Ask the experts

Our panel of experts give advice on a range of topics including buying in a hot market, interest only or principal & interest repayments, as well as claiming depreciation on repairs

The experts

Margaret Lomas
is director of Destiny Financial Solutions, a qualified financial advisor, and author of a number of books about property investing. She is also the host of *Your Money Your Call* and *Property Success with Margaret Lomas*, airing on SkyNews Business at 8:30pm Sunday nights.
Visit www.destiny.net.au

Conny Torney
Conny is the winner of the inaugural *Your Investment Property* Investor of the Year Award. A self-employed clown and children's entertainer, Conny currently owns and manages about $4m in real estate.

Tyron Hyde
Tyron Hyde is director of quantity surveying firm Washington Brown. For more information visit www.washingtonbrown.com.au

Michelle Coleman and Lee Dittmer
Collectively, Lee and Michelle have 36 years of experience in the finance world. They are both award-winning brokers and are active investors. Visit www.whofinance.com.au

Buying in a hot market

Q I live in a suburb that's so hot that properties are selling above their asking price less than a week after they are listed. I want to buy here, but I can't seem to find a house for less than full value as there are many qualified buyers looking at the moment. Do I just sit around and wait for the market to slow down, or should I look elsewhere, perhaps in another state? Are there good deals in a hot market?
Thank you for your help, Angela

A My first question is – what is your reason for buying? You say you live there already, so I wonder if this is a property to live in, or one to invest in?

If you would like to live there, your motivation for buying is a different one to that of an investor. You will have certain things you want in a property, and only a few properties may qualify as being suitable for you. Trying to guess when the market will slow down, or even if it will, may be dangerous. It may mean that you miss out altogether on getting a property that you truly want.

Even if you buy now and the market does cool a little, you are buying a property to live in and presumably this is not a short-term purchase. This means that over the years any short term losses will smooth out and, when you do sell in the future, you should still make a gain. Any discount that you would otherwise get in a cooling market – presuming it does cool and you get the property at a discount to the listed price – will probably become insignificant. This is especially true if you are also committing funds to debt repayment once you do buy. You will be 'owning' a property sooner (by making principal repayments) as you will be buying it sooner, rather than continuing to pay rent and then starting on debt repayment at a later date.

If this property is for an investment, then the viewpoint changes significantly. You have the choice of the entire country, and paying a little more for a property in that area may be a bad choice if you can find property with similar growth prospects at lower or more reasonable prices elsewhere. Your aim as an investor is to get the best possible price in the area showing the greatest prognosis for future growth – and the areas which are currently being pumped up by emotional buyers taking advantage of the First Home Owner Grant boost may not be the best areas in which to buy right now.

You need to do a lot of research and expand your horizons to the areas which show the best potential in the coming few years. As an investor, emotion should never come into the process and you need to have your commercial hat on. Sit back and let the emotional homeowners go ahead and outbid each other on local property, while you explore the country for the best bargains and the next hot spot!

– Margaret Lomas

Interest only or principal & interest?

Q I have two investment properties. One is fully paid for, and the other one still has $220,000 owing. Using my equity, I am about to purchase another property for $360,000. I wish to own all three properties eventually, so I am paying principal & interest. What are the advantages to moving to an interest-only loan? I have heard you never own the property by just paying interest – help! Rico

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A There are advantages and disadvantage to this, but what is true is that you never own the property by just paying the interest. What makes the real difference is what you do with the money that would have gone to the principal component of the repayment.

So what can you do with the extra cash if you aren't paying off the principal? What are the advantages of paying interest only?

There are a few different thoughts here and the effect it has on you will depend greatly on what your personal situation is and what your long-term investing goals are. Without knowing more of your personal details (eg, is it your own home that is paid off?), we will discuss some general advantages of paying interest-only repayments. You can decide if they relate to you.

Many investors will use the extra funds to pay off their own home. As soon as they have paid this off they have more cash flow and equity to use for other things – this could be another property or shares or any other purpose.

By only paying the interest repayments you will have greater cash flow to sustain more investment properties. The amount of money you would pay in principal with one property could equal the shortfall of another property's interest repayment. This, over the long term, means that you have more potential for bigger capital gains, as you will own more properties that will eventually grow and give you a larger equity base.

