THE FUTURE *of*

PROPERTY INVESTING IN AUSTRALIA



DON'T RISK BUYING REAL ESTATE BEFORE YOU READ THIS BOOK!

SAM SAGGERS

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Understanding that it has taken Australia 228 years since European settlement to reach a population of 24 million people but it will only take a further 35 years to add another 16 million people is something that is both exciting and somewhat disturbing for property investors.

Acknowledgements

Any book on a subject as complex as property investing depends extensively on borrowed thoughts. While the interpretations I give here are my own, I have also relied on the numerous contributions from members of my profession who have, over the years, provided information for property investors. I have not named any of the many people who have enlarged the understanding of property investing in our small fraternity, and you can be sure that in their next books they will not name me. Over the years, I have gained much knowledge from my peers and they are truly an inspiration.

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PREFACE

MY PROPERTY STORY

My name is Sam Billy-Budd Saggers … and yes, that's my real middle name, but that's a story for another time. I own one of Australia's largest property investment firms, Positive Real Estate, that will celebrate its 15th year in operation in 2017. I am also the Head of Projects at Australia's oldest real estate firm Richardson and Wrench, which is over 158 years old. I employ nearly one hundred full-time staff nationwide, and have teams in New Zealand and the Philippines. For more than 20 years I have been personally involved in brokering several billion dollars in real estate deals, many of them multi-award-winning properties.

I enjoy helping others with real estate and have done this through books and education programs. I am a contributing author to *Think and Grow Rich in Property* by Stuart Zadel, and to date have written three books for property investors: *How to Be in Debt For Millions and Be Happy About It, How to be a Part Time Property Millionaire* and *Property Success in 7 Lessons.* My works are the realistic result of 22 years in the real estate industry, adapting, modifying, testing and applying the techniques of buying real estate well.

Where it all began

I am very much a property investor first before a realtor or entrepreneur, and today I'm still buying property and making my own investments, which leads me to address you as a successful property investor rather than a real estate agent. I come to you with well over $20 million in assets from property, businesses and equities – property being my number one choice of investment! But I wasn't born rich; I came from a lower middle-class world with not much money at all. Property has made me wealthy because, thankfully, I learnt about real estate from a very young age.

The house I grew up in was small. My family enjoyed living there, yet we were seen as the neighbourhood pariahs. We were poor by the local standards. Our house was gloomy, old and dark, with a kind of Alice in Wonderland feel. We had one bathroom, which was pretty basic, and our kitchen and living areas were in their original 1940s condition. This was in the 1980s. But to me it was home. My siblings and I would often invite friends over for the weekend, and my father would entertain us all with his antics and my mother would treat everyone to good food. Yet none of the kids would ever visit more than once. On arrival to collect their kids, the parents would look at our house and stare disapprovingly. The mothers would give my mother a fake gesture of approval and rush off, never to allow their children back into our basic home again. It was then I realised that poor people are seen very differently in the eyes of the wealthy.

My father bought the house a decade before I was born. He explained to me that it was the worst house in the best neighbourhood, and that turned out to be a fantastic real estate principle for becoming rich – I can vouch for that. It was a poor home surrounded by the very best properties you can imagine. My parents had made a decision to buy a very inexpensive property in Hunters Hill, one of Sydney's most exclusive areas. They bought there for many reasons, but mainly they wanted to give their children the opportunity to grow

up around wealthy kids. At the time Hunters Hill was full of millionaires and even some billionaires.

We certainly did not fall into the millionaire, let alone billionaire, category. My dad and mum worked seven days a week to own that home. My father, never to shy away from who we were, had a wagon full of market goods, from baskets to fridge magnets, with which he would proudly and loudly drive through the suburb and to the local markets, selling his goods. It was easy for everyone to know the Saggers family as the local market folk. Our car was a Datsun bomb, and, at the very least, the next poorest person in the area drove an Audi instead of a Mercedes. We were certainly different and stood out as misfits; we made rich people feel uncomfortable. But my parents seemed proud of their bravery. As for the children of the Saggers clan, we grew up very uneasy and rather awkward. We were poor kids in a rich world!

The three sons of retailers

The first public school I went to was Hunters Hill Public School, which many of the local rich kids also attended. Naturally, children, without prejudice, make friends easily, and many wealthy kids began to play with me. My two best friends didn't even know they were rich, and neither did I – at first. We would play in the neighbourhood together without the slightest interest in each other's social status. I really only began to comprehend their vast wealth in comparison to mine the first time I visited their homes, particularly Ted's. Theodore was the heir to Grace Brothers, now known as Myer. His house, known as *Clifton*, resembled a kingdom, like Buckingham Palace. Though Ted has long since left this home, it remains special today. If you've watched any episodes of the first three seasons of the Australian *The Bachelor* you would have seen Ted's old home – it's the mansion used on the show. We would play at Ted's house for hours on end. He and his older brother Nick even taught me tennis on their very own tennis court, a game I still play today.

Sean, my other best friend, was the heir to Franklins supermarket chain. Ted and Sean were next-door neighbours, and I lived up the street in a house that was barely standing. We considered ourselves the three sons of retailers: Ted was Myer, Sean was Franklins, and I was the market stallholder kid. We became great friends and had a natural bond beyond something as trivial as money.

Both Sean's and Ted's parents had significant real estate holdings. As we spent so much time together, I could see that was a major reason why they were so successful. They had properties just about everywhere we went. I knew I wanted to be like that.

In my early life I learned to love property from these people, who have mentored me from being poor to being wealthy. Sean, Ted and I are still friends, lifelong friends. Sean has gone on to become a billionaire, listed in *BRW* 200 Richest Australians, and I have gone on to enjoy multi-millionaire status. I am proud to say we have both made our fortunes by investing in real estate, something Sean's dad in particular exposed us both to at a very young age.

My first business venture

As for business, I successfully own and operate many enterprises, from stand-up paddleboard companies to finance firms. I began my first business very young. My father has been importing goods from Asia for as long as I can remember, and I grew up surrounded by amazing and novel merchandise. I was always eager to try selling it myself. At the age of 10, I asked my father if I could buy some water balloons that he had imported and sell them on to friends. He agreed, and my first transaction as a businessperson was made. I paid the large sum of $20 from my pocket money for 500 water balloons. I took the water balloons to school and tried to sell them. Over the first few days I learnt that the balloons were not going to sell since the market was unable to pay 50¢ for a balloon. Kids at the primary

school I went to just didn't have much money; they brought packed lunches with them, and didn't have disposable income to spend on water balloons. So, in the end I was stuck with hundreds of balloons, and after a few weeks of trying I gave up out of frustration.

Naturally, I went back to my father for a refund. He had long since noticed that my untrained eye would lead me into trouble. He refused to refund my purchase, saying that it was 'the law of consequence', and he went on to say, 'Success is a game, for the more you re-try things, the better you get'. This is something I agree with to this very day! Dad encouraged me to try again, and to figure out a way for the students to have money to spend this time.

I'm sure he meant well, but perhaps what I did next was a little cheeky. I learned that the school was having a fundraiser for *The Pirates of Penzance* play they were running, and, on a particular day, students were asked to bring $1 each to buy a pirate eye-patch so the entire school could act like pirates. On that day I entered the school with over 400 water balloons. I sold 300 in two hours, one to just about every student, except this time I sold them for $1 each. Just as I expected, my product was a lot more enticing for my market, and not surprisingly I outsold the pirate patch. Once the headmaster found out, the story took a turn for the worse … but that's a tale for another day.

Despite my slightly inappropriate actions, I learnt a valuable lesson from my water balloon venture that I still live by. I discovered that you learn from failures, and the more times you do something, the better you get. This applies to most things in life, especially real estate. You will never come across a person who is a 'natural property investor' or a 'born property expert'. Becoming a successful property investor requires the same commitment that learning a trade does; it takes time and persistence.

My first property investment

When I started buying property I got it very wrong; my first property was a dud, to say the least.

I was green and naive when I bought my first property. My honest belief was that all I had to do was buy property and watch its value increase. I had seen friends such as Sean make money through the process, and knew the pride it gave him to know his assets were growing. I knew I could do the same, so I raised the funds I needed to invest.

I chose my first property because it overlooked a park, and it was the most I could get for my money in the area at the time. I lived and worked in the same neighbourhood, so I thought it was the right place to buy – but of course I was totally wrong. We all pay for our education in one way or another, and mine cost me my life savings of $30,000. I had to sell my first property within 18 months of buying it. The property was a very bad choice and not a smart investment at all. I sold it because it was falling apart, the repairs were eating my back pocket and it was in a terrible location. It really was the wrong choice, but I have persevered and have since gone on to make some better choices. It was a costly experience, but it led me to where I am today.

And so today ...

My current property portfolio is worth over $10 million and consists of many different properties across Australia and New Zealand. I know people usually like to talk about their portfolio in terms of how many properties they own, but I think market exposure is far more important. At 41 years old I have 21 properties. Not too bad considering I started with $30,000 – and lost that.

The reality is anyone can achieve this too if they choose. I have a friend earning $70,000 a year who has bought a few properties.

Within a few years she ended up buying her dream home and stopped working, replacing her income with her own investments. Today, she works her properties hard through short-term rental ideas and lives off the cash flow. She was determined and keen, and that's what it takes, along with some knowledge and some smarts to get the job done and get out of the rat race. I have also seen others on $200,000 a year blow their money on silly things and not challenge themselves, and still, to this day, they have no assets for their future. The approach of taking money and time for granted is fraught with danger. People need to get on with creating a plan, as life is always full of surprises.

Being wealthy for me is more about the journey than the result; I've had a wonderful time as I have become wealthy. I've done things that at one time I could only dream about, from funding and building nine school projects across the developing world to helping rebuild communities in Vanuatu after Cyclone Pam devastated the region, to more personal challenges such as taking care of friends who are less wealthy in times of need. It is my belief that money was created to be shared, particularly with those you love – but you have to find it first!

Investing is more important now than ever

What is daunting for many Australians is that the government has recently started to increase the age at which people can access the age pension, with the aim of eventually increasing it to 70 years of age. People just can't afford to retire at 55 or younger any longer, which is a shame as we all know that there is more to give to the world than just work. So learning to invest and creating a great real estate wealth plan is more important than ever. It's not about how much you earn, it's about taking some action so you can live the life you want. I will retire in five years from property. Well, I'm on course to, but maybe the enjoyment of my life's work will keep me involved in property and investment longer than I need to, but that will be

my choice. I'm now in charge of my own economics. The big, harsh question is … are you?

Every day for the last 22 years of my life I have woken up with my first thought being about how to win at property. I would like to share with you my proven techniques and offer simple and practical ideas that will propel you along the path to financial freedom. One of the greatest things you will discover about investing in real estate is that you can do it part time while you go about your normal life and enjoy whatever else makes you happy! You will not need to dramatically change your existing busy life, hobbies or commitments.

My aim in writing this book is to provide the best advice to my readers and have you feel safe in a turbulent property market. My intent is to permanently change the way you approach buying real estate in Australia.

I wish you all the best with your property investing.

Sam Saggers
Sydney, February 2017

INTRODUCTION

A NEW ERA OF PROPERTY INVESTING IS HERE

We live in a world that is constantly changing and expanding. Ideas evolve and spread quickly today, particularly when it comes to technological developments. And it is important to remember that in property, as in all aspects of life, past periods are not necessarily the same as the time ahead of you, so developing new ideas is essential for getting – and staying – ahead.

The investing challenges we all face today

Today we have to invest in a business landscape that moves daily, but it is also one in which people are trying to harm us financially. A very challenging paradigm indeed! It's easy to see why doubt often drives people into a state of paralysis, particularly when we talk about investing. In fact, people make careers within the property industry based on other people's lack of knowledge and skill. The real estate industry is rife with agents who prey on ill-informed buyers and sellers.

Another conundrum for investors is that there is a lack of skill in the property industry. Today you may have to buy property from an agent who has done only a short course to work in real estate. Scary! And making things even more volatile: people take 'advice' from property agents who don't even own real estate!

For these reasons (and more), understanding real estate has never been more important. Successfully investing in real estate is about understanding the fundamentals of a secure property. In this book I will share with you simple, proven ideas and techniques that will propel you along the path of prosperity that many other investors have discovered in recent years. Reading is one of the most important forms of self-education, and by absorbing the things you read here you will increase your chances of buying the right property in this rapidly changing market.

The changing landscape

The real estate world is constantly evolving. We live in the age of disruption, and real estate is not immune to this. New disruptors affecting the sector can make it harder for a property investor to know what to focus on and what approach is right. I will delve into these disruptors and how to crack the code of investing beyond today, to capitalise on the rise of a new real estate era. This book will share the importance of understanding the future of real estate. With the new information you will gain you will have the instruments to create your own property wealth and be responsible for your own prosperous life and, therefore, be accountable to the most important person in your life: yourself. Sounding knowledgeable is easy but persisting and delivering is a lot harder.

It's my belief that real estate investors need to look at property very differently now because the past 50 years of property insights are virtually obsolete. This book is looking ahead into a new era of property. Property investors need to keep up with the ever-changing

marketplace, and I will educate you about the way you need to view property now and when investing in the future.

In the end, everyone wants a quality experience in property and to make the right investment choices. One of these choices is holding on to property over the long term, which I consider to be vital for successful investing. Property can change your life for the better over three, five or ten years, or even more. There is a common preference today in the marketplace to rely on short-term, less consistent indicators, from daily media grabs to weekly sales stats, and react accordingly, rather than thinking with a long-term view and sticking to a big-picture plan.

In this book I want to help simplify property, because the idea of owning property investments can certainly stifle you if you let it. Property is not like a shirt that you buy from a department store, take home, realise you dislike, and so you return it to the store! Once you buy a property you have made a large investment, and if it turns out you chose poorly you can be stuck with it for quite a while.

In the last few years we have seen big property price growth rates in places such as Sydney and Melbourne, which have been disrupted by intense overseas investment. This has made a lot of money for those who bought property well before the boom, but has halted progress for those yet to invest. Foreign investors stormed into the Australian market with an almost reckless appetite to buy, with locals putting up little resistance to this influx as the overpowering global dollar changes our property landscape forever.

There is a mentality in Australia that makes it hard for those in the lower and middle wealth brackets – and those who are sleeping their lives away – to paddle upstream. They are very much being washed away with the outgoing tide, as property values climb and jobs disappear. This is all occurring against a backdrop of constant innovation and disruption that both excites and frightens.

There are positive and negative consequences to real estate globalisation, and there is no question that the industry itself should be more accountable to change and how to teach change to consumers. Banks and government should also be more answerable; they need to work more closely together as often both have counterproductive and opposing policies that cause unnecessary tension in the property market.

As a property investor and a veteran in the industry, I do my best to be a futurist and a guide for people. This book is largely driven by my belief that everything we have ever known about real estate is due for a major overhaul. If you don't own real estate yet that may just be a blessing in itself as it is often easier to learn than unlearn.

Today, investors are exposed to over-exploited suburbs, high prices, and a lack of property knowledge, which together are a wrecking ball for the unsuspecting buyer. Even harder to understand is the changing nature of Australia itself – and it *is* changing! What will the future of investment be and what will Australia become? All great questions that we will explore together.

These days it's vital to understand that there is a new normal within the property marketplace that is very different to the past. Being an investor today takes more than guts, and, more than ever, people will lose money in real estate if they don't learn how to invest properly. It saddens me to say this but this book contains some home truths for Australians. The reality is the Aussie dream is hard to find these days. You can't just stumble across it; it requires planning and guile.

Success is sometimes hard to determine. What is success in life? Even the most altruistic people I know realise that if you want happy relationships, to live a productive life contributing to the wellbeing of others less fortunate than you, and to look after and provide opportunities for your family, you can do that by actually becoming wealthy yourself first. So when I talk about prosperity, I don't just mean it in a 'dollars and cents' sense, I mean across-the-board wealth.

This book is written in two parts. The first is a comprehensive overview of the terrain and environment that property investors face in this very disruptive world. In part II I then go on to explain the formula to becoming a great investor.

PART I

THE PROPERTY INVESTMENT LANDSCAPE

CHAPTER 1

OUR CHANGING WORLD

Oscar Wilde once famously said, 'Give a man a mask and he will tell you the truth'. Perhaps this book is my mask. Written words are my best form of expression, and sometimes the truth is hard to hear but easier to read.

Australia today

The real estate market has changed forever. In fact, everything you may have learned about real estate from past cycles is becoming redundant. The facts today about Australian real estate are that it is exposed to world economics in such a way that it is now very turbulent. What is current and real today is:

- there is a lot of supply of property
- many global investors want to invest here
- a lot of overpricing is catching many people out.

As such, there are some serious new rules to understand and apply so you can make sure you control your own economic wellbeing.

Knowing your terrain

To comprehend why we need to rethink real estate, we need to first understand the landscape we are buying real estate in today. The famous book *The Art of War* – revered by many for its insights that can be applied to business and critical thinking – has various learnings that are useful and accurate. One of them is: 'Know your terrain'. This lesson applies to property investors, for an investor must know their environment and understand what is coming next. The world and real estate metrics are rapidly changing, and this is catching out uninformed people. Our economy is moving from a fast-growing resource-rich 'mining boom' economy to the next plan, 'the knowledge boom' economy. There are many lessons to learn, and property will link to this new economy.

This is critical: the mining boom created a rise in real wages across the country as less skilled workers became better paid, not only at the coalface, where driving a heavy vehicle meant a wage of well over six figures, but also in the offices, where wages grew off the back of the nation's riches in mining. A person at the reception desk went from earning $35,000 per annum to $55,000 because of the labor shortage that required workers in the resource economy. But in 2016 real wages began to fall in many sectors, or at best were stagnant for the less skilled after a 13-year run of growth.

The next big shift in the economy is being driven by skills, and those with greater expertise will soon make more than they do today. Ability will once again be highly valued, rather than manual labour, as Australia enters the chapter of its life that some have called 'the knowledge economy'. Perhaps the easiest way to understand what is next for Australia is to see that we are moving from 13 years of the 'blue economy', in reference to the blue-collar worker, to the 'white economy', reflecting the rise of the white-collar worker. The dynamics have now shifted, and influence rests once again with aptitude.

According to the Federal Government's *2015 Intergenerational Report: Australia in 2055*, over the past 40 years Australia has enjoyed a strong economic performance, underpinned by its growing population. This economic success has greatly enhanced our quality of life. Average incomes have doubled in real terms since 1975 (the year I was born), and this increased wealth has been shared broadly across the community, leading to the wonderful Australia we all know and love.

As a result of 24 years without a recession, Australian families currently enjoy access to a well-functioning health system, good schools, a strong social safety net, and options for recreation and leisure that our grandparents could only dream about. It is fair to say the majority of Australians share aspirations for economic security and an even more prosperous future – a better place for our children and the generations beyond. But it is not enough that we share this aspiration; we now have to work out how to grow again.

So how did we get to this point, and what is forcing such monumental change? Some of the key drivers are:

- Australia's Federal Government is driving business growth in innovation and doing its best to inspire critical change as the world economy opens up.
- Today it is less expensive for many Australian businesses to offshore much of their workforce rather than house it in Australia, so less critical jobs are being pushed away.
- Technology is also replacing many normal jobs globally. Cognitive computer systems are now a reality. IBM's Watson already knows more about medicine than many doctors – and it's a computer! The future could mean we will be finding cures in medicine not through a doctor but via a supercomputer that is cognitive. The video *Did You Know, in 2028…* by The Centre Online sums up in 2 minutes and

44 seconds what life will be like in just over a decade. (It is a fascinating video – I encourage you to watch it online.)

We live in a troublemaking economy that is full of change, and real estate is not immune from the interference.

The landscape of what Australia will become has actually been planned: it is already mapped out. It is government policy for Australia to grow, and what will be impacted will be the way we live, work and invest. Australia's transformation can be linked to an initiation many years ago in 1996, well before the mining boom economy began. Two politicians in particular created a growth plan for Australia. The then Prime Minister, John Howard, and his Treasurer, Peter Costello, made a decision that paved the way for where we are today. Howard and Costello foresaw real challenges with tax revenue, problems with an aging Australian population, and pending shortfalls and an inability to fund the future. They consequently made some critical decisions about bringing more people into the country via open immigration under the skilled migrants scheme. This scheme was designed to bring more taxpayers into the system, and to add more skills to our economy to enable the country to grow and to pay for critical infrastructure and, as a result, build a bigger and better Australia.

Our booming population

This decision has seen our population reach some remarkable milestones. According to the Australian Bureau of Statistics Australian population clock, on 16 February 2016 Australia reached 24 million people, and by the end of 2016 Sydney reached five million people. By 2051, as per the growth target led and inspired by government, Australia will reach 40 million people. Australia is growing faster than ever before.

The idea these two men had was fairly bold: 'more people, more tax, more skill, more growth'. And they went for it. And while the rest of

the world suffered a global financial crisis, Australia kept growing. For a while we were the envy of the economic world.

Deciding to change the size and structure of our population was a far-reaching decision at the time for Howard and Costello. It influences how quickly our economy and our incomes continue to grow, and therefore the rate at which our future living standards will increase.

Our increasing life expectancy

Australians have one of the longest life expectancies in the world. According to the Federal Government's *2015 Intergenerational Report: Australia in 2055*, in 2054–55, life expectancy at birth is projected to be 95.1 years for men and 96.6 years for women, compared with 91.5 and 93.6 years today. This is a dramatic increase, and we have well over 300 times the number of Australian centenarians compared to 1974–75, which was 122.

Not only will Australians live longer, but improvements in health mean they are also more likely to remain active longer. However, on the flipside, this also means people may have to work for a lot longer than before to self-fund their retirement. One set of my grandparents retired at 55 years old and lived to 65 and 67, a common age to pass away in the 1980s. They were able to fund themselves during their golden years, but had they lived any longer they would actually have been broke in retirement. Today they would need to fund themselves for at least another 15 to 20 years. This means people are pressured more than ever to choose the right approach to investing. And quite frankly, not participating is simply not a good option. We now live in a time when personal planning for our future is not a marginal idea, it is a must.

