

SOME TIPS for Asia-based investors in Australia Property

What is driving people to invest in Property? Why are so many Australians investing in the property market, and why are Australia's property markets attracting so much world-wide attention?

Most people know the "obvious" benefits of investment property – capital growth potential, rental income etc, but the purpose of this article is to explore some of the "lesser known" benefits, that can substantially benefit investors.



Power of Leveraging:

If you have \$100,000 cash to invest into stock market, you exactly got \$100,000 worth of stock. If you invest into real estate, you can buy property up to \$500,000, so if the property market moves by "10%" the value goes up to \$550,000 and you've made \$50,000 on your \$100,000, or 50% return on your capital (if the stock market moves 10%, you've made 10%).

Example:

<u>Capital</u>	<u>Invest Into</u>	<u>Value of Investment</u>	<u>Grow</u>	<u>Profit</u>
\$100,000	Stock Market	\$100,000	10%	10,000
\$100,000	Property	\$500,000	10%	50,000



This is the concept of leverage. They panic and worry about the market going the "other way" and then finding themselves with "negative equity", as has been happening recently in the stock market. The property market moves in cycles. But the upwards cycle is much higher and stronger than the down cycle in Australia property, as can be seen over the past 20 years. Sometimes go wrong is because the investor not holding for the long term.

Example, Sydney apartments. If you had invested 5 years ago in Sydney, your growth would have been just 25% over the period. It's well known that Sydney has been in its down cycle in that time. But what if you had invested 10 or 20 years ago? Even including the "down" period since 2003, Sydney apartments have shown an excellent growth of 102% over the past 10 years, and 397% over the past 20 years.

And with the financing and leverage mentioned above your return on **“cash actually outlaid”** are exponentially increased into the thousands of percent.

In spite of the benefits of leverage, many investors continue to pay cash or borrow just 50% of the value.

They argue that “leverage can also work against you.” That is, if the market goes down, then the downside is magnified, just as the upside is when the market moves up.

And certainly, in some years, some investors have lost 50%, 70% and even 90% (or more!) of their stock market investments. Can this happen to Australian property?

If you think back to all the properties you’ve bought, or nearly bought in the past, or even the ones you’ve sold in the past 10 or 20 years, are any of them worth 50% or 70% less than you bought them for?

Of course none are. In fact are any of them even worth 10% less?



Rental Income :

How else can you benefit from property? Well, of course there is the rental, which in most cases will pay the bank back its interest for you.

Add On Value on property:

As the property ages you can “add value” by doing a simple refurbishment. It is not hard to add an immediate 20% to the value of an older property.

Refinancing for extra cash – to pay for retirement, education or holiday

Let's say the value of the property has gone up. Should you sell, and take your profits? Well, why not refinance, and take out your profit that way? It's tax-free.

Let's say you borrow 80% to buy a Melbourne apartment today for \$600,000. It is worth \$800,000 in 5 years, and you owe \$480,000 on it. Your equity now \$800,000-\$480,000 became \$320,000. So, you can take some or all of this \$320,000 from this property and use it to buy another property up to \$800,000.

Then if the market moves by 6% a year over 5 years, your 2 properties have gone up to \$2.14 million. And your initial capital only \$120,000 outlay!

AUD\$7 billion was let by the Banks in May alone to property buyers!

And don't forget the tax benefits on new property. Even if the bank interest is more than the rental, which is usually the case in the initial years, this extra interest can be "quarantined" and used by you anytime in the future to reduce your tax.

Then, there is depreciation. New buildings qualify for a 2.5% construction cost depreciation rate.

This doesn't sound like much, but in effect what it does is allow up to one third of your rental income to be tax deferred.

These investment benefits-the capital growth, plus rental, plus tax benefits plus leverage plus adding value it is understandable to see why so many people look at Australia Property as a low-risk, high return investment.

Don't Sell Too Soon

People go to all the trouble of buying, of getting a loan, and arranging tenants, and then want to sell! The costs involved in buying an selling quickly can eat away a lot of your profit, if you sell too soon.



Australian property, well selected and financed correctly, will continue to provide safety, security and wealth for those who embark on a planned acquisition program of property investment, especially if they continually add to their portfolio.

Previous 5 years, more than 30% of property investor had sold an investment, with another 20% "intending" to sell within 2 years.

This is a common investment error. The ideal holding time for an Australian property is 7 to 10 years to maximize investor's returns.

Property Investment – Tax implications

Not only is Australian investment property a popular investment choice, it is also the best tax planning tool whilst living overseas.

As a general rule, borrowing to maximize taxation benefits should be in the order of 60 – 80 percent of the purchase price, and care should be taken to select the correct finance purchase. At this level of debt, the rental will normally cover a large amount of the interest expense. Any surplus interest you can use in the future to reduce any tax.



Most people aren't aware that the full construction cost of a property qualifies as a tax deduction.

For example, an investment house that costs A\$350,000 may qualify for a major tax deduction of A\$10,000 a year for 5 years, and then A\$4,500 per year for the next 35 years!

At the highest tax bracket, this is equivalent to a cash back in the investor's pocket of around A\$2,200 per year, for 40 years.

Non-residents can also uses the tax benefits to eliminate or greatly reduce capital gain tax.

Rental

You will, however, need to lodge a Return on the 30 June each year and declare your rental income received in Australia (and any other Australian sourced income).

Providing you follow some simple strategies, this rental income should not be exposed to any tax.

Potential new migrants and expats thinking of returning should also be buying at least 2 years in advance of their arrival, if they wish to utilize the tremendous tax relief available to property investors.

You may need an Accountant to organize your Australian tax affairs, or lodge your property tax return, and get every last deduction, all at a very reasonable cost.

And don't forget too: if you already own a property, less than 30% of all investors are claiming the full depreciation allowances.

Avoid These Investments

There are certain properties that tend to under perform the market, yet, many investors, especially first timers, still jump into these.

“SERVICE APARTMENTS, AND STUDENT ACCOMODATION”



Many first time investors in Australia still jump into these types of investments. Our rule for these is simple: **FIRST, IF THEY ARE UNDER 50 SQ METRES, DON'T TOUCH THEM.**

Loans for these small properties are hard to obtain, and when you try to resell, the next buyer will also have problems. Most will resell for less than you paid.

Second, be very wary of “**Serviced Apartments**” especially if they promise “**high**” rent returns.

Again, loans are difficult and capital growth lower, as they can not be resold to owners, only other investors. Why cut out over 70% of your re-sale market?