



# Invest in a Cottage with Confidence

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# Contents

Introduction	3
1. Where do I start?	4
2. How to find the right Cottage Property	5
3. Proximity	7
4. Who Manages the Property?	8
5. How to manage your money	10

## Introduction

### **Investing in Cottages with Confidence: How to get into the Real Estate Investment Market with a Rental Income Property**

Most people look at investing in a cottage as a nebulous and tricky thing to get into. There appears to be so many potential issues, that for many, it doesn't seem like it could ever be a viable option.

But what if they had the confidence to invest in a cottage? Markets all across Canada have skyrocketed in the past 10-15 years, cottage country included, but even more than that, people have increased their monthly cash flow by investing intelligently in real estate and renting out their properties to cover their mortgage and property expenses, and generate extra income!

Whether you're in it for the long-term equity play, or you want to earn extra cash month to month, there is a strategy and plan for you.

This document is intended to show you how you can get into the cottage investing world with confidence, with strategies for systematizing your rental income property to work, without you having to.

## 1. Where do I start?

One of the most common reasons people don't get into cottage investing is that they don't feel like they can make the down payment. They already own a home so how do you get started on a cottage as well?

You might think you don't have the cash, but do you have equity in your current home? You can use that equity to put a down payment on a property and get the cottage you always wanted!

Most people don't think about the equity in their homes because it's not "ready" cash. It can, however, be used to invest in real estate and thereby grant you the opportunity to start earning a regular cash income.

You can get a line of credit on your home, and it's a good idea for a couple of reasons:

- 1) If you get sick or there's an emergency for which you need ready cash (and to prevent mortgage fraud – more on this later)
- 2) If you want to invest!

So, the first step is understanding where you can get the money required for your down payment. Banks aren't exactly keen on handing out loans these days, and so you have to be smart about how you can take advantage of the equity you *do* control.

If you're thinking of getting a cottage, and plan to use it to generate income when you're not there, think of the equity you already have in your home. Or, see if you can increase it.

Then, it's a matter of waiting for the right opportunity to come – and it's not always the first one. Rookie mistakes can be costly, and one of the most common ones is to act too quickly without doing enough due diligence to ensure the cottage and the financials work for you in every way.

Read on to find out how you can make sure that, once you've decided to take that first step, you don't make any *missteps*!

## 2. How to find the right Cottage Property

Let's assume that now you have figured out the whole "where do I get the money" idea. Now we move into finding the right property. It's easy to get excited once you've made the decision to buy a cottage, but you must be careful. What you buy isn't necessarily something you'd want to live in yourself!

Most people want to buy that Canadian dream – a beautifully restored cottage with bay windows overlooking prime Muskoka lake frontage. While that would be amazing, it's not always feasible.

You actually want to buy the *opposite* of your idea of the dream cottage. What you should be looking for is perhaps a simpler cottage, close enough to the main Muskoka lakes to appeal to renters, but not close enough that the price is out of reach.

This is where working with a realtor has its benefits - an industry professional can help you hone in on undervalued areas and pockets of value close to popular areas in the Muskoka region. We do it for our clients all the time!

Finding an undervalued property in a prime location is the most important part of an investment property because of the long-term equity play - the property will continue to "make money" as it rises in value.

There are two options for renting out a Muskoka cottage:

- 1) **Monthly Rental Contracts:** This is the safest option for property rentals as a longer contract term means guaranteed mortgage payments, for the duration of the rental agreement. The only caveat to monthly cottage rentals is that the market slows down considerably in the off season.
- 2) **Weekly Rentals:** This is a great option to maximize your investment income potential as weekly rentals allow you the opportunity to charge a higher premium on the rentals and cash in on the demand. The only downside is that if your property doesn't get rented, you don't get paid.

Let's look at two examples so you can see how this would play out. Although the rental potential is low in off season, properties can make enough money to cover their costs and generate cash flow by renting May to September. Also, if you buy a four season cottage, you may be able to capture renters who love the winter (snowmobiling, cross country skiing, etc.)

Example 1: Monthly Rentals

Property: Cottage on Pine Lake, Muskoka

Purchase Price: \$400,000

Mortgage: \$320,000

Monthly payment: \$1424

Rent: \$4000-6000 per month, including utilities

Estimated monthly cash flow: \$2576-4576 per month\*

Example 2: Weekly Rentals

Property: Cottage on Pine Lake, Muskoka

Purchase Price: \$400,000

Mortgage: \$320,000

Monthly payment: \$1424

Weekly Rent: ranging from \$1000-2000 per week in low season/**\$2500-3500 per week in high season**

Estimated monthly cash flow: **\$2556-\$12,576\***

The potential for cash flow properties is higher the closer the property is to the more frequented parts of Muskoka. There is a huge demand each summer season for weekly rentals, which makes this option the smartest bet to make a huge profit, which can offset the slower off-season rental periods.

\*These numbers are estimates only, many variables will impact cash flow.