The structure of Australia's population will also continue to change. This has major implications for the demand for health and aged-care services as well as retirement incomes. Soon a greater proportion of the population will be aged 65 and over. The number of Australians

in this age group is projected to more than double by 2054–55 from today's levels. Both the number and proportion of Australians aged 85 and over will grow rapidly. In 1974–75, this age group represented less than 1% of the population, or around 80,000 people. The intergenerational reports conclude that in 2054–55, it is projected that they will account for 4.9% of the population, nearly two million Australians.

The primary growth of people according to the Australian Bureau of Statistics will be in Sydney, Melbourne, Perth and Brisbane. Melbourne will be our biggest city and will house over eight million people, closely followed by Sydney. Brisbane and Perth will grow as innovative and dynamic new world cities, and will both be home to more than four million people.

So what does it all mean for investors?

These trends are truly monumental. Understanding that it has taken Australia 228 years since European settlement to reach a population of 24 million people but it will only take a further 35 years to add another 16 million people is something that is both exciting and somewhat disturbing. That is a lot for our city planners to deal with! It also means our way of living is very much going to change as town planners struggle with the next steps.

Of course, this will impact on property investment choices regarding where you should be investing. Investors who haven't kept up with these trends will be left behind, making decisions on old paradigms that are no longer relevant. Skilled, knowledgeable investors will be well placed to capitalise on these trends.



Want to know how?

Come and see how we do it at a Property Investor Night.
If you want to learn about strategies like these, we invite you to join us at your local investor night. It's free and anyone can join us. We'll give you some great investing tips as well as info on how to reduce your tax, pay your home off faster and where to invest. You'll also have the chance to talk to one of our expert coaches and have your questions answered.

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CHAPTER 2

THE URBANISATION TREND

Australians today enjoy a booming economy by world standards. Australia is bursting with people far more motivated and competitive than you may believe, and so many more people want to migrate to Australia. We are a nation that has grown up via intense immigration, and we are seen worldwide as a land of opportunity where you can change the course of your life for the better. New immigrants continue to drive Australia's competitiveness, and our population growth rate is the envy of the Western world. The multicultural society that has been formed is filled with people with a strong desire to succeed.

All humans have a desire for more living space and a better economy; it comes with the tide of urbanisation that is sweeping the world. According to the United Nations report *World Urbanization Prospects* (2014), more than 55% of the population of the world today live in urban areas, and in much of Asia and Africa people are still surging to cities in numbers swollen by a population boom. With Earth's population headed towards eight billion people, dense cities are the best hope of lifting people out of poverty without wrecking the planet.

This being the case, it is easy to see how property becomes a highly desirable asset class. The fact remains that as long as there is a growing population and a desire for living space, real estate remains valuable. Economics embraces real estate as it is becoming simply harder to build at an affordable rate when there is progressively less land available yet more and more people.

According to the A.T. Kearney Global Cities Index, in 1950 there were 74 cities in the world with at least one million people; today there are 442 such cities. This trend won't slow, as the efficiencies that cities bring make life far more sustainable than in rural areas. Simply put, there is no such thing as a poor urbanised country and there is no such thing as a rich rural country. So cities and the economics they provide are the future of mankind's prosperity.

Australia today has five cities with populations over one million people: Sydney, Melbourne, Brisbane, Perth and Adelaide. It is these cities that will attract the most new people and the majority of new economic investment for many years to come.

It is common practice for governments and private enterprises to develop and enhance our cities, often at the expense of regional Australia. There is only so much money to go around and our cities continue to win taxpayer enhancements.

Mahatma Ghandi famously said, 'India's future lies in its villages'. He was wrong. Today, we see India's future in its many emerging cities. The Global Cities Index states that India has 46 cities with over one million residents each. In comparison, the US has 42 and China 102. Like India, Australia's future is not its regional areas (its villages), it is in fact its cities that will boom. The Aussie bush is sadly dying. Australia doesn't have a great business plan for the bush, but it is something that should seriously be considered. I think that approach may begin many decades from now, as our cities become overcrowded megacities, but as a nation we are not ready yet to work out what do with our many satellite areas. One day someone will be

brave enough to spend $100 billion to build a high-speed rail link from Cairns to Melbourne. People who live four hours outside the city by car would then be less than an hour's rail commute away, as is common in Western Europe and Japan.

People should not be drawn away from the fact that cities will lead the world into the future. In its simple form, real estate should be easy: knowing what we know about the world's population and people's desire to live close to employment, just buy close to a major city's economic heartbeat and surely you will do well in time.

The cities of Australia

Global and new world cities

Australia currently has just two **global cities**: Sydney and Melbourne. These cities get their title as they are alpha cities in their region and are apex cities for economics. In reality, these are fabulous property investment zones as they not only benefit from local growth but also global influences. Similar to New York, London and Hong Kong, these cities sometimes stand out as expensive, and in many parts they are. They are award-winning cities; for example, Melbourne was awarded the world's most liveable city by the Economist Intelligence Unit (yes, that's a thing) for the sixth year in a row due to its excellent work and life opportunities. To be blunt, owning real estate in these great cities is a must for Australian property investors!

Beyond our global cities, the alternative choice into the future for Australian property investors is Australia's two **new world cities**: Brisbane and Perth. So what is a new world city? According to Jones Lang Lassalle (JLL), a large commercial real estate firm, 'New World Cities are an evolving group of cities that are redefining what it means to be global. Typically mid-sized, they have strong technology credentials, are highly liveable with favourable infrastructure and are often supported by global specialisms.' New world cities

include places such as Munich, Boston and Brisbane. According to JLL, 'These cities are attracting talent and corporations as well as a disproportionate share of global real estate investment.' JLL predicts that these cities will be at the forefront of innovations in real estate, living and work styles by virtue of creating urban development models that are smart, sustainable and resilient.

Global and new world cities make up the big four in Australia, and will do so for a long time. They are investment musts. Beyond these cities, the choice funnels down.

Primate, secondary and feeder cities

Primate cities are those that are dominant in their area, and they can also be safe areas to invest. These are cities such as Adelaide and Canberra. They are capital cities in their own right but are not as advanced as global or new world cities. **Secondary cities** such as Newcastle and the Gold Coast are growing and are part of Australia's bright future, as are smaller **feeder cities** such as Toowoomba and Wollongong. These types of cities are lower ranking than global cities and new world cities for property investors but can offer a less expensive or alternative diversification option, and will certainly get uplift over time as a result of their connectivity, exposure and geography linking them to our biggest four powerhouse cities.

Regional areas

There are many other **small towns**, **regional areas** and **smaller cities** in Australia, such as Orange in New South Wales and Rockhampton in Queensland. According to the ABS, Australia is home to over 1.9 million people living in over 20 small regional towns and cities with fewer than 100,000 people. Many of these towns and smaller cities lack a major plan for the future, so be careful investing in these areas. They are still in the political wilderness and struggle to attract broad-based investment.

So what does it all mean for investors?

My simple tip for investors is to start by investing in global cities and new world cities first as an investment principle, and work your way down. Put your money in the best markets first. Buying in a small town because it seems inexpensive can often be speculation and not long-term investing. Bigger cities are liquid real estate markets, meaning properties trade well and commonly. If you need to sell you can typically do so in less than 60 days. Smaller areas are usually illiquid and you can often be on the market for longer than 12 months. Stick to liquid markets, as you never know when life might throw you a curve ball and you need to get out of an investment quickly. Big cities are liquid and usually more profitable because they never stop growing.



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CHAPTER 3

THE TWO MAJOR PROPERTY DISRUPTORS

Every industry has disruption and innovation that alters the market landscape forever. If you think of share trading, in the old days shares were exchanged live at the stock exchange or over the phone. This changed when the internet allowed anyone to trade at home, and this brought faster and more trading than ever before. So, the internet was a major disruptor of the share industry.

The real estate market currently has two major disruptors that are changing the dynamics of real estate forever in Australia:

- The first big disruptor in real estate today is **foreign investment**, which we will examine in the next few chapters. The globalisation of real estate is everywhere in Australia, and – now more widespread than ever before – it's very disruptive. Foreign investment and capital are also affecting the supply of real estate in Australia as the government wants money to grow and so allows foreign capital to be fuel for growth.
- The second disruptor is the dawn of **great property design**, and what is known as the flight to quality marketplace,

which we'll consider throughout the book and especially in chapter 6. In Australia, there is enough demand to sell just about anything at present. However, I predict that this will soon change. Consumers will soon shift their buying patterns to not only choosing a locality they can afford but, beyond that, they will expect more than just a property. Living experience will be at the top of the minds of future buyers! We are in a new cycle and we are seeing changes in consumer habits that pertain to the way supply is delivered. I will get into detail about the design disruptor later in the book.

Disruptor 1: The property market is now global

Today you can buy a property just about anywhere around the world and effectively be on your pathway to a form of citizenship through an investment visa class. To put it in simple terms, by investing money into a country's real estate market, immigration laws often favour the investor to pursue a form of residency. This may take a few years, but property investment is seen as a favourable way to activate visas that can eventually lead to residency in the country of investment.

The global economy floats and changes and creates extremes. For example, the Sydney boom from 2013 to 2017 saw property values virtually double. This has priced out many families from living in Sydney as homeowners, and local Sydneysiders buying today will be paying the global market rate, which is a lot more than the 2013 local market rate before this disruption commenced on scale. That's just the way it is now. Sad for many, but life is just a little bit of luck, a lot of planning and a series of choices. Many people missed the opportunity to make lots of money in the Sydney boom.

However, what does seem unfair is that with the falling Australian dollar (there's been a 35% decline in its value since 2015), buyers from around the world, especially China, are looking at real estate in Sydney today. However, they are actually paying only 10% more than

2013 prices as they are hedging currency as well. The decline of the Australian currency offsets the increase in real estate values that we have seen locally. This creates competition at the top of a property cycle, a phenomenon that is a new normal in global cites and very distinct to current property economics, but which was not as common in past property cycles.

How does this affect our market?

A lot of capital is pouring into Australia from abroad, fuelled by open investment policies and a desire from our government to provide more housing. So what does this new capital do to a marketplace? In the past, after a boom, sentiment would typically change and supply would slow or stop as developers did not have the funds or the market locally to attract buyers to their product. However, developers can now use money from international lenders or from wealthy international partners, and so can still produce property even when the market here slows! The adverse effects are softening rents, increased supply of real estate, and price movements that often defy local logic. The supply may have reached its zenith right now as banks deploy a plan to slow it down by limiting lending, ever concerned about a property market under threat. After all, it is their money, but Australia wants the capital and it will keep coming. For investors it means that they need to really have a sharp eye on what and where to buy.

Why is globalisation of real estate such a disruptor? Almost anywhere on the planet, someone can use the internet to study Google Earth, look at current stock lists through Australian realtors, and buy a property in 15 minutes; it happens that fast. The idea that people need to touch and feel real estate before investing is dinosaur thinking. Today, more property trades than ever before are done sight unseen and across international borders. Long-time Sydney or Melbourne buyers and residents are not competing for a property with someone they grew up next to or went to school with, they are actually competing on a global scale.

Australia has foreign investment limits but they are very high for the most part. For example, an overseas company can spend up to $55 million on any agribusiness in Australia and not need to gain government approval to do so, or a government – be it State or Territory – can now sell a company with state assets in it for up to $250 million without the need for Foreign Investment Board approval.

Fuelling our next growth phase

There is a famous Australian saying, 'Australia was built off the sheep's back', referring to a prosperous time when Australia's economy and population grew rapidly during the 1950s, trading off the production of and worldwide demand for wool. A very profitable time of growth! The vast revenue built much of Australia's infrastructure at the time, such as the Snowy River Scheme. Australia is now effectively broke; it has no money to build anything unless it borrows. We live in a land of deficits. The Federal Government is in the red, not the black, and every year we struggle to keep our Standard & Poor's AAA credit rating. So Australia has devised a plan to build the country on the back of foreign investment. Infrastructure Australia, a statutory authority of the Federal Government, has big bottlenecks, and it needs to invest in rail, road and other infrastructure to keep the country moving forward. It cannot afford to spend its revenue on housing and urban planning, so it has outsourced this to foreign investment, which has been an effective strategy. Today, developments that would not seem feasible are being funded and built. Overseas developers are buying and developing sites from Australian developers, who at times think they are mad to do so.

The logic is different between private and public thinking in this matter. Government loves the increased supply to keep property affordable and to cater for population growth. And more production means more tax. On the other hand, for foreign investors, the logic is not about the benefit of the local public realm for Australians, the truth is it's about money migration: the manoeuvring of funds, new

citizenship, hedging currency and bailing money out of sometimes unpredictable countries. The practice of spreading money across tax systems and borders is not a new one at all, it just seems new to Australians. After all, it only costs a few million dollars in investment to become an Australian citizen. Why not invest here if you are worth a few million dollars? Even if you lose money you get citizenship, something that is priceless.

Real estate as a way of parking money

Some people in Europe have been hiding money in Dubai for years. Bernard Salt, a demographer at KPMG, one of the world's big four financial services companies, coined the concept of the 'Dubai Effect'. The term refers to when a city is chosen to safeguard capital. In Dubai's case, wealthy Europeans buy and invest in real estate in the United Arab Emirates to park capital.

Why would a foreign investor want to own a property in Dubai? It's typically not to live in its 40-degree days, nor to holiday. Simply put, a major reason for Europeans to buy real estate in Dubai is to park money outside the European Union. The city exists as a home for money – and Australia's global cities are no different. They are safe havens for our region. Australia is part of Asia and our country has a relatively stable political scene (despite having had five changes to the office of prime minister since June 2010). Australia is seen as a safe place to stash money.

The net impact of foreign investment on the supply of housing and the housing market balance is difficult to quantify due to limited reliable information about the number of unoccupied foreign investor dwellings that are owned today. Yes, foreign investors buy properties today in Australia on zero or extremely low interest rates from overseas lenders and do not need a rental return at all. In some cases, the philosophy is to leave the property empty for personal use in a time of need rather than even accept a return and a lease that restricts the

use. Docklands in Melbourne is the best current working example of the 'Dubai Effect' here in Australia. If you walk through the suburb you will find it is virtually a ghost town, despite being the supposed home to thousands of people. It is more than a suburb; it is, in reality, just a bank. Rich overseas investors don't want the $20,000 a year income these properties offer, they want the safe haven for their money. They'd rather not be bothered with the paperwork and the Australian Taxation Office.

Many Chinese people do not trust their government and think, *why not buy a second property outside mainland China, perhaps in Melbourne, and pay the interest at a low Chinese rate, leave the property empty and, if push comes to shove and the Communist Party of China sniffs too deeply into our affairs, we'll just leave town, knowing we have an overseas home that is only nine hours away?* If I lived in that environment and felt continuously unsafe under a government permanently accused of human rights violations that was unpredictable and known for being corrupt, but also consisted of the best capitalists in the world (yes, capitalists), I would surely feel confused, unsafe and want a new home for my money.

So what does it all mean for investors?

By 2028 there will be two billion middle-class citizens worldwide, many of whom have an uneasy relationship with their country of origin and are wealthy enough to pay a million dollars – or two – for an Australian property and passport. Property investment in our cities for foreign nationals is safe as Australian rules offer a good alternative to the likes of Dubai. The true cost is what this does to local pricing, elevating Australian property to a worldwide price index. The best example of price escalation is seen in Sydney, where locals who are for the majority middle class or who have not yet invested in property are for the most part priced out of the city unless they intend to take on very high debt and buy property now priced at a global level.



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CHAPTER 4

HOW OUR CITIES ARE EVOLVING

Beyond its population growth and the funnelling of overseas capital, Australia's plan is to grow as a knowledge-based economy. The prosperity this offers goes hand in hand with the growth of our cities and the people and property within them. To succeed in the economy of the 21st century, our cities need to be productive and accessible, but they also need to be liveable with a clear focus on serving their citizens. Great cities attract, retain and develop increasingly mobile talent. These people build the best companies, create further jobs for others, and create and support new ideas. So what changes will happen in our cities? How will we live? And how will this affect you as an investor?

(This chapter contains information from Australia's Smart Cities Plan, a government study from the Prime Minister's office.)

Our outdated urban planning model

While the opportunities have never been greater for our cities and people within them, congestion, poor access to jobs and services,

reduced housing affordability and increasing pollution can challenge the quality of life they offer. Cities emerge and evolve for economic reasons, which make them the best places to invest. People settle around sites or landmarks that offer an economic advantage, such as transport and trading hubs. It's been happening for thousands of years and is only going to continue and on a larger scale. The benefits of this co-location are what economists describe as 'agglomeration'.

Urban sprawl areas are sometimes known in property economics and town planning as areas spurred on by a theory known as 'drive till you qualify', meaning homebuyers drive as far out as they have to until they hit a price range they can afford, and then stop and settle in a home that matches their needs, sometimes in an area that has little to no infrastructure. Right now, a $500,000 home in Sydney is more or less 65 kilometres from the CBD, or a one-and-a-half-hour drive in peak hour. You are going to need a comfortable car and a willingness to travel for up to three hours a day if you want a high-paying job, usually in the CBD of Sydney.

But things have to change as we have just sprawled too far. With more people in our outer suburbs, more people are travelling longer to get to work which is creating dysfunctional cities. According to the Australian Smart Cities Plan, in Western Sydney, for example, a net outflow of 200,000 people leave the region each day for work, and this figure is forecast to grow to 340,000 by 2041 – a heavy burden on a city. Furthermore, these outer suburbs often present less choice in education, transport and essential services, so planners are changing tack. Urban congestion is also estimated to cost over $16.5 billion every year, and is forecast to reach between $27.7 billion and $37.7 billion by 2030. One way of responding to our problem of urban sprawl is to recreate and push inner urban living as the dominant plan again – a significant lesson for investors of today!

In the new global environment, success for Australia depends on being more innovative than offshore competitors, so our economy is

advancing by growing its financial sector and ensuring its workforce is highly educated in research and the development of ideas. Today's economy is known as the 'knowledge economy', and – unlike in previous property booms such as that created by the mining boom – big cities will be the dominant players for the next few decades as the economy shifts gears. Australia has real advantages that position us to be a leader in high tech, knowledge and service-oriented sectors.

As economic activity becomes more concentrated in cities, demand for housing and land in nearby areas rises. In Australia's cities – especially our global and new world cities – rapid increases in house prices have made living near work unaffordable for many. To deal with these rising prices, Australians have typically taken on relatively high levels of household debt or moved to outer suburbs, or both. This is a practice that will change as we see town planning methods evolve to bring more people and property to the inner areas at the most affordable rate possible. This means more people living in areas closer to the central business district but also less debt on property, as larger homes that are typically more expensive will be less dominant and be overtaken by more affordable smaller options as people in Australia learn to live in smaller dwellings. This is wise!

Being a property investor sometimes means you have to become a little prophetic at times. Typically, the investments that have performed the strongest have been houses, particularly those located in the middle ring known as 'suburbia'. However, with planning schemes in favour of more people living more compact lives closer to the CBD, and with many residents now preferring to live on top of a shopping centre and train line rather than next to a suburban park, will this continue? What property will grow into the future? The plan that will evolve through town planning and will be led by state government planning schemes is that more people will live closer to their place of work, with easy access to transport and services. And the opportunities to choose active transport such as walking and cycling will grow substantially.

So will vertical living begin to rule our bigger cities? It is my opinion, and the view of many others, that suburbia and the inner-city areas of our metropolises will be great areas to invest in, but sprawl, or the area on a city's edge, will not be. But why are urban sprawl areas dying out?

Urban sprawl is something that past town planners openly admit they got wrong. After the Second World War, the idea of everyone needing space and a home meant that cities grew and sprawled further and further out. But the fabric of society has been killed by sprawl. Today, living in Sydney, I can say that it is like a prison at times. I live on the Northern Beaches, and rarely travel outside of this area because of the traffic mayhem. I have good friends who live all over the city, but most of us give up trying to spontaneously see each other. If we do meet up, we have to plan around traffic and how to beat it, or just be prepared to battle. Twenty kilometres is not far, but in poorly orientated and transport-stretched cities it can be quite a journey. Cities designed around cars will be a thing of the past in the years to come.

The '20-minute neighbourhood'

Urban sprawl designed around freeways is fast becoming a less attractive option for city planners, who now believe the idea of the '20-minute neighbourhood' is the future for our societies, and for property. Cities need to be planned around people first and not around sprawl and traffic. What's more important now than ever before is your ability to walk to an amenity, to live within a few streets of usable transport, and your ability to cycle. Yes, cities are becoming green. Why? Because the next 50 years is not comparable to the last 50 years. Living 30 minutes away from the CBD in 1980 and driving was not such an issue. Now, it's a huge issue, and there are simply more and more people trying to cram themselves and their cars into cities. Right now over 55% of the world's population lives in cities, and by 2050 75% of the entire human population will jam into a city somewhere (United Nations World Urbanization Prospects, 2014).

Planners believe the best hope for the world is to change people's ideals about what city living is, thus pushing people closer to denser parts of the city so they can walk as their primary form of transport. Urban renewal of forgotten streets in inner-city areas is well underway and bringing apartment living to the fore in our cities, thereby changing the way we should view real estate and our selection criteria.

The idea of the '20-minute neighbourhood' isn't simply about the convenience of shorter commutes, it could also have a significant impact on health and overall wellbeing. Many western urban planners – such as Jeff Speck, author of *Walkable City* – believe urban sprawl has led to poor health and put a lot of pressure on our wellbeing. Think about the challenge for middle- and lower-income workers. They raise a family, have a home to pay down, travel two to three hours a day, while trying to stay healthy and spend quality time together. Where do they find the time? Is this why we are becoming obese and have high divorce rates? Some scholars think so. Further, being close to amenities can improve quality of life in terms of having a sense of place, belonging, and opportunities for participation.

Urban sprawl is a dead concept – the homebuyers of tomorrow don't want a larger home in an area that they have to fight tooth and nail to get to. The fight back against the social misalignment of past decades' town planning has already begun. The fact that people will now pay a lot of money for a unit close to the city, even more than a house in a suburb, shows the commencement of a vertical world for Australians. Most Australians today need a car just to leave their home. This is largely due to poor planning and a lack of investment in infrastructure, especially transport. Clogged motorways are something Australians are used to, but these are considered rather backward in many other parts of the world. When I was 22 I lived in Sweden for a year. What amazed me most about that country was that, despite being one of the leading car manufacturers in the world, most people preferred a life of public transport and bicycles, making congestion

virtually non-existent. The lifestyle benefits in Sweden include a feeling of community and social collectiveness that is very much evident even to the untrained eye, driven by walkability, cycle ways and transport.

