My thoughts on property for Doctors.

By Paddy Guildford
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Part 1: Why is property a good investment?

I have often tried to write about the principles of property investment, but it is difficult because it is such a wide area and everyone including the experts have different opinions, emotional and factual. So what I am going to lay before you are some simple and basic considerations that reflect my experience over the years.

Firstly, the choice for growth investments for most of us is either shares or property. You will see below the research report provided by Russell Investments that shows that over a long period, shares and property provide a similar return.

Results:
20 years to 31 December 2014.
Most asset classes performed strongly, with an uptick in returns from global assets across to the domestic fixed interest assets. Australian shares performed better over the longer 20-year period to 31 December 2014, as the poor performance in 2014 was stretched out over the longer timeframe, diluting its impact.

Comparison across asset classes on a before-tax basis: 20 years.
Australian shares and Australian residential investment property continued to perform strongly over the 20-year period. Residential investment property returned 9.8% p.a. over the 20-year period, while Australian shares returned 9.5% p.a. This was followed closely by global listed property (unhedged) which returned 8.9% p.a.

Global shares (hedged) came next, returning 8.6% p.a. Its unhedged counterpart, global shares (unhedged), returning 7.1% in the same period. Hedging added an additional 1.5% p.a. over the same period.

Global fixed interest also performed very well, returning 8.6% p.a. Its domestic counterpart, Australian fixed interest, returned 7.5% p.a. over the same period.

Australian listed property finished with 7.7% p.a. while cash returned 3.7% p.a. All asset classes beat inflation, which rose by 2.7% p.a.
However, there is a major difference in the opportunity on how to purchase either of these assets, and it comes down to financing. We can arrange a 90% loan on investment properties, with no Lenders Mortgage Insurance (see page 8 for more details). Banks will generally only lend up to 50% on an individual’s share portfolio without any other security.

**Example: Why we like property.**

Let’s assume you have cash of $50,000 to invest.

<table>
<thead>
<tr>
<th></th>
<th>Investment Property</th>
<th>Shares</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Purchase value</strong></td>
<td>$500,000</td>
<td>$100,000</td>
</tr>
<tr>
<td><strong>Cash</strong></td>
<td>$50,000</td>
<td>$50,000</td>
</tr>
<tr>
<td><strong>Loan</strong></td>
<td>$450,000</td>
<td>$50,000</td>
</tr>
<tr>
<td><strong>Value in 10 years</strong></td>
<td>$1,000,000*</td>
<td>$200,000*</td>
</tr>
<tr>
<td><strong>Less loan</strong></td>
<td>$450,000</td>
<td>$50,000</td>
</tr>
<tr>
<td><strong>Net gain</strong></td>
<td>$500,000</td>
<td>$100,000</td>
</tr>
</tbody>
</table>

* Assuming an average annual gain of 7.2%.

Accordingly, by the use of OPM (other people’s money, i.e. the banks) you can create a gain of $500,000 in property versus $100,000 in shares for the same cash deposit; this is why we love property as a long term investment. Your next question should be ‘But what about servicing the property costs over that period?’. Here is an example of how this would work: assume the above property and that the Doctor is earning above $180,000 per annum.

**Annual Costs:**

- **Interest** $19,233***
- **Rental costs** $5,016 (rental management, rates, insurance)****
- **Total** $24,249

**Annual Income:**

- **Rent** $26,000*
- **Tax saving** $4,819**
- **Total** $30,819
- **Net income** $6,570 per annum

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So this property has an excess income of $6,570 per annum, giving you plenty of room for interest rate increases if (or when) they come along. Now do your calculations on a prospective property, and if you need a hand, contact me - I have a financial model that does all this and I’m quite happy to share it with you.

**What are the main take-away points from this example?**

1. **Look for properties that have a yield of around the 5% mark.** In some of the older areas close to the CBD this may be hard to achieve, but generally these areas have a superior chance of values increasing. So the purchase decision is then based on your ability to ‘cash flow’ the property.

