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HOW TO MAKE MONEY FROM **SERVICED** APARTMENTS



Toby Hone

This is an excerpt from Lawpack's book *How to Make Money From Serviced Apartments*.

Landlords: To find out more new ways to increase your rental yields, [click here](#).

How to Make Money from Serviced Apartments by Toby Hone

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Introduction

A lot has changed in the last 12 months. The onslaught of the credit crunch has had a serious impact on house prices with mortgages falling away daily. The one redeeming factor has been the dramatic fall in the Bank of England Base rate which has gradually filtered through to lower interbank lending.

Great – so money is cheap!

That may be the case but the problem is there is very little available. Banks are more stringent on who they lend to, and are asking for much higher deposits too. I remember back in 2006 when 90% BTL mortgages were available. Now the best is a 75% LTV! Combine that with the fact that house prices have fallen around 15% over the last 12 months means many people can't remortgage because their house prices and existing mortgages are crawling closer together.

There has also been another side effect from the housing slump and that is that there are more accidental landlords entering the market. Many of the 'For Sale' boards have been replaced with 'To Let' boards and this has had a marked effect on rental yields in many areas with some areas experiencing rapid drops in rents because of a dramatic rise in the stock of rented property.

This all points to a need to find new and different ways to improve rental yields and this book will show you how to utilise one of the most potentially lucrative ways of doing this in the current climate, namely through offering short term lets or serviced apartments.

The current economic climate poses an uncertain future for anyone involved in property. From home owners struggling to pay their mortgages with the constant threat of redundancies and unemployment, through to tenants struggling to pay their rent, as well as landlords having to deal with a lack of mortgage funding and increasing rental arrears.

It may seem a strange time to even contemplate investing in property in any form. Indeed the reported house price falls of around 15% in 2008

point to even further falls in 2009 with little hope of any immediate recovery as banks and governments try and stabilise the financial system.

So why even consider investing in an asset that is likely going to lose value in the foreseeable future? Simple. Because through leverage, property offers scope to produce significant cash returns over and above what you may achieve by investing your money in a bank. Current savings interest rates offer unattractive 2% (if you can find them) interest rates which you still get taxed on. If you then discount your interest received by the level of inflation you will see that keeping money in a low interest bank account is actually losing you money. That does not leave a whole lot of money left for you to live off.

That said, in my previous book *How to Beat the Credit Crunch* I discussed the many ways in which existing landlords can improve their positions. I also included an overview of the four main methods I have, and am still using, to make money in the credit crunch. However, that book focused on dealing within the buy-to-let arena with tenancies of at least 6 months.

Serviced apartments are a whole new ballgame!

A serviced apartment is a type of furnished, self-contained apartment designed for short-term stays, which provides amenities for daily use.

Wikipedia

Based on the definition above the primary differences between serviced apartments and buy-to-let are:

- You are typically dealing with short term stays instead of assured shorthold tenancies.
- Your tenant turnover is much higher with tenants only staying a few days or weeks in serviced apartments.
- Serviced apartments are able to offer much higher rental returns – potentially 300% more than normal buy-to-let.
- You have to provide a fully furnished property with more services included, whereas buy-to-let is usually provided on a unfurnished and tenant pays bills basis.
- The running costs within serviced accommodation are much higher due to the inclusion of bills and services, whereas tenants usually are responsible directly for these under buy-to-let.

- The channels of marketing to the different sets of tenants are quite varied and as such, thought needs to be given as to the most effective methods.

Throughout this book I will refer to ‘serviced apartments’ and ‘serviced accommodation’, however, it is possible to provide serviced accommodation including whole houses. For the purposes of this book I have assumed and referred to ‘apartments’, but it is worthwhile to remember that all the points discussed in this book can just as equally apply to a 2-bedroom or 6-bedroom house.

It is also worth noting that although predominantly located in urban and city centres, serviced accommodation is also provided in remote or rural locations also this makes it more difficult attracting regular tenants.

When I first thought of serviced apartments I initially envisage minimalist luxury designer apartments with top end furniture and finishes, with loads of sparkling accessories and that is often what is provided.

It is worth remembering though that just as there are different levels of hotel accommodation with different standards, so there is a differing level of service and specification within serviced accommodation and I will show you how to judge what level you need to provide for your targeted tenants.

