is the lowest-performing commercial real estate asset. With the rise of online shopping, retail stores find it difficult to compete, resulting in lower returns and slower growth. Keep in mind that some commercial real estate sectors have more excellent vacancy rates since they may only have one tenant, such as an industrial warehouse or a single office space.

To reduce the potential risk, some property developers and real estate investors choose properties that contain multiple tenants.

Before you make any investment, ensure to perform thorough research of each asset class. You need to identify the investment potential of that sector, use any of my tools to receive accurate calculations and make a firm decision.

Rule 2 - Risk Is Equal To Yield

As I have told this several times, Real Estate is a pool of unlimited risks and rewards. You might have heard this before - the higher the risk, the better the reward. Similar to this, we can't deny that the lower the cap rate, the lesser the risk. In other words, the market capitalizes on rental revenue with a low cap rate for a low-risk investment (i.e., a large factor). A high cap rate (small factor) would be applied to the income from a risky property.

As a result, the goal isn't necessarily to find the property with the highest return, but rather the property that offers a good balance of risk and rewards appropriate (and lucrative) for your situation. If you can find a property that has a low risk (low market cap rates) yet a high return, you've found the deal of the century.

You should start the preparations for your first property development project. Be the Game Changer and prepare your first project faster than your competitors.

Rule 3 - Understand Market Cycles

The profitability of commercial real estate is directly related to the economy's health, unemployment rate, and GDP. All these are the parts of the commercial market cycle which you should know. Understanding what precisely the market cycle is and how it works is highly beneficial for you.

This commercial real estate investment rule will assist you to avoid purchasing at a high price and having to sell at a low price. Furthermore, understanding sure market cycle signs can aid in determining what possibilities are available right now and making more informed investing selections.

Rule 4 - Control Your Liabilities

"Liabilities are just assets in hiding."

While it has been seen that people have huge control over their assets and not on liabilities, but the Golden Rule of Commercial Real Estate Investment says that property developers or real estate investors must have some control over their liabilities.

In some places of the World, it is nearly impossible to fix the mortgage interest rate for more than a few years. Ensure to fix your interest rate if you find any such opportunity.

One of the significant advantages of the US real estate market over many other nations is securing fixed-rate mortgages, even 30-year mortgages.

You are just a click away from living the life of your dreams. Check this ultimate guide to get started with real estate development.

In my career in property development, I have met a lot of property investors who choose not to fix the rate. For saving a minimal amount (0.5% lower interest rate), they get fooled by the interest rates touching roofs in the future. It's a blunder perpetrated not only by legions of typically rational investors but also by armies of mortgage brokers who, no doubt, make more money on loans that turn out to be more profitable for the banks.

I advise all my students to avoid providing personal guarantees on any real estate loan. There are two reasons behind avoiding personal guarantees in the loan.

First and foremost, a real estate investment should be self-sufficient. The risk of having a personal guarantee is that it could be called up, forcing you to repay the principal on loan taken out by a limited-liability company. Of course, signing a personal guarantee dismantles this liability barrier.

The second reason is that banks will frequently ask for a list of your contingent liabilities or liabilities that may fall on your shoulders when applying for future loans. The longer this list becomes, the more reluctant a bank will be to offer you money.

Rule 5 - Know The Supply And Demand Of Your Market

One of the most crucial things to keep in mind when investing in commercial real estate is that each market is unique. You're putting money into a specific geographic area with its supply and demand dynamics when you invest. Certain property kinds may be doing well on a macro level, yet you may find an oversupply in your city or vice versa. Investors frequently fail to undertake sufficient market research to identify whether there is a risk of market saturation.

Researching the market supply in your surrounding area is a great place to start, considering both the present rentable square footage and any new square footage that will add due to current activity and planned developments.

If you've found an undersupplied property type in your market, you can undertake a feasibility study to determine the sector's future growth potential and the chance of success.

My structured property development courses will provide you with all of the knowledge you'll need to succeed in the property investment and development process. Not only you will reveal my secret success strategies, but you'll also get a taste of real estate's practicality with these courses.

Rule 6 - Perform Thorough Due Diligence

A prospective buyer's due diligence period is when he or she can perform extensive research on an investment possibility. This can entail looking over the former owner's financials, records, tax returns, profit and loss statements, and doing surveys, property inspections, a feasibility study, or any other research required.

Don't forget to look over the 26-question Property Development Due Diligence Checklist, which will help you lower your risk. Many of my students request this checklist to ensure a smooth and error-free property development project. You can trust and make this checklist part of your own due diligence process as they are mine too.

It is quite common for new real estate investors to become so enthralled by the prospect of purchasing their first commercial property that they overlook something important during their due diligence. You will minimize potentially costly mistakes if you have a strong awareness of what needs to be studied, properly examined, and inspected before you buy.

Rule 7 - Ensure Safety First

"The Safe Way Is The Only Way!"

Mind my words here. Whether you're new to property development or have a lot of expertise, making sure your projects are safe should always be your top focus.

Return on capital or return of capital: which is more important? What good is a 25 percent annual return if the investment fails after two and a half years? Make sure your money is secure. It includes obtaining adequate property insurance to ensure that your assets are protected in the event of an earthquake, fire, or another natural disaster.

Developing and investing in real estate entails several hazards. As a real estate developer, you should know various real estate development risks and ways to manage them.

Rule 8 - Love Your Deal And Add Value To It

One of the most common mistakes investors make when purchasing or investing in real estate is falling in love with the property. When it comes to commercial real estate, the tenant and the lease are usually the most critical factors.