As a property investor, this is important to remember as it links to a key real estate fundamental: owner-occupier appeal. Not only is it critical to consider what people in the area want now but what they will seek in the future. If your property is not in line with the future of the city then it will become unwanted down the track.

Master-planned communities

Sprawl is now only well captured within master-planned communities. Master-planned communities differ from regular subdivisions as they are estates designed specifically to incorporate a range of recreational and commercial amenities such as parks, walking tracks and shopping centres. They also often bring significant infrastructure to the area and are designated to be part of transport links.

Land that is being gentrified, where rail investment by government is bringing those areas closer to the city, is the best hope for today's investors of getting some land content in their investment portfolio at a low price. If land is what you want to invest in, it can be lucrative, however sprawl that is not serviced by rail or within a few minutes of great amenities won't be in demand into the future. Walkability is now the new hot sector of home consumerism. Can you walk to something? Even in the outer suburbs there is consideration of what is close to you and within a 20-minute walk or cycle from your home.

Activity centres in suburban hubs

Another substitute for more sprawl is to create activity centres in suburban hubs or to connect areas of urban sprawl and greenfield zones and make them '20-minute neighbourhoods'. Being connected to activity zones and transport provides sprawl that still offers a

good lifestyle, as opposed to land and communities disconnected from others.

Activity centres are designed to provide community access to shops and services, as well as to be a major focus for the city's future commercial and employment growth and its public transport system. *Made in Australia: the future of Australian cities* by Richard Weller and Julian Bolleter is a fantastic book on the future of Australia. It takes an in-depth look into the people, places and property needs that make up Australia's future. According to their insights, 'Activity centres are a key component of contemporary strategic planning for large dispersed cities like those in Australia. Activity centres can vary greatly in size from the central districts to neighbourhood shopping centres. They are an important concept in urban planning and introduce the idea of transit-oriented developments (TOD) … TODs seek to intensify land use around public transport nodes to facilitate greater sustainability in the way people move around cities'.

A great example of this is in Queensland, where new homes on the Gold Coast are being built along the train line to Brisbane. These homes are now connected to a CBD. They are also connected to local malls, such as Westfield Helensvale, meaning people do not have to go far to shop and to socialise. If they want to work in Brisbane CBD, where there are many more employment opportunities, the transport is available to make this possible. These areas were cut off for 20 years, which made them less desirable. Now they are becoming more desirable, simply due to this connectivity.

There are now walkability websites – such as www.walkscore.com – that capture and rank just how good a location is for amenities within walking distance. I highly recommend using websites like this as part of your pre-purchase research, as buying investments now and into the future is going to be driven by green concepts, not by old urban sprawl planning ideas.

So, why is it green? Well, the world has a carbon issue and it's driven by the overuse of cars. We all drive more than we need to and we are killing the planet off, one car trip at a time.

The only way to fix our carbon problem is to create more clean energy, reduce factories' emissions, and to over-regulate industries, such as the automobile industry. For town planners the goal is to lessen the impact of driving by us all. Today in Sydney, unit developments within 500 metres of public transport don't require the developer to provide car bays, just cycle bays. Car bays in properties are already being phased out.

Across Australia new homes now also need to be energy efficient. All new homes, major home renovations, alterations and additions need to comply with the 6 Star Standard in the National Construction Code, which applies to the thermal performance of a home.

But it doesn't stop at houses. Commercial property is also heading in a green direction. In Barangaroo, Sydney's most famous new commercial and lifestyle regeneration area located on the CBD foreshore, residential one-bedroom apartments are over $1.5 million, but it is the commercial property that is driving change in the way the commercial real estate market works within the CBD of Sydney itself. What is being built is the new financial hub of Sydney where banks such as Westpac and companies such as KPMG and PWC are now to be housed. In the past, it was areas such as Martin Place in midtown Sydney CBD that were home to such corporations. Now they are moving to Barangaroo to be part of a new, green, energy-efficient world. What is interesting, though, is that these huge buildings with tens of thousands of workers have no real parking for workers – a significant change in multinational business policy.

Another example is 1 Bligh Street in Sydney's CBD, which was the city's first green star energy efficient building. It houses thousands of workers but has only 90 car spots, something that was unthinkable

15 years ago. This forces workers to use public transport or make the choice to live closer to the city.

Melbourne's new town plan is embracing the '20-minute neighbourhood', and is very much geared towards an urban life, not sprawl. The ability for Melburnians to get where they need to go within 20 minutes will be a remarkable change to the way the city develops. Melbourne officials are attempting to put lifestyle first and sprawl second. Sure, Melbourne has a plan for designated sprawl areas, but it also has a huge infill plan and future gentrification programs, such as the Fisherman's Bend scheme. No wonder Melbourne is always a winner when it comes to being most liveable city. Melbourne today is attracting 10,000 new people a month to its inner five-kilometre radius to live.

One could argue that Melbourne is producing too many inner-city apartments. Sure, property investors need to be prudent when choosing a property in these inner areas, but the fabric of what is on offer may just turn out to supersede past property cycle logic that apartments near the city are risky. This market may actually do the opposite and become lucrative to an investor in 10 or 20 years' time because the real estate world and consumer habits will be remarkably different from what they are today.

Melbourne is not the only city moving towards '20-minute neighbourhoods'; this practice is now also occurring in Brisbane and Perth, and recommencing in Sydney after it was long considered a fringe idea to live in an apartment on the doorstep of the city. We have now come full circle; sprawl is dying while vertical living is thriving.

So what does it all mean for investors?

Productivity is vital for Australia's future prosperity and wellbeing, and Australia's cities are crucial to its productivity. Cities are centres of economic activity, where the workforce, businesses and

institutions come together. Australia's major cities are home to four out of five jobs in Australia's high-growth industries. The linkages between people, property and place are now key to unlocking riches in property.

The Australian Government has recognised that good infrastructure is fundamental to the productivity of the nation and has established Infrastructure Australia, an independent statutory body that advances significant infrastructure nationally. This is great for property investors as we can now see pockets of infrastructure and transport change – a key element to success! This can allow us to target high-quality investment in infrastructure nodes. Investing in infrastructure is vital to lift the productivity of our cities and our nation.

In many Australian cities population growth has outpaced infrastructure, leading to inefficiencies and greater costs to the economy and underperforming property areas within cities. By studying cities, we can find property opportunity and property calamity side by side. The foundation of future property investment is intrinsically linked to how we work, and this makes the choice for future investment less complicated as residents, who create property demand, will choose to live on transport lines or walkable distances to workplaces as the world moves past the automobile.



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CHAPTER 5

CHANGING SUPPLY AND DEMAND

What it means to be a property investor has changed significantly over the past 30 years. When my father, a New Zealand immigrant, bought his first house in the 1970s he was not worried about international buyers. Nearly half a century later, our world is changing and there are some home truths we need to tackle.

How property supply works

In past property cycles, investing was rather simple. Australia was undersupplied, with a lack of dwelling approvals and a shortage of properties just about everywhere. Even if you were a little late to the property party, you did fairly well out of real estate; it grew and you were happy. This was no different in my father's case, who has seen his $30,000 investment become $3 million over 45 years.

Supply has always been chasing demand in Australia; that is, until now! The year 2017 marks the dawn of change. We are now in a very different landscape, and it is here to stay for quite a while – something my father's generation never had to face.

So how do we actually invest when, broadly speaking, supply now outweighs demand?

A new dynamic for property investors

This is a new dynamic for property investors to work within. Supply and demand is one of the most fundamental concepts of economics, and it is the backbone of the property market economy. Supply is coming to Australia, and it's something you have to get used to. We have to learn to be better and more informed investors than in the past, and we need to beat the supply chain – as we saw earlier, capital to develop property is now hard to stop, and it will keep coming. (Later in the book I'm going to teach you about area investing so you can beat supply, but right now you need to know how supply works.)

Today, banks that would have the most at risk in a housing slowdown are doing their best to sideline supply, which is helping in the short term. They are making it harder to get investment loans and much harder for international property investors to borrow money here, meaning a lot of international buyers are being chased off or are having to use cash outright to buy here. It is also making some developers think twice about producing stock. However, right now I am more discussing longer term trends and the plan for Australia.

Supply is coming, and it's best you know how much is on the way. Here are some considerations you may want to digest for mid-century, should Australia maintain current levels of population growth and hit the 2051 target of 40 million people that I mentioned earlier.

The supply chain of property isn't stopping, but it will go through periods of lows and highs where investors can pocket profits. But, in general the next three cycles will be about targeted buying and not just buying anything – those days are over.

Below are some confronting facts. You may want to sit down, as your work as an investor is now to find great property in what seems like a never-ending supply chain. According to research presented in the

book *Made in Australia, the future of Australian Cities* by Richard Weller and Julian Bolleter, Australia will go through some robust supply trends, which include:

- Across Australia, the government is targeting 40% greenfield development and 60% urban infill development.
- To keep up with population projections, Sydney needs to build approximately 1.1 million apartments by 2051. This equates to over 17,187 eight-storey buildings with 64 apartments in each.
- Greater Brisbane, also known as South East QLD, will be delivering 680,000 apartments, or around 10,625 eight-storey buildings of 64 apartments, by 2056.
- Brisbane CBD is essentially surrounded by 200 kilometres of community. Stretching from the NSW border to the Sunshine Coast, it is one of the longest communities for a major city to service anywhere in the world.
- Melbourne unit supply trends are ahead of pace and a good example of what the next level of supply may look like for all Australian major cities. The plan, similar to Sydney, is to build a further 1.57 million properties by 2051.
- Perth will be delivering 620,000 apartments to meet population demands.
- Adelaide needs to deliver 249,000 apartments and 88,000 detached homes.
- Adelaide has the best urban design plan in the nation for urban growth but has the lowest population growth among the big cities.

Disruptor 2: The flight to quality

In today's global market many developers have come on board and started constructing new dwellings to meet the opportunity to play global real estate in Australia and move capital into Australia. This is now normal, and is a part of the new property process that is here

to stay. Can you join the dots of a big population plan, a country with no money, and a need for cash to build our properties of the future? What does this all mean for you as a property investor? For a very long time we will be in what is called a 'flight to quality' property market, meaning the right property will do very well but the wrong ones will suffer mediocrity or, worse, no increase or even a loss in value.

Anyone can be a developer, but not every developer adds value to our cities or neighbourhoods. The reality is there is no barrier to entry to be a developer other than money. There are no laws stopping developers practising their skills in the market. Horrendous properties are regularly being built across Australia; there is a real lack of skill and understanding around design principles. For future investors, great design will determine how you make profits from real estate investing; we are past the days of just buying anything and waiting for the gains. Great design is important for property investors as it allows us to individualise property in the saturated market that we find ourselves in today. The greatest driver in worldwide real estate is supply versus demand. So, simply put, the playbook today and into the future is to find well-designed real estate, or real estate that can be redesigned as it is in high demand and in very low supply.

Not all properties are built with a pedigree and to a standard that owner-occupiers want to live in; some properties are a 'rent-for-life' product at best. Certain properties even struggle to attract tenants because they are built and designed so poorly. These properties into the future will miss the mark. You now – more than ever – have to find design and amenity that people want. (We will discuss this in detail in later chapters.)

The costs of development

It is normal for real estate prices to grow based on the cost of new dwellings, and some supply is not bad for property investors. In fact, in land gentrification areas and urban renewal areas (which will both be discussed later in the book), supply can create sharp price increases.

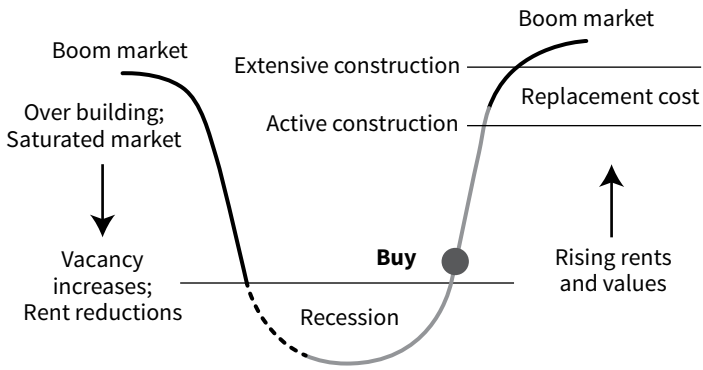
There are three elements to the rise in costs of new dwellings:

- the cost of land
- the cost of the build
- the cost of labour.

The good news for property investors is that, despite the expected high levels of future stock, new supply usually comes through at a more expensive rate than past or older supply, or simply stops for a while.

Property costs are made up of variables such as the costs of bricks and mortar and wage levels. Then there is the land itself. New supply of land tends to be diminishing across our cities or is being squeezed through densification, so land prices tend to go up as the city crams together. To understand long-term supply, in simple terms *land generally goes up slowly, as does the cost to build a dwelling.* This naturally drags up the market over time, as the new properties are sold.

Real Estate Cycle



The above graph shows the cycle of development and construction.

So how do you monitor supply? Well, a great way is to study what developers are paying for development sites. Developers are the ones that deliver supply, so we can make some assumptions on value by researching what they pay for land that they can develop.

I'll explain with some simple maths. Let's, for example, say that a developer buys a property in an area during a period of low demand and gets a great price for the development site. It is a buyers' market as there is little competition. Now, let's say that the land the developer buys has an approval to develop 10 lots on the property. Let's assume the developer pays $300,000 for the property, or $30,000 for each lot.

$300,000 ÷ 10 lots = $30,000 per lot site

Let's now presume the properties are constructed, as apartments. One of them is sold to a shrewd investor, someone who – seeing a bargain – is buying early in the cycle. Remember, it is a buyers' market for the small retail investor as well – a normal process! Let's say this early investor pays $400,000 for one of the developer's 10 apartments.

Perhaps a year or two passes and demand and sentiment are now stronger, and everybody wants to buy real estate. Of course this is a very exciting time for early adopter investors and early developers.

As development sites and real estate tend to go up in price as demand goes up, developers who buy later in the cycle will often pay three times the value of land, which they would have avoided had they purchased earlier. Developers tend to have to compete to buy sites to develop in this high-demand period. So, now let's use the same logic later in the cycle. The same developer, maybe a few years later, now has a huge demand pool willing to buy. The developer may now be paying a lot site price of $90,000 in the same area to buy land suitable for developing. Following the same rationale, the developer is now paying $900,000 to build 10 apartments. This increase in cost is common, as the landscape becomes a 'sellers' market'. In order to be feasible, the developer now has to sell for some $60,000 more for each apartment to accommodate the price variation, meaning the developer will pass on the additional $60,000 cost to the buyer.

And usually it doesn't stop there. As demand picks up, tradespeople and builders tend to be in shorter supply and prices for labour and materials go up. We see at the peak level of the value chain that build costs are often 5% to 8% higher than at the beginning of the cycle. In other words, the developer may now need to actually increase prices not by $60,000 but by closer to $80,000 to develop the product profitably. And still it doesn't stop. Now developers are being squeezed on just about everything, so they often skimp on the costs of design, architecture and landscaping, supplying the market with a substandard property.

Remember, the early adopter investor bought a high-quality product for $400,000. When you compare that price and property to the one built later in the cycle, you can see the price variation. Rather than getting a bargain, the laggard buyer has to pay $480,000 for an inferior product.

What does this do for the early adopter buyer? Well, they have the possibility of making $80,000 in equity based on the new price benchmark, and own a superior property – a flight to quality! Equity and quality really is a winning formula!

The availability of land

Much of Sydney's most recent boom from 2013 to 2017 has been with new supply much higher in price than older stock, but older properties are still selling because of the demand in the market. If you are caught at the end of the supply cycle, you'll find that it is usually followed by a period of downturn where demand falls and prices correct themselves. You may have just paid a little too much for that unit or house. At the time of writing in early 2017, in most cases investors are paying too much for brand new properties in Sydney, as the boom nears an end.

The supply cycle of new available land follows a similar trend. Land can be tightly controlled at times, and this is very much linked to

demand levels. As demand increases, publically listed companies that primarily control the master planned land estates around the country often feed a supply of land to the market. The rate at which they feed land is a good way to gauge value.

Early on in the supply cycle, land lot sizes can be bigger. For example, a master plan may start selling land within an estate offering 600 sqm blocks at $250,000 a block. A few years later, as demand increases, they will cut land sizes to, say, 400 sqm a block and sell these for $250,000. In dollar terms it's harder to gauge the value increase. Within this example, in percentage terms we effectively see a 33% increase in land price.

Early on in the cycle there is an element of little demand. Generally the local market is flat, owner-occupiers are choosing to hunker down, and tenants are not leaving the rental pool, preferring the safety and the limited commitment of renting. During this period, savvy investors are generally buying real estate in great locations and developers are stockpiling and land-banking the best sites.

Early in the real estate cycle, what you are really buying is market position. In a strong market, the well-positioned suburbs grow in value rapidly, and quickly become unaffordable and options dry up for buyers.

As the market firms up, buyers are pushed further out from the better suburbs to secondary suburbs. To buy in the better suburbs you pay a lot for the privilege in a bull market, so you may have to buy further away from them. For example, in 2008 I bought a townhouse-style strata property in Dulwich Hill, Sydney, for $415,000. The total usable area was 118 sqm. It was hardly a bull market back then because 2008 was when Sydney was at the bottom of the price cycle. I bought position, being six kilometres from the CBD. Subsequent years have seen the property climb in value to about $800,000. I didn't get instant growth in 2008, or for a few more years, but I did get location. Today, Sydney has boomed, and so now a $415,000

investment will get you a dwelling of similar size in Kingsford near Penrith. Kingsford is 66 kilometres from the Sydney CBD, not six kilometres. Beyond that, now the cost to develop in Dulwich Hill also sees new supply being sold at a higher rate. Two-bedroom units off the plan are as high as $1.05 million for an 85 sqm apartment. Again, this is great for early investors as the new supply brings higher prices.

The steps in the supply cycle

So what are the steps to the real estate supply cycle? Let's go through them.

At the bottom of supply levels:

- Period of little activity and price growth.
- Gross rents grow as new housing supply is scarce and more people rent than buy.
- Interstate and savvy investors enter the market, seeing a bargain to be had.
- Smart developers are land banking.

As the supply begins to recover:

- Established markets firm up (that is, older housing).
- Developers become more confident to develop, sell and deliver stock.
- Local buyers slowly re-enter the marketplace.

As the supply rate begins to improve:

- Rapid expansion in the building of new dwellings.
- Credit eases and lending is cheap.
- Demand levels increase as local buyers become confident.

As the supply reaches its peak:

- Available land diminishes as new dwellings take the supply.
- Build costs and development sites surge.
- Property prices surge.

- Rents lose value and compress.
- Credit is limited.
- Many new developments fail to be delivered.

A great benefit of the Australian property market is that there are so many good big cities to buy in, so you can always find a new opportunity and a start to a new value chain while others are ending. At the time of writing, beyond some of its inner-ring suburbs Sydney's real estate cycle shows signs of ending as stock is simply not affordable, so where could you buy next?

Brisbane and Perth are low in their cycles; there are still very affordable, undervalued pockets. Melbourne also still has great value in its global market.

Let me give you an example. I recently settled a property in a development awarded Australia's Best Residential Building of 2015, a building called *Austin* in Brisbane. It is a larger two-bedroom apartment with two bathrooms and a secure undercover car park. Needless to say, this was a 'flight to quality' purchase. Can you believe I settled a breathtaking piece of real estate just 14 metres from Brisbane's Gallery of Modern Art! Yes, 14 metres. To use a golfing term, the property is a short par three to Queen Street Mall, the main retail hub of Brisbane, and a short pitching wedge to Queensland Performing Arts Centre. In fact, the land is the closest residential land to the CBD of Brisbane. Further, my unit will have world-class views of the soon-to-be-developed Brisbane Casino precinct by Eco Entertainment. Google it; it's worth a look!

The property I purchased off the plan was $670,000. Now, a mere 30 months after I first noticed the property, it is worth $915,000, a significant gain in a short time! There has been no overall capital growth in Brisbane during this time; I obtained growth through buying the right property in the right area. And I still have capital growth from the market to come! To put some context around this, similar properties in Sydney sell for over $2 million.

Can I see this property doubling in value in 10 to 15 years, or maybe even less? With over 220,000 office workers at this property's doorstep and a downsizing population with money and a hunger for property that offers walkability and convenience, well, absolutely I can!

Evidence of property supply becoming more expensive is already noticeable. Site costs in the same area mean that right now it's impossible to build an inferior property in a less impressive street for the same money. The next supply in the best streets of this suburb are around $110,000 more expensive, as the supply cycle is now on the move.

How property demand works

Let me now explain how demand works within real estate.

What goes up ...

A few years back, I was asked to comment on Moranbah, a small town of around 7,000 people near Mackay, Queensland, by *Smart Property Investor* magazine. At the time, many experts suggested it was the best growth marketplace floating around in property. And there was no doubt it grew. In 2011, I described that market as 'crack cocaine' to property investors, which caused a stir to say the least. Many experts wrote to me explaining their point of view and suggested I was wrong. Basic properties were over a million dollars and renting for an expensive amount of up to $3,000 a week. The bubble was surely ready to pop.

The town has seen a massive drop in value, and you can now buy a home there for as little as $190,000 – but you may not even get a tenant. This capitulation occurred because first-time buyers were not shopping, upgraders who wanted their second home were not spending either, and downsizers who wanted to sell their big family home and nestle into a smaller home were not relocating to the area for their golden years. Overseas investors were not clamouring

to buy into the market as they had never even heard of the town, and institutional investors and super funds were wary. The only buying group shopping in the town was investors who wanted unreal rental returns. They were buying late in the supply chain as the boom had begun some six years before. When the mining boom ended and jobs began to dry up in the town and rents dropped, the market began to fall sharply. In the end, the investors imploded as they could not find a market that was local to sell to. A market with zero interested buyers is a very scary notion! Prices have dropped significantly now, up to 85% in some cases, and now opportunist investors can probably nab a bargain as the supply cycle begins again. But it's a boom and bust town as it lacks buyer groups, which we will discuss next. The horror story of Moranbah was recently well documented on *60 Minutes*. Worth a look if you get a chance to find it online.

