

Special Edition

6th September 2011

Dear Owners and Investors,

Before I start, there are many of you on my list now. If you would like to be taken off this list, please let me know so I can remove your email. I send these emails out, in hope that just one of you will take the leap of faith and do something to change your financial position for when you retire. It is pretty awful being poor, but to be poor and old is even worse. Thank you to all of those that have written to say you enjoy my newsletters - oh and to my sister to say that I was much younger and skinnier in the photo I sent with Peros de Mer.

I was going to write an email to a client I am working with, but I thought I would write it to all of you to maybe prompt you to do something. Yesterday I was asked by another agent why we weren't buying in this market. The truth of the matter is that we now have 40 income producing properties and are at the end phase of our retirement package. We have no children to leave it to, so there is only so much that we could possibly need or want - the wants are far more expensive than the needs just ask Ramon.

Each person has a level of what they want as passive income when they retire.

As we saw in this link, just living comfortably is expensive.

<http://www.superannuation.asn.au/RS/default.aspx>

For a couple that owns their own home outright it will cost \$54,562 to retire comfortably. Many will be shaking their heads right now saying that isn't possible, but think about it - just because you are retired your food, electricity and general expenses won't stop or become cheaper. Gone are the days when you could pull into the service station and put in \$5 and it would last you for a few days! What is even scarier is that this figure probably won't allow you to buy a new car every 10 years or a cruise twice a year! Yes, people my real motivation is to get you investing so that you will be able to meet up for cocktails at the Skywalkers Bar in retirement.

Every investor has a different plan on how they will get this \$54,562 passive income. Ours was to buy as many properties as we could, buying well so that there was a good capital gain almost immediately. Our strategy changed in the last buying phase when we had a bigger equity base, we bought complexes outright that we could value add to. Once the market starts to turn, we have ear marked some properties that we will sell to reduce our debt that is the size of a small nation currently.

We have a duplex on Bruce Highway and it is one of the last blocks on the way into the city that hasn't been developed. It is already zoned commercial and is ideal to be knocked down and a purpose built office/showroom be built on it. We bought this for \$220K and to be totally honest we have done absolutely nothing to it since we bought it. The same tenants live there and it is as basic as you will ever get. They are more than happy because they get cheap rent - and every one is happy. At the moment it brings in \$11780 income (rent less council rates and insurance), no allowances has been made for the interest component. Our aim is to get \$800K for it when the market picks up. The interest for \$800K at 6.5% is \$52,000 per annum.

We will be losing the income from the duplex, but this will still put us \$40,220 per annum better off. We have only sold one property, lowered the debt and still have all the other ones producing income and increasing in capital value.

That paragraph was the very condensed version, and there are lots of other ifs and buts and I probably have explained it really badly but I hope you get the message.

There are a lot of people around that are not keen on buying in a strata block because of the insurance, and I tend to agree with them to a point. On the flip side, if you can only afford to buy in a strata environment then it is better to do this than to do nothing. There are still some very good options available, but I can't stress enough - you have to be able to hold it for a minimum of ten years. If you aren't going to make this commitment, then don't go into property - strata or otherwise.

I am going to pick out a few properties that we would look to invest in, and go into them in more detail.

<http://www.realestate.com.au/property-unit-qld-cairns-107589573>

This property is located in Scotsdale Apartments. It is a bedsit unit and it is approximately 42 square metres in size. The complex is very financial with over \$70K in the sinking fund and all works already done - I should know as I do all the budgets and get the work done! The insurance is still a big issue and it has seen an increase in the levies. The total body corporate levy for this unit is \$1449 per annum. The asking price is \$89K. At the peak of the market units like this were selling for \$115K. These are consistent renters, and even in the down turn we still rented them with minimal vacancies. The rents did go up to \$150 per week, and in the low they went as low as \$140. The rents have stabilised off at \$145 per week, but after the demand we had for the last one we will be trying to achieve \$150 for the next one that comes up.

Below is a very basic income and going calculation.

