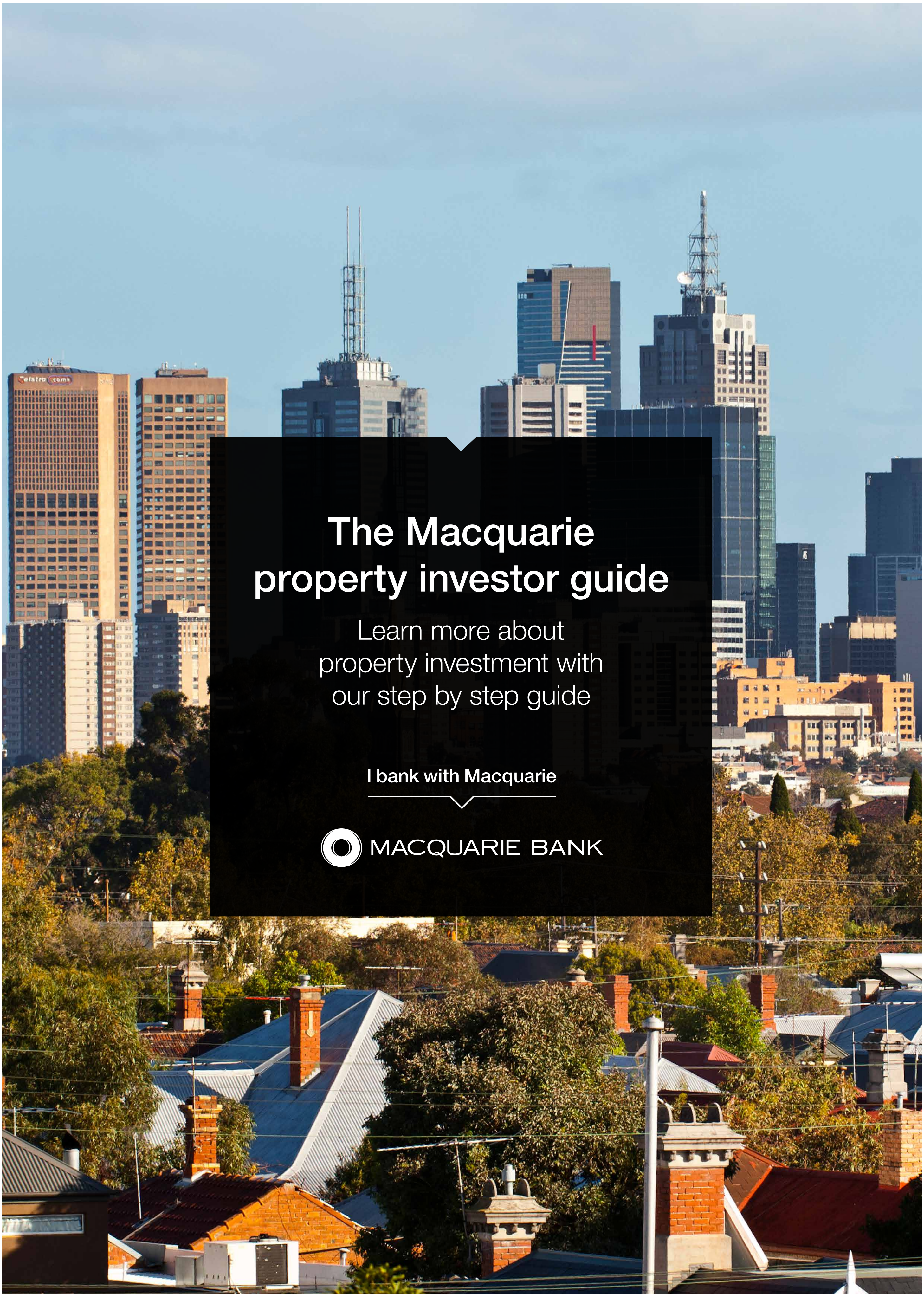

The Macquarie property investor guide

Learn more about property investment with our step by step guide

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Property investment: Understanding the appeal

The property market has more immediate familiarity than many other investment classes, making it a popular option for many investors.

For the vast majority of us, property is something we're familiar with. We grew up living in property. We may have rented property. It's something that's all around us — and we've developed a sense of what we like and what we don't like about it.

According to Macquarie Private Bank's head of debt advisory, James Duffell, that familiarity offers us comfort when assessing property's potential as an investment.

"Property is tangible – you can touch it, drive past it and from an investment standpoint, that gives buyers a sense of security," says Duffell.

We've experienced the ups and downs of the property market, too — either firsthand or by reading the news.

As CoreLogic data show, dwelling prices have been shown to increase over a long time horizon. However, property can also decline in value, depending on your investment timeframe. In the 12 months to July 2019, national property prices dropped 6.4%, for example. [Figure 1]

Figure 1. Australia Dwelling Prices, Hedonic index, seasonally adjusted

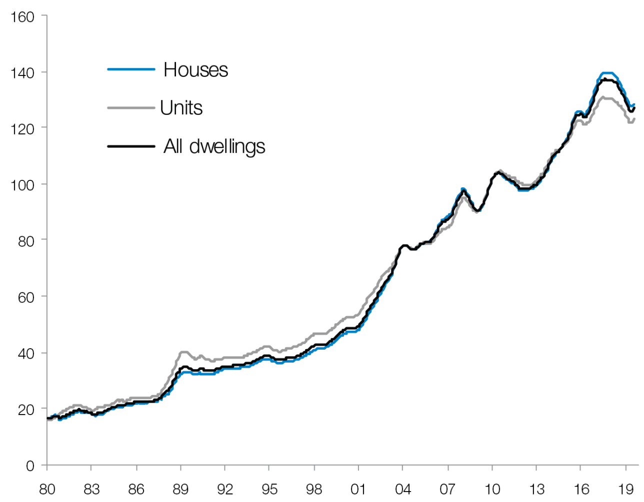


Figure 1 source: CoreLogic RPData, Macquarie Macro Strategy, September 2019

Over the following pages, we explore the practical and financial realities of property investment to help you decide whether or not property could work as part of your overall investment strategy.