Back to the ending of the boom in Sydney! Now, there is no doubt there will be a small price correction into the future; there always is. But will the bottom fall out of the Sydney market – like it did in Moranbah – and prices free fall? No, because there are just too many demand groups who are shopping. Each group has its own challenges and opportunities, but given the risk exposure is spread we won't see a train wreck occur. Don't get me wrong; prices may dip in pockets, but unlike Moranbah, Sydney is a demand-led market and very strong even if darker clouds appear on the horizon.

Who's buying?

The demand cycle has buying groups that make up the marketplace, some of which I mentioned in the Moranbah example. They are:

- first homebuyers
- upgraders
- downsizers and retirees
- investors

- overseas investors
- institutions, super funds and self-managed super funds.

What investors need to gauge is what buying groups are shopping at any one time, as usually not all groups are spending at once. Generally, in slower periods half the groups are stagnant and not in the market. Conversely, when all groups are shopping aggressively at once we have a property boom on our hands.

I like to review markets and see who is shopping and give them a score out of five.

As an example, let's rate Sydney at the time of writing, with 1 being weak and 5 being very active at the end of 2016.

- first homebuyers: 5
- upgraders: 5
- downsizers and retirees: 5
- investors: 5
- overseas investors: 3.5 (slowed from a 5 as a result of banking changes)
- institutions and super funds: 5

I recently conducted a focus group in Townsville and asked a group of locals and realtors to rank activity in their city. As you can see, demand there appears a lot less exciting:

- first homebuyers: 4
- upgraders: 1
- downsizers and retirees: 3.5
- investors: 1
- overseas investors: 0
- institutions and super funds: 1

There is not enough horsepower right now in Townsville to spur on a property boom. Activity is moderate at best; that's not to say it won't

come, but it is just not there currently. Mid-level demand – for example, a market with all 3s or 4s – tells me demand levels are poised for more activity and competition is occurring. Competition in real estate leads to more sales and eventually a boom. If all the groups are shopping collectively, the level of activity tells me we can expect capital growth ahead.

The demand cycle for buyers usually begins with one group and spreads from there. It could be argued that the Sydney boom began with first homebuyers back in 2010, followed by downsizers and overseas investors in 2012, then trailed by upgraders going to auction when demand was strong in 2013 and Sydney hit over 80% in auction clearance rates. Then in 2014 the foreign investor demand surged. The yin was that the overall demand grew in Sydney across every group, and the yang was that prices grew and many savvy investors made much money.

The institutions group also did well through the boom, cashing in and selling off sites that they had land banked. Many local Australian firms that owned sites ramped up the cost for overseas developers to buy sites and produce stock for the community. Charter Hall, a funds manager, sold its St Leonards development site in late 2015. The site, known as 500-520 Pacific Highway, St Leonards, Sydney, sold for a reported $150 million to a Chinese consortium. This was a windfall for Charter Hall shareholders! Just six years earlier the site was valued at $21 million. The new supply in that building produced by the new developer now sees one-bedroom dwellings being sold at over $1.5 million. These properties had to sell at this price, given the price paid for the site. The rewarding part for me is that just six years earlier I helped some investors buy one-bedroom apartments in that area for $340,000. They have made some extraordinary gains both through local demand and the rising cost of the new supply.

So what does it all mean for investors?

The demand of all the groups buying at once and the rise of the supply costs in Sydney has led to a massive boom. It is now up to us as investors to watch other cities and research which demand group is actively buying in the market and who is not, what sites are selling for, and what supply is costing in real terms. Supply is about finding value, in terms of quality, location and price. Demand is about understanding who is shopping in the marketplace.



Want to know how?

Come and see how we do it at a Property Investor Night.
If you want to learn about strategies like these, we invite you to join us at your local investor night. It's free and anyone can join us. We'll give you some great investing tips as well as info on how to reduce your tax, pay your home off faster and where to invest. You'll also have the chance to talk to one of our expert coaches and have your questions answered.

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CHAPTER 6

THE FLIGHT TO QUALITY

'Flight to quality' is the disruptive action of investors and property buyers moving their capital away from riskier properties. In today's property market the riskier investments are homogenous, basic cookie-cutter properties and properties in substandard regional areas. People are choosing to buy the safest possible investment properties; that is, better quality dwellings in safer locations. The flight to quality within real estate refers to stock that appeals to owner-occupiers. Homeowner-grade stock is considered safe in real estate as homeowners don't typically sell in a downturn.

What is causing the flight to quality?

In simple terms this flight to quality is caused by too much supply of substandard property. Let's have a look at the issues.

Too much substandard property

When there is a high supply of substandard property in a market, renters tend to flock towards well-designed properties as they see more value in living in a quality dwelling, even if it means paying

slightly more. The lifestyle benefits of quality-designed properties with superior amenity become more obvious when there is an oversupply of lesser quality developments. This also applies to reselling a property to an owner-occupier.

A recent *Domain* article had the headline 'The Dawn of Good Design'. The properties in demand right now – and for the next few decades to come – are going to have fantastic design elements that allow them to be more homelike than ever before. People want to feel like they are living in a home and a community. These undersupplied great properties are very disruptive to the mass market that is often made up of very simple dwellings, which means that many substandard properties are quickly losing their appeal. Good design is now a massive market disruptor. Some properties are growing in value today despite the market being soft where they are located. Award-winning designs are creating growth in marketplaces that are otherwise subdued as buyers find a shortage of supply of affordable yet high-quality dwellings.

Today, a homebuyer or investor can purchase a two-bedroom apartment featuring a private cinema, a rooftop wet kitchen, a 22-seater private dining room that can be booked via an in-house concierge or smart app, swimming pools with private bungalows serviced by solar energy, and not pay a multimillion-dollar price tag; in fact they can buy this luxury at an affordable price. So why buy a property that is the same price without these lifestyle benefits? It's a no brainer!

These amenities are so good that people can now see apartments as homes for families, since many older houses within suburbia or sprawling areas are not able to offer these amenities at an affordable rate. This is an interesting development in real estate, as quality apartments are now offering more liveability than ever before. How many homes in our big cities' sprawling areas have private gold class–style cinemas within them? One would assume not many. Today, quality

is driving consumer habits in all sorts of ways, including property buying; people want more for their money.

Once upon a time the investment thought process would be to avoid properties with additional amenities because high-quality amenities mean increased levies. But the shrewd investors' view on this has since changed as people have come to realise that those extra amenities bring a higher yield to offset the extra cost, with one significant advantage being that these properties are achieving much higher resale prices as there is less supply of well-designed properties with good features. There is a massive shortage, meaning they are more desirable than ever before. Avoiding properties with such amenities based on 1980s investment logic is not necessarily smart. As Bernard Salt reminds us, Australia is now an Anglo–Mediterranean–Asian–Indian fusion culture, and much of the future growth of property is in areas influenced by a dominant culture who were raised in apartments.

In our current market, two buildings can be next door to each other. One can rise rapidly in value by $100,000, based on being well received by consumers and hitting the right lifestyle notes. Next door, a property can lose $100,000 rapidly by being built poorly and being viewed as just more property pollution; it gets overlooked by consumers as it offers little lifestyle enhancement. Rather, it is just a substandard apartment or house and therefore just more bad supply. In the past, these properties would typically grow or fall together in value. But these days inferior properties are failing as investments, and may well continue to do so into the future as better properties outshine them. We see the world rapidly changing and growing, with a middle class wanting luxury at an affordable price. Better-designed properties are performing in today's world; it is a fact! The flight to quality has well and truly already begun.

Buyers want a home, not just a dwelling

Why do properties that appeal to this market seem to fetch the most and sell the fastest? How does a property worth a million dollars, with a really low return, become two million in a relatively short period of seven to ten years? The answer is the emotional appeal and inspirational aspects of such properties. Properties that fail to look good or offer lifestyle enhancements often fail to grow nowadays. It was once better to buy the worst house on the best street, but too many people are now buying the worst house on the worst street and are getting stuck.

Sure, basic properties that have great land content or perhaps catch a zoning change can be great investments, but as a general rule, properties that fail to appeal to the owner-occupier market as a home fail as investments and will continue to do so into the future. You need to hold an investment that consumers identify with as a 'home', not just as a dwelling. A significant change in real estate logic! We often lose sight of what people will pay more for, based around spreadsheets and numbers, when real money is often paid for real estate based on its form, style and appeal.

Character now often defines how a property will perform – from the design of a home to its ambience. I like the description that property is rather like wine. The best wines on Earth are rich in texture, usually very sought-after, and have become rather expensive as they age. Homes such as Federation homes, Edwardian, Georgian and art decos are all rare today and so continue to rise in value. They are bought often based on their emotional appeal rather than simply numbers. They are like a Grange Hermitage wine or a fine piece of art, and they continue to increase in value and will be worth lots of money as time goes on. Even new properties that have great appeal and design will appreciate based on their architecture and desirability.

When I look at my worst performing properties in my portfolio there is a common theme. The worst performers have been very

ugly, basic properties and, even after some refurbishments, they just didn't do well as they simply were not desirable. They get low demand as they have never created a sense of delight for someone and have not reached the highs that my other properties – which have been seen as homes to people – have achieved. My worst performers have never attracted owner-occupiers' dollars or lifestyle buyers; they are just basic rental properties and suffer longer than usual vacancies and lots of turbulence now the market has embraced that better design is a key metric for success.

Emotions are now driving the market, not numbers

People want what they can't have, and they also want a good living experience. Your job now as an investor is to offer the market both. Ask yourself, would your current investment properties be homes and enjoyable to own and live in, or would you have to discount the price of a property to sell it because it lacks desirability? If you want to find out how appealing one of your investments is, write an advertisement as if you were going to sell it. How would you turn your property into something appealing? Does it meet the mark? Most don't.

More than simply location, the property's appeal is extremely important. Remember, don't become caught up purely in the numbers and pass up what people really want: lifestyle and amenity. The flight to quality is about emotions driving the market, not numbers, so broaden your criteria past just mathematics, as those days are well and truly over for a property investor.

Investor logic around maths is to consider elements such as:

- macro-economic drivers
- suburb profile
- supply and demand
- predominant property type
- last year's sales

- supply-to-sale ratio
- zoning and density
- local government plan
- vacancy rates
- demographics (who will be your tenant?).

All of the above is great research and logic, but is neither what owner-occupiers nor tenants look at and has nothing to do with people's emotional need to buy a home. Emotional buyers think of other benefits and have different priorities; numbers are not even on the radar. Investors now need to learn about and explore what these benefits are. Luckily, I'll help you understand what they are in this book.

Remember, one day, to get big money, you will have to sell your property to the emotional and aspirational market, otherwise you will have just two markets to resell in:

- selling your investment-grade property to other investors, usually meaning your price will be capped
- selling to homebuyers who can only buy on affordability and therefore cannot drive your price up.

If your property is not great it won't sell on its merits to the aspirational market, it will just sell on price. I know which type of property I am now targeting, especially given the new level of investment-grade stock in the market and the lack of quality properties with great amenities. For some property investors it is easier to look at price and barter numbers rather than consider value. Cynics have no clue what it takes to understand good design, architecture and great builds. Many investors treat the property market like a used car lot – the cheaper the better! But things are usually cheap for a reason.

You can still find quality at the lower end of the market

As people start their investing journey they are often unable to break into this higher-end market, but property that has lower-end pricing,

if you get it right, can still be very lucrative. When people buy their first investments, often they do so in the sub-$700,000 range, which is the mass marketplace. Here, properties are less rare, but investors still need to try to find a great property that appeals to a broader range of people. If you are buying a cheap property with no appeal, it's probably going to struggle. A lemon will always be a lemon. To buy property and steer clear of the bad stuff, you have to consider architecture and form. It can improve your chances of getting it right.

Achieving a great design

The best new properties today have a team of dozens working on their design, including a great development group or builder, a designer, an interior decorator, a draftsperson, a landscape architect, an architect and a property stylist, just to name a few. It takes a lot of different skills to bring about a stunning design.

Let's have a look at the cleverness involved, so you can understand why some properties fly above the rest.

An interior decorator's and property stylist's role is generally to improve the look of an existing space. An interior decorator typically holds a qualification in interior decoration (normally a diploma), and is concerned with dressing an interior with things such as paint, furnishings, floor coverings and fabrics. Stylists understand what buyers are looking for, what they are drawn to, and are aware of current design trends, so their job is to advise builders and developers in this area.

Despite this, many developers or builders don't have such people on their team. This could be due to budgetary constraints or a lack of understanding of the value of good property design, or a combination of the two. Generally, these developers miss the key elements that make a property's form and function appeal to an owner-occupier. They just whack up standard properties to make a profit and move on to their next project. (At times, no-one knows who they

are as they close down their company to avoid future backlash and start again under a new name. This is a skullduggerous practice that is endemic in our country.)

So what does it all mean for investors?

The flight to quality starts with the pedigree of who you are dealing with and their skill, especially when it comes to new builds. In Australia, there are three main professions associated with getting great properties to market: architects, building designers and draftspeople. They tend to all work together under a head architect, who usually has years of university training and much industry experience. The best new properties have great elements to them but also a quality team behind them with a strong skillset. They are not built to cater for the rental market; they are built to attract emotive owners. Australia is a unique country in that there is no legal requirement for a developer or builder to engage a professional design team. They can do what they want, and around 80% of them are doing just that.

Supply is being driven by developers who skimp on their developments and leave buyers with properties that are not adaptable or have not been well designed from the get go. Most real estate hitting the market today is going to fail, which is alarming and needs to be stopped. This is one reason why the flight to quality is now so important to an investor: in the past this was a non-issue because there was more demand than supply, but now properties will remain cheap and fail to get better with age as broadly there is more supply than there is demand. I have a few of these properties in my portfolio, and I speak in all good conscience when I say steer clear of this 'cheap property pandemic'. Don't construe this stock as good just because it has a decent rental return or because you could get a discount. Consumers are climbing over each other to live in superior properties, making it critical for investors to ensure they purchase from quality-conscious developers who are backed by a qualified and experienced design team.

Owners-occupiers' emotions drive up capital growth. So what do owner-occupiers want? How can we find the flight to quality areas? We will discuss flight to quality dwellings further in the design chapter, but here is a checklist of 14 elements that make up the appeal of an area and property:

1. It is safe for people, and their property is safe.
2. There are good employment and economic opportunities nearby.
3. It is a desirable place with a good standard of living.
4. It is a clean, well-maintained and unpolluted area.
5. There is good public transport service.
6. There is a good road network and minimal traffic congestion.
7. There are good schools and other educational facilities.
8. There is a range of quality affordable dwellings.
9. There is a range of recreational outdoor environments (such as parks, playgrounds, cycle paths, beaches and countryside).
10. There is a range of cultural entertainment options (such as cafés, restaurants, markets, theatres, nightspots and sporting events).
11. The property has good natural daylight.
12. The natural environment is attractive or artistic.
13. There is a diverse range of people in the area who get along well.
14. There are good approaches to environmental sustainability in the property and in the area.

Success via capital growth for properties that have the right look, design and appeal is the true flight to quality occurring today, proving its worth in our big, oversupplied cities right now. People are responding to this stock and disregarding what was typical investment-grade real estate as C-class property. We are seeing price uplifts in well-designed property in markets that have seen zero growth as a whole. This is a new phenomenon that investors must take heed of.



Want to know how?

Come and see how we do it at a Property Investor Night.
If you want to learn about strategies like these, we invite you to join us at your local investor night. It's free and anyone can join us. We'll give you some great investing tips as well as info on how to reduce your tax, pay your home off faster and where to invest. You'll also have the chance to talk to one of our expert coaches and have your questions answered.

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PART II

SUCCEEDING IN THE NEW INVESTMENT ENVIRONMENT

CHAPTER 7

THE FUNDAMENTALS OF SUCCESSFUL INVESTING

Buying property successfully is, no matter the market, about having a plan. Too many people buy real estate without really mapping out what they want in their life, and as a result the investments do not go well.

Investing in property is generally for the long term, so it is essential that as an investor you have an investment strategy that reflects your goals and will assist you in achieving them. If you don't have a plan yet, that's okay – you can borrow some ideas from my Five Cities Strategy, which we'll look at in the next chapter. But before we do, we need to make sure you have some fundamental property concepts bedded down.

The fundamentals of buy and hold property investing

I believe it is worthwhile examining the major advantages of investing in general and also considering the fundamentals of a 'buy and hold' approach to property. As an investor, you have to create a plan

that leaves no stone unturned and that ensures you have no issues in the future.

I often meet people who have done just about every property education event that's been offered in Australia. They will explain that they have continuously researched property, yet when questioned whether they have taken action and bought a property or followed any of these lessons, the answer is a resounding 'no'. In real estate, this is known as 'analysis paralysis'. This occurs when someone knows they should invest but doesn't feel comfortable doing so and really has a lack of skill around how and where to invest, resulting in them simply taking no action at all. If this sounds like you, thankfully you are reading this book in which I will help crack that code for you.

Creating a plan will be the first step that helps you move forward because it will serve as a road map. You can be the most educated individual on the topic of real estate, but without action that education is useless.

To help lessen the paralysed feeling, it's wise to first understand the fundamentals of a 'buy and hold' approach to property investing. So let's tackle the things you need to know at a basic level:

1. You must have goals.
2. Be prepared to change.
3. Why invest?
4. Why property?
5. Why holding property is a simple plan and works in the right areas.
6. Leverage.
7. Houses or units – what to buy?
8. Due diligence.
9. Teamwork.
10. Finance.
11. Running the numbers.
12. Capital growth.

13. Buying, holding and retirement.
14. Inflation.

Let's have a close look at each of these issues.

1. Have goals

Having goals means that we can direct events in our own lives rather than have the events direct us. Goals define and measure success, provide us with a basis for making decisions, and are a huge driver behind successful property investors.

However, many people fail due to setting unattainable expectations for themselves. Don't fall into the trap of creating enormous goals that you won't be able to achieve. Instead, have goals that can be broken up into short-term, bite-size chunks. Setting a goal of having a property portfolio of $5 million in 10 years is wonderful, but can be overwhelming and might lead to inaction rather than action.

A simple tip with property is to create impact goals that strive to keep it simple. Below are a few examples:

- Sort out your finances so you are ready to buy when you find the right property.
- Get your first property revalued to release equity.
- Speak to your property manager to increase your rental return.
- Save 10% of your wage to invest in real estate.
- Get your tax return lodged with the ATO.

2. Be prepared to change

If you want to be wealthy you have to do more than just talk about it! There are many ways to slowly become financially free. You have to make small transitions in life, and you cannot wait forever.

Being wealthy is actually a lot of little wins added together. Here is just one idea or small win, so you grasp the concept. Living in your own home with a mortgage has no benefit for your cash flow as it is

debt that is not deductible, unlike an investment property that is considered tax-effective personal debt. Why? The ATO allows deductions on investment properties. So here's an idea: move out of your home – perhaps it's not in your dream location anyway – and rent somewhere that you'd prefer to live. Instantly, your home creates more cash flow. Usually you can rent a better lifestyle for less money than having a mortgage, so you may just find a place you really love. And at the end of the day, if you are not happy, you can always move back again.

But what is really interesting, and where the small win begins, is the extra cash flow you have just created: $100 to $200 a week in deductions may not seem like much, but the compounding effect can be huge. Possibly this one idea will allow you to get another small win on something else that then leads to a bigger win. All it takes is some out-of-the-box thinking!

3. Why invest?

Many people never feel comfortable because they simply don't have enough money in life. For example, if you are single with no dependents and have $10,000 in the bank that money makes you feel like you have clear air and zero turbulence. Without that amount you feel unsafe. Now, the further you grow in life, perhaps when you start a family, you need much more to feel safe. This could be $50,000 or $200,000 in net wealth.

If you are right financially, it changes everything else in your life. When you are safe, you will feel you can grow. You never want to live month-by-month, and the sooner you start creating wealth, the safer you will feel and the more fun you can have. Some people never get out of their unsafe zone; they simply don't set themselves up for long-term success. Being successful with investing is about growth.

4. Why property?

Property is very stable. There are a lot of vested interests in making sure the property market is stable. Banks lend to lots of people

to support them in buying a home or investment property, and will often lend as high as 95% of the value of a property. This tells us that institutions see the property market as very much a protected bet. Our banks have so much money in property they simply have to step in when it gets a little overheated and make it work again.

The government also sees the property market as something they have to look after. They gear the economy and can try to influence interest rates to look after households and property owners. For example, they wouldn't interfere with the price of gold if it was tumbling. They will, however, step in and put pressure on the Reserve Bank in less positive times to lower rates in order to support people so they can pay their mortgages. After all, mortgage holders elect politicians and they have to look after their electorate.

Property is also very safe because people require shelter. It sounds so simple, but it is a fact. Unlike shares or businesses, we *need* property to keep us warm and safe.

Corrective measures are part and parcel of the real estate economy; it's one industry that corrects its own mistakes. At the time of writing we are in a period of oversupply, so these corrective measures include tougher funding, builders rejecting work based on risk, and major banks restricting investment lending to many people.

5. Why holding property is a simple plan and works in the right areas

Property is a slow and simple way of making money. If a property market grows by just 5% in value per year it would take just 15 years to double. But what does that look like weekly? A $500,000 property is actually growing by $500 a week at 5%. That is so simple and such an easy plan to follow. If you have five properties worth $500,000 each, you are making $2,500 a week, which is much higher than most people's salary!

Holding property for the long term is such a great way to become steadily wealthy. A lot of people I meet stay in property for a short, harsh period because they don't understand how to create a long-term plan. If you are holding property for the long term, choose properties that are not going to grow just for a few years but for a very long time. Desirable properties in proven suburbs are the key, as they will always be in demand even as the market goes through flat periods. This real estate will transition with you, and as you become older and want to retire it will still be valuable.

Many properties don't follow the way your life evolves; some properties simply won't shift with your life, usually the ones in marginal areas with no backbone. The day you retire, the day you want to sell, you have to have a property that is in a good area that will sell. To ensure this, why not just stick to the basics: good area, solid property, and great city.

6. Leverage

Owning property and shares are both ways to increase wealth, and of course there are pros and cons to both. I prefer property for a simple reason: it is easy to leverage.

