NEWSLETTER | ISSUE 12

Trilogy news

"the property investor's mortgage broker"

1 | 7 key market indicators every property investor should understand
2 | Why fear can be the investor's friend or foe
3 | Are property investors responsible for rising household debt levels?
4 | The great negative gearing debate – how does it end for property investors?

7 KEY MARKET INDICATORS EVERY PROPERTY INVESTOR SHOULD UNDERSTAND

To be a successful property investor doesn't require a PhD. What you do need to know is how to look at certain key indicators and from there, create a big picture view that recognises not all housing markets are one and the same.

Residential property is a unique commodity and behaves in a unique way here in Australia, because we have a very emotional response to real estate. We love being homeowners almost more than any other collective nation of people.

We love it so much that our relationship with housing is a key factor in the ebbs and flows of our economic tidings, supporting other industries in its wake of consistent reliability, like retail, transport and infrastructure development.

Just think about the resource boom in some of our outback towns, where the existing housing supply was too prohibitive to establish a mining operation.

Suddenly a flurry of development started and new infrastructure was built to support the community that grew overnight, driven largely by a swell of investor demand that spurred new housing construction activity.

Now, almost as quickly, we're seeing some of these resource boomtowns become shadows of their former selves. And landlords, who were enjoying double-digit returns, are at risk of going down with a sinking ship.

Property investment has its fair share of victim statistics; people who harboured visions of grandeur when it came to making millions, buying and selling houses.

Many start dabbling without understanding what keeps our perpetual property clock ticking away.

So following on from last month's reality check around 'big picture' market fundamentals, here are seven statistical indicators that smart property investors keep a close eye on when reviewing, assessing and growing their portfolio.

1. People

I sometimes wonder if you need to be a little bit of a 'voyeur' to be a great property investor. I don't mean you have to get all up in other people's business, but chances are you find people interesting to observe.

Understanding how and why the general population does what it does at any given time should be part of your asset selection process, because 'behavioural bias' tells a story about our changing lifestyle and accommodation preferences.

An example that comes to mind is more of us choosing to marry later in life, in favour of climbing the corporate ladder. The flow on effect has been city-centric employment growth and in turn, above average long-term value growth within select inner city property markets.

2. Vendor activity

Are sellers confident in the potential to move their home or investment property? Or are lots of vendors being forced to reduce their expectations and prices to accommodate a slower moving market?

This type of vendor activity is always a good one to test the current property waters, so to speak. You can usually tell if temperatures are boiling, tepid or cold by vendor behaviour.

Of course not all lulls are indicative of a changing market. Some are just reminders that a footy final or major holiday event is approaching, or that it's getting colder outside.

But if you can spot any reliable signs of vendors adjusting prices down, it could represent an opportunity to secure your next investment at below market value.

3. Stock levels

Because house prices tend to fluctuate according to supply and demand, the ratio of available accommodation to purchasers in any given area can tell you a lot about the property market.

Logically, the more housing you have that people don't seem to want anymore – think mining 'ghost towns' – the more likely it is that prices will stagnate indefinitely.

On the flipside, in areas where new stock is difficult to come by (think tightly held land across inner city regions) and resident demand is high due to amenity and employment opportunities, you'll usually see steady price growth.

4. Time on market

Lots of houses for sale, vendors taking time to adjust their lofty expectations in line with prevailing market conditions and diminished buyer demand, all equate to properties languishing on the market for months at a time.

The longer motivated vendors have to wait for a potential buyer to bite – those who have a compelling reason to offload their house - the more likely they'll be to accept a lower offer as the weeks roll by.

5. Vacancy rates

High vacancy rates can be indicative of a number of things, so when you see them, it's worth digging a little deeper.

Generally you'll find a glut of new stock or a slowdown in tenant demand, or perhaps both happening simultaneously.

Vacancy rates often shoot up in places like Melbourne when hundreds of new OTP apartments come on line all at once. As always though, seasonal influences can impact this type of data.

6. Rental yields

If median house prices are steady, but yields start to decline, it's safe to assume that tenants are not paying as much for rental properties. Are there too many investors buying into the area, creating an accommodation oversupply?

What if the rental yield suddenly increases? Could this mean more owner-occupiers are snapping up stock, leaving little for potential landlords?

Noting what rental yields have done over time in any given area can provide a valuable insight into what kind of market make-up you're buying into.

7. Median prices

While they might be confusing at times, and not always consistent across different agencies, median prices can provide valuable insight into market changes.

But they're not to be taken at face value. A suburb's median price might suddenly shoot up overnight. So should you assume that every property in that postcode has suddenly enjoyed a 26 per cent price rise in the last 12 months?

