Australian Property Investor - Melbourne

PROPERTY INVESTMENT ANALYSIS (DESCRIPTIVE)

07-May-2012

Prepared for:
Consultant:
Property: 1 Somewhere St, Elwood
Description: 1 Bedroom Apartment

SUMMARY

Assumptions		Projected results over	10 yrs
Property value	$400,000	Property value	$716,339
Investment	$40,000	Equity	$346,688
Gross yield	4.84%	After-tax return /yr	22.79%
Net yield	3.68%	Net present value	$214,698
Growth rate	6.00%	**IF SOLD**	
Inflation rate	3.00%	Selling costs & CGT	$97,490
Interest rate	5.99%	Equity	$249,198
Taxable income	$65,000	After-tax return /yr	18.72%

COMPUTER PROJECTIONS

Investment Analysis		Projections over 10 years				
End of year	2012	1yr	2yr	3yr	5yr	10yr
Property value	$400,000	424,000	449,440	476,406	535,290	716,339
Purchase costs	$4,800					
Investments	$40,000					
Loan amount	$369,651	369,651	369,651	369,651	369,651	369,651
Equity	$30,349	54,349	79,789	106,755	165,639	346,688
Capital growth rate	6.00%	6.00%	6.00%	6.00%	6.00%	6.00%
Inflation rate (CPI)	3.00%	3.00%	3.00%	3.00%	3.00%	3.00%
Gross rent /week	$380	19,365	19,946	20,544	21,795	25,267
Cash deductions						
Interest (I/O)	5.99%	22,142	22,142	22,142	22,142	22,142
Rental expenses	23.41%	4,625	4,764	4,907	5,206	6,035
Pre-tax cash flow	$-40,000	-7,402	-6,960	-6,505	-5,552	-2,910
Non-cash deductions						
Deprec.of building	2.50%	5,000	5,000	5,000	5,000	5,000
Deprec.of fittings	$24,000	3,850	5,043	3,487	1,795	526
Loan costs	$4,851	970	970	970	970	
Total deductions		36,587	37,919	36,506	35,113	33,703
Tax credit (single)	$65,000	6,189	6,466	5,688	4,568	3,037
After-tax cash flow	$-40,000	-1,213	-494	-817	-984	127
Rate of return (IRR)	22.79%	Your cost /(income) per week				
Pre-tax equivalent	33.52%	23	10	16	19	(2)

Disclaimer: Note that the computer projections listed above simply illustrate the outcome calculated from the input values and the assumptions contained in the model. Hence the figures can be varied as required and are in no way intended to be a guarantee of future performance. Although the information is provided in good faith, it is also given on the basis that no person using the information, in whole or in part, shall have any claim against Australian Property Investor - Melbourne, its servants, employees or consultants..

Detailed Notes on Spreadsheet Items

PROPERTY VALUE

The property (or market) value refers to how much the property is worth (i.e. how much you could sell it for). Its book value, on the other hand, refers to how much you have paid for it plus the cost of any immediate renovations.

Property price:	400,000
Renovation costs:	0
Total book value:	400,000
Property market value:	**$400,000**

PURCHASE COSTS

These include your solicitor's conveyancing fees and, where applicable, State Government stamp duty charges. In Australia, stamp duty varies from State to State and is a function of purchase price whereas, in New Zealand, it has been abolished on all property transfers since May 1999. Conveyancing costs may also be dependent on purchase price and may be negotiable. In some States of Australia (e.g. A.C.T.), purchase costs are tax deductible in the first year of the investment, though normally they will only be taken into account in Capital Gains Tax calculations in the year of sale.

Conveyancing costs:	2,000
Stamp duty:	2,800
Total Purchase costs:	**$4,800**

INVESTMENT & LOAN

Your initial investment is usually just the total of all monies outlayed at the time of purchase. These may include contributions toward any, or all, of the costs listed below. The remainder will largely determine the size of the loan. If you have sufficient equity in other property, it is possible to outlay nothing, and actually borrow the lot (i.e. the purchase price, purchase costs, loan costs, any renovation costs, and even additional monies to cover such things as fittings). If you are modelling an investment from some point in time after purchase (e.g. to assess the return on major renovations), your investment might also include the equity you already have built up in the property.