This book was written with a view to providing a step by step outline of how to analyse the viability of providing serviced apartment accommodation in a specific area, highlight the key areas that need to be considered and dealt with, and where viable, implement a strategy to attract tenants through key marketing efforts.

You may be looking at buying a new or existing apartment and rent it out, or perhaps you already have a number of apartments but want or need to increase your rental income because of the economic downturn. Perhaps you purchased a city centre apartment and are finding that the over-supply of these types of units combined with the existing economic climate has substantially reduced your investments value whereby you can’t sell, and you can’t achieve a rent that will cover your mortgage.

You may even be in a position of being unhappy with the low levels of interest on offer by high street banks and may want to investigate other ways of improving the return on your money.

Whatever your reasons, I will show you how it is possible to provide serviced accommodation starting from researching whether there is a market for it, through to crunching the numbers and getting your first property fully fitted out for the smallest outlay, to getting your marketing up and running, your own website (if you are so inclined) functioning and getting tenants into your apartment!

As with anything there are risks, however, by careful research and careful planning it is possible to take advantage of a real opportunity to make healthy profits from providing a valuable and growing service.

CHAPTER 1

An overview of the UK serviced accommodation sector

Over the last few years more and more serviced apartment providers have been entering the market with many thousands of rooms available throughout the UK. For example one Manchester based company is intending to open over 120 units in Birmingham and Aberdeen with additional properties in Liverpool, Bristol, and London.* This expansion is despite the current economic turmoil and is supported by a number of macro and micro economic changes which are actually supporting the growth of this sector in the current doom and gloom.

Other companies also point to increasing opportunities in this sector with record years on the cards for 2009 and expectations being that the economic downturn will aid the growth of serviced accommodation – both in the UK and internationally.**

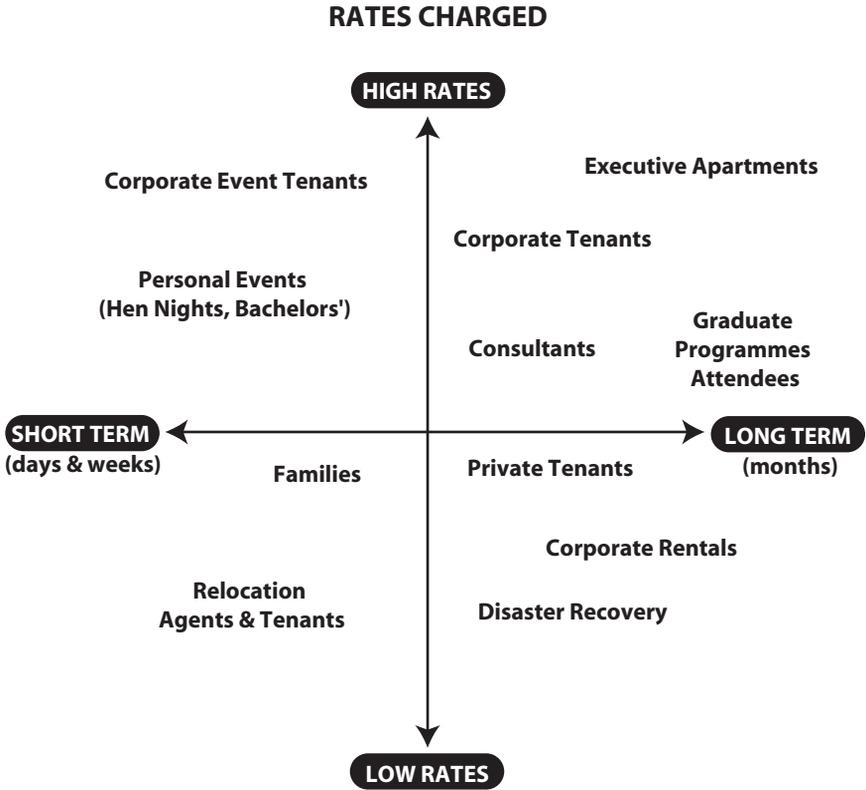
The growth has been prolific in both the provision of new units, and also the networks that have sprung up online offering tenants seeking this type of accommodation.