   You may have heard of yields around the 10-12% level, generally these are out in the regional areas like mining towns. The problem facing these areas is that when the mines close or reduce staff, these properties can’t be rented...or sold. This is happening right now; stay away from them.

2. **Build a new property,** providing you with higher depreciation for tax savings and less maintenance costs.

3. **Use any excess income to reduce the loan.**

4. **Understand and consider the risks.** There are three main ones:

   a. **Interest rates may increase.** They certainly will go up and down during the course of ownership. Add another say 2% to the interest rate and see if the numbers still work. Remember, rents also do have a habit of going up.

   b. **I can’t find a tenant.** Part of your research should be to check out the demand for rental property in the area. We don’t find vacancies a problem as 30 % of the population rent, so just focus on good quality areas and a well-designed home for the demographics of the area where there is strong rental demand.

   c. **Cash flow is king.** Make sure the numbers work for you, add a bit to the costs and reduce a bit from the income. If it doesn’t work, forget it and move on.

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***You should be able to get a minimum yield (annual rent as a percentage of the cost price/value of the property) of 5% on a property in a good area that has a good chance of future gains.

****The calculation of this relates mainly to the depreciation factor. You can depreciate a new home over a 40 year period, at 2.5% of the cost of the building plus you can depreciate all the internal fittings, carpets, drapes, appliances etc over terms from 3-15 years.

****Based on an interest rate of 4.27% p.a., which is subject to change.

****Based on rental management costs of 6.6%, building insurance of $800 and estimated rate costs of $2,500.
Part 2: Six property tips to get you started.

1. You don't have to be an expert in order to achieve satisfactory investment returns. But if you're not, you must realise your limitations and follow a course certain to work reasonably well. Keep things simple.

2. When promised quick profits, respond with a quick ‘no’.

3. Focus on the future returns of the asset you are considering. After doing your homework, if you don't feel comfortable with the asset's future earnings, just forget it and move on. No one has the ability to evaluate every investment possibility. Omniscience isn't necessary, you only need to understand and be comfortable with the actions you take.

4. If you instead focus on the prospective price change of a contemplated purchase, you are speculating. There is nothing improper about that. However, I know that I am unable to speculate successfully, and I am sceptical of those who claim sustained success at doing so. Half of all the coin flippers will win their first toss, none of those winners have an expectation of profit if they continue to play the game. And...the fact that a given asset has appreciated in the recent past is never a reason to buy it.

5. Think only what the properties will produce over time and not at all about the daily valuations. Games are won by the players on the playing field – not those whose eyes are glued to the scoreboard.

6. Forming macro opinions or listening to the macro or market predictions of others is a waste of time. Indeed, it is dangerous because it may blur your vision of the facts that are truly important i.e. the opportunities that are right there, under your nose.

You may have heard or read about the ‘Property Cycle’. There is such a thing, and the timing of it differs in each state, each town and each suburb. The three main drivers are:

1. **Demographics**
   - Population levels/growth
   - Net migration
   - Employment levels
   - Number of people per household
   - Rental vacancy rates
   - Scale of property construction

2. **Financial**
   - Rental levels, rent per week
   - Return on investment
   - Rental affordability
   - Property affordability
   - Finance availability
   - Property values

3. **Emotional**
   - Average days on the market
   - Number of listings
   - Sale levels (volume)
   - Gentrification – Upgrading of amenities, facilities and/or property

The above is rather clinical, so let’s go through an example to bring it to life.

**Example: Drivers of property growth.**

At the end of the day, the value of your property will be dictated by the market i.e. Supply and Demand. If demand outweighs supply, the value of your investment will go up over time (and vice versa). So the goal is to find an area where supply is limited and demand is high.

Let’s assume you have studied the locations and decided on one; the next thing to check is what product is in short supply in this location i.e. family homes, townhouses, or units and apartments.

