8 Considerations To Successful Co-Ownership Of A Property Investment Portfolio

This Issue:
November 7, 2017

TRILOGY news
"the property investor's mortgage broker"

Brothers and sisters are doing it. Parents and children are doing it. No doubt, aunties, uncles and second cousins are all doing it too.

When an individual effort isn't financially sufficient to break through the housing affordability barrier, no matter how hard you try to save, it makes sense to combine forces and resources in a joint venture ownership arrangement with people you trust. And who better than your friends and family?

While the actual data is a little patchy, there's a great deal of anecdotal evidence to support some of the numbers produced by new-ish kid on the block coHome, which assists young Aussie homebuyers to, well, co-purchase a property obviously.

Late last year coHome surveyed 250 Millennials, and found that 60 per cent would consider joint ownership arrangements with friends or family. And this isn't just about home ownership either, with many building the beginnings of a property investment portfolio through such arrangements.

But before you jump headlong into something as substantial as the acquisition of an investment property with any type of significant "other", be it a sibling, sister-in-law, spouse or friend, there are a few considerations (or rather 8 as the title of this piece suggests) that need to be carefully weighed up…

1. Will it make or break your relationship?

Is your relationship solid enough to withstand any type of dissent in the ranks should things go pear shaped? I'm not suggesting it's a given that they will. But if you want to take on friends as business partners, you also have to be prepared to lose them as friends. Remember that, at the end of the day…property investment is just another business proposition.

Relationships are much more open to change when you start to inject large sums of life savings into the equation.

2. Business or pleasure?

As per the above comment, you need to be honest with yourself and your co-owners about your intentions when it comes to the proposed partnership. This is an agreement that should be planned and executed with the same acumen as you would a business plan.

Everyone needs to be in mutual agreement and happy with the co-ownership terms…everything from the breakdown of dividends accrued through the portfolio's short and long-term returns, to the percentage of financial contribution, taxation and borrowing implications, each investor's financial goals, and administration responsibilities.

3. Talking money with your 'team'

If you cannot be open and honest about your own financial situation with friends and family, and they're struggling with the same level of personal disclosure, drop the entire idea of investing with others.

There's no room for dinner party politeness in a property investment joint venture. This is the time to lay your cards on the table and ask your friends to do likewise.

4. Co-borrowing blunders

Most lenders are cracking down on cross-collateralisation structures that involve securing a loan against one person's property to find the acquisition of another property investment with other parties to the transaction. Hence, if anyone has their equity tied up, this would likely need to be released beforehand.

Whatever you do, don't think you can traverse the increasingly tricky home loan landscape yourself when co-investing with anyone…particularly if you want any ounce of flexibility to go your own way down the track.

5. Will it compromise your personal credit position?

As above, the other serious consideration when it comes to being jointly and severally liable for a mortgage is that all of the associated debt, in its entirety (not just your agreed portion), could be deemed your sole responsibility when it comes to future loan applications.

Hence, while you might only have a 30 per cent share in a $400,000 investment loan, some lenders could attribute the entire $400,000 commitment as your mortgage, meaning your future borrowing options could be seriously impacted.

6. Go your own way

Imagine a scenario where you successfully grow a property portfolio of ten, high growth assets alongside three of your best buddies. You decide after a time that you'd like to expand that asset base, borrowing against the equity to purchase more housing investments. But your friends are content to sit on those ten properties indefinitely.

What do you do? Unless all three partners agree, you can't go off and borrow the cash anyway. Now you have to decide whether to hang in and hope that when it comes to a four way split, those ten properties will pay sufficient dividends to meet your nest egg dreams. Or, consider some type of exit strategy…

7. It's been fun but…the exit strategy

So who decides how it all ends my friends? Let's say you enter into a joint property investment ownership arrangement when you're young, footloose and fancy free, and then you meet the man or woman of your dreams and decide it's time to settle down.

What if you want to release the money from your portfolio to buy your family home and start a life with the love of your life, but your still single friends won't have a bar of it? These are the sorts of things you need to really think about, before working a well thought out exit strategy into your arrangement.

8. Have you covered everything?

As with any property investment endeavour, make sure you are adequately covered in case something goes awry. Have up to date and well structured policies in place for income protection insurance and life insurance just in case, as well as the obvious landlord's insurance.

While there are many potential pitfalls to consider when investing with friends and family, this is undeniably a clever and plausible option, worthy of investigation. It could mean taking a few steps up the property ladder sooner and with less risk exposure, if approached in a businesslike manner, with careful planning and good communication.

Are you covered? 8 ways to ensure your insurance is enough

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When it comes to investing in property with some level of surety and mitigating any associated risk, one of the things that is perhaps least talked about – but really deserves more attention – is insurance coverage.