A closer look at the sector via the diagram below will illustrate different tenant groups and their requirements and will give a clearer idea of the different types of markets that can be targeted:

*www.moveandstay.co.uk/serviced-apartments-offices-news-uk//labels/UK%20accommodation.html

**<http://mag.digitalpc.co.uk/ActiveMagazine/print.asp>

Some of the groups are self explanatory but those a little more ambiguous are:



The corporate tenant

The majority of short-let clients come from the corporate world and they may be looking for short- to medium-term accommodation for important visiting staff/management or to make the transition more comfortable for employees they are relocating between offices.

The corporate event tenant

These include employees and management attending conferences, exhibitions and trade shows. This group can also include sportsmen and sportswomen and their audience when major sports events are held such as annual events including Wimbledon, or any major local events.

The relocating tenant

Individuals relocating to the UK or from elsewhere within the country may decide to try before they buy and with the downturn in the housing market this is even more prevalent as nervous prospective buyers wait for the housing market to stabilise. Not wanting to restrict themselves to a six- or twelve-month tenancy agreement, they may wish for the flexibility of a short let to allow them to continue searching for a home to buy or wait till prices stabilise.

The disaster recovery tenant

Insurance companies often put people up in hotels while their homes are being repaired after a disaster. However, if a family is likely to be kept away from their home for an indeterminate amount of time, the insurance company may consider it less traumatic, and more financially agreeable, to rehouse them in a short let.

Now it may be tempting to assume that the best type of group to target would be the highest rate and long term group, however, not only does this require significant start up investment to satisfy superior specification and location requirements, but this is perhaps the sector with the most competition.

On the other end of the scale the low rate short term lets may require less start up investment, but they will carry higher advertising, marketing and running costs and are perhaps most closely competing against hotels.

The diagram above is not an exhaustive list of market segments and could just have easily included a number of additional segments and variables such as level of investment needed, operating costs, advertising and marketing costs, degree of competition etc. The key is to recognise that before deciding which type of client you wish to target you will have to match the factors at your disposal to the right market segment.

So don't try and target executive apartments if you have a semi-urban apartment and little investment capital available. Equally trying to target a high tenant turn-over market segment such as hen nights without having the resources to aggressively market and commit additional resources and time to managing the property may mean you won't succeed in attracting

these tenants. Match your resources and unchangeable factors to the right market segment!

The housing boom over the past few years (excluding the current difficulties) and resultant growth of apartment blocks has created an increasing supply of units. Although the immediate outlook for apartments is bleak with many off-plan investors delving into purchasing units that were either horrendously overpriced, or did not have realistic achievable rents (and in many cases both these factors applied) the fact remains that serviced apartments are still an attractive investment.

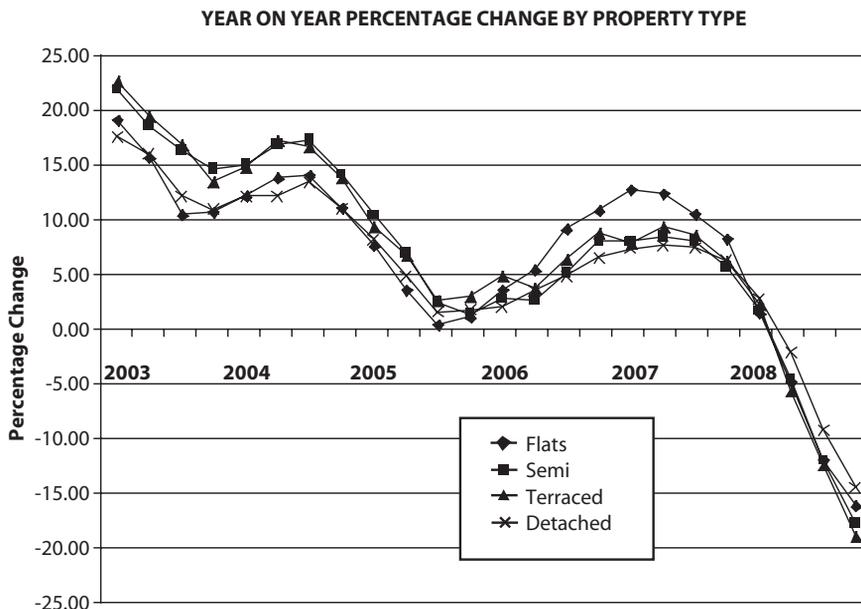
Looking at the current housing price correction, of which apartments have suffered severely over last year, this can actually be viewed as a good sign for the serviced apartment sector. The prices, through falling, have resulted in more scope to acquire these units at better prices. There has also been upward movement in the yields achievable as rents remain static, however, asset price falls mean the rental yields increase. The graph overleaf shows the year on year percentage change by type of property and was compiled based on the latest Nationwide house price data - www.nationwide.co.uk/hpi/historical.htm

You should notice that all property types have fallen by between 14.8% and 19% when compared to last year. One of the surprising figures is that flats actually performed 3rd worse, falling on average 16% from last year. The worst performer was terraced houses that fell almost 20% since last year.