Property investment: Is it right for you?

In this section we'll break down some of the key considerations you need to explore to understand whether property investment is right for you.

1. Understand your risk profile

Your risk profile is your appetite to take risks with your investable funds. You should always understand your risk profile before making investments of any sort.

When considering property investment, it's particularly important to come to terms with your own level of comfort in borrowing to invest. Taking on additional debt is not something you should do lightly, especially if you already have a mortgage on your primary place of residence.

Tip: Talk to a professional financial adviser, who may help you understand whether property investment matches your risk profile and if it suits your broader investment and lifestyle goals.

2. Cash flow management

Many people invest in property to rent it out and enjoy a regular income stream. Of course, things may not always go as planned. For example, you may have issues with tenancy.

Managing cash flow is one of the most important elements of owning an investment property. Plan out your incomings and outgoings using a budget calculator, to get a real sense of the financial commitment you're contemplating.

Tip: When you're planning your cash flow, model different scenarios. Take into account interest rate rises, no tenants for prolonged periods, increases in maintenance costs or tax rate changes.

3. Develop a life plan

According to Duffell, property is a long-term investment, so it is wise to think about what you might be looking to do and achieve over the next five to 10 years. You might be planning to have children, travel, change jobs or retire. Property investment may suit your lifestyle now, but major life changes will affect whether it's a good or bad investment decision over the appropriate time horizon.

Tip: Make sure your financial adviser knows about your future goals. They could provide advice on whether property investment suits your medium and long-term plans.

4. Research the property market

If you currently own property it may feel logical to purchase an investment property nearby. After all, you know the neighbourhood, and you are close by if you want to manage it yourself.

Other people might see better growth opportunities interstate or in another part of the city because of a new suburb that is forming.

Investing in a different suburb, state, or in a different property type, may offer diversification benefits if you already own your primary place of residence or have existing investment properties.

Tip: Your investment objectives and time horizon can determine where you buy. Weigh up the prospects for capital growth with the likely rental yield and talk to real estate agents to better understand suburb profiles.

5. Sense check whether property is a suitable asset class for you

As well as exploring your risk profile and life plan with your financial adviser, it's good to understand why property is your preferred investment. Depending on your personal circumstances, there may be investment opportunities that are better suited to your needs and financial goals.

Liquidity, for example, is a key risk to consider before investing in property. There are high transactional costs in buying and selling property and, depending on the property cycle, it can be difficult to find the right buyer at the right price when you choose to sell.

"It may sound obvious, but property is an all or nothing investment. You can't sell off a bathroom to free up cash," says Duffell.

Tip: When it comes to investing, diversification is important. It could be diversification across asset classes, such as shares, property or bonds. It could also be diversification across regions, exposure to both Australian and international assets as well.

What should you look for in an investment property? Head to page 17 for some tips.

Read now

Understanding your risk profile

To decide whether or not property is the right investment choice for you, it's important to understand your risk profile. A financial adviser will use a comprehensive questionnaire to determine your appetite for risk.

Your life stage and investment horizon are vital to determining what type of risk you should take on.

"Different life stages come with different financial and family commitments — and this has implications for the risk you can bear," says Duffell.

While there's no one-size-fits-all approach to risk profiling, there are, broadly speaking, three main categories.

What risk profile do you think you fit into?

Many people are surprised at their result when they complete a formal risk profile assessment with a financial adviser. Make sure you speak to a professional before making any big financial decisions.

Conservative investor

Conservative investors are generally prepared to accept lower returns with lower levels of risk to preserve their capital. Their portfolios tend to be allocated predominantly in defensive assets, such as cash and fixed interest, with the remainder in growth assets.

For this reason, people in retirement (in the wealth protection phase of their investment path) may adopt a more conservative attitude to risk. They have less time to ride out the ups and downs of the share market and tend to have less of their portfolios allocated to shares and other high-risk asset classes. People in retirement may also look for assets that can pay regular income, such as annuity investments and rent.

Balanced investor

Balanced investors generally have more of an equal mix of growth and defensive assets. They're usually more comfortable taking calculated risks to achieve good returns, and often have less of their investment portfolio allocated to shares and other high-risk asset classes.

Growth investor

Growth investors are comfortable with a higher level of risk to achieve potentially higher returns. They may have more wealth, so feel comfortable risking a higher proportion of funds, or they may have a longer time horizon to ride the market ups and downs of assets that are further up the risk spectrum.

Investors in this category can, therefore, expect to have the majority of their portfolio allocated to growth assets, although still diversified across shares, property and alternative assets.

Getting your finances sorted

If you've decided property investment is something you'd like to explore further, now's the time to get your finances sorted.

In this section, we'll walk you through some of the things you'll need to consider before deciding how to fund your investment property purchase.

Some would-be investors who currently own a home may want to leverage the equity in their place to invest in property.

If this sounds like you, familiarise yourself with some of the key considerations.

What is equity?

Equity is the difference between the current value of your property and the amount you have left on your loan.

Say, for example, your property is valued at $700,000, and you owe $250,000 on your home loan. In this case, you have $450,000 equity in your home.

Banks will usually lend up to 80% of your property's value, subject to your ability to repay the loan. In the case of our example, you may be able to release up to $310,000 to invest elsewhere.