By only paying the interest, you can actually borrow more. Some lenders will assess your serviceability based on your actual repayments. If they are interest only, it means that you can either purchase a better property and/or another property.

There are no tax advantages to paying the principal off your investment properties, so as time goes by the negative gearing benefits will reduce along with your loan balance. Of course with anything related to tax, you should always check with your accountant. However, if you have the cash flow and your goal is to own three properties then there is no reason to change your game plan now. It has worked for you well as you have already paid off one property and will soon have the three properties that you wanted. You just need to continue principal & interest repayments and you will own them all.

Have you thought that by paying interest only on these properties it could help you own them faster? This is a different strategy again, and may or may not appeal to you, but you could use your equity to purchase another property and be more assertive. You could create equity by renovation or development/construction and sell these properties off. The profit you make could be used to pay down the balance of the two investment properties. You could keep doing this until it's paid off. During this time it would be easier on your cash flow if you were paying interest only. But by doing this you will actually pay off your loans faster rather than just chipping away slowly with principal & interest repayments.

– Michelle Coleman and Lee Dittmer

Investing in a changing market

Q I've just started doing my research for my first IP but the market seems to change every time I'm done doing my due diligence in one area. Any tips on how I could adopt to the constantly

changing market? Also, one of my friends recommended I attend property seminars. Are they worth it? Thanks, Annie

A Your letter identifies a real challenge for the first-time property investor. In my role as a property investment mentor I'm regularly contacted by frustrated clients who are far too quick to blame changing market conditions for their inability to make the correct investment decisions. I find this really surprising given the current economic climate. In fact, it is incorrect investment strategy, a timid mindset or just plain inexperience that is the basis of this problem. Moreover, I believe that investment seminars may be inappropriate for you at this stage of your property investment development.

Although we have different individual expectations, investment security, capital growth and the investment yield are fundamental to any investment strategy. In my view, property investment should always be for the long term and not influenced by supposed mini-cycles. In any event, property conditions with low interest rates, falling property prices and government largesse guarantee investment opportunity. Yet, like you, many investors cannot get their timing right.

Usually, this is a simple matter of not understanding the mechanics of property investment. In many cases, the investor locates the property and then begins the research process. I believe it makes much more sense to target a specific area.

Due diligence demands you understand government planning, infrastructure, population demographics and historical price patterns for the chosen area. Only then can you take full advantage of investment opportunities. In many respects, good timing is created by the investor's response to opportunity in the selected area.

You must situate yourself in the right time and place to both recognise and exploit an investment opportunity. Luck is a lovely asset, but the seasoned investor realises that proper research, courage and a positive mindset are fundamental to investment success. It is essential that you learn to read the play. This is a developed skill that enables the investor to be prepared for any situation.

In my opinion, first-time investors often try too hard and are propelled by raw enthusiasm from missed opportunity to missed opportunity.

Can an investment seminar provide the necessary tools to deal with this type of situation? They will certainly allow you to network, expand your information pool, and even provide the occasional nice bonus. And we all have been excited and motivated by a talented speaker. Unfortunately, herein lies the rub for the inexperienced investor: can they separate the salesman from the product, and recognise a good deal within the framework of their limited experience? It is not an easy task to deal with sophisticated in-house brokers, financiers and salespeople.

I would suggest your investment deficiencies will leave you vulnerable in this environment. Seminars, reading material and audio format and expert opinion can all be beneficial provided they are consistent with your learning type and are thoroughly investigated. We all have access to so much information in modern society. But there is also an X factor that is common to investment success. It is ultimately the ability to understand yourself and operate within your own personal parameters that is fundamental to investor success. In the end, it is this sense of self and investor confidence that will give you the awareness to recognise a good deal. This is more important than perceived external market conditions.

– Conny Torney

Claiming depreciation

Q I own a unit and will be living there for the next six months so I can fulfil the requirements of the FHOG. The apartment could use some aesthetic improvement such as repairing/replacing the dodgy old carpet and cupboards. My question is, is it tax deductible or even depreciable if I fix the apartment while I am living there? Or should I delay it until I move out? Thanks, Daniel

A If you carry out any repairs while living there you are unable to claim the cost of that work. However, by the sound of your question, you are going to replace all of the carpet and cupboards.