The downside of the fall in property prices is that if you have not already purchased these units, you will generally have to put a sizeable deposit down due to lenders regarding this housing sector as the highest risk sector due to an apparent oversupply of these units in the past few years. This over supply is being corrected though as many developers who specialised in building these types of units, now struggle to raise the capital and many developments that have gone through the planning stages have been curtailed until the economic situation improves. *

There is however an upside to the stigma surrounding apartments and that is through the proliferation of below market value purchasing methods which can enable you to utilise discounts off of RICS valuations to secure apartments at very attractive prices.

*<http://mag.digitalpc.co.uk/ActiveMagazine/print.asp>



The methods used in these BMV purchases are typically in the legal ‘grey’ area in that not all information is given to all parties involved in the purchase of the property. It is because of this that I tend to steer away from using this method and prefer to rather find alternative ways of putting the deposit down, and extracting this after 6 months through re-mortgaging.

The reason for the 6 month wait is that lenders generally will not re-mortgage a property (especially apartments) unless you have owned it for at least 6 months. If you are able to negotiate a sizeable discount (e.g. 35%) off of the purchase price of the property then you can realistically extract this upon re-mortgaging after 6 months of ownership and ensure you maximise your return on investment.

What this means for those wanting to get involved in providing serviced accommodation, is that capital growth prospects do not look that attractive, although there is still lending and hence leveraging available (although higher deposits are required). So don’t expect to buy an apartment and be able to sell it for a profit 6 months later – plenty of off-plan investors have burnt their fingers in the past 18 months trying this. Rather, the appeal of entering the serviced accommodation sector will be the prospects of increasing your rental returns by as much as 300%! So the focus will be on cash generation and not capital growth.

There are also additional criteria imposed by lenders which specifically limits their lending exposure to any development or area which is applicable if you are considering purchasing more than one unit.

Other restrictive criteria include the conditions relating to the age of the property and whether it is an initial occupancy property (IOP) which increases the risk to the lender and can further reduce the amount you can lend, and increase the interest rates and fees lenders will charge you.

That said, there has still been significant growth in the serviced accommodation market, which is expected to continue.*/**

Why? A number of the reasons are mentioned below.

Cost cutting: In the current climate companies are looking at cutting costs and serviced accommodation offers a cheaper alternative to hotels. Apartments are typically 25% cheaper than hotels and with many companies having to increasingly cover the accommodation requirements for contractors and employees working on projects running over many months, it can add a significant saving to use serviced accommodation. Company travel managers are increasingly realising the significant savings that serviced apartments offer over hotels.* Also, telephone call costs are drastically cheaper in serviced accommodation than compared to hotels.

Flexibility: The current economic climate has meant that companies are moving employees around on a more short-term basis as opposed to committing to long-term assignments, as short term assignments can be terminated more easily. So instead of having to commit to a 6 or 12 month tenancy, companies are opting to use serviced accommodation due to the flexibility that it offers.**

Convenience: The ability for tenants to do what they want when they want to means they are not as restricted as they would be in a hotel. So they can clean their clothes, make breakfast or dinner, have a snack, or make a cup of coffee whenever they want without having to wait endlessly for room service.

Shift in employment methods and globalisation: The proliferation of contractors in virtually every sector of the UK job market means that there are more project workers, managers, specialists etc than ever before being

*www.servicedstays.com/news

**www.relocatemagazine.com/ - summer 2008 publication

moved between locations to fulfill different key business functions for varying amounts of time. This has given rise to a need for ‘a home from home’ for these people who can work in a specific location from one week through to a number of months. There has also been a shift in globalisation meaning that consultants and teams from all around the world often work for a few months at a time in specific geographic areas.*

Comfort: There is also the element of comfort and having a home from home. Having all the creature comforts available makes staying away from home that more pleasurable and as they say ‘a happy worker is a hard worker’, and companies are increasingly realising this. Living out of a suitcase can cause worker fatigue and having a larger space to live in, as opposed to just a hotel room, means that it is even possible to conduct business meetings at the apartment in a relaxed and comfortable environment. This would not be that easy to do in a hotel room where the primary purpose is to sleep and clean.* Apartments also offer greater privacy and freedom than a hotel, as well as in many cases free allocated parking and free broadband.