Generally these extremes are more likely to signal perhaps two or three high-end homes being sold within the same month. While rapid price dips could be caused by a surge of lower priced stock flooding the market and dragging the local median down with it for that particular period.

For this reason, it's best to rely on more long-term median statistics when researching an investment location. The short term ones can be very misleading indeed!

WHY FEAR CAN BE THE INVESTOR'S FRIEND OR FOE

We've all experienced it at various points - the fight or flight response born from a chemical reaction in our brains that's triggered by an emotion: fear.

We're taught from a young age to associate fear with negative occurrences. It indicates a situation that poses potential danger to our physical, mental, emotional and/or financial wellbeing and hence, makes us anxious.

You can see how all of this snowballs into a self-perpetuating cycle of negativity and yes… more fear. Fear feeds on itself and on our negative inner voice.

We associate something with a fear response and then whenever we face that same thing again, we immediately start up a baseless inner dialogue and begin to feel fear. Irrational? Perhaps. But that's emotions for you!

What if we learnt to have a different perspective of the things we once considered 'scary' though? Could changing our perception, change the emotional response?

Consider investing. As with anything, building a property portfolio has a degree of risk attached, and risk is generally something that makes us 'fearful', because risk generally represents the 'unknown quantity'; the thing that could go wrong and entirely derail your Plan A.

But what if you had a Plan B?

Moreover, what if you had done such a comprehensive analysis of your profile as an investor and come up with such a well thought out strategy that much of the associated risk would be mitigated?

In this sense, fear can be a great motivator. Rather than allowing it to immobilize you, let that adrenaline surge spur you into action.

Instead of running away when you feel a bit vulnerable, keep putting one foot steadily in front of the other until you reach your destination.

Maintain control of your journey by trusting your own instincts enough to know when you should ask for help or advice from the appropriate experts and when you should go with your gut as an educated investor in your own right.

Acknowledge the fear and then make it work for you by inspiring positive action.

Fear tells us when opportunity is knocking. Think about how much more anxious you feel when the stakes of any given situation are high.

A work presentation that your dream promotion hinges on will incite more of an adrenaline rush, than say a chat around the water cooler with your colleagues on Monday morning.

Without this chemical kick that makes our palms sweaty, our heart beat faster and sets our analytical mind into overdrive seeking out the best chance for survival, we may not recognise those often life changing opportunities.

We might also forget, without fear reminding us, that we're alive and breathing in this very moment.

Even though we're taught a healthy respect for fear, we still seek it out actively at times.

We take (albeit relatively calculated) risks in the form of roller coaster thrill rides or bungee jumping, and love that rush you get when skirting around the safety barriersof 'acceptable behaviour'.

Fear and the adrenaline that comes with it breaks up what can easily become a daily monotony of work, rest and work. Emotions like fear and love – those that incite a more overt response, remind us why we're alive.

Face your fears head on today, by taking calculated investment risks and who knows? You might be facing your fears head on in retirement by jumping out of an airplane, over a Hawaiian volcano!

The point is, you can either use fear to your advantage as an investor, or allow it to overcome and paralyse you into inaction. It's all about perspective and choice.

ARE PROPERTY INVESTORS RESPONSIBLE FOR RISING HOUSEHOLD DEBT LEVELS?

Recent reports from the banking sector have warned those of us at the front line of an emerging new economic order – where historic low interest rates are stimulating our housing markets, but doing little to budge the overall economy – that a rise in credit arrears is on its way.

According to a survey by data analytics and credit scoring company FICO, collections managers across Australian banks, telcos and utility providers are expecting a substantial increase in the number of collections cases over 2015.

In fact 80 per cent of respondents said they anticipated cases to jump by as much as 20 per cent across the coming year.

Awash with debt

Doing little to allay concerns over this anticipated rise in the number of families who'll struggle to pay for basic services, are statistics regarding household debt levels.

Analysis from UK based Barclay's Bank showed that Australian household debt is equivalent to 130 per cent of our GDP – up from 116 per cent before the GFC - making us the honoured title holders of 'most indebted' nation in the world.

The average household debt to GDP in other developed economies is 78 per cent.

Barclays' Australian based chief economist Kieran Davies, expressed concerns that our current low interest rate environment could contribute to higher future debt levels.

Reserve Bank says 'nothing to see here'

The RBA itself seems a bit 'all out at sea' right now when it comes to standard policymaking protocol.

But the head banking honcho continues to play it cool, publishing research last month showing how the household sector remained resilient to scenarios involving asset price, interest rate and unemployment shocks throughout the 'noughties'.

This was despite the fact that our aggregate level of indebtedness increased from around 40 per cent in the 1980's, to around 150 per cent by mid-2000.