With that said, you have to understand lending to invest well. For example, you need to know how to *not* cross-securitise your lending. Most banks have clauses in their home loan documents that entitle them to review any one of the home loans you hold with them. Some property owners get caught napping, as the banks can demand additional funds if they believe an investor's property value has decreased overall; they do this by offsetting one property's loss against another property's gains via loan-to-value (LVR) ratios. It is the property market's version of a 'margin call', albeit – unlike shares – you won't be made to sell your property that has lost value (unless you make a real mess of things).

The alternative is: never face this challenge! Borrow money from various institutions, so that your assets are not intertwined and you cannot get caught out like this. If banks do not have more than one property with you as a lender, you cannot be cross-securitised and therefore cannot suffer a property margin call. For example, if you want five properties that are uncrossed and not securitised, use the big four Australian banks and then try one smaller bank. You will have five separate loans, with five different parties. If one property loses value, the other four will be protected from that loss.

You can leverage shares as well, but they are subject to margin calls. For example, if a share has an LVR of 70%, the maximum amount you will be allowed to borrow is 70% of the value of the share; you must provide the other 30% yourself. An investor receives a margin call if one or more of the shares they have bought with borrowed money decreases in value past a certain point, usually the LVR. What happens then? The investor must either deposit more money into their investing account or sell off some of the shares to bring the portfolio back into balance. And this is being done because some of the investor's shares have fallen in value, so the shares may be sold at a loss. This can catch even the smartest share investor off guard.

Let's consider an example. If you put $100,000 into property, you could easily buy a property for $500,000 based on the bank lending you the extra $400,000 on an 80% LVR. Let's assume the property goes up in value by 30%. You now have $150,000 extra in value, which is what you want.

But let's also play the bad luck card. Let's assume it goes down 30% and your asset is now worth $350,000. In this case, you are $50,000 below your original $100,000 deposit. If this were the sharemarket you would be margin called. In property, you are left alone if you are not cross-securitised! With property you won't be called in by your lender and asked to sell your property or asked to make up the $50,000 difference if you are not cross-securitised as the loss is really

only on paper rather than a realised loss anywhere. With property we also know that the longer you hold, the more likely you are to gain, despite any short-term pain.

7. Houses or units – what to buy?

I try to keep this debate fairly simple: houses are great investments because they carry more land content. However, the more expensive the house, generally the lower the rent return is. The best land is in the superior areas within a city, and this land grows the most in value, especially over a longer period of time. If you're investing for the next 30 years, you want the best land in your portfolio even if that means owning an apartment and a smaller piece of that prized land.

The most aspirational suburbs have high land costs with nice homes. These properties actually get fantastic growth but have lower rental returns due to the higher entry points. For example, a $2.3 million home in a top suburb in Melbourne may only rent for $1,400 a week. The suburb may be exceptional but the numbers just don't work to hold the property, as the rent is too low compared to the purchase price.

In great suburbs it is common to see a big gap between homes and apartments. Let's assume an apartment is worth $700,000 in the same area, but it can rent for $650 per week. Why? There are more people in that part of the rental market than the higher end. When we do the overall maths the growth in that suburb may be stronger in houses, but when you combine the rental return rate and the apartment growth rate, the apartment is very competitive, even mathematically better. The reality is that, within these better areas, we probably would not invest in the more expensive home as that is usually not affordable, but an apartment is, and that makes it an excellent buy.

This also works in reverse. In some suburbs apartments make more economic sense but in other suburbs houses do; it depends on their

pricing and rental return. Perhaps a house in an area has a median value of $650,000 but would rent for $570 per week and a $500,000 apartment will rent for $380 per week. Reasoning suggests the apartment is not worth buying and the house is very much the better buy. It is affordable and makes more economic sense.

8. Due diligence

It amazes me how many purchasers buy a property after just inspecting it themselves, or buy a property in an interstate location without understanding the city's town plan and exploring the area. So many people buy without performing proper due diligence, such as employing the services of a valuer, building inspector, pest inspector and surveyor. It's pretty simple: unless you are qualified in these skills, you should not buy a property until you have had experts analyse it or until you get to know the area yourself well, or ideally both. Intelligent investing is not spending $500,000 on a property in a town that you have never been to. I advocate diversifying, but I also advocate diversifying and spending the money on a flight to see what you are buying.

9. Teamwork

Investment done alone is often very tough. To be an efficient property investor you will need the services of people such as lawyers, finance brokers, accountants and advisers, to name a few. The importance of a strong team is especially evident for time-poor people, which is most of us these days. It is best to value expertise, then branch out and buy skill. Find an accountant who understands property; find an agent who knows a deal.

So many people turn into 'part-time property experts', yet they have never done more than look at property online. If a person has an illness, you would assume they would seek the advice of a doctor to find a remedy. Yet, many people who are financially ill and in disarray

do little about it, and if they do, they try to self-diagnose a $500,000 problem. This is simply financial madness!

10. Finance

Ideally, investment property loans should be interest-only because an interest-only investment loan is fully tax deductible, making it the most attractive loan type to investors. It is usually the best cash flow solution when used with a good capital growth 'buy and hold' plan. As the name suggests, with an interest-only loan your repayments are initially set to cover the interest component of your loan only, which allows you to keep your repayments on your investment property to a minimum. Generally, interest-only loans are for a maximum five-year term (depending on your lender), reverting to a principal-and-interest loan at the end of the interest-only term. However, a further interest-only loan can usually be negotiated at this time.

A standard variable-rate loan offers more flexibility than a fixed-rate loan. There are also extra options available; for example, a redraw facility, the option to split between fixed and variable, extra repayments, and so on.

11. Running the numbers

This is of huge importance! A property could look great on the surface, but until you measure the rental return, outgoings and all associated costs, you won't know how much the true cost is per week.

You never want to be too income negative with property – the property expenses should not be more than 30% of your income production. Why? Because then your wage or income will become a major contributor to the property's upkeep. With a growth 'buy and hold' plan, it is common to contribute a little bit along the way, as the long-term goal is to achieve bulk wealth. We don't, however, want to contribute too much: in the early years of ownership, perhaps $50 to $100 a week until rents grow.

Really, your tenant and the tax deductions should pay for the majority of your real estate running costs, including the mortgage, so avoid properties where the gross yield is 1%, 2% or 3%. Start with a 4% return or above in this current market in 2017. The idea is for the yield to mirror the interest rate as closely as possible. In a high interest rate market often you see much higher rents as a result, and in a low interest rate market you will see much lower yields, like today, where the average capital city has dropped over 1% in yield variation. In a higher interest rate market, rates could sit around 7% or more. In this environment, it becomes less affordable for people to own real estate so fewer people buy property. Consequently, more people stay renting, and rents rise accordingly. A property with today's 4% return may actually become a 6% yield in such conditions.

Australia has a historic low cash rate today of 1.5%, which is linked back to what banks sell interest rates for from around 4.5%. Lots of people have now leapt out of the rental pool and bought property for themselves, and now form part of the 'homeowners club'. In many places today it is just as affordable to pay a mortgage as it is to rent real estate.

These rates are so good that this climate provides a lot of people with their best chance to acquire real estate in their lifetime. Why? When rates are much higher, it is a lot harder to afford property and for people to get into the marketplace. It is a much higher barrier to entry. In a low interest rate market you have higher sales volumes, which are great for growth, but you also get lots of supply, as seen today.

A good way to understand how to calculate rents is the following formula, which determines the percentage gross yield:

Weekly rent × Number of weeks rented in the year = Annual rent
÷ Purchase price × 100 (to get a percentage)

For example:

$500 per week rent × 52 weeks fully occupied property
= $26,000 per annum in rent ÷ $500,000 (purchase price)
= 0.052 × 100 (to turn the sum into a percentage)
= 5.2% gross yield.

A balanced real estate market has a 3% vacancy rate, meaning on average properties are vacant 3% of the year, which is seen as a fair period for a property being unoccupied. A brand new property can have a higher vacancy rate as it goes through a period of being absorbed into the broader marketplace. Generally this is a challenge for the first few weeks of owning new property, but this seldom reappears as the property gets immersed into the standard vacancy of an area.

12. Capital growth

Capital growth properties tend to be associated with higher growth but lower cash flow. As a general rule, you are more likely to achieve good capital growth closer to economic hubs and large cities.

Investing your capital in growing real estate markets is the only way to have a 'buy and hold' plan; it is very much geared to the 'hold' part of the plan. If you hold a property for many years, it grows. It's not a matter of *if* but *when*! The profit or equity you gain in buying growing assets is what wealth is about. With capital growth property the rental return in the early years is usually anywhere from 4% to 6% gross. This also grows over time to become more attractive. Real estate is a long-term wealth creation strategy – you can't expect overnight success.

13. Buying, holding and retirement

There is a common misunderstanding about 'buy and hold' real estate, which is that when you retire you have to sell. This is not

always the case. I know many self-funded retirees who still own real estate despite being in their seventies or eighties and very much retired. Many of them began investing long before retirement. They achieved growth over their many years of investing, which served them well, but now that they are older they care less for equity and do not even seem to monitor the capital growth sector of the market: they actually love the cash flow, using it to run their lives.

My 77-year-old father is a great example, owning six investment properties. His debt versus value is a low 20%: this means he owns 80% of his properties and the bank owns 20%, after 30 years as an investor. However, his rental returns have risen over the many decades of the hold phase of his strategy, and today his properties collectively return him enough cash flow to fund his lifestyle in retirement. They yield a staggering 31%.

How does this happen? Time in the saddle. You have to hold and not let go. The day you buy an investment property, your rental clock begins. The longer you hold it, the more chance you have of seeing your rents double, and then double again. When you have so much cash flow pouring out of your investments, your rent can fund your life.

14. Inflation

Inflation occurs when the economy grows as a result of increased spending. This leads to price rises, and as such the currency within the economy is worth less than before. This basically means that the currency won't buy as much as it did.

The fact that things seem to grow at a sustained level over time is important for investors to understand. Australia's Reserve Bank targets a core inflation growth rate of between 2% and 3% on average per annum. For example, a pack of mints that costs $3.00 now will cost $3.06 in a year, assuming 2% inflation. Too much inflation can see the costs of goods and services soar.

Inflation represents the average amount goods and services rise by. This is important as the investments you choose need to perform better than the inflation rate, otherwise your investments are actually going backwards.

Inflation is one of the primary reasons why people invest in the first place. Investing happens as people attempt to keep ahead of the cost of living, and that cost of living is always rising.

Let's consider how this works.

Let's assume you stuff some of your cash under a mattress, and five years later you decide to spend it. Inflation dictates that cash now has less buying power than the day you hid the money, as goods and services have become more expensive but your cash has not grown. So, by not putting your money somewhere that it will grow, you have effectively decreased your wealth. Of course, banks offer returns around or above the inflation rate for savings deposits, but investing will always be the best way to beat inflation.

Inflation is an important concept for an investor to understand. If you remain still and stay in the same job without growing your skills so you become worth more, and your salary does not grow quickly enough, and you don't invest, as you grow older and the years pass, the cost of living continues to rise and you become stuck. You then cannot escape the rat race. This sees people work themselves to an early grave as life becomes a seemingly endless chase just to stay afloat, with little reward or purpose.

You cannot stop inflation, and because of inflation and people's lack of financial mastery, many people actually fall deeper into a financial hole as time passes, making it harder to get ahead. The longer you choose not to invest, the more challenging it becomes. Everything goes up, from food to housing. Some years things will deflate, but the long-term average of our economy is to grow. As a property investor

you should do better than the inflation rate, so even as the cost of living rises, you are still earning enough to stay ahead of the inflation rate, and you are therefore increasing your wealth.

Now that you understand some context around property and why it is a sound investment, let's delve into building a property strategy.



Want to know how?

Come and see how we do it at a Property Investor Night.
If you want to learn about strategies like these, we invite you to join us at your local investor night. It's free and anyone can join us. We'll give you some great investing tips as well as info on how to reduce your tax, pay your home off faster and where to invest. You'll also have the chance to talk to one of our expert coaches and have your questions answered.

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CHAPTER 8

THE FIVE CITIES STRATEGY

Most of us were not taught about the idea of borrowing money to make a fortune. One can go to school and be university educated in Australia and still graduate with little or no economic understanding or fundamental credentials for fostering wealth. Think about your years at school – were you ever offered wealth creation, or anything similar, as a subject option? The reality is we are not often taught to understand money, so creating a financial plan is a difficult concept for many people.

The challenge for many people

The challenge for many people is that they are not building enough foundations early in life to build a nest egg for later. According to the ABS, the average Australian male at age 55 has $128,371 in superannuation savings, and for females it is much less at around $73,298. This is not enough to self-fund retirement. This is going to lead to people spending their twilight years on a pension as we live longer than previous generations, or a life where people actually don't get a retirement. Fortunately, we live in a society that offers a pension. If we didn't, the average Australian would really be in trouble.

I know for myself after 20 years of work I only had $130,000 in my superannuation. Now, I'm turbocharging my superannuation and investing it harder through a self-managed super fund. In fact, in five years of running the fund I have doubled my net super worth. I won't get into the details of how I did this in this book, but my point is that it's critical Australians understand that if they don't take steps to ensure their financial security early on, it's unlikely they'll get to live the way they want in retirement.

I look at life like an 'attraction bucket'. What are you putting into your bucket and how are you doing it? I call these 'attraction tools', which are like magnets. Along the way, we want to put some great people, stories, adventures and hopefully a small fortune that we attract into our bucket. The main principle of this is if you take something out of the bucket, you need to invest it into something better and gain more magnets that attract more beautiful things to your bucket.

Let's assume you bought a property, made $100,000, and held the property as a future asset. Well, now you have $100,000 with which to add more magnets to your life and more magnets to attract to your bucket. This may mean you choose to invest in shares, in a savings account or some other asset. It doesn't matter, as long as it's well thought out and adding to your bucket.

Why you must have a plan

I have already mentioned that I personally prefer property as an investment class (or magnet) due to the control it gives me as an investor. Unlike shares, it is a roof over someone's head, and shelter is one of our basic human needs, meaning there is always demand for it. Property is also slow and steady, so overnight success as a property investor just isn't going to happen. Property is something we have to learn to adapt and evolve with. It is, however, possible to make money, and quite a lot of it, from property over time and use it to fund your retirement. So, if you wanted to live off $100,000 a year as

passive income by investing in property when you retire, which is a nice sum of $1,923 a week, how easy would this be to achieve? Based on an average rental return of 5%, you would need to own $2 million in real estate debt free. This would give you $100,000 turnover of gross rent.

But you can't just say you want to be wealthy; you have to go out and make it happen. You have to go and take the risk and, at some point, collect the rewards.

As you can imagine, this may require you owning well over $2 million in real estate at some point in your property investment career, to end up with $2 million in property debt free. Given that paying that debt is not practical from a wage, you may have to one day assume your investments today totalling $2 million may well be worth $4 million 20 years from now, so you can sell some of your real estate down, pay some capital gains tax and use the profits to pay down debt on some of your best real estate, leaving you owning property debt free. Yes, indeed a big commitment! But that is the life and terrain we are in!

So, setting up a plan is paramount or you will never reach your dreams.

The Five Cities Strategy for growth

Here is a strategy I use all the time. I call it my Five Cities Strategy. It is a growth plan in which the key principle is diversification to reduce risk and increase the likelihood of success.

Spreading your portfolio

Imagine you own a property each in Sydney, Melbourne, Brisbane, Perth and one of the smaller cities, such as Adelaide or Newcastle. You would have a well spread and balanced portfolio. When you look at the historical performance of real estate in Australia's largest cities, there is typically always one city performing well while the other property cycles remain slow or flat. The great thing with this is all

those markets grow at different times. Generally, one is always working and creating capital growth, so you are making equity out of at least one market year in and year out.

If you do the maths based on average properties in those cities, you can make over $50,000 per annum from five properties in five capital cities in just growth alone. If you owned a median-priced property in the five big capital cities, your portfolio would look something like this (based on 2016 house price medians from RP Data CoreLogic):

One property in Sydney	$872,811
One property in Melbourne	$614,479
One property in Perth	$615,280
One property in Brisbane	$489,128
One property in Adelaide	$469,097
Total portfolio:	**$3,060,795**

Remember, there is usually at least one property doing well just based on the market, so one-fifth of your portfolio is growing. This is typically above 10% per annum for a market rising well in value. As one of your cities rises, the others will flatten off. As the city you extract growth from cools, another city will begin to grow.

With the above property portfolio, this would mean:

$3,060,795 ÷ 5 (being one city) = $612,159
(average value of portfolio growing as one city rises)

$612,159 ÷ 10% (annual market growth rate in a bull market)
= $61,215 growth per annum

> A basic overall assumption with this strategy is that a person needs a 20-year plan to end up with a sound passive income of $100,000 upon retirement. This is broken down into stages: five years to acquire the properties and 15 years to hold them based on 5% capital growth year on year for the properties to double in value.

Remember, for a goal of $100,000 passive income from property you need at least $2 million in net property assets with an average growth rate of 5%. You need a yield of 5% over 20 years to create financial freedom. If you do nothing more than acquire that and wait and float in the market, you should reach your goal. Of course, we can speed this up by buying well and in the right locations, but even if this was the worst-case scenario it is not bad. Today, it is taking well over 13 years for a property to double in value, hence why I suggest a 15-year investment plan. Even with the slow nature of property, this is better than most people's superannuation, I'm sure you would agree …

Five Cities Strategy summary

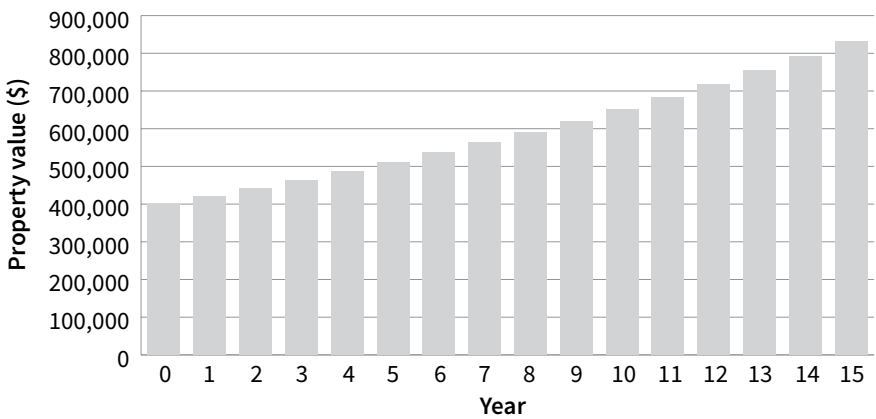
Acquisition time	5 years
Diversification	5 markets; 5 safe areas
Market growth predictor	5% across portfolio compounding
Time to double	15 years
Overall time	Up to 20 years including acquisition of properties
Average starting property value	$400,000 × 5 = $2 million
20-year hold plan	$4 million in property assets

This plan is a fundamental approach to investing for someone who has a 20-year timeframe and is ideally hoping to purchase a property each year for up to five years. If we look at the numbers represented in the table above, we see that, historically, over 15 years we

can conservatively get a growth rate of 5% compounding from the market. Some years will be better and some years worse.

Assuming we bought a property once a year consecutively, we would end up with five properties after five years of buying. We then see that after 15 years of holding the real estate, the first property in our portfolio would have doubled, and at the start of the 16th year the second, at the start of the 17th year the third, until we reach our fifth property doubling in year 19. In turn, our overall portfolio value has increased and we have gone from $2 million in real estate and are now at $4 million. For most people this means a substantial equity base that allows them to move forward and gives them choices in life that they can use to supplement their income, retire earlier, and maybe have better flexibility, or do something they enjoy more.

The magic is that property allows for compounding results, which Albert Einstein once called 'the eighth wonder of the world'. With this in mind, please see the example chart below of a $400,000 property compounding at 5% and doubling in value over 15 years.



The example used above is based on a purchase price of $400,000. A property at this price is still achievable, especially in the major capital cities.

The cash flow component here is $100,000 based on no rental growth. Assuming a 5% yield does not remain stagnant, a 5% return today could be a 10% return in 20 years due to rental inflation, or so one would assume. As such, this plan alone can create well over $200,000 in passive income if our rents also double.

You must start thinking differently

ABS statistics reveal that out of every million people who buy real estate only 10,000 will end up owning a wealth portfolio of more than five properties. Not many people are hitting my Five Cities Strategy! Yet, it is so uncomplicated! Property does not have to be more complex than a simple 'buy and hold' plan. In fact, often people overthink it, and my job is to help them understand that at its very core it is a simple and solid strategy.

Only a small percentage of investors think and act differently and get this right. This small group ends up paying very little or zero tax and they end up wealthy as their property portfolios grow and grow. They turn a small asset base in to a multimillion-dollar empire. They are police officers, cab drivers, teachers, doctors, farmers and nurses. They are people with ordinary jobs. The main difference between them and others is that they develop the skill of thinking differently.

Many people base their investment decisions – or their lack of investments – on other people's stories. These fables are often passed around but often have no sound economic basis. Some common statements are:

- 'You shouldn't invest in property because it's too risky.'
- 'I bought a property and didn't make any money from it.'
- 'Only buy a property near where you live.'

With so much misinformation floating around, no wonder so many people get derailed and don't make the '1% Property Club'. We all have to endure those we love telling us we couldn't and shouldn't. We

need to think for ourselves or we will end up living according to the dogma of someone else's life.

So what is this '1% Property Club?' According to the ABS, fewer than 1% of Australians own three or more investment properties. In fact, only 7.9% of the Australian population own any investment properties. How many Australians actually own more than one investment property? Let's have a look at this in the below table.

Percentage of Australians who own investment properties

Number of investment properties	Percentage of investors	Percentage of Australian population
1 only	72.80%	5.75%
2 or more	18.00%	1.42%
3 or more	5.50%	0.43%
4 or more	2.00%	0.16%
5 or more	0.80%	0.65%

Real wealth starts here!

So what does it all mean for investors?

People have a low willingness to act differently to the masses. Learning some skills in real estate is ultimately more important than the act of rushing in to just buy real estate. The attitude of just doing with no regard to the facts or of having a plan has serious consequences. Facts and knowledge count! Enthusiastic thinking and a positive attitude are not going to change the facts. Today, you need $2 million in real estate paid off, yielding 5%, to make $100,000 from property in retirement. That is a fact!



Want to know how?