If this is now an investment proposition, investigate the demographics of the location. This should give you an idea of the age and income of the local population, which in turn will give you a product to concentrate on.

For example, the majority of older residents don't want to move into high rise apartments, they want to stay in the same area, but have a smaller home. A town house product where they can still have a small garden, but is still easy to lock up and go travelling, is more suitable.

Financial demands are now dictating the requirement for them to downsize to increase their retirement incomes.

What is the local rental market like and what are the agents telling you is in short supply?

All the above is the science of property investment but you also need to add your artistry to it. Think about how you see this property in the future and what it should look like, visualize what sort of people would want to rent, or buy this property. Then think about what you need to do to the property in order for it to appeal to those demographics. Finally, take a step back and forget all the emotions, and ask yourself... 'does this all make sense?'
Part 4: Understanding the ‘the property cycle’.

Property research people and the major valuations firms do provide a ‘property cycle clock’ every quarter or so. These are put together based on the drivers of property growth outlined above. Below is an example of a ‘property cycle clock’ published by the valuers.

Looking at the above property cycle clock, you can see how this all works. By reading your local paper, talking to local real estate agents, referring to the above and asking the right questions you will get a fairly good idea of where your local market is in the cycle. I am often asked how long a cycle is. The answer is, it’s all over the place; it can be really slow and then it can go from one quarter to the next very quickly.

So obviously the aim of the game is to buy when the clock is at the lowest point and sell (if you must) when the cycle is at its peak.

But…the problem many of us are faced with is finding the time to do all this effectively, including following the market through its cycle and knowing when to pounce. Now you will never get it spot on, but property is a long term investment, i.e. a minimum of 10 years.

So you should pick up a cycle over that period and that’s when you will get your gains. My belief is that you buy quality property in a quality area and hold onto it for the long term. The art is to catch the cycle at the right time and finance it correctly. This leads me onto financing.
Part 5: Did you know about ‘Doctors–Only Finance’?

Now this is not a sneaky pitch, but it would be doing you a disservice if we didn’t mention this to you. We have created an arrangement with Westpac especially for Doctors and the medical fraternity. This is an exclusive arrangement for us and it can’t be obtained through Westpac’s branch network or the broker network.

The benefits of our Doctors–Only Finance Product:

1. Home finance: a 95% loan without Lenders Mortgage Insurance (LMI). This is a huge saving!

2. Investment property finance: 90% loan without LMI for all investment properties you may purchase.

3. 24-hour personal access to bank personnel in Australia.

4. Interest rate discounts that stay with the loan for its life.

5. Full range of bank accounts and credit cards.

Most of the other banks have special Medico departments but none of them have these products. So you have a distinct advantage here.

As you continue to go through this guide, you will see examples of how financing can be done intelligently. These examples are not set in concrete, as all of our personal circumstances are different, and so financing needs to be moulded to ‘fit’ our personal situation.

Before you make this big decision, talk to me or someone who knows how to deliver the right advice.

Dual townhouses we built for a Consultant Doctor in 2015.
Part 6: The different methods of property purchase.

Be aware too that there are a number of ways of investing directly into property. Each way has its own nuances and relative advantages / disadvantages. It’s important to understand these before making a decision:

**Buying off the plan.**

Buying a property that is still some months or years away from being completed means you agree to a price for the property, put down a deposit now, and pay the remainder once it is built. This suits those who may not be quite ready to purchase a property but will be before the property is built, or others who believe the property is undervalued and will be worth more than they paid for it once the building is finished. However, in a market that falls, a bank may lend you significantly less than what you paid for the property, meaning you have to find additional money to fund this shortfall. As I write this, it is happening in Brisbane and Melbourne. I don’t like it, don’t do it!

