Top 20 Property Investment Criteria

Rich Harvey, CEO

propertybuyer

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As a buyers' agent I am constantly asked "where is a good place to invest" and "what type of property do you recommended I buy to maximise my returns?" As a property investor you need to take a step back and ask a more fundamental question…"what do I want this investment property to do for me?"

Taking a strategic approach to investing in property means you need be clear on your goals and the returns you are seeking. Are you chasing high capital growth? Or is positive cash flow your number one priority? Perhaps you are seeking the best of both worlds? When it comes to property investments there is no "one size fits all." Your financial position, your risk profile, income and equity will all have a part to play in determining what type of property will suit your chosen strategy.

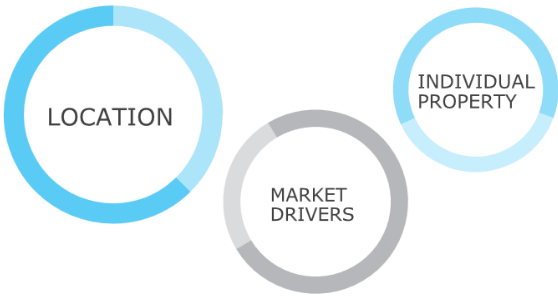
Your property investment strategy will therefore determine what criteria will apply when selecting an investment property. Choosing the right strategy and criteria is so critical to your investment success. No one wants to pick a lemon! So here are some very important criteria that you need to carefully consider when weighing up various property options.

Don't be swayed by glossy brochures and slick marketing material when choosing your next investment. Look at the fundamental drivers of supply and demand. Examine the data and crunch the numbers. It will make a world of difference when you look back in seven years time.

There are three broad categories that you must consider when evaluating investment property. These are:

1. **The location**
2. **The market drivers**
3. **The individual property**

My Top 20 Criteria is built around assessing a combination of these factors.



1. Location

Location, location, location…very similar to position, position, position. Real estate is all about buying the most well positioned dwelling that will deliver the best capital growth and yield. What are the prospects for growth in your selected suburb? Does it have the right demographics and physical appeal to create high demand from both owner occupiers and tenants? We like to find areas that have a consistent history of capital growth or areas that are being gentrified. Look for the "Ripple Effect"; i.e. surrounding areas that are cheaper or undervalued relative to a major suburb. Aim to pick suburbs that will deliver a growth rate of over 7%. Combine this with a 5% rental yield and you should earn a total return on the property asset of at least 12% pa.

2. Price/Affordability

Picking an area purely based on its price point is like picking your partner because their birthday fell on a certain date – it's far too risky. The relative "affordability" of a suburb will become one of the major factors in determining price growth in the future. A suburb is considered "affordable" relative to the average incomes for those living in that suburb. A classic measure of affordability is the price to income ratio. Sydney's median dwelling price is approximately $500,000 and median income is approximately $75,000p.a. so the ratio is 6.7 times. Melbourne's ratio is 6.6, Brisbane 5.8 and Perth 6.0.

So picking a winner suburb doesn't always mean choosing cheap suburbs – it means looking at the incomes and demographics - covered later.

Suburbs coming off a low price point <u>and</u> positioned next to major amenities, lifestyle features and with rising incomes is likely to perform better in the long run. It's generally easier to sell a property in an affordable suburb than an expensive one. The number of days it takes to sell a $2m property is typically a lot more than a $400k property. The affordable end of the market is less subject to wild market fluctuations as common in the prestige market.

3. Rental Yield – the Cash Flow

The yield you obtain from a property is a key indicator of the gross rental return (cash flow) you can expect from a property investment.

Yield is calculated as: Rent per week x 52 (weeks) / purchase price.

Example: if a property is rented at $500 per week and purchase price is $490,000, then yield is calculated as: (500 x 52)/ 490,000 = 5.3%.

A yield that is 2% to 3% higher than the variable loan rate should result in a property that is cash flow positive, depending on your borrowing position.

If yields are falling in a suburb, it can be an indicator that there is a possible oversupply of rental accommodation or that property prices are rising (or both). And conversely, rising yields can be an indicator of a shortage of rental stock or that prices are falling.

Choose properties that have high tenant appeal, that are well located to shops, schools and transport and have the right features that tenants love….such as internal laundries, security car space or garage, secure entry, storage space and open plan living areas.

You could also consider increasing the rent by adding a furniture package if it's located in a tight rental market.

4. Population Growth & Demographics

The demand for housing rises as population increases. However, property prices do not rise automatically in response to population increases in a suburb/ area. You need to take into account the stock of existing housing and see how much absorption will take place. Critical shortages of accommodation in some regional areas and towns due to large infrastructure or mining projects has often seen property prices skyrocket for a period of time. A large influx of workers creates heated demand for rentals and owner occupied homes.