Rental Income @ \$145 per week = \$7540

Less

Council Rates = \$2100

Body Corporate = \$1449

Landlords Insurance = \$250

Management Fees = \$995

Interest \$89K x 7% = \$6230

Total Outgoings \$3484

This unit was constructed after 1987 and will be entitled to building allowance. I would guess that this would be between \$1000 - 1500 per annum. If you are paying a high tax rate, this could give you a tax benefit which could partially subsidise the outgoings. You will need to speak to your accountant about this and the implications.

Assuming you have no tax benefits what so ever, it will cost you \$67 per week to hold this property. If it does just go back up to the high of \$115K and you buy it at full price of \$89K, you could make a capital gain of \$26,000 very easily.

<http://www.realestate.com.au/property-unit-qld-manunda-107561226>

This unit is actually in the same complex but it is a two bedroom unit. The body corporate is essentially double that of the bedsit, but the council rates remain the same. This is a very big two bedroom unit, and they don't build them this big any more.

Instead they pretty them up and squish another one in, making them all much smaller. These went up as high as \$240K and have come crashing down in price. This one is up for sale at \$139K which is at prices we haven't seen for at least six years. The rents have remained fairly stable for the past four years, and we have consistently rented them out for \$200 per week fully furnished. When the pressure comes back onto the rentals, I believe we will see increases quickly.

We have had no real increases for the past three years, and it would not be difficult to see them go to \$220 per week as a minimum.

Rental Income @ \$200 per week = \$10,400

Less

Council Rates = \$2100

Body Corporate = \$2898

Landlords Insurance = \$250

Management Fees = \$1372

Interest \$139K x 7% = \$9730

Total Outgoings \$5950

This unit would also have building depreciation allowance and I would guess that it would be between \$1500 - \$2500 per annum. Again you will need to speak to your accountant about this.

Now assuming that you have absolutely no tax benefits, to hold this unit will cost you \$114 per week. If we assume that you pay \$139K and it just goes back up to the height of the market in 2007 of \$240K you could make a capital gain of \$101,000.

I have just picked out two in the body corporate environment for this exercise. There are some others, but I will be very picky about the ones I suggest - due to the rising body corporate insurance. Many of you will say that body corporate levies are not making it viable to invest in units. I agree - but only up to a certain point. What you must take into consideration is that the levies include all the exterior maintenance and upgrading.

The pool man comes once a week and does his thing, the lights come on every night and the power bill is paid for, the gardener comes once a fortnight and then every so often mulches the gardens and does an improvement, the boundary fences are replaced, the gutters are cleared out, the pathways are pressure cleaned, the building is repainted externally, there is money set aside for big projects like new gutters and a new roof - all you have to worry about is the inside of your unit. Most of these are built pretty tenant proof, and with a very small budget you can transform the inside of your unit. For an investor that doesn't live here, a well run body corporate is still a good way to look after your investment. You are all very fortunate that I am a control freak and look after all our complexes really well.

I am seeing a new duplex on Wednesday afternoon. It isn't on the internet so I can't send you the link. I did look at this from the outside and discounted it as there wasn't a lot of value adding ability. The price may have come down to a level where it is worth looking at again. The price may be under \$300K, and the location is good. If anyone would like more information on this, please let me know.

<http://www.realestate.com.au/property-house-qld-edmonton-107725541>

This is three bedroom, one bathroom house in Edmonton. It is listed at \$249K. We personally haven't invested in houses, but for some investors it works well. This is in suburbia, and it should be a fairly easy rental that will consistently bring you in rent. It won't be fantastic rent as there is so much competition out there. I would suggest it would rent for around \$260 per week, but when the market picks up this should go up. When you consider we rent out 2 bedroom duplexes for up to \$250 per week, there is room for the rent to go up.

Rental Income @ \$260 per week = \$13,520

Less

Council Rates = \$2400

Maintenance Allowance = \$2000

Landlords Insurance = \$1800

Management Fees = \$1784

Interest \$249K x 7% = \$17,430

Total Outgoings \$11,894

I have added in a maintenance allowance, so that we are comparing apples with apples. You can't say a house is better value than a unit, if you don't allow the same level of maintenance to be done. Assuming there is no tax benefit, or building depreciation allowance this will cost you \$228 per week.