	Investments	**Loan**	**Total Cost**
Property costs:	40,000	360,000	400,000
Renovation costs:	0	0	0
Purchase costs:	0	4,800	4,800
Furniture costs:	0	0	0
Loan costs:	0	4,851	4,851
Totals:	**$40,000**	**$369,651**	**$409,651**

CAPITAL GROWTH & INFLATION RATES

Rate of capital growth is your anticipated annual compound rate of increase of the property value. It will undoubtedly vary substantially over the short term, but over the longer term (10 years or more), it has generally been about 2 to 3% above the rate of inflation.

Average rate of inflation (%):	3.00
Average rate of capital growth (%):	6.00

EQUITY

The equity is the difference between the property value and the loan. The equity increases in line with the increasing property value in the case of an interest-only loan. For a principal & interest loan, it also increases with the decrease in the debt.

Projected values over	**5 yrs**	**10 yrs**	**15 yrs**	**20 yrs**
Property value	535,290	716,339	958,623	1.283m
Loan	369,651	369,651	369,651	369,651
EQUITY	**$165,639**	**$346,688**	**$588,972**	**$913,203**
Approximate costs if sold......				
Capital Gains Tax	29,693	77,422	141,630	224,203
Solicitor's fees	2,676	3,582	4,793	6,414
Sales commission	12,502	16,485	21,816	28,949
EQUITY (after sale)	**$120,767**	**$249,198**	**$420,734**	**$653,637**

INTEREST COSTS & TYPE OF LOAN

The type of loan can be either interest-only and/or principal & interest. Repayments for interest-only loans, as the title suggests, consist of interest only. Repayments for principal & interest loans include a component of the principal. Interest-only loans are usually of a shorter term (e.g. 3 to 5 years) at which time they are usually rolled-over.

Loan type:	I/O Yrs 1-40
Interest rate (yr 1) (%)	5.99
Loan:	$369,651
Loan costs (written off over 5 yrs):	$4,851
Monthly payment:	$1,845
Annual payment:	**$22,142**

RENT

The potential annual rent is simply the rent per week times 52. The actual annual rent must account for any period that the property is vacant. Annual rents are assumed to increase in line with inflation.

Rent per week:	380
Potential annual rent:	19,760
Vacancy rate (%):	2.00
Actual annual rent:	**$19,365**

ANNUAL RENTAL EXPENSES

These are all the real operating costs associated with the investment property with the exception of loan interest payments. The first cell of the spreadsheet represents the expenses expressed as a percentage of the potential annual rent. As a guide, expenses could vary anywhere from 13% to 30%, depending on the maintenance and whether a professional property management agent is used. For holiday letting, with higher vacancies, the percentage can be more than 50%.

Normal Expenses:	
Agent's commission (7.70%):	1,491
Letting fees:	380
Rates:	1,200
Insurance:	254
Body corporate:	1,300
Special expenses:	0
Total expenses:	**$4,625**
Normal expenses as % of annual rent (%):	23.41
Net yield or Capitalisation rate (%):	3.68

PRE-TAX CASH FLOW

These are all of the monies that flow out of your pocket before tax is taken into account. Normally, it would represent the gross annual rent less interest and rental expenses. This will vary if interest or expenses are capitalised or rents used directly to reduce the loan.

Year		**1yr**	**2yr**	**3yr**	**5yr**	**10yr**
Rent		19,365	19,946	20,544	21,795	25,267
Cash invested	40,000	0	0	0	0	0
Principal payments		0	0	0	0	0
Interest		22,142	22,142	22,142	22,142	22,142
Expenses		4,625	4,764	4,907	5,206	6,035
Pre-tax cash flow	**$-40,000**	**$-7,402**	**$-6,960**	**$-6,505**	**$-5,552**	**$-2,910**

DEPRECIATION ON THE BUILDING

This represents the capital allowance on the construction costs.

Property value:	$400,000
Construction costs:	$200,000
Depreciation allowance rate (%):	2.50
Depreciation allowance:	**$5,000**

DEPRECIATION OF FITTINGS (diminishing value method)

Item	**Value**	**Effective Life (yrs)**	**Depreciation**
General fittings	12,000	15.00	1,600
Low-value pool	12,000	4.00	2,250
Total	**$24,000**		**$3,850**

LOAN COSTS

In Australia, the loan costs are written off over the term of the loan (or five years, whichever is the lesser).