Come and see how we do it at a Property Investor Night.
If you want to learn about strategies like these, we invite you to join us at your local investor night. It's free and anyone can join us. We'll give you some great investing tips as well as info on how to reduce your tax, pay your home off faster and where to invest. You'll also have the chance to talk to one of our expert coaches and have your questions answered.

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CHAPTER 9

UNDERSTANDING EQUITY

In the previous chapter we touched on a plan to get wealthy slowly: acquire five properties in five years in five different cities, then hold and pay down debt. Depending on your starting point this can be fairly simple – or actually very complicated. One of the factors to consider is how to manage your finances. To fast track yourself through the property acquisition phase, you need to understand how to best use your cash and equity.

So what *is* equity?

Equity is often misunderstood. To really understand equity, you need to consider that equity drives those life magnets in your bucket that we have been discussing.

In 2005 the Commonwealth Bank of Australia (CBA) started a series of rather fun television commercials depicting how Australians could use something that was poorly understood at the time: the equity in their home. This was the 'Equity Mate' series of commercials, which became quite well known. I'm sure many readers remember them well. At the time, the Sydney market in particular had seen house prices double in the preceding four years, but in 2005 the market

was rather slow and unsure. So the CBA in its wisdom showed Australians what they could do with their newfound wealth. It encouraged people to refinance and use the equity in their home to create a better life. And with purchases from home extensions, to overseas holidays, to new investments, many Australians got their first taste of leverage, something that has changed our property landscape.

See, there was a time when borrowing money was hard, far more difficult than it is today. In my father's era, from the 1950s through to the 1970s, borrowing money and buying property meant suiting up and visiting your local bank manager to state your case as to why you should be lent money to buy a property. More often than not you were declined, according to my father, and often the only way to leverage into property was through vendor finance.

So yes, believe it or not, we do need lessons on leverage, and there is no better form of leverage than using your equity wisely. Since those famous CBA adverts times have changed, but equity use is still very much misunderstood. We are in a period within the property market of a rebirth of equity. So what is it and how do we use it wisely?

It's fair to say after the latest Sydney and Melbourne booms there is a new wave of property owners who have substantial equity for the first time in their lives. There is also an older generation of equity-rich property owners who are downsizing, as they are equity rich but cash poor. The latest boom has created much new wealth in Australia, and we live in a very rich country by world standards. We typically have a growing economy and a GDP rate that's increasing. We have had 24 years without a recession – it could be said we are blessed. When I left school it was 1993, unemployment in Australia was close to 10%, and people were not earning like they are today. Six-figure salaries were not common. Equity was very hard to recycle because wages were so low that it really prevented people from borrowing again. How times have changed for the better!

But what actually *is* equity? Equity is a rather simple concept: it's the difference between your debt and the valuation of your asset. Let's assume you have a property valued at $300,000 and you owe the bank $150,000 on this property. You therefore have $150,000 in equity. This is generally not a physical amount of money but a theoretical one until it's ready for use.

Why does equity matter?

Put simply, your equity can be used to earn you more money. We can try to make equity work hard for us using a principle known as 'equity return', sometimes called 'cash-on-cash returns'.

When buying real estate you are required to provide a deposit, which usually isn't provided by a bank or lender and generally therefore has to come from your own savings. The deposit, usually anywhere between 5% and 30% of the property's price, is, essentially, your capital.

The formula that's used to measure the likely performance of your deposit is known as cash-on-cash return. Seasoned investors measure cash-on-cash returns in 12-month increments. For example, if you were to put $30,000 into a property and achieve growth over 12 months to gain a further $30,000, this would be considered to be 100% cash-on-cash return. This return allows you to retain your asset and have a readily available deposit to fund a new investment. This new deposit is your equity for the next investment. Remember, a new deposit means a new life magnet which could lead to another property during your acquisition phase. (If you're using my Five Cities Strategy, your goal is five properties – or more – in five different cities.)

Managing your equity

It's vital to comprehend that equity is something that you have to control. If you don't, it floats with the real estate market and will appear and disappear as the market forces change. For example, as

interest rates rise, your ability to service more debt changes, so you may not be able to borrow as much equity as you could before, even though you have equity.

The best way to control equity is to 'lock it in'. How do you do that? Well, you have to take out a new loan and create an offset account for use for a specific purpose, or use it as an open line of credit.

Lines of credit are effectively a source of funds that can readily be tapped at the borrower's discretion. You generally only pay based on money you actually withdraw. So, you can have your equity ready and waiting and in its own account for your use.

At the time of writing, in early 2017, Sydney prices are very high from a runaway market. For example, we have seen properties go from $400,000 to $800,000 in some areas. You might think there is the ability to access the $400,000 difference in value, but if you don't lock it in with your lender and create a new loan then that $400,000 will float. We are already seeing a suburb-by-suburb corrections in some areas within greater Sydney, and for many people who invested early that $400,000 uplift may have already slipped to $350,000. It's still a healthy profit, but unless the money is locked in it can decline as it floats with the market.

Continuing with this example, if you wanted to borrow on the equity of $350,000, you have to usually consider an 80% LVR. (This assumption is based on you having the income to support the loan.) So let's go ahead and lock in your equity at 80%.

Let's assume you have an existing loan at 80% LVR or a $320,000 loan on the property you bought many years ago in Sydney for $400,000. Now it's time to push the equity button, increasing it to 80% of your new value (remembering the property is now worth $750,000).

> $750,000 (total new value of property) × 80% LVR = $600,000 – $320,000 (debt on property) = $280,000 (new equity position)

You now have $280,000 in accessible equity if you have the income to support the additional new loan. This can now fund many more properties, so you can become a multiple property owner. (These figures would need to be adjusted if some of the initial $320,000 loan had been paid off.)

You don't have to become a financing genius to be a great property investor, but in addition to finding a great finance professional you should have at least a basic understanding of how the equity aspect of property investing works. These are concepts that will become very familiar to you over the course of your property-investing career. They will, in fact, become second nature.

An equity example

Let's see how using equity works in practice.

I like to leave LVRs low on my portfolio. One property I bought in 2008 in Dulwich Hill, Sydney, has served me well. I paid around $415,000 for the property and had a loan on the property of $330,000. Today, that property is worth around $800,000, meaning I have lots of equity in the property. Wanting to invest further, I have withdrawn $201,000 of this equity, so my total loan is now at $531,000 (still around a 67% LVR), which is on the lower end of property debt.

I decided to buy a property with the $201,000 and planned to build a duplex in Newcastle. I invested my $201,000 into a property I purchased for $670,000. I did this on a 70% LVR, mainly due to the fact I was making a small development application and the bank liked a 70% LVR. So I borrowed $469,000 and invested $201,000, effectively all borrowed.

The duplex now has been subdivided into two homes and two property titles, instead of two homes on one title, increasing my ability to create value. Both sides of the duplex are worth $420,000 each. This means my two newly created properties are worth $840,000

collectively against a debt of $469,000 on them. My gain on the property is $170,000 and my debt ratio is sitting at a low 55%. I used $201,000 in equity to create two new properties and I added $170,000 to add to my overall wealth position and life … not bad at all.

Will I use this money? Not yet, but it is sitting there for one day when I find the right property or need another life magnet.

This example comes with my years of experience and good equity to start. The more you have, the faster you can create more exciting and profitable opportunities. Most of us can't buy real estate on a 70% LVR and do a small development straightaway, but the principle is the same. These days you can get 90% loans and offer small deposits to try to make equity on standalone properties.

Equity returns are the fundamental instrument to building a successful property portfolio. As you should now understand, you have to recycle your equity and reinvest it to maximise your results. If you buy the right properties and have a good strategy around equity use, you will fast track through your acquisition phase and own those five properties sooner. If you're just starting out, give yourself three years to recycle your equity and buy again.

Tips to finding equity

Here are some tips to help you make the most of using or finding equity:

- Buy property with great design. It's more in demand and will usually grow faster despite flat markets.
- Follow property markets closely so you don't invest in the peak and get stuck. Ride the property bull if you can find it.
- Buy in low-supplied suburbs where there is lots of demand and the town plan restricts supply.
- Buy property well. Haggle and try to get a competitive price: it will increase your ability to fast track equity release later.

- Find benchmarks of properties that are more expensive than yours nearby to your property. This allows you to leverage off their value.
- Buy at the lowest price in the best areas or the worst house in the best street.
- Add value to the property: try a small renovation or improvement, as long as it creates new value and is not overcapitalising.
- Build for profit. Try to create equity via designing and building a great home for someone.
- Buy a property off the plan in a market that is ready to grow in value. This requires a sharp eye but can be a very good way to create wealth.

A word of warning: all markets and deals are different, so always do your research on each deal. Losing money in real estate is common so research is vital.

Other equity stuff you need to know

Here are some great concepts that will serve you well on your investing journey.

Using other people's money

Yes, you can buy an investment property using other people's money, usually the bank's. In fact, you should do just that! Well, *mostly* other people's money – you will probably have to kick in at least 10% to 20%, but that just means you'll have more deposit or equity from the start.

This is why investors love equity. Property investors rarely use their own money to buy property. Often the only time you use your own cash to buy property is your very first time, and even then the government will give you some free money via first home grants. From

there, as values grow, you can use equity to buy your second and third property. Investors generally don't want to sell their portfolio; they want to get access to more money without doing so. It was because banks and lenders wanted to create more loans that the idea of leverage and equity was invented; it serves both the banks and consumers. The banks can monitor the leverage they are offering you by understanding your risk profile and your equity position over your debt position.

How to be equity ready

To be equity ready you need a plan. I like to review the equity every 12 months in all my properties. Once you have examined the numbers and feel there is some hidden treasure to unlock, it's time to take action.

A reason many people fail to use equity is they keep their financial particulars very messy. It's a good idea to be up to date with your tax returns, your payslips and all your rates and levy notices. Banks will not allow you to access your equity if you can't demonstrate good financial management, and that starts with good bookkeeping practices. Managing your personal finances well allows you to submit a strong loan application which gives you the best chance of approval. You wouldn't apply for a job without an impressive CV, so don't let people look at your finances or credit file if they are not in order.

So what does it all mean for investors?

There is one frequent theme that directs the real estate market: it is equity. It is as exciting to me now as the first time I discovered its power. The ability to use it to become wealthy is unsurpassed. Having equity commands opportunity. Equity can create deposits, which is the seed capital for property investment. It will enable you to succeed at the five cities buy and hold plan.



Want to know how?

Come and see how we do it at a Property Investor Night.
If you want to learn about strategies like these, we invite you to join us at your local investor night. It's free and anyone can join us. We'll give you some great investing tips as well as info on how to reduce your tax, pay your home off faster and where to invest. You'll also have the chance to talk to one of our expert coaches and have your questions answered.

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CHAPTER 10

PRINCIPLES FOR BUYING WELL

Becoming a successful property investor requires the same commitment that learning a trade does. You will have to study systematically, observe trends in your trade, and create activities that will allow you to measure your competence. Within any market, primary or secondary, there are indicators of the market's ability to perform. But we can also buy right to begin with and use some strategies to fast track results. (The information in this chapter must link to what you have already read. It all has to work together.)

Capital growth properties tend to be associated with higher profits. As a general rule, you are more likely to get longer term capital growth closer to economic hubs and large cities. I always ensure that I have a strong capital growth portfolio. Investing your money in growing real estate markets is your seed for future prosperity. As discussed, the profit or equity you gain in buying growing assets can become a liquid line of credit, so you can actually maintain the cash

flow of many pieces of real estate in a portfolio for years and still have capital to invest in more property.

Some great ways to buy real estate

Let's look at some great ways to buy real estate well. There are four methods that I love to use regularly:

- **Buying well** – getting a discount on property and finding benchmarks.
- **Renovation** or **rejuvenation**.
- **Paper profit**.
- **Pre-construction real estate** – building and designing for profit.

Let's dig deeper.

Buying well: discounting and benchmarks

Discounting is as old as commerce itself, the last three thousand years being a mixture of opportunity and adversity. Property discounts follow such a formula: take an existing property, understand the true value of the property and the motivations for the sale and find adversity, and you're sure to find opportunity and good property profit.

Important to discounts is finding benchmarks. Benchmarks are properties that are similar to the one you are considering but are more expensive. This may mean you can just pay the advertised price for the property, knowing other properties in the area are on the market or have sold for more already, meaning you have found yourself a good deal.

Properties can be discounted for many reasons, including a death in the family, divorce, or distress from financial problems.

Getting a good deal in real estate sometimes follows the idea of the six Ds:

1. **Divorce:** couples breaking up can provide fast tracked sales and better buying.
2. **Death:** families usually want to settle estates quickly, which can lead to good buying.
3. **Dummies:** many vendors don't see the potential in their own property and/or sell at the wrong time.
4. **Developers:** developers are always good to try to get a deal from.
5. **Deadlines:** properties struggling against deadlines usually mean price adjustments begin.
6. **De-bank:** people stretched and facing economic hardship often sell for a discount if they need to fast track a sale.

Finding benchmarks is a great way of ensuring you are buying well in your chosen suburb. Focus closely on the suburb and find properties that have sold well and then simply buy better. Benchmarks provide evidence of sales and increased prices, so they are very important. In real estate there is a phrase 'worst house, best street'. This is a long-winded way of saying 'benchmark'.

The real estate market often exposes investors to a mixture of new property and old property. Investors are often perplexed as to what to buy, new or old, and what variations exist. There are two benchmarks you can find and then compare. One is a new benchmark – a newly built property in the area – and one is an older style property – old homes in the area. Beating both benchmarks is a winning property move.

Renovations, rejuvenations or banking on change for the future

A lot of renovators prefer older properties. Personally, I find them more costly and risky to renovate, and often a unicorn to find. We have all heard stories of an old property bought for a massive

discount and flipped for huge money in three weeks. In truth those deals are hard to find, although they are out there. With older properties renovations tend to get tricky, and I'm just too time poor to get involved. I prefer properties around seven years old to renovate or cosmetically improve. I often bank the potential in properties, knowing I can maximise profits later if the property has good bones.

Older properties tend also to be low yielding as they can be in a poor state at purchase. They take longer to renovate, often need major works and extra certification to become energy rated, and they do not get great tax benefits from gearing. Overall, I leave renovating older properties to people who carry a trade. They often swap being paid to work on other people's properties to DIY or project manage their own renovations – a win for the right person.

I prefer properties with good bones and that are a few years old because they have good rents, good tax benefits, can be renovated quickly (usually it's just redesigning), and I can manage them while doing other things that make more money for me via my normal job. I like renovations that are more about design than building permits, things such as new flooring, new lighting, new kitchen benchtops, and adding better window coverings, tapware, gardens and decks. I love creating indoor/outdoor flow to a property, and have found over the years it's a fast way to improve the living experience for my tenants, push rents up, and get better value from the property.

Rejuvenating for profit is a great way to chase down higher priced properties in your area. Find benchmarks that look superior and redesign your property to match and compete. Every property I buy goes into this pool for the future. If benchmark sales happen and markets move, I know my job is simple: chase the benchmarks with new design ideas and redesign my properties accordingly.

What does that mean exactly? Take a property that is inferior but with a solid base and spend some extra money redesigning or renovating

the property to hit new highs. This gives you a way of creating equity, and banks will consider that you now have a superior property for the area and match your value to the more superior properties. Making equity from rejuvenation is about taking a good property with the right fundamentals but that is considered inferior within its suburb based on its age and look and giving the property some TLC to get it into the superior price range of properties in that area.

Let's assume you buy a property that is basic but new and still good quality. You hold it for a few years, and watch superior properties that are new hit the market and resell for much more. After all, people want the good properties and will pay a premium for them. This then allows you to unlock your property's potential and upgrade using simple elements. (Every property you own is at some point going to need an upgrade.)

It is widely assumed a bank is where you safeguard your cash and receive a small return. Banking property for renovation, redesign or rejuvenation later is no different. It can take a few years to unlock, but with a sharp eye and in the right area it works every time. With a new supply flurry of properties hitting the market it can be a great way to make money.

Remember, generally speaking, units, townhouses and houses that are less than seven years old are perfect to rejuvenate with a mild renovation. Sometimes it is about owning them for seven years and getting all the benefits that new properties have, such as structural warranties and tax incentives. In a flight to quality environment properties built after yours tend to be more attractive, particularly over time. The property that you buy today may well be a prime candidate to chase down a superior property five years from now. This may mean upgrading your inclusions as the core part of your buying plan to improve the value and desirability and/or resale.

What you could focus on as a suggestion list, by way of example, will be discussed in great detail in the design chapter later in this book.

Paper profit

This plan might seem a bit too simple to be true, but it works. I call it adding **paper value**. There are many blocks of units and townhouses in the market that are still all owned by the one owner and are not yet strata titled, with lots of land that can be subdivided and two or more properties created. I mentioned a paper profit property that I achieved in the equity chapter, where I described creating two titles on a duplex. The profits came via titling.

The idea is to negotiate and control a property that's on one title. You then get the council to 'stamp it' and approve new titles, then it's worth more money because you own extra titles compared to what you initially held.

Anything requiring a development approval can carry risk, and you do need a higher deposit to play the game. I always recommend to people that they should have at least a handful of properties as a minimum, and have owned them for a while, before they develop or play with paper profits. It's a harder skill than to buy and hold, and a good 'buy and hold' plan is a must. I've met so many developers who have boomed and busted with the market, and so many who have risked it all on a project and ended up with no property and broke. It does seem silly to me. If you are going to be involved with this approach, make sure you have some money to fall back on, are well funded, can handle the basics of a 'buy and hold' portfolio first, and are willing to handle losses.

As you become more skilled as a property investor, trading and developing real estate can become a passion.

Pre-construction real estate – building and designing for profit

There are a few ways to handle pre-construction real estate.

Off-the-plan purchases

The first is **off the plan**, which is an 'add value' idea. By entering into a contract to buy a property that is not yet built, you gain time up your sleeve. Imagine you liked a property that was finished today and suggested to the vendor that you wanted to delay settlement for two years. This would and could work in your favour as you can save more money, you get the time in the market to plan your life and finances, and you get time in the market for values to improve or even take off. A delayed settlement is a similar principle to off-the-plan purchasing. However, be aware that off-the-plan purchasing requires a sharp eye around the pedigree of who you are dealing with, and timeframes can be unpredictable.

Off-the-plan transactions occur because of a need to eliminate debt risk for those involved. Developers are required to provide the bank with details of the sales of their development prior to receiving funding from the bank in order to be granted construction money. These off-the-plan purchases guarantee the bank that the market will buy out their risk and so they are not gambling on the back of the developer's project.

Developers must meet a presale target prior to the banks offering money to develop the property. Buying from the wrong developer can be problematic because they may not reach this presales target and the property won't be built, and sometimes this means you will miss out on a great opportunity. A proven development history of the developer is key to avoiding this issue.

We, as investors, can apply this add-value idea to create equity by using the market and 'time' as our add-value function. I like off-the-plan deals as they can provide great leverage for a small amount of money as a deposit. Generally, a developer will need a deposit of 10%, so let's say we are buying a property off the plan for $350,000 (in a good location and in an upward market cycle); we will need to put

down $35,000 as a deposit to hold the property now, however it could take years to construct.

For example, if we were purchasing a property right now off the plan at $350,000, a 90% loan of $350,000 equals a $315,000 mortgage and $35,000 to the developer, plus $15,000 for costs. This means we are spending around $50,000 in total to get going. However, if the project is to take 18 months to build and settle, and we are savvy to the market cycle, the property may increase in value by 10%, which is $35,000, to an end value of $385,000 in that time, and we have had zero mortgage costs.

I do recommend to people that they should consider negotiating a deposit that can be invested at bank rates during construction. Holding your money at bank rates or better when you don't have a mortgage can bear fruit. I recently invested a 20% deposit with a developer at 5% interest, which is better than my bank. I should make close to $10,000 during construction.

With off the plan you may have to wait 12 months after settlement to then look at the possible new value and equity withdrawal. I prefer an 18-month construction period. In total, 30 months should have passed, and you have a good chance of gaining equity from your property if you bought right. Meanwhile, you could have saved more money yourself as two-thirds of the ownership period is under a term where there is no mortgage.

I look at off-the-plan transactions as a delayed settlement and use some of the advantages associated with this. Governments also assist first-time homeowners and investors in some states with off the plan as they offer stamp duty concessions and grants. I measure the success of off-the-plan transactions over three years, and have had very good equity gains using this form of buying.

Housing estates

Another popular method for securing an investment property is to buy in a new housing estate that is yet to be completed. This strategy consists of purchasing a house and land package, and is often known as **building for profit**.

Although a house and land package is an excellent way to acquire a residence as well as a plot of land, not all of these packages are ideal investments. Every piece of real estate you have interest in will need to be heavily researched.

The principle behind examining a house and land community is that investors need to find the best property and estate from which to extract value, so let's examine some of the variables we need to consider when looking at these packages. We fundamentally want to design a great home; not the worst and not the best but somewhere in the middle. We want equity to come from benchmarks and the lack of land.

When considering a house and land package, look at investing in premium localities and high-quality estates (often known as 'blue chip' estates). If you do not locate a house and land package in one of these areas, do not consider the cheaper estates of the area. The cheaper ones suffer the same flight to quality issues we discussed earlier in chapter 6.

A new house and land neighbourhood or suburb may be made up of several estates. As the state government releases land, major developers, who have been waiting for the zoning changes, dominate the landscape. These big-time developers then allow smaller developers and builders to control land in their estate and sell the properties accordingly.

To minimise their risk, some major landowners will sell to developers who sell only to investors, which then creates a community of

tenants rather than a house-proud neighbourhood of owner-occupiers. This often creates a poor-looking and non-family environment, which can minimise your profit potential. You should buy in areas where landowners and developers are targeting owner-occupiers, and will only sell limited positions in their estate to investors, in some cases less than 10%. These are great estates to buy in because of the upside of a house-proud community that will take better care of the area than tenant-driven areas.

House and land packages are also often released in stages so that the developer can attain higher profits. The first release will generally have the lowest entry price point, whereas the last release will most likely have the highest price. The major difference when purchasing house and land packages with developers that are catering to owner-occupiers is that land is only released when the developers know they have more interested purchasers. This tight control of land usually sees prices rise year on year.

