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Property Management News

How's the Rental Market

Expensive suburbs in Sydney have seen a dampening in rents due to the huge influx of new apartments pushing rental prices down.

Fortunately, for our Hornsby Area, rental affordability is perceived as good value. Prices are significantly cheaper than even in suburbs close to us like St Ives or Chatswood where we have witnessed downturns. So, we have seen a healthy turnover in rentals with minimal vacancies and continued growth.

How's the Sales Market

In July 2015 I made "the call" that the Sydney home market boom was coming to an end. Again see my December Wrap Up Newsletter regarding where the market was heading.

Now in the first quarter of 2016 Sydney house prices (which includes Hornsby Area) have fallen 3%! This is the largest quarterly drop on record. Unfortunately, I believe there is further pain to follow.

How Negative Gearing Works

Negative gearing is a part of life for Australian investors, and a property buzz word. So what is it? Gearing simply means borrowing money to buy an asset. In the case of property, you have taken out a loan to purchase a property.

Negative gearing means that the interest you are paying on the loan is more than the income. As a result you are making a loss.

Neutral gearing means that the interest you are paying on the loan is equal to the income.

Positive gearing means that the interest you are paying on the loan is less than the income. As a result you are making money.

So, if negative gearing means that you're making a loss, why is that a positive? Obviously, nobody wants to get into property investment to lose money. Even though most property that you will buy will be negatively geared, that is the rental income is not as much as the interest payment, the benefit comes from the capital growth. Let's look at an example below to clarify this point. There are other expenses related to owning property but to keep this example simple let's just focus on the interest expenses.

Let's imagine you bought a \$440,000 property and took out a \$400,000 loan at an interest rate of 7%. The annual interest payable on the loan is \$28,000. Let's also imagine that you are earning \$430 per week in rent, which adds up to an annual rental income of \$22,360. Based on the above example, you are paying \$28,000 in interest but only earning \$22,360 in rent which means there is a shortfall of \$5,640 per year. That's the bad news.

The good news is that the property should be going up in value and it is worth more as times goes on. If the property went up in value by 10%, it has increased its value by \$44,000. At the end of one year, you have paid out \$5,640 in interest but the property has increased in value by \$44,000 which means that you are \$38,360 richer than you were 12 months ago. It would be great to be neutrally or even positively geared and still make a net profit but these sorts of properties are very hard to find.

In summary, negative gearing works IF the money you make from the capital growth is greater than the loss you make in rental shortfall.

Regards



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