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bricks and mortar

with John Mlikota

Our love affair with property has Australia as one of the highest levels of home ownership in the world. Real estate's attraction is based on the belief that bricks and mortar offer stable and permanent return. The very real characteristics of being able to drive past it, touch it, leads investors to a feeling of greater control of their investment.

Even when property is purchased through a listed trust, investors can still identify with office towers, shopping centres etc. Property definitely has a place in everyone's portfolio but the decision needs to put through a normal rigorous decision making process. Just like any other investment, property provides income and possible capital gain.

Real estate valuation is no different to valuing any other financial asset in that current prices are determined by the present value of future cash flows. Many people unfortunately believe that property is on an eternal upward trend and that you can never lose from bricks and mortar. It is this belief that has property investors happy to hold their asset through any market fluctuation.

Property prices are as volatile as shares, maybe even more so. However, as the individual cannot check the price of their real estate each day in the newspaper or the internet, they are ignorant to the volatility.

Moreover, the property investor is not bombarded with media reports and expert opinions on what their asset is worth. Between 1980 and 1987, real property prices fell by 29 per cent, property prices jumped by more than 73 per cent over a two-year period after the stock market crash of 1987 to June 1989, then took more than a 30 per cent fall. Over the following nine years, property prices increased by a total of 12 per cent. If you are looking to buy property with a less than five-year time horizon, this market is not the right time to make your move.

History shows the markets will show a more sustainable growth pattern, and in some areas, values may soften further. In this environment, short property play is not a wise option. The main short-term determinant of property prices is the movement of interest rates. The Reserve Bank

of Australia has expressed many times its desire to make housing more affordable.

If you've been renting for a while and you're trying to decide whether to buy, you need to consider a couple of issues. First, are you in a secure job? Not all properties or locations grow at the same rate, research is limited, and affordability is determined by free cash flow and budgets. There's no sense in buying an investment property if in a few years you need to upgrade your family home. Emotion: many investors fall in love with the features of a property, effectively skewing their ability to assess the value objectively, the same can be said for all investments. Undoubtedly property plays an important role in every portfolio. Therefore, careful analysis needs to be undertaken. ■

Independent Capital Advisers, Cairns
4031 4575
www.incapi.com.au

(John Mlikota is senior investment manager and director of Independent Capital Advisers)

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