Predominantly owner-occupied estates with limited investor owners will have not many tenants living in the community. However, tenants love living in these communities and will often pay more rent weekly to the owner than in neighbourhoods that have a greater investor influence and where everyone is a tenant. The desirability of the estates drives up the rental return. Rental returns are a significant factor in the investment success of many areas. If yields are high, growth usually follows.

Not all housing estates are created equal. Well-planned infrastructure focuses on underground power, lots of green space, and facilities such as supermarkets and day care centres. They all add up to explain why one housing estate will be a success and another will not. Good infrastructure leads to gentrification, an important principle discussed later in this book.

It is also important to use a proven builder with a successful track record. Too often, investors engage a less expensive builder only to have their project delayed, costing them both money and opportunity. New homes come with a warranty of six years, so you will need to engage a builder with a long-tail approach to business, rather than a less expensive alternative. Less expensive builders can't get the right tradespeople, have terrible systems and deliver poor experiences.

How can you make money from building such a home? Here are the factors at play:

- **Annual average increase in build costs:** The cost of building tends to rise. This gives new homes the ability to develop equity as other new properties in the area come to market slightly more expensive as time goes on.
- **Low entry point against benchmarks:** Buying a good home near more expensive homes allows for equity to be chased down in the area.
- **Pricing increases stage by stage in land developments:** In good areas land is released in stages, and often at more expensive rates with each new release. This allows for the land in the area to increase in value, creating equity.
- **Build rate and terms, and building deductions:** If you negotiate with the right builder with the right pedigree, you may just get a better than market build rate and terms. This can mean paying less and building more quickly than the market, both great for creating equity.
- **Stamp duty:** You typically only pay stamp duty on land, not the build, so you are already up by not spending equity on at least half of your total purchase.

So what does it all mean for investors?

When you are putting your investment plan into place, consider these issues and learn from the great examples of the past. We are

not reinventing the wheel in what we are doing, but we are following cases from the past to better our future. These value-add ideas are simple but when understood they are very successful methods of fast tracking success in property and wealth.



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CHAPTER 11

UNDERSTANDING DESIGN AND PROPERTY GROWTH

It's a common misunderstanding in real estate that growth only comes from the property market and its growth drivers. Beyond this concept – for example, the idea that Perth, Melbourne or Hobart will boom and you can catch the wave there – are other ways to make money from real estate.

There are four forms of capital growth in property, which we will discuss over the next four chapters. They are:

- property growth (dwelling value movement)
- area growth (location performance)
- market growth (broad base market movement)
- over market growth (achieving better than the market).

Growth from property can come from the property itself if it's the right type of property, because if it is then it's usually in demand. Location also has proven itself to provide growth. Some suburbs periodically grow more rapidly than others, and can actually grow in even a flat or falling broader market. In other words, some locations defy trends. For example, you may see Sydney fall slightly in

percentage terms in value on a broad scale in 2017 or 2018, but this will occur after many years of strong growth. Despite this, certain areas or suburbs within Sydney will defy that trend and stay firm or possibly grow in value, as will certain dwellings.

Beyond the macro market and broad-based economics, extra rewards from property come from one day selling the property for above its true worth or above market value.

Using all four of these growth elements to buy and own real estate is very powerful. I call this my '**4 × Plan**' for growth.

Understanding property growth in today's market

So how is individual property growth achieved?

We discussed the principles of buying in the previous chapter; for example, off the plan, which allows us time in the market (an add-value concept), or building for profit by designing your own individual profitable property to encourage the market to see your property as worth more and drive price improvement. However, property growth these days comes predominantly from the style and character of the property, which I'll talk more about soon. At the end of the day, you can't just rely on the broader market to bring demand to you. You have to entice demand as well. Property growth is governed by the law of attraction. Often the best properties that are growing in our economy are beautiful and in keeping with the ambience of their location and their environment.

Property growth today is about delivering on every detail and getting results. People will pay a 10% premium for the right property in real estate today; your job is to buy the right property at a great price.

So what am I looking for within an investment property? I'm looking for a funnel that makes me money. I want to put a great property at the top of the funnel that one day spits out the bottom of the funnel and sells for a handsome profit. No real surprise.

Drilling down, what are the important factors that drive people to a great property, given that we are now in a tale of two markets: one an oversupplied, poorly designed house and unit market, and the other an undersupplied, well-designed house and unit market.

How to we spot a great design?

Choosing a well-designed property

As I've mentioned previously, when it comes to property today, the demand – and therefore the potential growth – is in good design! So what should property investors be looking for into the future when choosing a property?

- The living experience and quality of life for the occupant has to be the number one priority as it drives emotion, and emotional buyers are willing to pay more for properties.
- Numbers are important, but you need to tie your purchase to an eventual emotional buyer and what will be important to them as a homebuyer. This drives decisions and action for an owner-occupier. Great yields don't necessarily translate to a great property.
- Design and amenity need to be first rate. This removes alternative choices for the buyer.
- If the property fits the bill it should be easily sellable at auction or quickly by private treaty; that is, it should be highly liquid. This removes uncertainty for an owner-occupier buyer and creates 'fear of missing out' (FOMO), bringing a higher price to the investor.

So what are the key design ideas for buying a successful property, and how do you even gauge what success looks like? There are seven key design principles to understand:

1. **Pedigree:** A great architect and builder/developer.
2. **Space and/or volume:** Internal floor plan/flow, and frontages.

3. **Daylight, lighting** and **ventilation**.
4. **Quality inclusions:** Fittings and fixtures, or the ability to easily upgrade or adapt.
5. **Outdoors and outlook:** Outdoor space and aspects such as a view.
6. **Amenities:** Within the property and/or local walkability.
7. **Parking** and/or **storage**.

Let's look at each of these.

1. Pedigree

Poorly constructed buildings and those that are made of poor-quality materials struggle to attract resales. Properties can become old fast if they are not designed well; the best new properties in current terms are built properly and developed by long-term, responsible developers who care for the public realm. Today, great properties that tick all the boxes with design benefit from experienced architects, builders and developers.

I liken the current inventiveness of the best property teams to being the Teslas of property. Tesla is not just about cars, it is hope for a better world. The best construction teams today look at property like Tesla looks at their cars; change the world through design and energy and add value to the public realm, don't take away or pollute society with rotten property. I mean, how many homes and apartments have you walked past and seen them as an eyesore? Properties that have no pedigree are in my view property pollution.

It is a fact that buildings, apartments, homes and floor plan designs that have won awards hold and increase their value better than properties that have not. In fact, when tracking performance of award-winning real estate, there is evidence that such properties have increased in value faster and more than other properties, despite market conditions. Society now rejects ill-conceived ideas. The new wave of property success is only working with the best.

2. Space and/or volume

Today, property is being built smaller than ever before. Town planning guidelines restrict bigger lots as impracticable. As a result, it's harder to get larger units or homes, and consequently volume is more important for investment properties. Volume and height is really the next phase of property, not so much overall size. For example: 2.7m+ ceilings for a unit and 2.8m+ for a house can create great space and volume for a home – the higher the better.

Too many investors buy property not knowing what makes a good design. There are a lot of aspects involved. Total living area is an important consideration for both indoors and outdoors. Good design ensures efficiency in the floor plan and reduces wasted spaces, such as large hallways in units. Frontages of both homes and units should be wide: 6m minimum for a unit and 10m minimum for a home, depending on if you are building or buying a cottage or house, so that it doesn't become narrow and confined.

Many parts of Australia are warm and so people want to spend time outside, so understanding the indoor and outdoor flow of a property is worth looking into to ensure the living experience is at a high standard for your occupants.

3. Daylight, lighting and ventilation

It's no secret that few people want to live in a dark home, so of course light is a key selling point for property. Whether it is direct sunlight, daylight or design-inspired lighting, it is a critical factor to consider when deciding on a property.

Lighting and ventilation can be maximised with the following:

- Floor-to-ceiling windows can change the dynamics of a unit or house based on the amount of natural light washing through the property.

- Well-placed downlights are a modern way of bringing appeal to a property and more light to typically dark areas, as are skylights.
- Windows and doors that can open widely – such as bi-fold windows, or doors or louvers to create natural ventilation – are sought after by buyers and transform smaller spaces into open spaces. Every property I buy, be it a house or an apartment, gets bi-fold doors to transport light and air.

4. Quality inclusions

Investors often overlook fixtures and fittings, yet for owner-occupiers fixtures and fittings are often the reason they buy a home to live in. Fixtures and fittings are items that are fixed to the property or into the grounds of the property – pergolas, built-in barbecues, lighting fixtures, taps, stoves and blinds are normally included in the sale. They will remain on the property after the sale and form part of the overall purchase price.

People love to design and construct comfort, and if you have adaptable appliances that look good and are reliable and provide comfort, you attract more value and better results. Many owner-occupiers want a nice property; after all, they will be paying a fair amount to live in the property in our bigger cities. Gone are the days you can put an air conditioning unit on a 6 sqm balcony that no-one can then use, or not offer adequate kitchen space or storage space for residents.

One of the challenges we have as investors is we don't typically want to spend $2 million on a property, so we have to find a balance. More often than not, success is about building a property portfolio with assets starting below $500,000 and watching them grow. Nevertheless, it is still possible to buy good inclusions.

Here is a list that may help you identify desirable fixtures in your next property:

- ducted air conditioning (with condensers on the roof or in a car park, not on a balcony)
- modern ceiling fans in all living areas and bedrooms
- full stainless steel kitchen appliances, including dishwasher
- separate laundry, or laundry in bathroom with concertina door set-up at a minimum
- porcelain rectified tiles to living areas, porch and alfresco areas
- 20mm stone kitchen benchtop at minimum
- dual kitchen sink recessed in stone top
- designer tapware, pull-down/swivel tap in kitchen
- bedrooms separated from living areas where possible, or separated by wardrobes
- mirrored robes in all bedrooms
- well-designed shelving, hanging robes and drawers in walk-in wardrobes
- linen cupboard(s) for adequate storage
- study nook where possible
- U-, L-shaped or island kitchen at minimum, with adequate overhead cupboards, including above fridge
- water point in fridge space
- soft-close drawers in kitchen
- full-height tiling in bathroom
- recessed shelving in shower
- stone benchtops on bathroom vanity
- wool blend carpet
- wooden floorboards, or laminated timber-look flooring at minimum
- tiled wet areas and connectivity to dry areas
- storage cage for units, or extra shelving in garage
- window dressing – quality blinds and/or curtains

- dual-flush toilet suites with ceramic cistern
- two-heat lamp/light/exhaust in bathroom and en suite
- extra soundproofing
- smart technology.

And here are some 'X factor' inclusions, to really attract buyers:

- built-in wine fridge
- outdoor built-in BBQs
- outdoor built-in seating and decking
- 40mm stone island benchtop
- 900mm stainless steel canopy range hood
- pendant lights
- feature lighting.

5. Outdoors and outlook

It's important that your investment has some appeal, including usable space, from a nice garden or deck to a great terrace or balcony that adds to the living experience of the occupants. Views – such as of a park, city, waterway or garden – are always great for owner-occupiers. Large balconies or terraces can provide a sense of space, as can a yard.

If you have an outdoor area, make sure you use it well and landscape it. Too many investors underutilise their yards and wonder why people see their house as inferior. Apartment balconies are also often poorly utilised. You can easily add value by creating a breakfast bar to allow people to enjoy the space as a living area, or installing built-in seating that creates a nice quiet corner. The balcony should be considered a room of the home.

6. Amenities

Good amenities nearby is a plus for attracting buyers on resale. Having transport, cycle ways, shops, schools, cafés and entertainment hubs in close proximity can add a lot of appeal to a dwelling, and

is one reason why many people choose to owner-occupy a home or unit. Location is something you cannot change in real estate – it goes hand in hand with the property you buy. Due to the lack of good public space in city landscapes and increasing populations, we are often forced to entertain ourselves within the area we buy in, so bear in mind the need for good amenities close by (but even better is good amenities in the home).

For units, properties with internal amenities such as pools and sundeck areas are becoming increasingly popular and attract buyers who want to have a good lifestyle and living experience. Great amenity within an apartment can stem from simple ideas, such as deluxe interiors, a butler's pantry, dual vanities and plunge bathtubs, study areas and walk-in his and hers wardrobes, or extra storage. Modern buildings are very energy efficient, and the cost of incorporating such amenities is dropping.

As well as the above, amenity within houses could also include media rooms, separate living and dining areas, or even space down the side of the house to park a boat. Houses are about creating lifestyle in every corner of the home, from shelving in the garage to a lemon tree in the backyard. A house needs to be a home, not just a dwelling. Great areas also have lifestyle features nearby, from parks to shops to recreation facilities to good schools.

Here are some 'X factor' amenities for units:

- temperature-controlled wine storage room
- function amenities, such as bookable dining areas
- integrated restaurants and cafés
- cinema rooms
- concierge service
- green technology (which can reduce levies)
- rooftop gardens.

Here are some 'X factor' amenities for houses:

- external deck, porch and/or alfresco areas
- built-in BBQ or external wet kitchen
- landscaping
- swimming pool with cabana.

Buy a property that stands out from the crowd, is well designed, and takes into account the lifestyle choices of its occupants. After all, people pay big money to live in well-designed property, so as an investor your primary focus should be desirability.

7. Parking and storage

For owners seeking a property to live in, one of the most significant considerations is parking. In an era that may see us soon use our cars less or opt to car share, it is still important to have safe, reliable and close access to your vehicle. I like to cage my car spaces in apartments, which is usually an extra cost, but it creates a private zone and a 'shed effect', which, of course, is another space to use, usually for a male occupant. Sometimes this requires owners' corporation approval, but this is generally not a problem.

In all homes, houses, townhouses and apartments, storage space is important both inside the home and in areas such as car bays, storage cages and garages. Properties that resell well have good storage access and lots of spare space for unused items.

So what does it all mean for investors?

Trends towards new designs and amenities have come a long way. In the 1950s homes were built to cater to families, and construction costs were kept as low as possible. Less thought was given to lifestyle; homes were built very similar to each other, which is why we have terms like 'the burbs'. In the past a typical home was a rabbit

warren of rooms. The home was about separation and privacy; life was a series of compartments.

Many older properties are box-style rabbit warrens based on old design principles, and need significant renovations to open them up. Perhaps a black hole renovation!

Living principles were very different from today; now open-plan fundamentals dictate results. Remember, growth is about good design for today. Our job as investors is to provide the occupant with a great living experience that gets great rent and capital growth, and that can be understood by a buyer in a heartbeat when you want to sell. Changes in design since the 1950s focus on the indoor–outdoor flow and connectivity that is desirable today.



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CHAPTER 12

UNDERSTANDING AREA GROWTH

There are so many suburbs and towns to choose from when buying property – how do you know where to start? With over 4,000 possible suburbs at our disposal it can get very confusing.

Getting capital growth from an area is about identifying a suburb to buy in that has a plan. Area growth is about your location being hot property in its early years and in the medium term, regardless of the broader market conditions. You are not, for example, focusing on just buying in Brisbane because reports say Brisbane will boom – *where* in Brisbane should you buy?

Secular market trends

To find a great location to buy real estate within, we are looking for what is often known as secular or independent marketplaces. Here we will find area growth, as part of the 4 × Plan. So what is a secular market trend? These suburbs are part of the broader market but have their own unique fundamentals. It is a market trend associated with

some characteristics or phenomena that is not cyclical or seasonal but exists over a relatively long period and is confined to a certain area. This is what we are looking for as investors. A secular market is its own phenomenon. If an area is desirable and it is indeed a secular market, capital growth will occur.

Most of the property market plods along and, as we have learnt, the average property is taking 13 years to actually double. By identifying secular markets, we are finding suburbs that can grow faster than the median growth rate and broader marketplace. This means your property investment may actually double in 8 years or 10 years and not 13 or 15 years. Location is an enormous principle of being a successful investor. Once you own a property, you can never change its location. Choosing a great area and a suburb that will grow faster than the norm is also known as looking for micro suburb growth.

Secular markets are areas that are tactically interesting to property investors and can be identified in town plans. Five attributes that I look for that can lead to secular markets and micro suburb growth are:

- urban renewal and inner urban gentrification
- gentrification of planned urban edge land (planned land)
- NIMBY suburbs
- rare pockets
- aspirational middle ring (suburbia).

Does all this sound confusing? Perhaps you have just read some terms you have never heard before? Well, read on and we'll delve in deeper.

Urban renewal and inner urban gentrification

The idea that an area can be considered an ugly duckling and then be recycled and improved is a proven winner for investors. Every city has pockets of cultural urbanism where change is coming and is impacting on its inhabitants. These are fantastic areas to invest in.

There is a slight difference between urban renewal and gentrification. Urban renewal begins with the government and developers working together to rezone urban areas and change the use of an area from, usually, commercial or industrial to residential. Urban renewal also starts with infrastructure upgrades, with a drive towards mixed-use development. In the early stage, urban renewal is often a blank canvas as the area concerned may carry a stigma and not be well received by the wider community. For savvy investors, this can be a windfall.

A town plan will show you the future urban renewal initiatives that will be occurring in a suburb. It's important to look at these areas with an open mind. There are so many examples of industrial areas that we once thought were undesirable but have quickly become fashionable and have become spectacular investment neighbourhoods. Some examples are Collingwood in Melbourne, Redfern in Sydney, and Teneriffe in Brisbane. Such areas show the extensive impact of urban renewal.

If an area is slowly starting to change but hasn't yet been fully transformed, it is a good time to see what opportunities are available. Don't forget that real estate saying: 'It is better to buy the worst house in the best street than the best house in the worst street.' And there is also a second saying you should keep in mind: 'It is better to buy into a suburb that is a blank canvas rather than into a suburb that is already a Picasso'. Meaning, if any area has well and truly grown and blossomed, you may be too late.

Developers and governments spend billions of dollars on infrastructure each year to open up significant urban change. They provide roads, schools, hospitals, transport, and commercial and office infrastructure to address the needs of the community. In doing so, the government and developers reshape and redefine the planning requirements of both the state and local government areas. You will find good investments if you can locate where infrastructure spending is being directed. Urban change works as it brings growth.

The idea of this is that the change in the neighbourhood brings a better socioeconomic income group to an area. In attracting higher incomes to a zone you often see a correlation in price growth.

Many inner urban areas also see gentrification. First, let's define the term 'gentrification'. It usually starts with a story of urban decline, followed by changes in a neighbourhood, driven by desirability and location, that then see an area emerge and become highly sought after. This is often led by the determined middle class at the expense of a lower class or economic group. Gentrification within property is the process of upgrading an area and making it in vogue. (The word 'gentrification' is of course based on the word 'gentry', which means 'people of good social position'.)

The stages of gentrification

Today's reality is that urban development and eventual gentrification, often led by the middle class, take place in stages. Gentrification is now a well-trodden path, and we now have enough examples to think about the phases of neighbourhood change that could result in gentrification. The stages work in order and may occur over 10 or 15 years:[1]

- **Stage 1 – Grassroots-level organising:** Residents engage in cleaning up their streets and begin to hold public officials accountable to the community.
- **Stage 2 – Planning:** Policy makers become involved in actively developing community-betterment strategies by working with businesses and developers explicitly soliciting change.

1 This list is based on stages in an article by David J. Maurrasse and Jaclyn B. Bliss, 'Comprehensive Approaches to Urban Development: Gentrification, Community, and Business in Harlem, New York': http://scholarlycommons.law.northwestern.edu/cgi/viewcontent.cgi?article=1008&context=njlsp. Step 8 is my own addition.

- **Stage 3 – Pioneering development occurs:** New residents begin to move in and a few new shops appear; real estate prices begin to rise.
- **Stage 4 – Intensive investment:** Policy makers, businesses, new residents and developers intensify their investments.
- **Stage 5 – Population shift:** Demographics and businesses are noticeably different, and the previous culture appears out of date.
- **Stage 6 – Displacement:** Fewer and fewer low-income residents can hold onto their rental apartments and/or long-time residents have sold their properties.
- **Stage 7 – Full transformation:** The old neighbourhood is largely unrecognisable; most residents are of the newer population, their culture dominates, and most businesses cater to them.
- **Stage 8 – Turbocharged gentrification:** The upper class buys into the neighbourhood, pushing values to an extreme.

Gentrification is for the medium term. The best investment zones are from stage 4–5 all the way through to 8. This is where we get the best results and valuations. It is also important to consider how quickly gentrification is moving.

Slow gentrification

As mentioned above, gentrification is the idea of improving an area, increasing its desirability in the marketplace. A great example of slow gentrification at the time of writing is Heidelberg West in Melbourne, a housing commission area that is now going through gentrification and change very slowly. It may take over 10 years to gentrify, but it's next door to ritzy Ivanhoe, where properties command multimillion-dollar price tags.

The simple idea of gentrification is to find a fairly rundown area where local aspirational residences go through a period of restoration that actually leads to lower-income people leaving and a new demographic entering the market. For instance, Tribeca (in New York) and Chelsea are good examples; 20 years ago you could have bought an entire city block for a $1 million in those areas, but now you cannot even afford an apartment on that budget as these neighbourhoods are so in vogue.

In Sydney, for example, this has also happened in the inner west. Balmain – which 30 years ago was mostly occupied by working-class folk – now has homes that are worth millions. The area is home to Sydney's 'chardonnay millionaires' who have long since bought up the area. Gentrification brings a new vibrancy that changes the landscape of people, habits and housing. Remember, we are looking for an 'ugly duckling' that may just go through dramatic cultural and economic change.

Turbocharged gentrification

Turbocharged gentrification occurs with an influx of affluent residents after significant change has already taken place, whereby there has been an exponential increase in values and an area is seen as in vogue. This stage can mean the involvement of more wealthy buyers. This final wealth bracket can lead to an accelerated rise in values. Bondi Beach, Sydney, would be a good example. It's now the playground for the cash rich, it's gentrified and it's great – if you can afford it. The rich are willing to pay high prices for property there, and that has an uplifting impact on investments bought well before they came along and 'turbocharged' price growth.