Remember: The value of your property is subject to current market conditions. You may be able to release more equity in a market where house prices are rising, than in one where they're falling.

How do I work out my equity?

Subtract the amount you owe on your home loan from your current estimated property value, and then divide the result by your property value. Multiply the answer by 100 to get the percentage.

$250k
Home loan

$700k
Property value

$$\frac{(700-250)}{(700)} \times 100 = 64\%$$

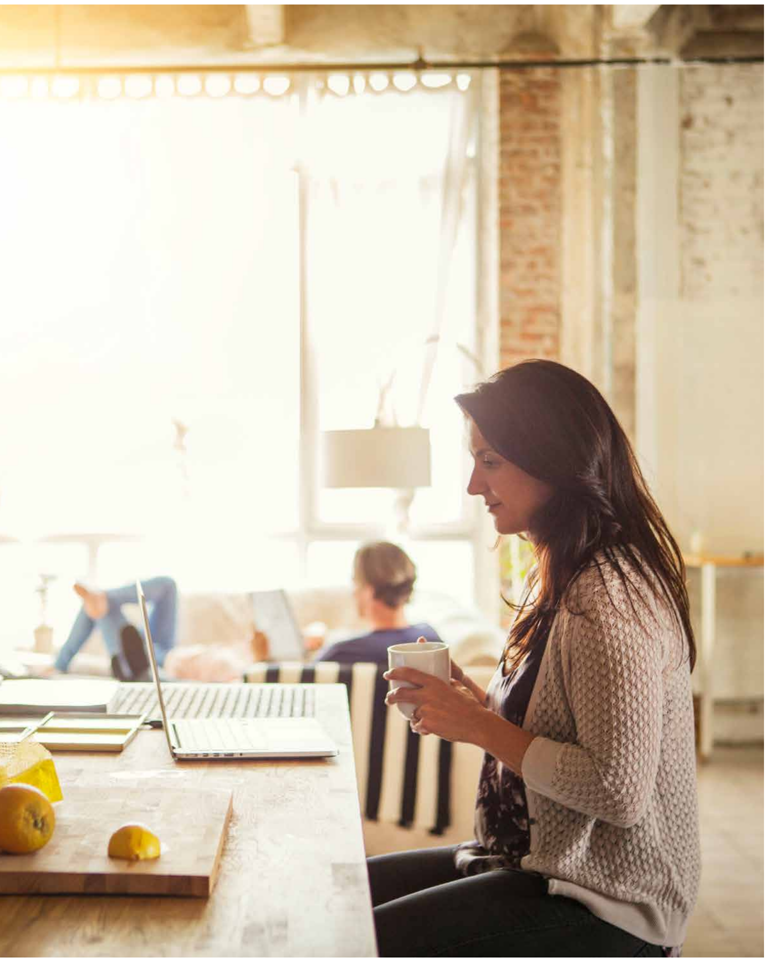
Equity

Home loan options

The interest rate you are offered for an investor home loan may be higher than an owner occupier loan for the same property. One of the reasons for this is lenders may calculate risk differently for different types of loans. You may also find that different loan terms and conditions apply.

There could also be a few extra documents you need to provide, beyond what is expected for an owner occupier loan. For example, your lender may need to see rental income statements, a tenancy agreement, tax returns or bank statements to verify that you can afford to service your investment loan. If you are purchasing a new investment property, with no previous rental history, you may be required to obtain a rental appraisal from a licensed real estate agent. As part of the application you may also need to declare your rental expenses.

At Macquarie, we offer two home loan products that can be used by property investors, an offset home loan and a basic home loan.



Offset home loan

An offset account is a transaction account that is linked to your home loan. Any funds that you have in the offset account, work to reduce the interest you pay on your home loan. You can still easily access any funds you put into an offset account with a debit card.

With Macquarie's offset home loan, you can establish up to 10 offset accounts for each variable interest rate loan account, and structure your savings in ways that work for you.

Straight into your offset

Tip: You may want to set up an offset account to receive rental payments from your tenants. You can also establish an offset account to accrue savings for property-related expenses, such as strata or council rates.

Find out more

Basic home loan

Our basic home loan gives you a simple solution with a great rate and no application or account management fees.

This home loan can be good for investors who want a simple loan structure with no additional accounts attached to it.

Find out more

Fixed, variable or mixed rate home loans

The majority of borrowers go with a standard variable rate home loan, but that doesn't mean it's the best option for everyone.

For example, fixed rate loans can appeal to property investors who aren't looking to pay off their loan faster and value the simplicity and predictability of fixed repayments.

Knowing your loan repayments makes it easier to budget and manage your cash flow and, if you expect interest rates to rise over the next 1 to 5 years, locking in a fixed rate today could save you money on repayments in the future.

That said, fixed rate loans limit a borrower's ability to pay off their loan faster by restricting additional repayments or capping them at a certain amount a year. Significant break fees can apply if you want to refinance, sell your property or pay off your loan in full before the fixed term has ended.