**I remember reading a research report a few years ago that stated that only 60% of renovation costs add to the value of the property. I would agree with that.**

**Buy and develop.**

For the right block of land in a great location, there is also the possibility to ‘knock down’ an existing house, subdivide the land and build two townhouses. This can be a fantastic way of providing a purchaser with two property assets, each with their own ability to grow and enjoy ongoing rental income. We have done a number of these and they have all worked extremely well for our clients. This is my favourite method; ‘adding value by changing the usage’.

Whilst this strategy may sound great, it has some associated challenges. Firstly, you need to have enough cash or borrowing capacity to fund the cost of redeveloping the block of land. Secondly, ‘the devil is in the detail’. What block and where? What needs to be considered with regard to town planning, design, councils and financing?

I have a great team around me now and we have completed a number of these small developments. Contact me if you would like to check some of these out.

As I mentioned earlier, being a Doctor you have access to finance that the general public do not have. If you’d like to tap into this opportunity, then please feel free to call me to discuss this or otherwise, find someone who can connect you with this massive advantage.

As with anything in life, surrounding yourself with the right team is all that’s required to achieve a successful result.
Part 7: Non-Residents and Foreign Investment Review Board (FIRB) Considerations.

Obtaining property finance can be seen to be ‘painful’ for foreigners, but this isn’t the case. We have helped many foreign clients successfully purchase investment and residential property. Here are the basics but if you need any further information, let’s have a chat.

Purchasing property when you are NOT a citizen or permanent resident of Australia.
There are special provisions for non-citizens or non-permanent residents purchasing property in Australia.

Under Australia's Foreign Investment Review Board framework, foreign persons need to apply for foreign investment approval before purchasing residential real estate in Australia. The Government's policy is to channel foreign investment into new dwellings as this creates additional jobs and helps economic growth.

Homes / Established dwellings.
Foreign persons are prohibited from purchasing established dwellings unless it is for the sole use of a residence whilst they live in Australia. If the foreign person leaves Australia, the dwelling needs to be sold.

So, existing dwellings can only be purchased for the foreign person to live in and you can only have one.

New dwellings.
New dwellings can be investment properties or a residence. There is no limit to the number you can purchase.

Foreign persons need to apply and receive approval before purchasing an existing or new residential dwelling and vacant residential land. On vacant land, construction needs to be completed within four years. These new properties can be rented as investment properties.

There is a fee for applying to the Foreign Investment Review Board for approval to purchase a property, which varies depending on the value of the property. For more information on this [click here](#).

Additional foreign acquirer duty (AFAD).
On 1 October 2016, an additional levy on both residential and investment property was introduced for foreigners (you are deemed to be a ‘foreigner’ if you are not an Australian citizen or permanent resident). A permanent resident holds a visa, or is a New Zealand citizen with a special category visa as defined by the Migration Act 1958.

Currently, this levy stands at 3% of the GST inclusive contract value of the purchase, added to the total amount of ‘transfer duty’ payable on the purchase.
Part 8: The process of purchasing a property.

So once you have found a property, what is the process in purchasing it? You will either purchase by way of a negotiated contract or through an auction. The process for each is set out below.

Process of purchasing by negotiated contract.

1. I always suggest getting a pre-approval from a bank before going out to the real estate market. You can get a formal pre-approval which is subject to the bank sighting the purchase contract and a satisfactory valuation. By doing this, you know exactly what your purchasing limit is and it speeds up the approval process when you find a property.

2. Once you have both agreed on a price, the agent will present a contract which sets out the details of the seller, their solicitor, the buyer and their solicitor, and the legal description of property. It then goes on to set out other requirements as detailed below. They will then get the seller to sign and deliver a copy to both solicitors. Make sure they email you a copy signed by both parties.