The reason we have not gone down this path is that with the same cost per week we can carry 3 bedsit units. The purchase cost would be about the same, but our rental income would be \$435 per week. If one is empty, the other two are still bringing income. If we want to sell one off to downsize the debt we can - not so easy to chop off the garage and sell that.

<http://www.realestate.com.au/property-unitblock-qld-woree-107446983>

For this one you will need to have a lot more equity to be able to secure the lending. It is not normally a property that I would look at - mainly because of the price, and it certainly isn't the area that I would normally look at. Given the reduction in price, it certainly is worth an investigation. It is located on Sandown Close, Woree and this area is... lower socio economic based. This is apparently at the better end of the street. That is one thing even I forget, Cairns isn't bad suburbs generally - after all 90% of Manunda is fine. It is now streets or just complexes that you don't buy into.

This has the existing structure of 4 x 2 bedroom units built in the 1980's. They are only small two bedroom units but none the less two bedrooms. The agent tells me they are very tired, and very little has been done to them since they were built. The tenants that go into these properties are hard on them, and without seeing them I imagine they would be run down. They are constructed of besser block, so it wouldn't take much to bring them back up to a good standard. I would guess if no maintenance has been done internally, then the same could be said for the external. Until I do an inspection I can't say what it requires.

At the side of the property a 2 x 2 duplex has been built. This was done in 2005 so you would guess that nothing much needs to be done internally. The rental income is low in my opinion against other two bedroom units, but this may be the case for this area and the state they are in. Currently the older ones are achieving \$170 and the new ones are achieving \$195 per week. The property is still on one title, and I don't know what the possibility of strata titling them down the track is.

The asking price for all six units is \$697,000. This works out to be \$116K per two bedroom unit. When things were near the peak of the market in 2007, you honestly could not find a two bedroom unit for under \$200K - in any area or in any condition. If they just go back to an average price of \$200K you could potentially make a capital gain of \$503,000. To get to this level you would need to bring the whole block internally and externally up to a good standard, and with this the rents will increase. The owners are taking a loss on the price they paid in 2007.

Rental Income @ \$1070 per week = \$55,640

Less

Council Rates = \$9600

Maintenance Allowance = \$3000

Landlords Insurance = \$4000

Management Fees = \$7344

Interest \$697K x 7% = \$48,790

Total Outgoings \$17,094

There would be a fair amount of depreciation on the new building, but assuming there was none and no tax advantages, this would cost you \$328 per week - or \$54 per unit, which is even cheaper than the bedsit. There are things you could do to improve this situation, increasing the rents by just \$10 per week per unit would give you an extra gross income of \$3120.

For this next exercise I will assume that a couple working in the mines both earning \$120K per annum. If they purchased this property, or one equivalent, the actual cash that it will cost them will be \$17,094. I will make a guess that there is depreciation of \$4000 over the six units. I am being conservative. This would put their costs at \$21,094.

Using the simple tax calculator on the ATO website, a person earning \$120K will be paying \$32,350 in tax. If we give each person half of the \$21,094 their taxable income will reduce to \$109,453 and their tax will be \$28,447 - or \$3,903 less in tax. As a couple they would save \$7,806 a year in tax. Again this is using very basic calculations you must check with your accountant before making any investment.

Depending on the state of the building, this may suit an investor that is hands on, and lives locally. This complex could also fit into a couple of categories - it could be the cash cow or it could be the debt reducer - it will depend on your investment plan.

I received an email the other day about the a new book. The link is <http://www.prosolution.com.au/books/sbh.htm> it is a must for you to read so you can understand the lending side of investing. You can buy this directly, or you can join our book club and receive it. The fee is \$50 to be able to swap the book within our collection as often as you like. You get to keep the book as long as you like and then when you want a new one just mail it back with \$5 to cover postage.

If you are interested in any of the above properties, or something else you may have seen and would like our opinion, please give me a call on 0412 828 842 or email me.

Hope all is well in your world.

Linda