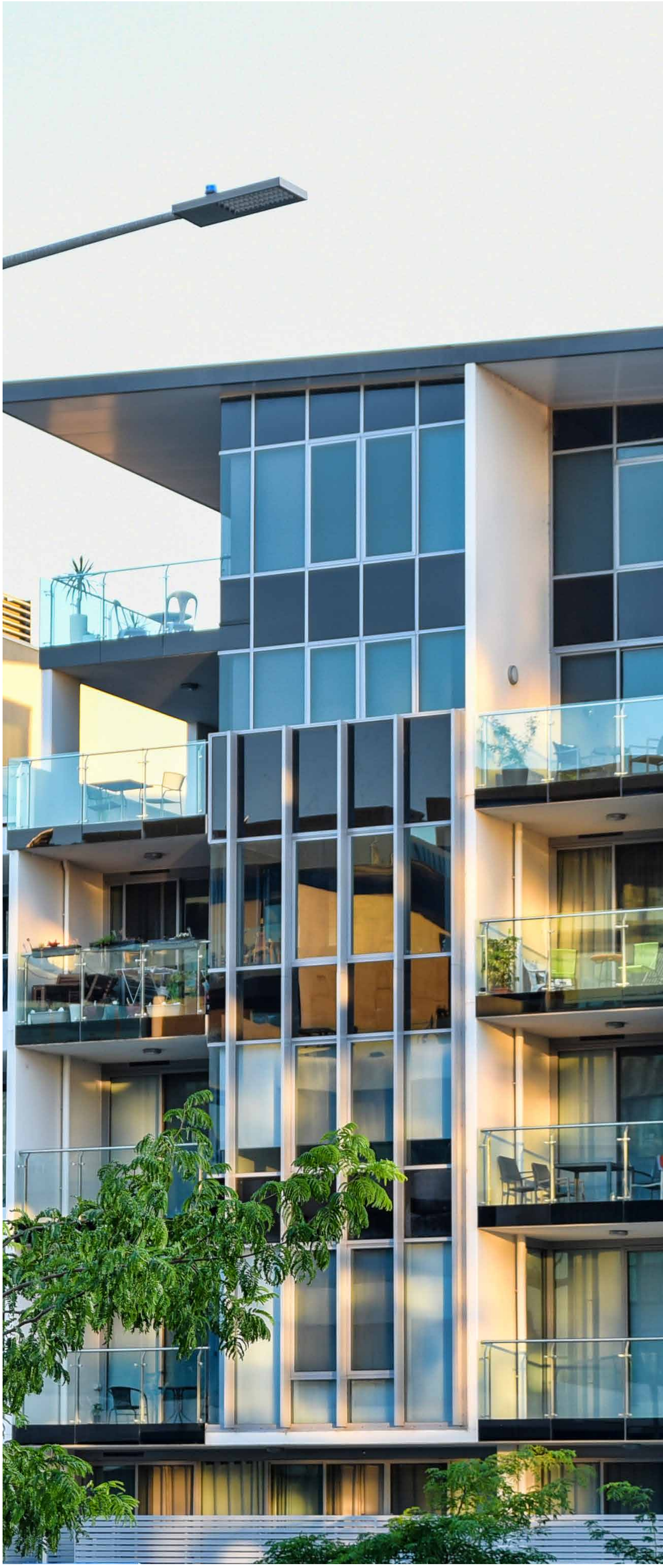
One way to hedge your bets on interest rates is by splitting your home loan rate. At Macquarie, you can divide your home loan into multiple accounts — to take advantage of both fixed and variable rates.

Allocating a percentage of your loan to a fixed rate might give you more peace of mind on your outgoings, if variable rates fluctuate. At the same time, keeping a proportion of your loan variable gives you the flexibility to benefit from offset or redraw capabilities on that portion of your loan and take advantage of falling rates, if they come up.

Understanding loan purpose

Investor loans attract a different interest rate to owner occupier loans and may have different terms and conditions. It is important to be clear about the purpose of the loan when applying, so your mortgage broker or lending specialist can help you find the right product.

If your circumstances change, and you decide to rent out your home, or move into your rental property, you should contact your lender to find out whether any changes need to be made to your loan.



Understanding property's return on investment

Before you make investment decisions of any sort, it's worth running through some scenarios on the return you can expect.

What is rental yield?

Rental yield is the income you make (or expect to make) from your investment property, as a percentage of its value.

If you plan to rent out your investment property, calculating its rental yield is a quick and easy way to understand the return you could get in the short term. A rental yield is also useful because it is calculated as a percentage, so it can be used to compare the cost of investing in property with other forms of investments.

Duffell suggests revisiting your property's rental yield throughout the life cycle of your investment. The dynamics of the property market can change over time and your rental yield is likely to change with it.

Why it's important to run scenarios

Real estate sites will often provide guides on a property's rental yield, and these can be a useful starting point. However, it's important to do your own research to build up a more complete picture.

If you're thinking of purchasing an apartment, for example, what's the weekly rent on comparable apartments in the same building? Keep an eye on the rental markets in your chosen suburb. How long are properties staying on the market for, before being snapped up? You might want to attend a few rental home opens or contact leasing agents to gauge interest.

Once you have an idea of weekly rent, run some scenarios to find out your best, worst and most likely case for annual income. Make sure you're comfortable with your lowest rental yield scenario and factor in a buffer for time on the market and property management fees.

How to calculate net rental yield

$$\left(\frac{\text{Annual rent received} - \text{fees and expenses*}}{\text{Property value}}\right) \times 100 = \text{Net rental yield}$$

*Note: Interest on your home loan isn't usually included in a net rental yield calculation.