If that is the case, both will be considered a capital improvement and both will be depreciable – just at varying rates of depreciation. As to whether you should wait to do the work, it is irrelevant in this case.

You will only miss out on a minor amount of deductions if you do the work while living there. For instance, carpet has an effective life of 10 years – which means that you can claim 10% of the carpet price as a deduction for 10 years using the prime-cost method.

If you replaced the carpet after three months and then lived there for another three months – you would only miss out on the three months of deductions while living there.

You would still continue to claim deductions on the carpet for another nine years and nine months when the property becomes an investment property. With the cupboards, you hardly miss out at all, as built-in cupboards are claimed over 40 years – leaving you 39 years and nine months!

So my advice in this case is not to worry about the tax implications – they are minor. Focus on whether the money you're about to spend will increase the rent and attractiveness to a tenant. And remember, it will be a lot easier to get this work carried out while living there as opposed to when you have a tenant.

– Tyron Hyde

Got a property question you need answered? E-mail your questions to editor@yipmag.com.au

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Property investment seminars

Andy Gale, secretary of Property Investment Professionals of Australia (PIPA) explains what to look out for when considering property investment seminars

In its June 2008 Green Paper on Financial Services and Credit Reform, the federal government identified 'property spruiking' as an area of concern, defining one method of spruiking as 'the seminar'. Specifically, it was noted that a 'property spruiking' seminar is different from general 'wealth creation seminars' where no interest in direct property is offered. Using titles such as 'The Secrets of a Property Millionaire', these types of seminars are conducted similarly – yet will offer either an opportunity to attend a subsequent, costly seminar which claims to provide a pathway towards property investment wealth or the opportunity to buy a property after attendance.

The Green Paper highlighted the following areas of concern:

- The method used by property spruikers to deliver their advice and market their products using high pressure, fast paced presentations that encourage attendees to make instant investment decisions without consideration.
- The misinterpretation or exaggeration of the benefits of buying property including the overstating of values, rental returns and capital growth.
- The provision of financial advice to encourage a purchase without possession of an Australian Financial Services Licence.
- Aggressive or harassing behaviour.

You should be wary of seminars that have any of these characteristics. The degree of 'spruiking' or 'wealth creation' as defined above may vary, but the fundamentals remain the same. These methods of selling advice and/or actual property are also seen in businesses which promote themselves as property investment advisors or even clubs/property networking groups, which ultimately take advantage of individuals under the guise of a trusted group.

There are industry professionals who conduct seminars on property investment or offer property investment strategies who are not considered 'spruikers'. Some may offer properties for sale, while others provide a range of property investment related services including the giving of advice to assist in making a purchase.

Protecting yourself

The current regulatory environment does not provide governance for those working in this industry, and so it remains a case of 'buyer beware'. You must identify the seminar and other service providers and enact a self-protection and due diligence strategy. Here are five ways to protect yourself:

1. Conduct ample research before making any property investment decision. Does the strategy being offered suit your current position, financial capacity, risk profile and investment goals?
2. Ensure you are provided with a written disclosure document outlining commissions. Commission is not a sign of bad business practice, but knowing how much is being paid can assist you to establish if what you are buying is at market value. Knowing who's going to benefit the most from the sale may influence your ultimate decision.
3. Obtain an independent valuation from a qualified valuer. This helps to ensure that any fees or commissions are not being added to the true price of the property and that it is at market value.
4. When you are being sold property using an advice model, and your personal financial circumstances are being considered by the seller, establish the qualifications of your service provider. If commissions are derived from the sale, the advice is not independent. This does not mean the advice is not appropriate for you – but you will need an independent opinion from a professional advisor before proceeding.
5. Always seek independent financial advice from a suitably qualified professional before making any investment decision.

PIPA is an independent industry association for property investment professionals where members adhere to a strict code of conduct which ensures best practice.
Visit www.pipa.asn.au and click on 'consumer information' for further details.