The house could be useless without a renter – or it could be a fantastic opportunity. It is entirely dependent on your level of education and experience. You can achieve this by opting for my Quick Start Property Development Course, in which I will reveal the methods and secrets of successful property development.

You'll have to wait for inflation to raise the value of your rentals and, consequently, the capital value if you acquire a wholly leased commercial property at a fair market price.

Alternatively, suppose you acquire property with some vacant space, below-market rents, unused rooftops, unleased storage space, and various other attributes that you can do something with. In that case, you may swiftly swap your ideas, thoughts, energy, and passion for significant sections of capital value. Ultimately, it is You who play a critical role in the real estate you buy.

Rule 9 - You Only Need One Single Deal To Make Dollars

"You can make a million excuses, or you can make a million dollars."

A serious property developer will opt for making million dollars. But what does it take to earn handsome money? JUST A SINGLE DEAL.

Commercial real estate isn't always about numbers, where the more properties you purchase, the better your chances of becoming financially independent. Two deals are better than one. Focus on one commercial property and manage it well rather than juggle five different projects and barely track who owes how much rent.

Mastermind your first and subsequent property development and create your successful property development strategy.

Rule 10 - The Tenant's Ability To Pay Rent Limits The Property's Value

This commercial real estate development rule defines the cap rate differently. If you can't find a tenant for a building, it won't be worth anything, and no bank will offer you money to buy or refinance it. Your capacity to build a portfolio, as well as the value of that portfolio, is contingent on your ability to find steady, long-term tenants.

More specifically, the value of a building is not solely determined by how much one tenant pays in rent. What if that one high-rent renter left? The worth of a building is determined by the amount of rent you can persuade any renter to pay in an acceptable amount of time. As a result, always strive to improve the environment for current tenants—it will make them less likely to quit. It will be much easier to find replacement tenants if they do depart.

Rule 11 - Ensure You Have A Contingency Fund

Any investment entails some level of risk. Unknown factors will always impact your overall yield, no matter how much study, verification, or preparation you do. Accounting for cost contingencies is one strategy to mitigate this risk.

You can set aside additional funds as part of your initial acquisition cost to cover unexpected expenses such as rent increases, management changes, renovations, rezones or building costs. These funds can be used to cover debt service costs until the property stabilizes. If there is negative cash flow, cost contingencies can be very helpful. They also help to improve the property's performance. Commercial real estate has a standard contingency budget of 5%-15%. However, this will depend on the asset and sub-performing properties.

Rule 12 - Choose Your Associates Carefully

Even if you have a great team of lawyers, real estate agents, accountants and private detectives, crooks are hard to beat. Even if you win the case and get what you believe you owe, the scammers may have taken something else. Not to mention the time and effort you spent dealing with them in the first place and cleaning up afterwards.

Only one solution is available: Work with ethical people. Although you may not make as much money quickly, it will last longer, and you will feel happier about it.

The most significant advantage of dealing with ethical people is that they are more likely to be friends with other ethical people. As you grow in your circle of friends, you will find yourself surrounded by people who are more open to fairness, kindness, compassion, and awareness.

Rule 13 - Invest In Commercial Real Estate With No-Money

Last but not least, learn how to invest in commercial realestate with no money. This last commercial real estate investment rule has transformed many developers' life. However, very few are able to pull execute the no money down investment strategy. Spend time learning how to structure deals, negotiate, run number on projects so you can put together investment projects for yourself and your investors in a way that requires little or no money investment from your side.

If you would like to learn more about investing & developing residential and commercial real-estate with little or no money, click here.

Is It A Good Time To Invest In Commercial Real Estate? [Especially In The Post Covid World]

Like everything else in the post covid World, the rules of investing in commercial real estate have changed. More businesses have realised that they can have their employees work from home. More employees have realised that they like working from home.

I already know people who now work from home [exclusively] as their employers have scaled down their office spaces. As technology allows us to be more productive and more fluid, workspaces will change.

Concepts like shared workplace, hot desks, 2 days office and 3 days from home get adopted on a broader scale; we will see a paradigm shift in commercial real estate. And that shift is already evident in the office workspace.

With uber concepts like cloud-kitchen and on-demand services will rise, which will, in turn, drive demand for warehousing. Most retail will move online, and office spaces will be repurposed to mixed uses.

Is Commercial Real Estate A Good Investment?

Irrespective of this shift, human beings are social creatures at the end of the day, so commercial spaces that offer [covid compliant] entertainment, support social gathering, and provide cheaper storage or shared spaces will be in high demand. So in a nutshell, although there is a paradigm shift in the way we use commercial real-estate, it still remains a good cash-flow investment.

FAQs

Is It A Good Time To Invest In Commercial Real Estate?

Absolutely, concepts like shared workplace, hot desks, 2 days office and 3 days from home get adopted on a broader scale; we will see a paradigm shift in commercial real estate. And that shift is already evident in the office workspace. With uber concepts like cloud-kitchen and on-demand services will rise, which will, in turn, drive demand for warehousing. Most retail will move online, and office spaces will be repurposed to mixed uses. Irrespective of this shift, human beings are social creatures at the end of the day, so commercial spaces that offer [covid compliant] entertainment, support social gathering, and provide cheaper storage or shared spaces will be in high demand.

What is the golden rule of investment?

Having a well-diversified portfolio is one of the golden laws of investing. To accomplish so, you'll need a variety of assets that will typically perform differently over time, allowing you to diversify your portfolio and lower overall risk.

Can real estate make you a billionaire?

Real estate tycoons, who own thousands of commercial and residential properties, are among the world's wealthiest billionaires. Residual income, predictable cash flow, tax savings, diversification, and leverage are significant advantages of real estate investing.