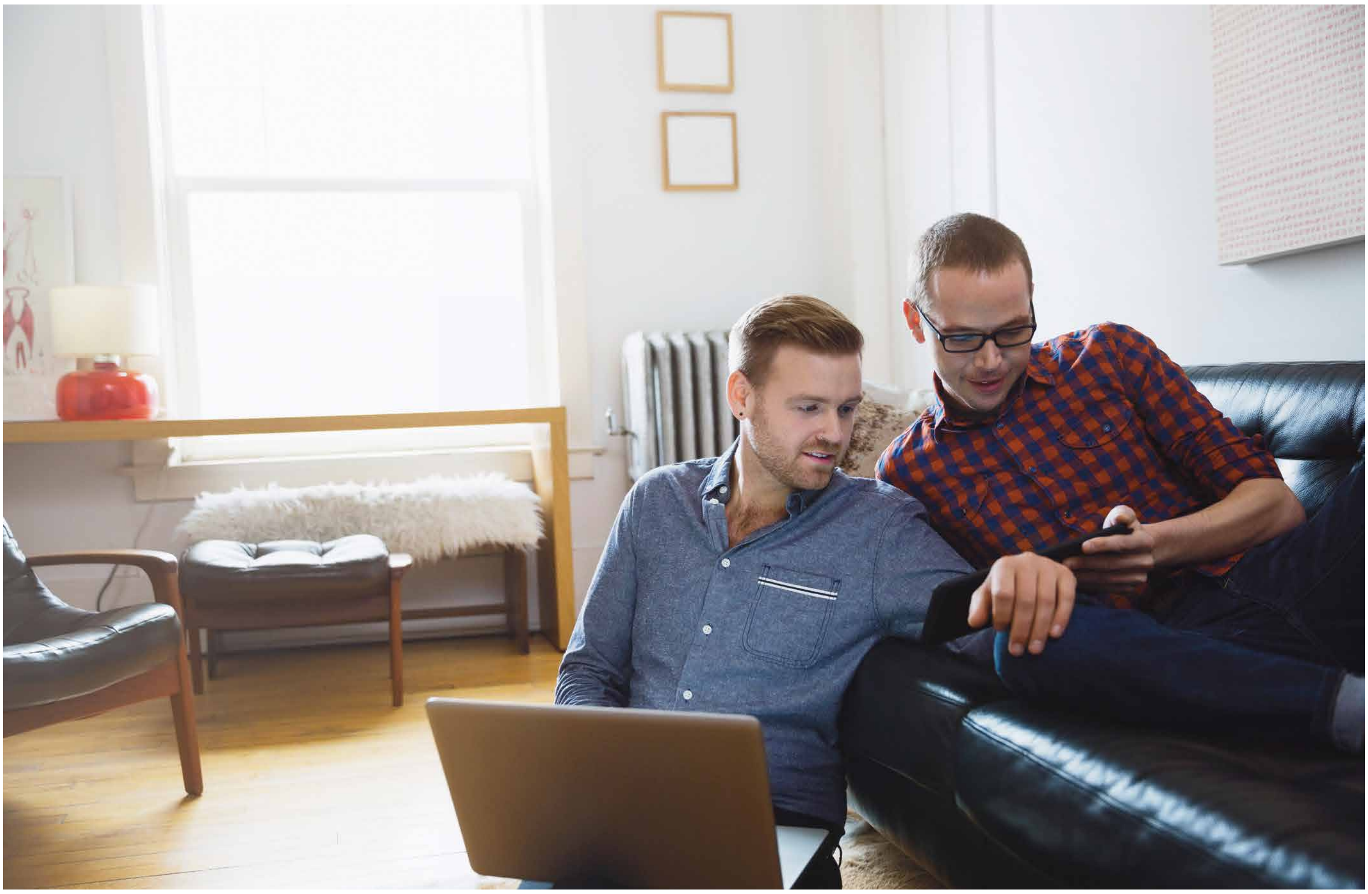
Gross or net rental yield?

When calculating your rental yield, make sure you take into account all of the ongoing costs associated with renting and maintaining the property (such as strata, council rates, water and property management fees). Some real estate sites will show an estimate of weekly rent, which can be used to calculate gross rental yield, but if you wish to compare property investment with other investment classes, it may be more appropriate to use net rental yield.

Looking beyond rental yield

While rental yield is important to consider, it's not the only thing to think about. Some investors are content with a lower rental yield because they plan to hold their investment property for the long term and expect to benefit from capital gains.

If this sounds like you, some suburbs may be a better investment than others for long term capital gains. Always gather as much information as you can to help you make a considered decision.



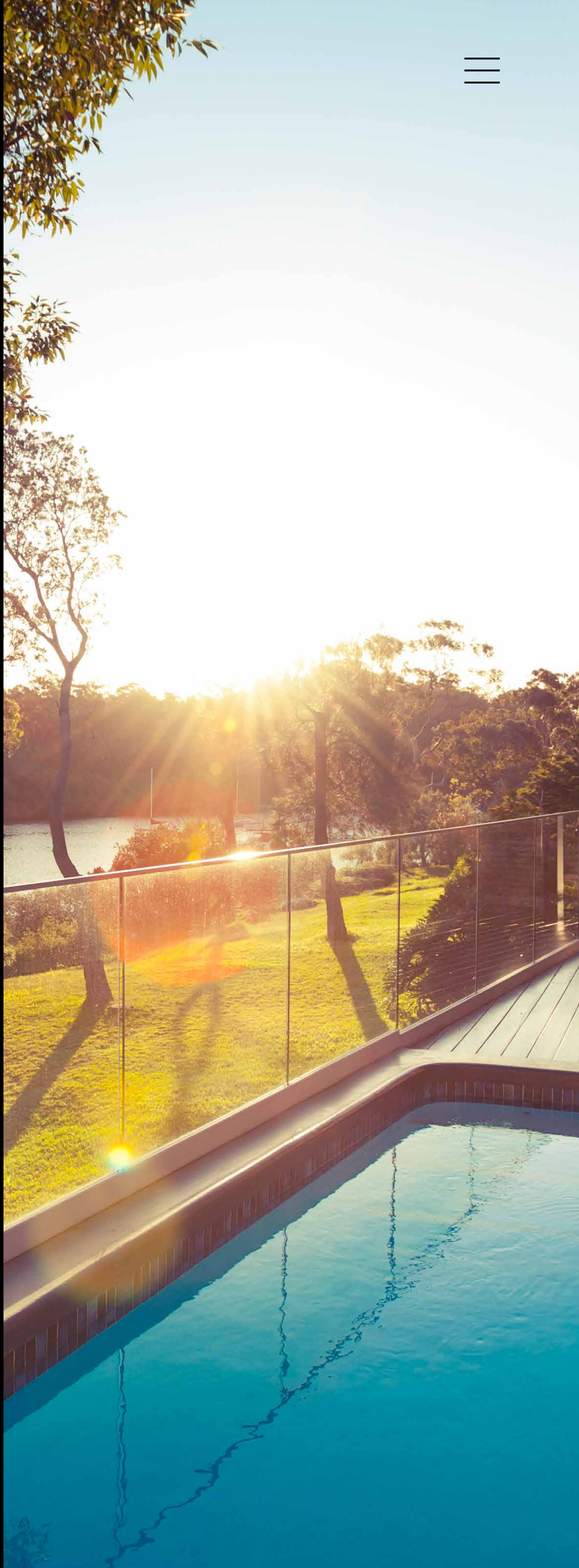
Debt strategies for your investment property