Appeal to a wide range of tenants: serviced apartments are ideal for extended business trips, short to medium term overseas projects and relocations, particularly while permanent accommodation is being found. They can even be a preferred alternative to buying or renting on the open market; with such dramatic drops in property prices many prospective buyers will be waiting for prices to stabilise before committing to a purchase, but will still require accommodation in urban centres.

*www.servicedstays.com/news

CHAPTER 2

My eureka moment!

I remember the first time I came across the concept of a serviced apartment. It was purely by accident. A tenant of mine who had been staying at my relatively new 2 bedroom flat in Milton Keynes had had a job offer in Australia and decided to give me their notice. In the 2 years since I had purchased the flat, a number of new build blocks of flats had sprung up (for those of you who are familiar with Milton Keynes you will know just how many flats have come in such a short space of time). The result was that I had been able to secure a relatively higher than average rent for my flat and was now facing the prospect of having a steep 15% reduction in my rent!

In investment terms that's not good!

So I investigated the competition and soon realised that the only hope I had of getting a tenant in was to drop my rent from £800 per month to £680. By chance I happened to read an article in one of the National Newspapers which discussed the concept of serviced apartments. It involved providing a fully furnished apartment on short term stays and was best likened to staying at a hotel, except someone doesn't expect you to tip them once they have delivered your bags to your room.

This gave me an idea and I started investigating the possibility of renting my apartment out on a weekly basis. I found comparable apartments renting out for between £80 to £105 per night, with weekly rates of between £475 up to £650 per week.

I then called up a number of different serviced apartment providers and enquired as to what kind of occupancy rates they had. Some were

unwilling to disclose those, while others had it openly available through their own online booking systems. On average the occupancy rates were 65%, however, there was one company with 60 apartments that were let out to an American firm on a long term contract, so it was possible to achieve a consistent 100% occupancy!

Using my powers of deduction I calculated that on a 65% occupancy and charging £550 a week, I could make over £1,500 rent per month! That represented a potential increase of 230%! And that was working off conservative figures. Using a 100% occupancy with a long term contract, and using a reduced rate of £475 (for a long term tenancy discount) the rent increases to £2,058! That represented a potential increase in rent of over 300%!

My initial reaction was: Why isn't everyone doing this!

As my research expanded I uncovered a number of risks in offering this type of rental accommodation and these will be highlighted later in the book. I also uncovered the key areas that need to be tackled to ensure that your serviced apartments stand out from the crowd and will bring in healthy rental profits. Many people assume that serviced apartments cater for a very niche tenant market, but as you will see later in the book, there is a very wide scope of tenant to target and each can reap healthy rewards.

Different serviced accommodation opportunities:

The diagram mentioned earlier in the book showed how different tenant groups were defined based on two variables, namely: the rates charged and the length of tenancy. It is worthwhile explaining from the outset that there are a number of different serviced accommodation opportunities. Let me illustrate by way of example:

If you consider a team of consultants brought in for a two-month project, they would be different from say a recruitment company looking for accommodation for people they are re-locating. Another example would be a company covering a wide geographic region (such as the UK) and having a requirement for 2 main serviced accommodation hubs to allow regional managers to spend time in their relevant areas as opposed to a tenant who is just looking at staying the night on their travels.

This illustrates the two main ways of handling serviced accommodation:

1. Directly target very short term tenants who only need to stay say 2 to 5 days, but charge a premium higher rate, although your occupancy will be less certain.

or

2. You could target contracts with firms that require accommodation for their contractors, consultants or employees. This way your occupancy is more certain but you will likely have to offer a better rate.

I personally prefer the latter option and if you consider the opportunity to utilise serviced accommodation in most organisations that have high accommodation and travel expenses, the idea of being able to sign a secure long term (12 months and longer) agreement with these companies can prove to be a very profitable exercise while at the same time giving a significant reduction in costs for the company.