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May 2017 edition

Investment Property Newsletter

This newsletter aims to provide helpful information for property owners seeking to better their returns and minimise risks and those considering investment property ownership.

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PROPERTY INVESTMENT FOR BEGINNERS

Don't believe people telling you that investing in property is easy. The truth is, it's a vocation that belongs to the brave, patient and resilient and should not be entered into lightly. If you're looking to invest in property, here are five tips.

1. Understand the investment

Property generates a return in two ways. If you can get the combination of this right you're off to a good start in maximising your investment.

Capital Growth – the property needs to increase in value. That is the sale price (after taking inflation into account and selling costs) must be much higher than its purchase price (including purchase costs such as stamp duty and legal fees). Different types of properties grow at different rates. That is, capital growth will be different between land, houses, units, apartments, offices, shops, factories, farms and so on.

Also, different locations will grow at different rates. For example, a house located in the inner suburbs of Melbourne will likely grow at a higher rate than an identical property located 25 kilometres from the CBD.

Rental returns – Different properties will command differing rental amounts. This is important because you want the investment to pay its own way as much as possible, to avoid the amount you have to dip into personal funds for any shortfall between rent and expenditure (including loan repayments).

Understanding property returns will help you to grade each investment opportunity. You will profit from the higher grade properties the most. The key is to get the highest possible grade property for your budget.

2. Understand the market

The market has cycles. It has times when demand is high resulting in high capital growth and rent income and it has times when the market is low.

In theory, you should do the opposite of the crowd. That is, sell when everyone else is buying and buy when everyone else is selling. Warren Buffet states it this way … "Be fearful when others are greedy and be greedy when others are fearful". In practice, this is hard to achieve and patience is important.

Notwithstanding the above, you can still make good property investments irrespective of timing when you are in it for the long term.

3. Understand finance strategy

No matter how good a property is, ownership will depend on finance. Sound finance is just as important as a sound property.

Without an understanding of your borrowing capacity and keeping to that limit plus understanding the importance of maintaining a financial buffer to see you through the difficult times (that *all* investors face), you're not going to get off the ground, or worse, if you do get off the ground you could be forced to sell your property resulting in potential losses.

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4. Become financially literate

Managing an investment property is a sizable extension of your personal finances. For those people that can't make ends meet by managing their personal budget will only have their problems magnified by adding the ownership/management of a property or a portfolio of properties worth millions. Investors need to be money smart and learn the ins and outs of budgeting, taxation, insurance, administration, and record keeping as well as using the best ownership structure for the investment.

5. Understand advice

The best business leaders are those that surround themselves with even smarter people. Property investors should be no different. Get help from the right people. You'll find everyone is happy to give you advice. Rather than listening to well-meaning friends, it's important to only listen to people who have achieved the financial independence you're looking for and who've maintained it through a number of property cycles.

Understand the difference between a sales person and an advisor. Many sales people are cloaked as advisors and while they suggest they're representing you, they are likely representing the seller or a property developer. Be prepared to pay for advice. Good advice is never expensive. It's much cheaper than learning from mistakes.

GENERATE A RETURN FROM YOUR HOME

If you have spare room in your house (and your family circumstances are flexible), consider renting out that room. The demand is out there and you can make some money on an asset that is otherwise idle. In essence, you're turning part of your home into a mini-rental property.

In these types of circumstances, the rent you earn will be taxed. However, you will also be permitted to claim expenses against that rent income.

You are entitled to claim 100% of any fees or commissions charged by the rental facilitator (such as Airbnb charges). For other expenses, an apportionment is needed since expenses are claimed for that part of the house that is rented.

As a general guide, expenses are apportioned on floor space based on the area solely occupied by the renter plus a reasonable amount of common areas. You can only claim expenses for the period the room was available to rent.

Apportionment example...
Size of room rented: 10 m^2
Size of common areas: 50 m^2
Size of house: 80 m^2
Number of days room rented: 150
Number of rental people: 1
Total number of people (including renter) in house with equal access to common areas: 2

Room proportion is:
(10/80 x 150/365) x 100 = 5.13%

Common areas proportion is:
[(50/80 x 150/365) x (1/2) x 100 = 12.84%

The property owner can therefore claim 17.97% of their house expenses (such as, electricity, water, interest on home loan, council rates) against the rental income.

Warning: Capital gains tax may also apply to the property when sold.

BOOST YOUR DEDUCTIONS

A tax depreciation schedule is a fancy name for a document that will boost your annual rental property deductions. You can use the bigger tax refund to pay back your loan faster or contribute towards another property investment. That's a clever way to build wealth.

As the depreciation schedule contains details of the property's construction costs and fixtures and fittings, it enables you to get a tax deduction for the cost of those items spread over a number of years. That adds up to substantial annual non-cash tax deductions.

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The schedules must be completed by qualified quantity surveyors, not accountants. The cost of getting a tax depreciation schedule is 100% tax deductible. It's highly likely you will recoup their fee in just the first year, as the depreciation claims can be several thousand each year.

Contact us to assess whether depreciation schedules suits your circumstances or to arrange for a schedule to be prepared for you.

IS YOUR BANK ACTING LIKE A PERSON OR A COMPUTER?

Financial institutions (mostly banks) have enormous budgets to pump into marketing to get more business; and they are extremely good at it… even friendly.

Once your signature is on the dotted line, the relationship with a friendly person ends and the relationship with the bank's computerised telephones and systems begin. Computers don't talk to you so they can't possibly know your circumstances which inevitably change over time. In the end, have you become just another "customer ID number"? Does the bank's system simply record your regular repayments and doesn't notice if you are ahead of your repayment schedule? For example, in times when the Reserve Bank is not increasing their rates, when was the last time your bank called you, unsolicited, to advise a reduction in your interest rate on your loan for your loyalty? Never?

Competition among the banks to gain new customers is enormous which gives you bargaining power to ask for a better deal in return for your loyalty or increased custom.

If you are curious about what rates are available or think you have an inappropriate loan, contact us and we will point you in a direction that will provide help.

MARKET UPDATE

Where is the market heading in 2017?

Bruce Renowden of Renowden Buyers Advocates advises "our response to this question remains unaltered. If the present environment of low interest rates and unemployment continues and this is accompanied by no overseas "shocks", then why should it change? We also maintain solid immigration which is continuing to provide demand for our property in the capital cities. In our view, it is probable a status quo situation in the presence of the above is most likely to continue."

www.renowdenbuyersadvocates.com.au

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- Point you in the right direction for lending agencies and mortgage brokers

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