The demographic you want to target include professionals, DINKS (double income no kids) and families with high disposable incomes. The main demographic to avoid is areas with higher proportion of retirees as their incomes are very limited.

5. Rental Vacancy

Select areas that have a low rental vacancy figure. The "vacancy rate" refers to the percentage of rental properties in a suburb that are currently vacant. A low figure is a positive indicator that there is a high demand for rental accommodation and tenants are fighting over the low number of possible properties to rent. Low vacancy rates area often a pre-cursor to rents starting to rise.

6. Days on the Market

Each property listed for sale will have its own unique features and flaws and the buyers will determine the market price. The number of days a property has been listed for sale is a good indicator of demand. The lower the number, the more quickly the property is snapped up by buyers' which means the suburb is in high demand. For example, it takes 43 days on average to sell a house in Engadine as compared to 280 days in West Nowra.

7. Stock on Market

The stock on market is a key indicator of housing supply. It is measured by the number of properties for sale expressed as a percentage of properties in an area. The lower the stock on market, the lower the supply of property, or the more demand for it (or both).

Suburbs with a high percentage of the stock on market, is not a healthy or balanced situation. It gives buyers ample opportunity to negotiate and be selective about what to purchase. A high figure for stock on market would typically result in a "buyer's market" which is not a good situation for long term growth.

8. Vendor Discounting

Vendor discounting is the percentage difference between the original asking price requested by the seller and the eventual sale price agreed by the buyer. It can be difficult to measure in suburbs where there are lots of auctions or private treaty sales where the price is listed as "offers over."

A high demand suburb will have a low vendor discount figure as sellers don't need to negotiate as much in order to get their property sold.

Suite 2, 47-49 The Centre (Darley Street) Forestville NSW 2087
PO Box 139 Forestville NSW 2087
T +61 2 9975 3311 F +61 2 9975 7944 E info@propertybuyer.com.au W www.propertybuyer.com.au Lic # 1265983

9. Auction Clearance Rate

In suburbs where auctions are frequently used, the auction clearance rate is a good indicator of demand and the health of the property market. The clearance rate is the percentage of properties listed for auction that actually sell. A struggling market will have an auction clearance rate of below 50%, while a balanced market will have a clearance rate between 50% and 65%. An active and thriving market has clearance rates above 65% indicating high demand.

10. Ratio of Renters to Owners-Occupiers

There are two reasons to pick suburbs that have a higher proportion of owner-occupied stock. Firstly, more owner-occupiers means there is a lower supply of rental accommodation in the suburb – you'll have less competition from other landlords competing for tenants and compressing yields.

Secondly, owner-occupiers tend to take better care of their property than tenants and improve the street appeal and streetscape of the surrounding area. We aim to select areas where the ratio of owner occupier to renters is above 70%.

11. Online Search Interest

The internet has revolutionised the way that buyers can search for property and provides excellent insights into what people are searching for. "Online search interest" shows the ratio of people searching for property online compared to the number of properties for sale. It is another measure of demand. The higher this figure, the more demand for property compared to supply for would-be buyers searching online.

12. Value Adding Potential

Another great way to increase your equity is to identify a property that has value adding potential. Examine the property in detail to see if it has the potential to be renovated, subdivided, extended or redeveloped. Look at the block size, internal and external features and assess what could be done profitably. A common mistake by novice investors is to find a "renovators dream" only to over-capitalise and spend far too much on a renovation. Discover what fully renovated homes or apartments are trading for, before committing to a costly (and time consuming renovation). Lots of simple things can be done to increase a property's value including repainting, carpet, polishing floorboards, and adding new kitchens and bathrooms.

13. Uniqueness

How unique is the property you have shortlisted? Is it a mass-produced apartment with little differentiation to neighbouring properties in a block of 200? If you are looking at a house, what percentage of the price is made up by land value? Aim to select apartments and houses that have some uniqueness value. Check with the local council to see if there are any other large scale developments or land releases about to be approved which could potentially increase housing supply and adversely affect property values in the area. Be careful about buying properties that are too "unique" or niche market. Make sure there is a resale market.

14. Employment Opportunities

Selecting a suburb or region with a diverse range of economic drivers is wise. Rental demand is driven by workers seeking and maintaining employment. An area with solid employment opportunities from a diverse range of industries will lower your vacancy risk. Strong economic vibrancy is a key factor to look for particularly in regional and rural areas. Mining towns are more vulnerable to downturns, but can be very profitable for investors that select the right types of properties. Avoid areas where the local economy is declining or there is only one major employer or industry type.

15. Proximity to Amenities/Lifestyle Appeal

Properties located in close proximity to major amenities are typically high in demand and tend to outperform the average. Tenants love being able to walk to the bus or train, grab a coffee from the local café and walk around the nearby parks. A good indicator of the "livability" of a location is its "walk score" http://www.walkscore.com. This gives a list of the local restaurants, cafes, supermarkets, parks, schools, community and recreation facilities within walking distance of the chosen property.