Even though more of us are taking on higher levels of debt, the RBA argues that indebtedness is only weakly correlated with financial stress.

Does more investor activity equal more debt?

Interestingly, there seems to be a growing world movement toward a two-dimensional economic framework at present, with populations diverging across a widening wealth gap of 'haves' and 'have nots' in most major economies.

Here in Australia, we're seeing this play out in the property markets.

You might have noticed that an ever-increasing number of investors are taking advantage of lower interest rates and buoyant housing values to leverage more debt and accumulate more assets for their portfolios?

All the while, we're hearing about young would-be homebuyers and tenants struggling to find affordable accommodation, in the classic 'haves' and have nots' scenario.

Notice the difference? The former owns real estate, and the latter wants to!

Given that investor borrowing accounts for an ever-larger piece of Australia's credit sector pie, one could surmise that this increase in geared, property related borrowings is in fact, pushing up average household debt levels.

Even if we can't entirely scapegoat property investors for skewing household debt statistics, you'd at least have to question the validity of general data around the topic in this new two-dimensional economy.

"With high levels of leverage by world standards, where debt is concentrated in the household sector, we see this as a vulnerability in the event of another global shock," said Mr Davies.

"However, we do not see this as a near-term issue for the economy as we expect leverage to reach new highs over 2015 on the back of lower interest rates."

Debt will always be a contentious topic and dirty word. But if you plan on becoming one of the 'haves', you'd better make peace with the idea of it. Please, just make sure you do it the right way!

THE GREAT NEGATIVE GEARING DEBATE – HOW DOES IT END FOR PROPERTY INVESTORS?

Negative gearing, or the ability to claim property investment related expenses at tax time, has been a contentious topic since its inception late last century. Some claim the circa 1980's legislation is the catalyst for house price inflation issues.

These negative gearing nemeses generally argue that the legal tax loophole gives investors a distinct advantage, as they systematically price first homebuyers out of the property market.

The most recent opponent of negative gearing to come out swinging is the Australian Council of Social Services (ACOSS) who says this, along with capital gains tax breaks, are costing the Federal Government a combined $7 billion per year and forming a budgetary black hole in favour of high income earners.

ACOSS chief executive Cassandra Goldie told the ABC that current property related tax perks are creating a clear inequity in our housing markets and widening the growing chasm between society's 'haves' and 'have nots'.

"The reality is that over half of geared housing investors are in the top 10 per cent of personal taxpayers and 30 per cent earn more than $500,000," said Dr Goldie.

ACOSS are calling for the abolition of negative gearing and CGT breaks for all newly acquired investment properties, shares or similar capital growth commodities.

Flawed thinking?

While ACOSS is understandably concerned about the difficulties a lot of young, potential homebuyers face when it comes to accessing affordable accommodation, their suggested tax reforms appear to be somewhat short sighted.

The social impact such a move could have is potentially more detrimental than the current rate of capital growth in the housing sector, whether negative gearing is to blame or not.

It's all well and good to suggest that this 'tax break for the rich' has contributed to housing affordability issues, but when you drill deeper, what would its restriction mean for the long-term accommodation pipeline?

Would it further impact the supply of affordable private rental properties in Australia, given there are already significant accommodation shortages in some of our more populated inner urban centres?

And has ACOSS even considered the extra pressure that would be exerted on an already tightly held public housing sector, should investors start bailing out of bricks and mortar?

Given that federal and state governments are finding it virtually impossible to provide sufficient public housing in high need locations, is it really plausible to discourage Aussies away from property investment at this time?

Then there's the question of our ageing population needing to support itself in retirement, with many unable to rely on superannuation or the aged pension to see them through. We are children of the GFC after all; in which a lot of casualties lost their entire life savings in one fell swoop.

The other thing ACOSS seem to have missed, is that fuelling debate around the possible closure of investment tax 'loopholes' will only add to the current investor maelstrom, as every man and his dog vies to get into the market in anticipation of any possible changes.

In other words, the organisation that claims to want better control over house prices could, in an ironic twist, actually be fanning the flames.

Positive news for negative gearing

In a statement released late last week, Prime Minster Tony Abbott indicated that negative gearing naysayers wouldn't influence conversations around tax reform.

"I would say to people who are running around looking to increase taxes on people, what we really need to do is to get our spending under control," said Mr Abbott.

While I don't think we've heard the last on this topic, it seems property investors don't have to worry about this particular bone of contention right now.

Negative gearing is one of the things that makes Australia's property sector unique on the world stage and while it has its opponents, there are many who believe that our more favourable tax environment has helped shelter our housing markets from any serious downturns in the last decade.

I for one am pretty positive that negative gearing is here to stay!