Property is a big investment and if you plan to use debt to finance it, you need to commit to an appropriate gearing strategy.

Some investors may prefer their property's rental income to exceed their mortgage repayments and other associated costs.

Others are comfortable for rental income to be lower than property-related costs, because they believe the eventual capital gains will outweigh these losses; and they may be able to receive tax benefits from negative gearing in the interim.

In this section, we'll explain some of the options to consider.



The lowdown: negative gearing

Negative gearing is the term used when the income from an investment property is less than the expenses associated with it. This is a relatively common scenario in Australia, because our tax system allows investors to offset their net investment property loss against other assessable income.

When considering negative gearing as part of your overall investment property strategy, you should be mindful of the forecast path of mortgage rates and the long-term property market outlook.

Gearing tends to work better when interest rates are expected to fall or remain flat, and property values are forecast to strengthen. In markets where the opposite is likely to happen, gearing can put property investors under financial stress. Make sure you speak to a financial adviser about whether negative gearing is a good strategy for you.

If you want more information on the types of expenses you can and can't claim on your investment property, refer to the [Australian Tax Office's (ATO) guide on rental properties].

The lowdown: positive gearing

Positive gearing is when your interest expenses, bills and maintenance costs are less than the income the property generates. If you're positively gearing your property, you'll make a profit on it each month. Any profit will need to be included in your assessable income at the end of the income year, meaning you'll have to pay tax on the profit.

Lower gearing is less risky than higher gearing because investment income can often be predicted over the short and medium term. This means overall investment returns are less contingent upon the realisation of long-term capital gains.

Understanding property valuations

When you're deciding which investment property is right for you, price is one of the many factors you need to consider.

While you may be pre-approved for a specific home loan amount, that doesn't mean you'll always be able to borrow that amount to purchase any property. Here's what you need to know.

What is a lender's valuation?

Essentially, your lender needs to be confident that the money they're lending is for an asset of greater value than the money you're borrowing.

Therefore, the lender's valuation may differ from a real estate agent's appraisal.

How lenders assess a property's value

If you purchase your property in a typical open market transaction, through an agent, where the property has been listed on the usual portals — then the valuer is highly likely to take the view that the purchase price represents fair market value. Particularly when the price is comparable to recent sales.

However, if the price seems inflated, they will look more deeply.

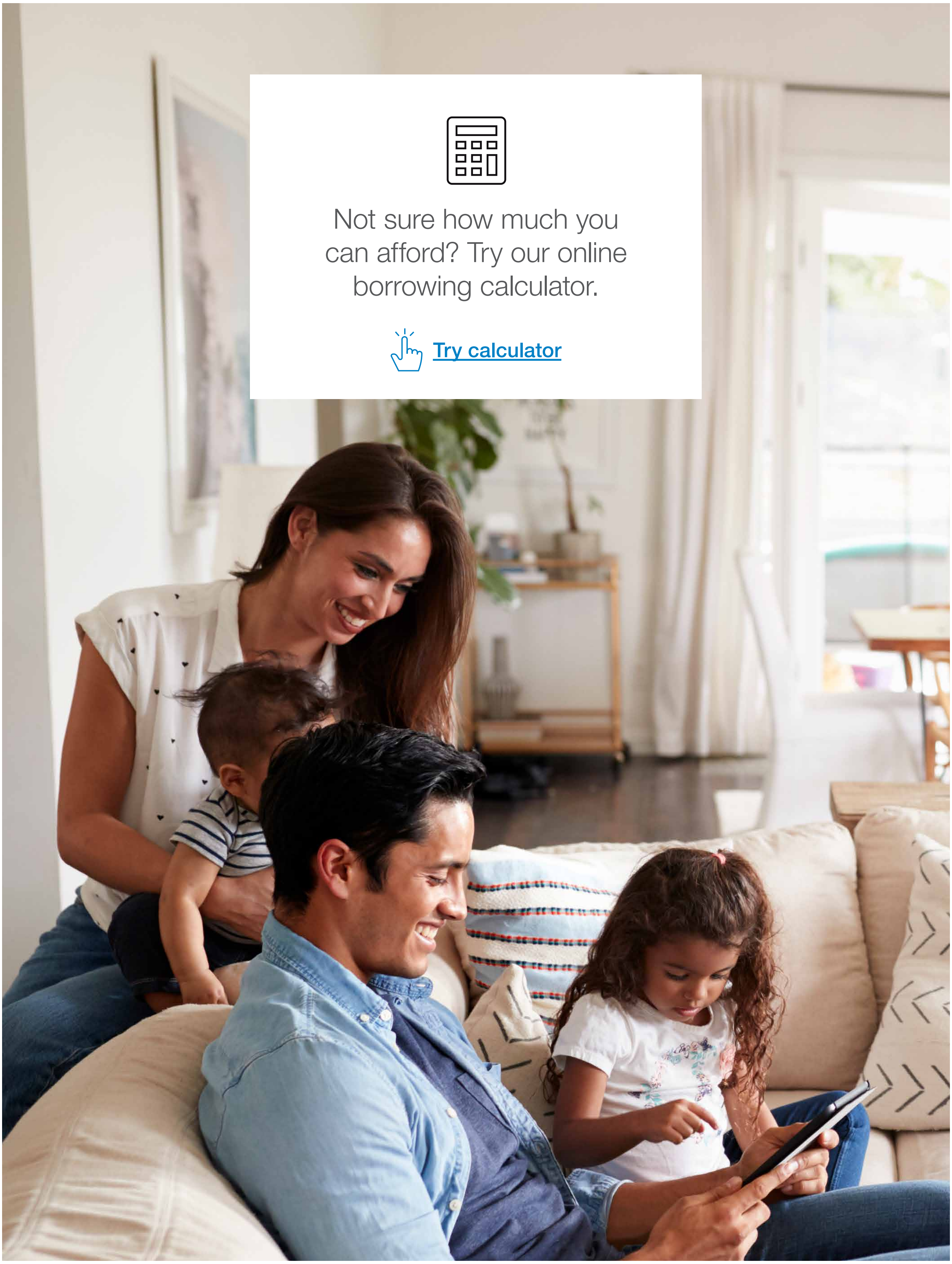
What happens if the lender's valuation is lower than the purchase price?