Many an 'expert' will instruct investors as to sourcing and securing the right kind of property asset and property loan, but rarely is enough attention given to the subject of how you assess and obtain the best possible insurance policies to protect yourself, as well as your property portfolio.

This is a somewhat timely subject to look at right now given the increase in insurance brokerage firms, product options and comparison sites flooding the sector, along with a marked rise in clients turning to financial advisers in a bid to identify the best policy for their needs.

But while these services promise to qualify products currently on the market for your convenience, the question remains; who is actually qualifying the brokers, advisers and comparison sites? And more importantly, how are they assessing and referring business to particular insurance companies?

Getting paid to point you in "the right direction"

Worryingly, a recent Australian Securities and Investment Commission (ASIC) survey found that more than one-third of consumers advised on life insurance by financial planners, received guidance that fell short of meeting relevant legal standards. And when advice did comply with regulations, there was significant room for improvement.

Interestingly, of the 202 files surveyed by ASIC, advisers who did not receive upfront remuneration had a far better track record at rendering meaningful assistance to clients, than those paid immediate commissions for converting a prospect, with pass rates of 93% and 55% respectively.

Unfortunately, commissions paid to financial advisers and insurance brokers can be incredibly lucrative, representing anywhere between 100 and 130% of the new business premium.

What does this mean for you and I, the consumer? Well, it seems there's a giant conflict of interest preventing everyday Aussies from securing the correct insurance premiums. You could be receiving inferior policy terms, paying too much for unnecessary coverage or end up making a claim that is denied because of restrictions you were not adequately informed of.

This is a deeply concerning trend for property investors in particular, who often hold numerous assets in their portfolio and may very well rely on these personal insurances to prevent losing everything one day down the track, should their health and wellbeing be compromised in some way.

Insurance is big business in Australia, with the premium value of individual life risk policies (including life, total and permanent disability, trauma and income protection – all things investors need to consider) totalling $8.4 billion in 2013.

So how do you ensure you are adequately covered when it comes to protecting your all-important cashflow, without falling victim to a less than scrupulous adviser?

Here are 8 things you should do when exploring insurance options, not just for your assets themselves, but also for you as a high net worth investor.

1. Assess your needs and make sure the coverage aligns with them.

This includes careful consideration of your life stage – do you have a family you need to take care of if you lose all or a portion of your income due to an injury or illness? Do you need to maintain loan repayments on a number of assets across your portfolio? Are you covered for all possible events that could impact on your cashflow?

2. Compare products.

There are so many different companies and products on the market now that it's essential you have some idea as to who offers what. Even if you intend on seeking expert assistance in eventually selecting a policy, you need to know what's out there as an informed consumer. This isn't just about saving money upfront either, but also potentially saving a lot of future heartache by making sure the policy you select is aligned with your requirements.

3. Qualify an adviser before taking their advice.

Regulatory bodies are considering how to enforce tighter restrictions on things like upfront commissions paid to financial advisers and insurance brokers that can create a conflict of interest for consumers. However, right now, it's most certainly a case of 'buyer beware'. Ask your adviser if (and how much) they are paid by the insurance company they recommend and what process they undertake in qualifying the best product for your needs. If they seem disinterested in finding out as much about your personal circumstances as possible before thrusting a product disclosure statement at you, be wary.

4. Get it in writing.

Never sign or agree to anything before reading through all related information carefully and critically to ensure the product summary reflects your specific needs.

5. Read the fine print.

Most insurance product disclosures are more complex than a Year 12 Physics textbook. Always read the 'fine print' and make sure you fully understand what happens in the event of you making a claim and any restrictions or excesses that may apply to your policy.

6. Ask questions and speak to an adviser from the insurance company.

Don't just rely on a broker or adviser to point you toward the right premium. If they recommend one company and policy over another, speak to a company representative and ask as many questions as possible before signing anything!

7. Be specific – find out if you are covered for all the little things you might need.

Depending on your career, you might have certain needs that others do not. Insurance is not always a one-size-fits-all prospect, so make sure the policy you end up with is adequate.

8. Review your policy annually and make any necessary changes. Never become complacent with your insurance.

You should review your coverage annually, in line with your portfolio review. Is the amount of coverage you have still adequate? Have certain circumstances changed that you need to advise your insurer of? Can you find a better deal?

Can Anything Dissuade The Desire For Our New Housing From Chinese Investors?

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Regulators on both sides of the water have attempted to deter the constant trickle of money making its way from China into the hands of Australian property developers, with red tape, tax hikes and borrowing barriers. But nothing seems to be slowing the overseas investor juggernaut.

