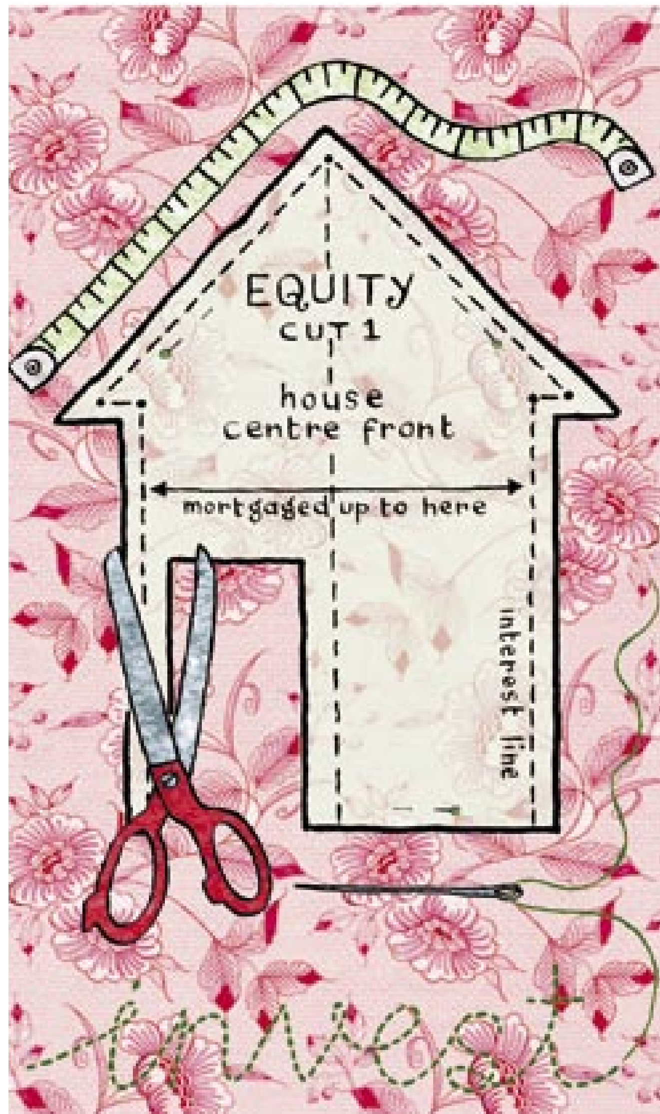
SAFE AS HOUSES

Pre-packaged property plans take care of everything – as long as everything goes according to plan. Susanna Stuart looks at the risks of no-risk investments

A **Next** reader visited me recently for a financial check up. She'd heard talk about property investment and wondered if she should jump on the bandwagon.

It's now common for investors to borrow heavily against their own home's equity to purchase a rental property. Pre-packaged deals – where everything is done for you from buying the property and managing it, to finding the tenant and collecting their rent – have evolved. It was one such deal that appealed to our reader.



Packages look good in theory. Borrow from the bank at 7.5 per cent and invest in an appreciating asset earning more. But there are pitfalls: unreasonably high fees and promised returns which can fail to materialise. Investors can be pushed to the limit by relying on tax breaks, generally including as expenses the deductibility of interest and depreciation on assets.

Ideally, all the costs of the investment property are covered by the rental. But this is not always the case. You may need to top up from your own money – which is hard if you've borrowed to the limit. Then, there are your tenants. What if they don't pay, or move on, leaving the house empty for weeks?

I advised our reader to look at an investment strategy to suit her own risk profile and circumstances – something tailored rather than off the shelf.

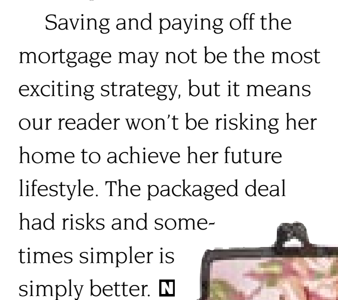
She was very risk-averse. I quickly worked out she didn't need to incur more borrowing risk as she has a great savings habit and is making inroads into reducing her existing mortgage.

She didn't have the time or desire to be involved with the hands-on side of property investment – chasing rent or dealing with tenants. But, even when managed by an agent, the rental is not guaranteed.

So what was the best strategy for her? Our reader had a tidy sum in the bank but it was only earning around five per cent. I suggested she take most of it out to reduce her mortgage (leaving a bit for emergencies). It makes no sense to be earning 3.3 per cent after tax and paying 7.5 per cent on her mortgage out of tax paid salary.

With the mortgage out of the way, she could start building her retirement fund. Already contributing a small monthly amount to company superannuation, she could increase this by the amount once spent on mortgage repayments. This will achieve her objective of having enough money for a modest retirement income. Later, she'll also be able to free up some capital from the property she now owns because she intends to move out of the city when she stops work.

Saving and paying off the mortgage may not be the most exciting strategy, but it means our reader won't be risking her home to achieve her future lifestyle. The packaged deal had risks and sometimes simpler is simply better. ◼



A world of difference

Country	Annual Growth		Last eight years
	To March 2004	To March 2005	Change 1997-2005
Hong Kong	17.4%	19.0%	-43%
New Zealand	23.3%	12.5%	66%
US	8.4%	12.5%	73%
Britain	16.9%	5.5%	154%
Australia	17.9%	0.4%	114%
Japan	-6.4%	-5.4%	-28%

From *The Economist Global House Price Indices* (June 16, 2005) on world trends.

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