Establishment fees (0.50% of loan):	1,848
Mortgage insurance (0.32% of loan):	1,183
Mortgagee's solicitor's fees:	1,000
Valuation fees:	300
Registration of mortgage:	230
Registration of title:	115
Search fees:	175
Total loan costs:	**$4,851**

TOTAL TAX DEDUCTIONS (Cash & Non-Cash Deductions)

These include both "cash" (e.g. interest, rental expenses) and "non-cash" (e.g. depreciation) deductions.

Year	**1yr**	**2yr**	**3yr**	**5yr**	**10yr**
Interest	22,142	22,142	22,142	22,142	22,142
Expenses	4,625	4,764	4,907	5,206	6,035
Deprec.-building	5,000	5,000	5,000	5,000	5,000
Deprec.-fittings	3,850	5,043	3,487	1,795	526
Loan costs	970	970	970	970	0
Total deductions	**$36,587**	**$37,919**	**$36,506**	**$35,113**	**$33,703**

TAX CREDITS & AFTER-TAX CASH FLOW

The after-tax cash flows are all of the monies that flow in or out of your pocket AFTER tax is taken into account. They represent the PRE-tax cash flow LESS any tax credits (or tax refunds). In this analysis, it is assumed that the investor has obtained a tax variation from the Taxation Office and thus the tax refunds are credited for the same year in which they are based.

Year	**2012**	**1yr**	**2yr**	**3yr**	**5yr**	**10yr**
Pre-tax cash flow	-40,000	-7,402	-6,960	-6,505	-5,552	-2,910
Tax credits		6,189	6,466	5,688	4,568	3,037
After-tax cash	-40,000	-1,213	-494	-817	-984	127
Cost /(income) per week		**23**	**10**	**16**	**19**	**(2)**

INTERNAL RATE OF RETURN

The internal rate of return (IRR) is the method of calculating the return on a series of cash flows where the time factor is taken into account. To understand it, think of the money you are outlaying on your investment property as being deposited in a bank account, with interest added each year. In this case the "deposits" are represented by the after-tax cash flows

Year	**2012**	**1yr**	**2yr**	**3yr**	**5yr**	**10yr**
After-tax cash flow	$-40,000	$-1,213	$-494	$-817	$-984	$127
Equity						$346,688

The total amount in your "account" (including interest) at the end of the period is the equity ($346,688) in the investment property. The IRR (22.79%) represents the effective "interest rate" that you have received, but with one important difference - because the interest remains in the property, it is not taxed. To receive an equivalent return from bank interest, you need to get 33.52% before tax.

If the property were to be sold at the end of the period, the after-sale equity would be reduced to $249,198 after taking account of selling costs and capital gains tax and the IRR after the sale would be 18.72%.

TAX BENEFITS

These are shown below for the given taxable incomes and are based on the specified tax scale.

Number of properties: 1

	Investor	**Partner**	**Total**
Ownership: single name	100.00%	0.00%	100%
Present taxable income:	65,000	30,000	95,000
Rental income:	19,365	0	19,365
Total income:	84,365	30,000	114,365
Rental deductions:	36,587	0	36,587
New taxable income:	47,777	30,000	77,777
Present tax:	14,000	2,550	16,550
New tax:	7,811	2,550	10,361
Tax saving:	**$6,189**	**$0**	**$6,189**

INVESTMENT CAPACITY

Buying 1 such properties (registered in single name), and taking into account current net incomes and living expenses as shown, the difference between total income and total committed expenses in the first year would be $10,721. Total initial outlay would be $40,000.

Number of Properties: 1		Registered: single name
Ownership:	Investor (100.00%)	Partner (0.00%)

Income

Present net income	
Current assessable income (investor):	65,000
Current assessable income (partner):	30,000
Total net income:	95,000
New rental income:	19,365
Total income:	**$114,365**

Expenses

New tax (investor):	7,811
New tax (partner):	2,550
Rental expenses:	4,625
Investment loan expenses:	22,142
Home loan payments:	35,565
Living expenses:	30,950
Total expenses:	**$103,643**
Net surplus (first year of investment):	**$10,721**
Total initial outlay required:	$40,000