### 3. Proximity

Most people fear having an income property that is a long distance from their primary home. But you needn't fear distance!

One of your chief concerns is going to be “Who's going to manage the property if I'm not close by?” and we'll get to that very important question soon! But it's important to get into the mindset of finding the *best* property, and not the most *convenient* property.

In any business decision, there are trade-offs, and so you must account for proximity being one of them. If you're looking only around the Muskoka Lakes area, or similarly highly affluent areas, finding an affordable investment property might not be the easiest thing to do. So, you have to go a little further afield to get the property that generates the results you need.

Take into consideration the distance from the major urban areas you'll be targeting – like Toronto and the GTA. Estimate how much time it will take for people to get there, and estimate that a 2-3 hour trip is likely going to be an acceptable distance. You'll get more rentals if people don't have to drive a great distance to get to your property.

But think also about when YOU and your family want to use it, too! How much driving do you want to do? How close it is to the amenities like grocery stores, gas and other conveniences? Again, the less distance to these local amenities, the more popular your spot will be (and the more you'll love it, too!).

#### 4. Who Manages the Property?

This is one of the most important details you will have to sort out, so do so carefully and cautiously. You have a decision to make: Do you want to manage the property yourself, or have someone manage it for you? To make this decision, you need some information so let's break it down.

Firstly, we're going to look at costs, because that's pretty well what it always comes down to. To hire someone to manage your property they will take a fee, usually based on the gross revenues of your property. For a single property, you could expect someone to take around 10% of the rental fee.

When entering any agreement with a property manager, it is important to review the fees and services offered in the agreement so there is a clear understanding of what the fee covers. A good rule of thumb is to ask about additional services offered that could incur additional fees down the road.

Don't select your manager based on price alone, though. What other services do they offer? Check their network of repair people and contractors. If you have someone that is cheaper, ask him or her if they'd be open to using your contact. Ask about their policies for repairs – will they show you their invoices? Transparency in costs is key to ensuring you net a good income. You don't want your costs to spiral out of control, and if your property management company is not being open with you, you lose control.

But let's say you want to do this yourself. It's absolutely possible, but there are a few very important considerations. The first is time: do you have enough? If you work full time, and have little extra time for your cottage, it might not make sense to try to take on property management as an additional responsibility. Can you manage the stress of finding and keeping renters, managing disputes, etc.? Not everyone can, and management companies are trained in landlord-tenant resolution and mediation.

Next, do you understand the various laws that govern landlords and tenants? Do you know what rights you have, and what rights your tenants have? You can educate yourself on these, and do just fine but there is a learning curve you'll have to overcome at the beginning, and mistakes are likely. If you have the wherewithal to stomach a few missteps but keep the ball rolling, then you can likely manage your own property.

Each area is different, so make sure you're aware of bylaws and restrictions to ensure that there are no surprises with your rental income property. As realtors, we are a resource and can help guide you with finding answers.

As to insurance, each cottage owner must advise their own insurance company that they will be using the property as a rental, at least for part of the year.

Lastly, you'll want to ensure you also have your own network of contractors and repair people you can call on, sometimes on a moment's notice if there's an emergency. As realtors, we can also provide a network of professionals.

So, do your calculations, but also think about your personality and ability to handle managing a property on top of all your other obligations. Once you do, you're off to the races and success in real estate investing is yours!

## 5. How to manage your money

Before you make your investment purchase, you must first determine how much you will actually need to spend annually to maintain your investment property in Muskoka. Annual insurance can range anywhere between \$1500-\$5000 depending on the size of the buildings, if there is a boathouse on the property, or additional outbuildings.

Annual taxes on a smaller property could average \$2000-\$4000 in the Muskoka area, and if your cottage is located off a main road, expect to pay around \$400 annually for plowing and road maintenance. Hydro and propane costs can be \$2,000 a year, and general annual maintenance ranges between \$1,000-\$3,000 depending on the condition of the property.

Making sure you can afford a cottage even if you have some months/weeks without rental income is essential. Work with your lender and realtor to build out each cottage scenario, work the numbers, and then go over them one more time! Avoid becoming cottage rich and cash poor, because eventually, you'll end up being forced to sell the cottage you worked so hard to get.

So get a good, solid, experienced financial advisor, someone who will watch over your investment and alert you to any issues, challenges, etc. If they're really good, they'll even be able to offer you advice or ideas on how to increase your income or decrease your costs. They're hard to find, so interview them carefully and closely about how they manage their clients, how often they'll be in touch with you, etc. They're part of your team, and treat them as if they'd be managing the money themselves!

Once you've determined the financial viability of getting a cottage, you'll want to create a bank account for your investment property. That way you can isolate your funds and track your income and spending more closely. All rent cheques go in, and any maintenance, update and management fees come out of it.

Look at your numbers daily – not weekly, and definitely not monthly! Build your power team, which should include your realtor, your financial advisor, your lawyer, contractors, and property management.

Schedule your call today to start the HUNT for your cottage investment property.

Let's get started!

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