3. At this point you will need to engage a solicitor or conveyancer to process the contract and to give you advice on any legalities affecting the property. My experience shows you have three choices:
   a. A conveyancer. They don't tend to make themselves available and the process is generally carried out via email. Cost = $600-800.
   b. A solicitor who will be available to discuss everything and answer any questions you have over the phone. There are some solicitors who charge $2,000 for who knows what, so forget them.
   c. A solicitor who will be available to discuss everything and answer any questions you have over the phone, but charges somewhere in the vicinity of $1,100-$1,300. This is my preference, so always obtain a quote first.

4. Understand your contract's conditions:
   a. If it is subject to finance, allow 21 days for this as the bank will have to process the loan application, have the property valued and then get credit approval. It does take time.
   b. Subject to a 'Build and Pest Inspection'. This needs to be done within a timeframe, get a registered inspector to complete this for you to check out any building problems or pest infestations.
   c. Subject to a 'Pool Certificate', if the property has a pool, then the pool fencing needs to be certified that it is a legal structure.
   d. Subject to a 'Safety Switch'. It is a legal requirement that every property has an electrical safety switch that is working.
   e. 'Settlement date', the date that you take over the property, usually a minimum of 30 days from when finance is confirmed. In Queensland all these timeframes start from the 'Contract Date' which is the date the Buyer and Seller have signed the contract and it being presented to their solicitor.
   f. Standard terms and conditions. These are pretty standard but have a read of them so that you understand how all this sale process works. I'd love to go on about the negotiation in this guide, but let's just say, everything is always negotiable. If you find problems with the 'Build and Pest Inspection', then renegotiate the price to cover the cost of correction...and hopefully a bit more.
   h. Once the seller has accepted your offer by signing the contract, the agent will deliver the contract to both solicitors and the 'Contract Date' starts. You need to send a copy of the contract to your financier and supply all other details required. The bank will process the application and give you an approval letter which needs to go to your solicitor who will then advise the seller's solicitor that the finance has been approved. The same happens with the Build and Pest Inspection report. When this is all completed the contract becomes 'unconditional' and the bank will arrange a settlement time with the seller's bank and solicitor to repay any existing loan on the property and change the ownership and register your loan on the property. Once that is all done, the keys will be available, normally from the agent. The agent earns a commission on the sale which is paid by the seller and will be paid to them from the sale proceeds.
Process of purchasing by auction.

You will attend the auction and will need to register yourself as a possible bidder. If you are the successful bidder, then you will be required to pay the deposit as set out in the auction document and sign an unconditional contract after the auction. So all the conditions mentioned above in the negotiated contract, such as a ‘Build and Pest Inspection’, are negated.

No conditions, no time to confirm finance, the deal is done. So you need to meet all the above conditions prior to the auction. Get a pre-approval from the bank for finance, get a build and pest inspection done, check out the pool and safety switch. The agent will then send the contract to your solicitor and the process outlined above kicks in.

Concessions for first home buyers.

Transfer duty concession
Transfer duty is a tax payable to the Government for transferring the ownership of an asset from one person or entity to another.

The Queensland Government offer a range of ‘transfer duty’ concessions for people buying their first home, which they will live in during the first 12 months after purchase.

There are some strict conditions governing your entitlement to this which include:

- Never holding an interest in residential land anywhere in the world.
- Never having previously claimed the first home vacant land concession.
- Buying a home valued less than $500,000.
- Living in the home as your principal place of residence.
- Being at least 18 years of age.

If you would like more information on this concession click here.

Grant for first home buyers
If you are looking to purchase vacant land and build a brand new property, the Government also offers a $20,000, once-off grant for first home buyers.

The eligibility criteria for this one include:

- You must be an Australian citizen or permanent resident (or applying with someone who is).
- You or your spouse must not have previously owned property in Australia.
- You must be at least 18 years of age.
- You must be buying or building a brand new home, valued under $750,000.

More details on this particular grant can be found at the QLD Government’s website.
I really love property as an investment option, and I hope you have enjoyed reading my thoughts.

If you want to have a chat about any of this, feel free to give me a call or send me an email; I’m always happy to help.

Take care,

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