On some occasions, a valuation may come back lower than the purchase price.

This is more common where there is a time-lag between the purchase and the valuation. For example, if you purchase a property off-the-plan, your lender will not be able to value it when you sign the contract of sale. They will only be able to value the property once it is completed.

If there is a discrepancy between the purchase price and the valuation, the lender will typically lend against the lesser of the two. For example, if you pay $500,000 for a property but the valuer thinks it is worth $450,000, the bank will lend against $450,000.

Getting a valuation before you buy is a great way to ensure you're not caught off guard. An independent valuer can do this for you.



Not sure how much you can afford? Try our online borrowing calculator.

[Try calculator]

What to consider when choosing an investment property

Choosing the right investment property is very different to choosing a home to live in.

Consider the property as part of your overall strategy and make decisions with your head and not your heart.

Top tips for finding an investment property

- Set your budget — and stick to it.
- Research the suburbs with your ideal tenant in mind: consider proximity to high street shops, transport and other amenities.
- Assess property values in those suburbs, both purchase price and rental income. How have they performed over recent years?
- Model rental yields to understand potential returns.
- Analyse the rental market by keeping tabs on the volume of properties listed and how quickly they're snapped up.
- Talk to leasing agents who manage rental properties to get a sense of the sort of tenants they see in your chosen areas.

In your tenants' shoes

Different properties and areas will appeal to different types of tenants. A young family may want to rent a two-bedroom duplex close to the local school. A young professional might be looking for a studio apartment that's two train stops from work.

"Before you start looking for an investment property, it's worth considering what sort of tenant you want living there and what they look for in a property," says Duffell.

Modern kitchen and bathroom

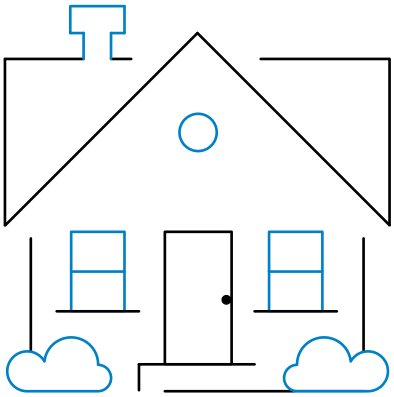
Most tenants place greater value on bathrooms and kitchens over other rooms. Consider including a renovation budget to spruce up these areas, if they need attention.

Low maintenance

For many investors, an ideal tenant is one that is rarely at home! Consider small, low maintenance apartments for these tenants. Properties with gardens or large balconies that might require maintenance may put them off.

Location

In general, renters tend to pay a premium to live somewhere close to shops, cafes and public transport. Properties close to schools will naturally attract more families, while those near universities may appeal more to students.



Aircon

If the property you're considering doesn't have a good air conditioning system, you might want to consider installing one, as this can be a sticking point for some tenants.

Security and parking

Is the area and property (or building if it's an apartment complex) safe and secure? Does it have allocated parking? These things might appeal to your desired tenant.

Connectivity

A good internet connection is attractive to most prospective tenants these days. This may steer your attention to newer developments in urban areas.

Managing your investment property

Property isn't a "set and forget" asset. Even if you hire a property manager to take care of the day-to-day interactions with tenants, it can involve considerable time, effort and expense over the life of the investment.

Make sure you arm yourself with knowledge. State government and industry body websites have lots of additional information for lessors.

Managing the property yourself

According to the 2016 Australian Bureau of Statistics (ABS) Census, approximately one in five Australian landlords manage their own investment property[1]. Taking on this responsibility is a significant commitment. However, it also brings with it a number of benefits.