This is of course good news for local investors who rely on continued demand to underpin residential real estate values and grow their portfolios. Not so much for government authorities and those attempting to overcome the increasingly problematic affordability barriers, however.

Despite most states imposing a proportionate sales tax on overseas investors, and the Chinese government introducing strict capital controls on local credit used to acquire non-local assets, Chinese interest in our housing market continues to expand. So much so in fact, that Credit Suisse researchers suggests Australia can implement higher taxes on foreign buyers without curbing their enthusiasm whatsoever.

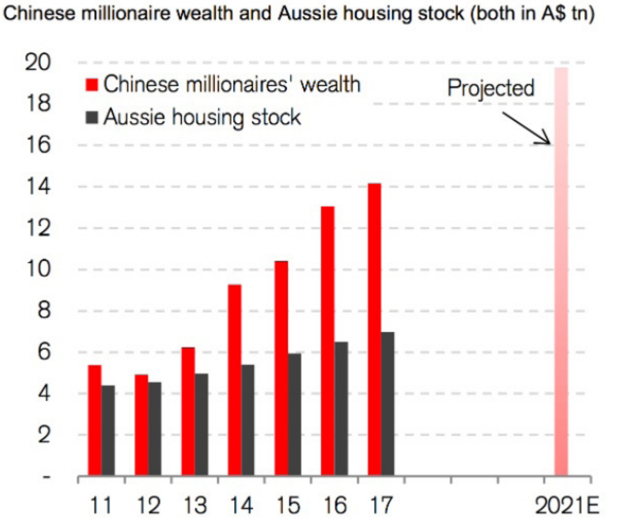
"Our tax receipt data helps measure how effective these (Chinese) control have been – and it seems they haven't been," reports Credit Suisse strategist Hasan Tevfik. "Chinese demand for Aussie property continues at a strong rate despite the government's efforts."

Please sir, I want more

With exponential growth in the Chinese economy set to continue, and its burgeoning national wealth being distributed broadly among its many citizens, most industry analysts agree that China will be a sustained source of local investment based growth for some time to come.

Figure 12: Chinese wealth growing faster than Aussie property values

Chinese millionaire wealth and Aussie housing stock (both in A$ tn)



Source: Credit Suisse World Wealth Report, ABS, Credit Suisse estimates

"We agree property in our major cities is expensive, but we also understand much of the housing market is supported by foreign buying," says Tevfik. "Chinese wealth creation suggests we should expect more."

More?!...(A little musical reference there for those playing along at home.)

Some experts suggest however, that if pushed too hard on taxes and other financial 'penalty' type restrictions, Chinese interest will invariably start to make its way to other, less heavily taxed housing markets in the world.

"Unfortunately tipping points are only really obvious in hindsight," says Jane Lu, Head of Australia for Chinese property website juwai.com.

"Australia runs the risk of overdoing taxes and killing the goose that lays the golden eggs. We don't think it passes the common-sense test to make it more difficult for foreign buyers to give their money to Australia. Foreign investment has provided huge benefits in terms of construction employment, new housing supply, and moderated price gains."

So how much is too much?

It's tricky to say what level of taxation is required to put a notable dampener on China's love affair with Australian residential real estate. Right now, we're still looking relatively reasonable in terms of our foreign buyer taxes, when compared to other countries.

Hong Kong's foreign buyer tax is now the equivalent of 37 per cent for the purchase price for property, while Vancouver introduced a 15 per cent sales tax last year.

"NSW has doubled taxes on foreign buyers as of July 1 to 8 per cent of the purchase price. This is in addition to a 1 per cent federal fee in international buyers and then stamp duty of around 4 per cent for a property costing $1 million," says Tevfik. "The foreign buyer is underwater 13 per cent before taking possession of her asset."

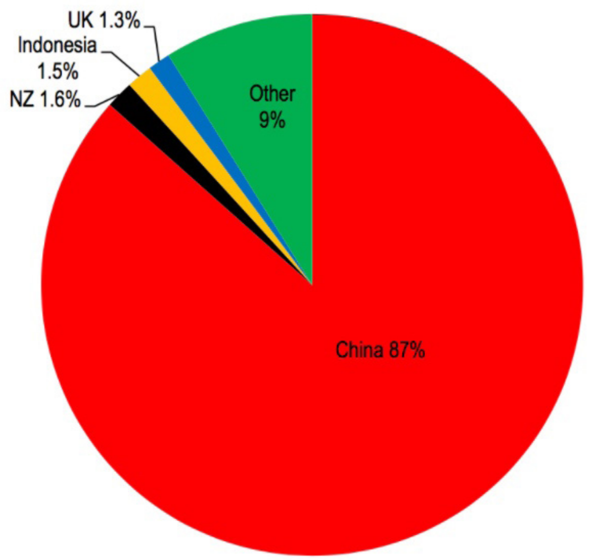
According to Tevfik, it's unlikely the most recent tax hike will be enough to dissuade future Chinese investors from snapping up a piece of the Harbour City for themselves however.

