

Leverage Your Property Investments Correctly

Despite successive interest rate hikes, and the prospect of more to come, property remains an attractive investment option, particularly if it is leveraged correctly

This is according to Jane Downing, head of New Business at BoE Private Clients. She says that the dramatic increase in property prices, which has pushed up capital values of real estate investments over time, has created large surplus value in many property investments and that this can be leveraged to finance 100% of the purchase price of any new additional properties.

“Innovative finance for individual investors – either a single facility secured by a range of properties or a number of separate loans secured by one or two properties provides flexibility and ensures borrowings that are most tax effective.

“Over the longer term, residential and commercial property still offers relatively attractive returns. This is particularly true of commercial property, but even with residential property a real return on investment can be achieved, not least in view of increasing tourism and growing demand in the run up to the 2010 soccer World Cup,” says Downing.

She notes, however, that rental yields – especially of residential investments – have been poor and have definitely not kept up with the very rapid appreciation in residential property prices in some of the wealthier suburbs in South Africa.

“Residential rental yields have hovered around 2% so it is essential for investors to enhance their returns further by taking advantage of the deductibility of interest incurred when gearing property investments,” she says.

Downing notes that investors look to property to provide both capital growth and a sustainable and increasing source of income, with a relatively high degree of capital protection compared to general equities.

She point out, however, that it is important to appreciate the risks inherent in the particular property investment, which need to be managed appropriately.

“When financing residential investment properties on these lower yields, it is necessary to ensure that the investor has a reliable source of income, over and above the rental from the property being purchased, to subsidise the installments on the loan.

“This is equally the case when it comes to the financing of commercial property portfolios, where engaging the services of a professional can have many benefits, including the security of having its valuers conduct thorough assessments of the property. A professional will review leases, assess tenants and compare rentals to market rates, and will also consider the ease with which the property can be re-let, should this become necessary.”

Downing says that Property Unit Trusts (PUTs) and Property Loan Stocks (PLSs) can be used as an alternative to direct investment in commercial property. The advantages of investing in listed property include the low entry and exit costs (no transfer duty / attorneys fees) as well as the high degree of liquidity and therefore the ability to turn the investment into cash within a short period of time. A further advantage is that the investor obtains exposure to a geographically diversified portfolio of office, retail and industrial properties, which are actively managed, without the hassle of being a landlord.

“Because these investments are priced constantly by the market, they tend to behave more like equities (than direct investments in commercial properties) and therefore the prices are typically more volatile on a day to day basis. However, over the longer term, the Net Asset Values will tend to mirror that of commercial property sector – and hopefully outperform it,” concludes Downing.