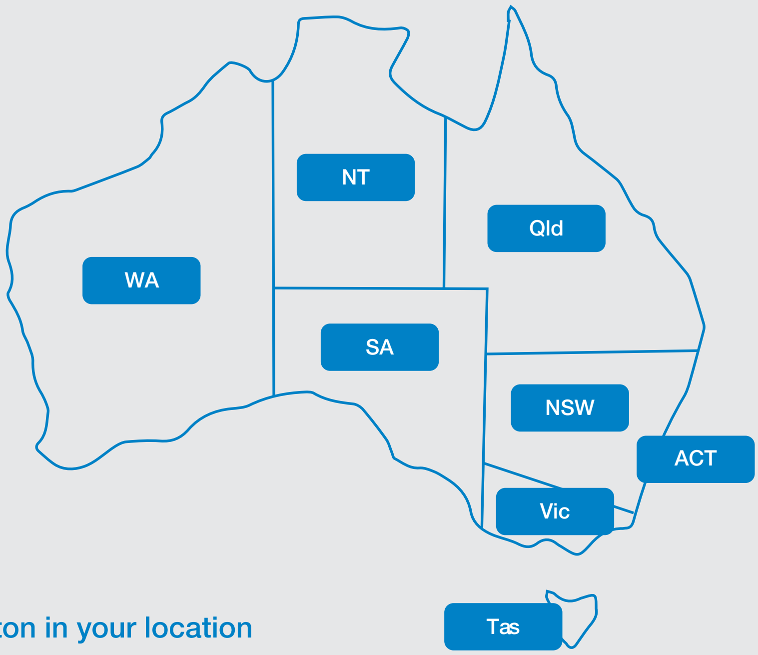
As well as having full visibility over how your property is being looked after, you will be able to vet your potential tenants more carefully. Of course, a benefit of managing the property yourself is the money you will save on a leasing agent and property management fees.

Tips for managing your rental property

Research your obligations as a landlord on your relevant state government consumer affairs or fair trading department website. The Responsibility checklist outlines some responsibilities that are similar across states and territories.

Responsibility checklist

- [ ] List and market your property on the appropriate channels
- [ ] Interview prospective tenants and check their credentials
- [ ] Collect and lodge the rental bond
- [ ] Take receipt of the first rental payment before handing over the keys
- [ ] Disclose important information about the property — such as whether the area is prone to flooding or fire
- [ ] Provide a standard residential property agreement, including the term of the lease, terms for future rental increases and the number of property inspections each year
- [ ] Provide a condition report
- [ ] Keep a rent payment record
- [ ] Chase late rent payments, and attend tribunals if necessary
- [ ] Respond quickly to calls for repairs and any problems with utility connections, plumbing, appliances, fittings or fixtures
- [ ] Complete a condition report on exit
- [ ] Refund bond



Click the button in your location

[1] www.abs.gov.au/census

Engaging a property manager

You may choose to appoint a professional to manage the property on your behalf. This approach can have significant benefits.

According to the Real Estate Institute of Australia (REIA) one of the most important factors when selecting a property manager is to consider someone who understands the relevant laws and how to apply them, as they'll typically take care of contracts, record keeping and disputes, should they arise.

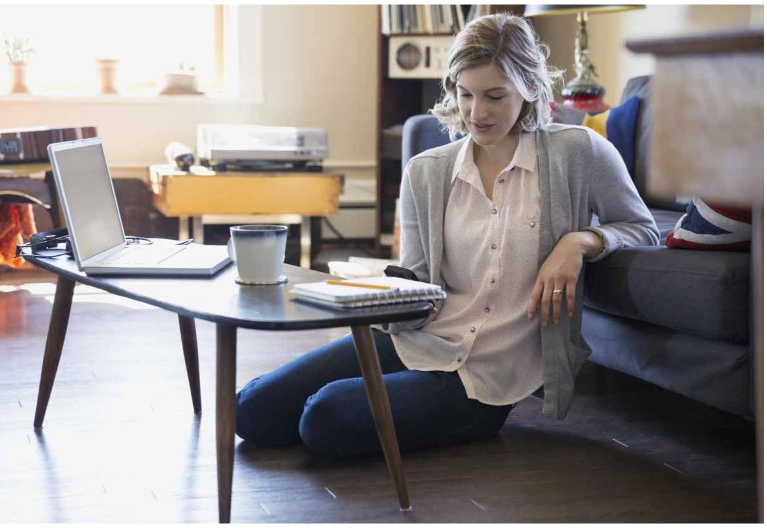
A property manager can also help you set the right rent and conduct regular fair market reviews to make sure you're getting a good return on your investment. Property management can be a lot more than collecting rent, so it's important to ask the right questions to make sure the service you're receiving is appropriate.

This all comes at a cost and it's worth getting quotes from a few different agents before making a decision.

There are pros and cons to both approaches to property management but the key factor to weigh up is whether the cost of professional property management is less than or greater than the time and effort involved in managing it yourself.

Vetting tenants

- Speak with past landlords
- Get references from employers
- Ask for proof of income
- Research online and social media



Property manager: ask the right questions[2]

- How long have they been managing properties?
- Have they had formal training in property management or related fields?
- How many properties do they manage at once?
- What is their fee for service and what does this include?
- Are they a member of an industry body?
- Do they have standard processes in place (checklists, forms, etc.)?
- How do they assess/vet prospective tenants?
- How do they manage overdue rent or problem tenants?
- Have they been to a tribunal before?
- How do they keep up to date with changing legislation?
- Do they have references from previous or current tenants/landlords?
- How often do they assess the market and conduct rent reviews?

[2] For a more comprehensive list, consult REIA's factsheet for lessors: www.reia.asn.au/consumers/renting-or-leasing-a-property/

Next steps

If you're ready to consider investing in property, speak with your mortgage broker or one of our banking specialists, who'll be able to walk you through the process.

You can get in touch with our specialists by calling **13 62 27**, or simply request a callback and we'll call you.

Request callback

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