Again, great news for those who want to see housing values continue to grow, but somewhat alarming for potential first time buyers who are being pushed further afield from our major cities, in the search for affordable dwellings.

The degree of influence that international buyers (predominantly the Chinese) are having on our markets becomes apparent when you consider where most of their money is going. Data from the NSW Office of State Revenue and Credit Suisse indicates that foreign purchasers are snapping up a quarter of all new homes constructed in NSW, with a whopping 87 per cent of those overseas buyers originating from China.

Figure 6: The Chinese love Aussie property

Breakdown of foreign property buyers in NSW (% of value). January to June 2017.



Source: NSW Office of State Revenue, Credit Suisse

Meanwhile, 17 per cent of all new home sales were attributed to overseas investors in Victoria and 8 per cent in Queensland. All states that are, coincidentally, continuing to enjoy a winning streak with regard to strong performing housing values.

The good news, according to Credit Suisse, is this strong foreign buyer demand will help to shield our major cities from any type of market collapse into the future, despite consistently rising property prices.

"We agree property in our major cities is expensive," reasons Tevfik, "But we also understand much of the housing market is supported by foreign buying. Chinese wealth creation suggests we should expect more."

The Housing Affordability Issue That Won't Go Away

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While the prolonged five-year property boom we've recently experienced has started to ease slightly of late, public anxiety around record level house prices in our big cities is on the rise.

When asked to select the three most important issues facing their local community, Australians have traditionally voiced concerns around healthcare, cost of living, crime and unemployment. Lately however, housing affordability seems to be the number one source of rising stress levels among our population.

According to the latest Ipsos Issues Monitor, which asks respondents to select the three standout problems people feel are impacting the community, breaking into the housing markets in our big cities is creeping up the charts.

In NSW, housing affordability has topped the list of concerns for three quarters now; with close to half of respondents suggesting this is one of the most critical hurdles our nation has to overcome, compared to less than a third in 2014.

In Victoria, housing is second only to crime on the locals' list of concerns, with over a third of those surveyed from the garden state rating housing as one of the top challenges they face.

Problems for the people and the pollies

While housing affordability has been on the political agenda for the past couple of years, it's always seemed as though there's been more talk than real action to curb the growing crisis among Australia's younger generations in particular.

This mounting disquiet among the masses however, is changing the somewhat dismissive response we've seen from past political leaders. Back in 2003, on the tail end of our last great housing boom, John Howard openly scoffed at citizens voicing concerns over rising house prices, suggesting "most people feel more secure and better off because the value of their homes has gone up."

Now though, politicians are less flippant when it comes to addressing this long running 'thorn in the side' among the voting public.

"Among younger people there was a sense of not being able to move forward in life while many older people didn't know what their children are going to do about housing and felt they may struggle to help their children," reports Ipsos director Jessica Elgood.

Property values are fast becoming a political nightmare for state and federal leaders, who are increasingly being looked upon to implement pro-active, viable solutions to the conundrum.

Of course it's a bit of a catch 22, with many in public office heavily invested in residential real estate, not to mention the increased associated tax revenue from property sales, and the fact that bricks and mortar has become the foundation for our relatively stable economy in these continued, uncertain global economic times.

What's the solution?

That is the million-dollar question right now. But while various potential fixes have been tabled and regulatory intervention has made a bold attempt to dissuade investors pouring increasingly large sums of money into real estate assets, there still seems to be a lack of viable answers.

Currently the focus in Sydney is around planning and development, with projects such as 'Smart Cities' attempting to address the somewhat haphazard development that's historically occurred around infrastructure and housing in the Harbour City, in a bid to deal with an ever-increasing population placing increased pressure on local resources.

"Reshaping Greater Sydney as a metropolis of three cities – Eastern, Central and Western – will rebalance it, fostering jobs, improving housing affordability, easing congestion and enhancing our enviable natural environment across the entire region," says Chief Commissioner Lucy Turnbull.

As with most government initiatives however, many are questioning the plan's success before it's even started, given the amount of cooks in the kitchen and how enthusiastic the new government will be to continue down this path.

Short term thinking from politicians, based more on their own career trajectory than seeking appropriate solutions, is one of the ongoing issues preventing a genuine response to housing affordability and always has been.

Only time will tell if the 'powers that be' can reinstate a sense of calm and certainty around the future of younger generations realising their own Great Australian Dream of home ownership. For now, it seems there's still quite a ways to go.