The lifestyle appeal of a suburb is a key ingredient for capital growth and yield. Select areas with attractive streetscapes, close to recreational and sporting facilities, entertainment, restaurants, cafes, specialty shops, beaches, waterways and parks. Talk to the local real estate agents and shop keepers and find out what makes people want to live and buy in the area. Does it have a family friendly atmosphere, a great "vibe" or some key attractions?

16. Zoning & Title Type

Before committing to a purchase check the zoning and title of the property. Is the area likely to be rezoned for multi-unit housing in the future? How would this affect property values in the street? Be cautious of buying an apparently cheap property if it is located too close to industrial zonings.

Make sure you understand your obligations for owning a property under different titles: torrens title, strata title, company title and community title.

17. Age & Condition of Property

Older properties will typically require more maintenance and have lower depreciation allowances than brand new properties. However, brand new properties also come at a much higher price tag. You will have to complete extensive research to identify if you are better off buying old or new.

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Engage a building and pest inspector to provide an expert report on the condition of the property. The building report will identify if there are any major issues with the property – but take this report in the right context – don't confuse structural issues with cosmetic issues that can be easily fixed. Many older properties provide excellent scope for renovation and value adding.

18. Floor Plan Functionality – Aspect & Light

A property with a good floor plan will attract more buyers and tenants. A "good" floor plan consists of open plan living and dining areas, kitchen/ meal areas flowing out onto a deck or outdoor area, spacious bedrooms, built in wardrobes, adequate storage space, internal laundries, internal access to car space or garage and plenty of natural light. Older style properties (often ripe for renovation) have the kitchen tucked away, small bedrooms and disjointed living areas. Modern apartments have some excellent designs used to maximise space and light and combined with balconies provide a very pleasant living space.

19. Construction Type

Looking ahead 10 years, think about the maintenance that will be required on your shortlisted property. Properties constructed of brick (single brick veneer or double brick) will typically have much lower maintenance than fibro or weatherboard. Look for properties that are well constructed and maintained. If you're buying a house, don't forget to consider garden maintenance.

20. Finishes & Inclusions

The types and quality of inclusions in a property are also important in determining the overall value. A rental property does not need to have top of the line Meile kitchen appliances to attract the best rent. However, good quality inclusions in bathrooms and kitchens help to create an overall "impression". When buying off the plan or brand new properties, check the list of inclusions carefully. Make sure light fittings, fans, carpets etc are all included in the contract.

Some of the superior features to look for in a property include:

- Ceaserstone or granite bench tops
- Timber floors
- Stainless steel appliances
- Double showers
- Built-in robes with detailed draw fit out
- Quality doorknobs and tap ware
- Under-floor bathroom heating
- Sisal wool carpets
- Ducted or split air conditioning
- Quality roller blinds

So how do you find a property that ticks all 20 criteria? Should you weight each criteria the same way? Property investing is both an art and science – the art is in researching, analysing and negotiating while the science is understanding and interpreting the market data to pinpoint the right suburbs. Researching is a time consuming business. To be successful you need to be serious and commit considerable time to the task. It's also easy to make a mistake and miss something important along the way. Buying a property is usually the most expensive purchase you are ever going to make in your lifetime. Getting expert help makes a lot of sense.

Buying your next home is both exciting and daunting. Lots of questions may be running through your mind as you start the search….will I find my "ideal home", how many weekends will I have to look, what is the property market doing, how much should I pay, what if I have to go to auction and...can I trust what the agent is telling me?

While there are several shortcuts, searching for the "right" property does take considerable time. This guide will give you excellent tips to ensure you are well on your way to becoming a happy home owner! Searching for the ideal home may seem like hard work, but taking a few moments to consider your plan of attack will make the whole process a lot easier.

How can I get further help?

RICH HARVEY
MANAGING DIRECTOR

To get a professional buyers advocate on your side sourcing and negotiating the best opportunities, please **call** 1300 655 615 (or + 61 2 9975 3311), send us your property brief, or email us to arrange a meeting to discuss your property needs.

Rich Harvey is founder and Managing Director of www.propertybuyer.com.au, Australia's most awarded Buyers Advocates. **Propertybuyer** helps property investors and home buyers search, appraise and negotiate the right property at the right price, every time. Rich Harvey is an economist, property investor and Managing Director of propertybuyer, Australia's most awarded Buyers Agents. Rich was awarded the 2009 national "Buyers Agent of the Year", the "Award for Excellence" 2004-2010 by the REINSW and the 2007 National Telstra Business Award. Find your next property faster, visit www.propertybuyer.com.au or call 1300 655 615.

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