Brisbane's inner northeast suburb Teneriffe would be an example of an area heading towards turbocharged gentrification, sitting as it does between 6 and 7 in its gentrification stage. It's unrecognisable in many parts to long-time locals. Vibrant retail, living and

entertainment precincts are replacing industrial decay. Derelict warehouses are now stylish apartments or craft beer bars. New public spaces and bike paths follow the riverfront where old wharves once lay idle. The abandoned former powerhouse has become one of the country's hottest arts precincts, an icon in the landscape alongside landmark buildings featuring cutting-edge subtropical design. Yet Brisbane's inner northeast remains a diverse and inclusive community. The area has become Brisbane's premier cosmopolitan, commercial and entertainment precinct with the iconic James Street. The city's most sought-after urban living communities are now here. This area is almost seeing a full transformation and the commencement of turbocharged gentrification. Apartments over $2 million are very sought after by locals.

If you can buy into an area going through some form of renewal or gentrification and change, you are using a very pertinent medium-term tactic.

Gentrification of urban edge land (planned land)

Gentrification of land sees often semi-rural properties replaced with new residential subdivisions (planned land), and it is a great way to make money on real estate that is released tactically by governments and landowners such as publicly listed development companies. Unlike apartments, not too many land estates in urban sprawl areas are owned by anyone but major players. These land parcels are released to the market based on demand rather than the need to develop supply and find buyers thereafter. Typically, we see well-planned and staged releases of land at the edge of the urban growth zone and in designated areas of affordability; this is driven by a desire for a bigger population base to sprawl to these areas.

One potential frustration for investors with planned land is that it is often hard to get registered land to buy as the demand outweighs the supply. Registered land is land that is titled and ready to activate or

build on. Planned land is always strategically released and not flooded to the market, so more often than not unregistered land is parcelled and buyers need to look at land off the plan before it becomes registered. In parts of Melbourne today homebuyers are waiting 18 months for the right block of land to become titled and be available to be built on. Many new homebuyers are then entering contracts to design their dream home, which is often taking another nine months to build. A very long process all up.

Land is in short supply in our cities. For example, in the northern corridor of Melbourne it is indicated by the many home builders that provide homes there that in 2017 there are fewer than 45 registered and titled blocks of land available at any one time for would-be buyers to settle and then build their dream home. Not many at all! With 4.5 million people in Melbourne it's a serious imbalance of registered land.

Thus land is great and has continuous growing demand. One could argue that the tight control of land release drives prices up and is thus a monopoly for the large firms that do it, which evidently contradicts the idea of opening up greenfield areas to help with affordability. Who wins? Property investors and the companies who use the practice!

Not all land is created equal on the urban edge of our big cities. The reality is most land is disconnected from the city and transport and lacks a real economic underbelly. The three major concepts to consider finding great urban edge land are:

- Land sprawl based around good amenities and transport nodes is good sprawl, as opposed to land that is not connected conveniently to services or transport and is only land that you can get to by car. This is the bad sprawl as discussed earlier in the book; disconnected land should be avoided at all costs.

- Good urban edge land gentrification that is well planned can be linked to one day being swallowed by the broader city. Effectively it means buying on the city edge today and waking up in 5 to 10 years and seeing that the area is now not sprawl but actually part of the middle ring of property in suburbia. People see value in suburbia and will pay big money for a home there.
- When considering a house and land package in an urban edge pocket, look at investing in premium localities and within estates often known as blue-chip master planned communities. If you do not locate a house and land package in one of these areas on the city edge, do not enter the cheaper estates just to win on price. Urban edge land areas are made up of several estates. You may find neighbouring estates are very different. Most are full of homogenous property; many lack good covenants to protect the neighbourhood and are seemingly on their way to being poorer communities where people struggle to pay the rent.

We are looking for estates that have a sense of community and lots of owners living within the community. Many urban edge estates are not house-proud neighbourhoods full of owner-occupiers, rather they are tenant-driven estates. This often creates a poor-looking and non-family environment, which can minimise your profit potential. You should buy in areas where landowners and developers are targeting owner-occupiers, and community spirit and planning ahead are high on the agenda. Establishing a community for the long term can include providing schools, offering public safety planning with CCTV in estates, running a community newsletter that brings residents together, cafés, restaurants and shopping precincts, and residents' clubs and sporting facilities. Today many of the best estates have community fees that are reinvested in the upkeep of the public realm, which is a good thing.

Some fun, fast facts on land availability

In the 2016 National Land Survey Program (NLSP) survey of new residential land supply conducted by the UDIA, these results emerged:

- The average median new lot size nationally is now 453 sqm, down by 4.3% over 2015 and down 12.2% since 2010.
- The greatest change in median lot size over 2015 occurred in Perth, which fell by 33 sqm to 395 sqm from 427 sqm in 2014, a 7.7% drop.
- The largest change in new lot price over 2015 was in Sydney, where the median price of a new lot rose by $100,975 to $440,725 from $339,750, an increase of 29.7%.
- The median price of land paid by new homebuyers nationally was $554 per sqm in 2015, up 4.9% from the previous year and up 30.9% since 2010.
- The largest change in land price was in Sydney, where the price of land increased by $228 per sqm, an increase of 30.6% over 2015.
- The largest change in lots released over 2015 was in Melbourne with an additional 6,874 lots released, up 53.3% on 2014.
- A record number of new lot releases were captured in 2015 with 55,656 new lots released, up 9.9% from 2014 and 43.6% over the level from five years ago.
- The average median lot price in Australia's five largest capital cities is now $250,658, up 1.4% over the year and 14.8% since 2010.

As for other ways of making money within planned land and urban edge land gentrification, we need to understand that land size changes as time goes on and is usually reduced to create affordability. Land prices are driven higher over time by the suppliers who are not vulnerable vendors that you would see typically in normal real estate marketplaces (that is, mum and dad vendors). Given the land

is controlled by very patient companies, it is seldom oversupplied. You may see, for example, a staged release of land being activated for $5,000 more per stage release, with four stage releases a year. This could mean $20,000 in equity for a buyer on the land parcel only. This creates inherent equity in the land, and as the years go on gives growth regardless of the overall market. This puts property investors back in control.

NIMBY suburbs

'NIMBY' is the acronym for 'not in my backyard'. So what is a NIMBY area? These areas are fundamental undersupply pockets in cities. They are hard to supply based on a town plan that has been protected by residents who have fought proposals for new developments and won.

These areas can be lucrative for property investors as they have more demand than supply and prices tend to grow consistently. NIMBY residents often believe that developments and new housing are needed in society, just not where they live.

NIMBY suburbs can be good investments because essentially they are suburbs controlled by the rich! Wealthy people like their lifestyles and they want to protect their positions, and they usually have money to argue about keeping supply to a minimum and protecting their area and investments. NIMBY suburbs are gazetted in the city town plan as low supply areas, making them amazing hot zones to invest year in, year out. Whatever the macro market is doing, they can do well. Wealthy people love making money and will position their investments in these zones as they are enclaves of smart money.

The wealthy inner zones that are typically NIMBY areas start from about 3km from the CBD and drift out to as far as the 15km ring in pockets, but can also be found further out in enclaves. The residents tend to make the rules to favour their areas and protect themselves, and they seem to get away with it based on the character of their older neighbourhoods. Restricting supply and sending it elsewhere is

smart. This creates a natural lack of stock, which leads to more property growth for NIMBY locals. Today, houses in these suburbs tend to be multimillion-dollar homes, so investors are more likely to look at apartments or townhouses within such areas.

NIMBY areas that are established suburbs – often as old as the city itself – are very hard to develop and have natural supply and demand restrictions based around culture and heritage overlays. They are often areas with early homes from past architectural periods. The areas are very much restricted by height limits; for example, they may have four-storey limitations for units to be built there, or even less. You will often find smaller unit projects in these areas, boutique in size.

Developers can still develop in these suburbs if they follow the height limits and other rules, but it is hard for new stock to come to market as these areas are generally older neighbourhoods with an expensive housing market. To actually develop, a developer has to usually amalgamate three or four expensive homes in one line and then build to a low height. This means it is very hard to develop density in these pockets, as it is often not mathematically possible for a developer to even get a project off the ground. This reduces supply accordingly, and creates a smokescreen to the wider market that NIMBYs are doing their bit. It is more common than not to see a block of 20 apartments over two levels with perfect street design in NIMBY suburbs, but you won't see much competition. Usually it's just one or two boutique developments at once – a very low rate of supply.

The natural population increases happening in Australia mean these areas will always be sought after. People aspire to live there and nest. They are often very appealing areas with a cosy appearance. I own real estate in some very NIMBY suburbs such as Armadale, in Melbourne, and Clontarf, in Sydney. NIMBY areas can be more expensive to invest in and will suffer from lack of intensive investment, but will remain sought after as usually the infrastructure has been in

place in these areas for well over a hundred years already, and they are not far from the core of what is good about a city.

How valuable will these areas be? If we consider that every major capital city in Australia will be adding another million people in the next 15 years, the answer is simple: very valuable! They are often the top of the desirability food chain within property.

Rare pockets

Rare positions or unique streets that are old established pockets within recognised neighbourhoods are very hard to develop, and the recycling of these areas happens only so often, making the real estate very valuable. Recently Millers Point in Sydney witnessed the release of properties that can only be described as rare and esteemed. Let me explain: for over 100 years, the Rocks (or Millers Point) was home to many housing commission residents who were living in historic terrace homes. The government decided in 2012 to sell the government-owned terrace homes off to the public, who duly snapped them up, a very rare release of just over 100 terrace-style turn of the century houses. This will never be repeated. These properties have gone on to double in value since their release just five years ago. The new owners of the houses now have properties that are protected and limited and will always be in high demand.

Rare areas have strong established property markets that sell well. Despite market conditions, these areas are seen as very desirable and unique. Can you imagine there are only a few hundred houses on the Brisbane River? Now that is exceptional! How many homes have a view of Manly Beach in Sydney? Not many! This infrequent real estate is always in demand because it is not part of the wider supply chain as it is exclusive.

Investors come across these opportunities from time to time in the land market. Land unused close to the CBD, perhaps only 10km out, is sometimes known as infill land, and the practice of repurposing

and selling such land is known as recycling land. As you can imagine, land that is available that close to a CBD is infrequent and finite.

Infill areas use existing infrastructure, so finding land being recycled in these areas is a remedy for urban sprawl. Sometimes very tightly held locations within suburbs such as dress circle streets are being recycled into town homes or apartments; it is not limited to just houses. Rare apartments or town homes in a unique location offering spectacular views that are never to be repeated are great property investments.

Obtaining a unique property or location is such a fantastic way to park your money in real estate. Today in my portfolio I have two never-to-be-built-out waterfront properties. I also have a handful of never-to-be-built-out city-facing properties. They are all exceptional, formidable properties, which are hard to get and rarely trade. They are and always will be in high demand.

Aspirational middle ring (suburbia)

The middle suburban ring is a smart investment zone. Suburbia has a large and growing population, good infrastructure, and is in high demand based on location and lifestyle, particularly for families.

Suburbia, which is the middle ring approximately 10km to 25km from the CBD, can be expensive, especially within the housing market inside capital cities, given the land content. But many investors would say that purchasing in an area where property is expensive and where a lot of people live is a smart approach.

Within suburbia itself there are rankings. Not all of suburbia is equal – 70% of suburbia is made up of sleepy-moving investment hubs. Much of suburbia is still rundown, lacking gentrification, and often is still cut off from prime amenities and infrastructure. It can make it difficult for investors to determine what area is appropriate to invest in.

Within suburban neighbourhoods we have five main drivers that determine growth. They are known as the belts. They are:

- the school belt
- the green belt
- the sand belt
- the ed/med belt (short for education and/or medical)
- the cultural belt (which is discussed in much detail in chapter 16).

All are driven by people's aspirations to live well. Let's have a look at these.

The school belt

The school belt is an important driver of property values that should be seriously considered by investors when building a property portfolio. Buying close to the most prestigious and well-ranked schools can have a positive impact both on rental returns and future capital growth for renters with families. Schools with a superior educational reputation have a positive effect on local property values as families want to give their children access to the best education possible.

Catholic, private and public schools all have rankings. Often by living in a certain postcode families can gain faster access to certain schools within the public system that are very successful education centres. Private schools are also highly sought after, so people like real estate close by, or close to transport that their children can use to get to the prestigious schools in a district.

The green belt

Green belt areas, sometimes known as 'green wedges', are another property value driver in suburbia. Within a city the green belt areas are suburbs that are often surrounded by national parks or protected wildlife zones that preclude over-development. They are designated

areas that provide a city's green feel. Australian cities pride themselves on looking green and having lots of trees, birdlife and green space, though some suburbs benefit from this more than others. Of course, green belt areas are often hard to supply as they are usually surrounded by bushland and can be well protected by supply policies, making them a unique phenomenon.

Green belt areas become protected and are great property areas because there are only a few of them in each city and they are very pleasant locations, making them highly desirable. Governments protect these areas for a few reasons, including their natural appeal, the recreation they offer to city residents, and the air quality they bring to a city. The green belt suburbs are usually within a 10km to 25km radius of the city. For city planners, they are a trump card against urban sprawl.

The sand belt

Australians love beaches. As such, in our major cities sand belts (or beach belts) are formidable areas to invest in. Lots of wealth is attracted to the water, and for this reason sand belt suburbs carry a price tag that seemingly continues to perform year in, year out. Many people love the idea of buying in a lifestyle community that has access to waterways. Going to the beach is part of our culture. In our major cities, beaches that are both close to the city and are culturally fun are premier investment zones.

However, the idea that *any* beach area is a formidable purchasing location is flawed. Many people choose to invest in regional beach areas as they are wonderful lifestyle areas. But most of these areas lack the simple community infrastructure for growth. They have no real drivers. These locations are not to be confused with sand belt zones. A typical sand belt area, for example, would be the beach zones starting at St Kilda in Melbourne and heading southeast for

20km, or the Northern Beaches area in Sydney that starts in Manly and ends up at Palm Beach. We are not aiming for regional beach areas, such as Forster in NSW.

These regional areas often have a real lack of growth within their local economy; the pretty beach may be only connected to a small town with, for example, a fish and chip shop and a bait and tackle store – not enough to create big growth. Sand belts only work where there is an economic underbelly; for example, Sydney's many ocean beaches are only a relatively short distance from Australia's largest CBD, with hundreds of thousands of jobs being in the CBD of Sydney itself.

The ed/med belt

Education and medical belts relate to our universities and hospitals that are significant to our cities. They are symbolic, and are a unique suburb attribute that can add to the long-term performance of the area and therefore to property in the area. Take a major hospital, for example; major hospitals are of huge strategic importance to a city. They provide employment to thousands of people and are geographically planned to sustain growth and serve the broader community. One hospital alone can employ up to 8,000 staff. It's not often that billion-dollar hospitals are closed down; some hospitals are planned by state town planners to be around for hundreds of years. Transport is then planned around them to ensure ease of use.

University areas often have an influx of extra residences based on the university itself. Larger suburban universities can attract 30,000 students to an area; the spin off effect is that the area's rental market is often a high-yielding area as the suburb's housing has less supply than the extra demand the university brings. Beyond that, universities require world-class infrastructure and transport to connect them to the broader city. Hence they are fantastic belts to buy within.

Buying in or close to the ed/med belt suburbs often means you attract a steady stream of tenants and higher yields. In these markets, often it is townhouses that we look at as the houses are now well over a million dollars. Townhouses offer land content and are not as expensive as houses, but they still offer a smaller home to an aspirational family. Ambition is an important principle of buying within the middle suburban ring.

Markets are usually cheap for a reason

A look at Australia's big cities' cheapest suburbs shows that the majority of these types of markets are not good places to invest in. These markets are usually cheap for a reason: they have social and safety issues, socio-demographic problems, and some of these locations don't have access to good amenities.

The tactics and secular markets I have highlighted in this chapter are affordable options but they are not cheap. These areas are in great demand from the buying groups that occupy the Australian marketplace, including activity from first homeowners, upgraders, downsizers and investors. This is a very healthy mix of constant pressure. There is also a good level of rental demand. It is becoming harder to play in the capital city market under $500,000, but it can be done – it just takes some enterprise and know how.

Some fun, fast facts on affordability

Here's some fun, fast facts (from RP Data CoreLogic) on property about affordability (all prices below are average house prices):

- Sydney has 202 suburbs, of which 20 suburbs are priced below $500,000, equalling 10% of the market. And 99 suburbs are now over $1 million.
- Adelaide has 91 suburbs, of which only 29 suburbs are priced below $500,000, equalling 30% of the market.

- Melbourne has 237 suburbs, of which 53 suburbs are priced below $500,000, equalling 22% of the market.
- Perth has 207 suburbs, of which 57 suburbs are priced below $500,000, equalling 27% of the market.
- Brisbane has 173 suburbs, of which 73 suburbs are priced below $500,000, equalling 42% of the market.

So what does it all mean for investors?

Not all of us earn $150,000 a year; some of us don't even scrape $60,000. And even if our salaries are higher, that doesn't necessarily mean we have the ability to save up the $50,000 or so in upfront costs necessary to purchase a property in a 'decent' suburb.

Faced with this challenging reality, what choice do aspiring yet cash-constrained investors have? Not invest? It doesn't sound like a compelling option. But there is another way. Most properties may be well beyond the mark of $500,000 but there are plenty of other areas that it is possible to purchase in for under $500,000. Use the tactics I have highlighted in this chapter, from following gentrification trends to buying in a NIMBY neighbourhood. For example, today you cannot buy in Sydney's best NIMBY areas for under $1,000,000, but in Melbourne and Brisbane you can below $500,000. So why not use this tactic there?

I'll let you decide.



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CHAPTER 13

UNDERSTANDING PROPERTY MARKET GROWTH

'After expansion comes contraction, but after contraction comes expansion.' This is a simple thought but it can have a huge impact on what you do and a massive influence on when you should buy. About 80% of buyers – usually novice investors – purchase property when the market is really hot or even at its peak; they are worried about missing out. But smart investors sell or lock in their gains rather than buy at this time. If you are canny and experienced, you can make money no matter what the market is doing; however, investors will always make more by running counter to the property cycle or buying well before the peak occurs.

As part of the 4 × Plan it is very important for investors to study the different Australian property market cycles and learn how to use the markets for capital growth. Market fluctuations are part of a normal cycle. Today, a cycle is running at about 13 years; in that time property prices can double. But investors often don't see property double as they miss the true start and finish of the cycle they are in, and may even be buying over two cycles, not one. Or, they may get lucky and see property double in just a few years.

What I like about the Australian property market is that different states and cities go through growth cycles at different times, giving us the opportunity to diversify our portfolios around the nation. And as you have learned, property growth and area growth are vitally important to help you speed up results and make money. We're able to use the varied growth cycles in the separate states and cities to always be investing in a market that's positioned for growth, rather than a market ready for a downturn.

So that you can learn how to capitalise on the ups and downs of the market, let's explore in more detail how property markets work.

The key components of a real estate cycle

During a property cycle in which prices take 13 years to double there will be three or four periods of steady price increases. There will also be two or three periods of slower growth, stagnation or moderate price corrections. Generally, there is also a boom period with rapid price acceleration.

There are four common approaches to the property market that you must understand if you are going to make the most of your investing:

- bottom of the market investing
- counter-cyclical investing
- rising market investing
- hot market investing.

Let's explore these.

Bottom of the market investing

Buying near the bottom of the market will give you maximum uplift later in the property cycle. The challenge with buying at the bottom is that nobody knows how long you will be at the bottom of the cycle, or even when exactly you *are* at the bottom. Sometimes the bottom can last for months, at other times years.

A common misunderstanding about our largest cities is that the bottom of the market sees a massive crash in prices; this in fact often does not occur. Buying at the bottom of the market allows you, usually, to buy a great position and a great property. You boost your property portfolio by not chasing a rush on growth straight away – you get a good price and position, as sentiment at the bottom of the market is low. When the growth comes, you have a better asset than the latecomers.

Buying property at the bottom may even mean it takes a few years to see growth, but it is well worth it based on the quality of the areas and property you can get. I love buying at the bottom of the market, as you obtain better assets in the long run. Unless you are desperate for fast market growth, I strongly suggest going for position over growth first, if you can afford it.

Too many people tend to buy later in the cycle in an inferior locality rather than being patient and prioritising position. In 2008 I was buying in Sydney at the bottom of the market, 6km from the CBD. By 2013, just five years later, for the same price you had to buy 36km from the CBD, and by 2017 … 66km! Sure, many people rode the boom in Sydney and may have bought in 2013 and seen the property accelerate from day one, but they didn't get the premier localities into their portfolio at a dirt cheap rate.

Investing at the bottom of the market can be summed up as 'position over growth'.

Counter-cyclical investing

Buying when there is a weakness in the market is smart as yields are low but great locations are available. This would usually be a period of trough and not the bottom of the market.

A trough in the market cycle is when sales activity is slow and there is an ability to buy well. This can mean securing a discount or even

just getting into a popular neighbourhood on sale, which previously may not have been possible. Generally, this is a slowdown period, or the counter cycle to a rising market. Provided you take care to identify a good location and deal, this is a sensible way to buy in the best suburbs or best street for a bargain price that perhaps just 12 months earlier was impossible. In this period we can see a reversal of yields that were dropping during the boom and a return of yield expansion and rental growth.

Tactically, you can make some better offers on property and play a game that – as horrible as it sounds – I love to call 'kick the seller'. At the bottom of the market, sellers are often wise to the fact that they are selling at the wrong time but know hope is around the corner. But, on the counter cycle sellers tend to be nervous and unsure, which means you can get a property for a good price as this is the period when many people feel the world is about to collapse. Doomsday vendors are a great target for property investors.

Some features of the counter cycle (and the bottom of the cycle) are:

- The property discount rate improves, so you can offer less.
- Suburb and location choices improve, so you can buy a better location with your money.
- The affordability rate improves as prices drop.

Diversification and getting ready for intended growth is the play here.

Rising market investing

A rising market is a smart time for most property investors to buy. They may have missed the counter cycle or even the bottom, but for most aspirational investors this is an advantageous time to buy. During a rising market property values tend to be increasing by as much as $1,000 per week, so you have to get in now or never.

This is buying during an upturn. This is where the most opportunity from the market can be found prior to a hot or booming market. It is

really your last chance to get a good property and good area before the frenzy begins. Without doubt, if your plan is to ride the bull then you have to buy in a rising market so you get some good market lead up and fulsome capital gains on your property. Once you've missed the rise, you have to then question if you should look elsewhere.

Hot market investing

Hot markets are harsh markets to buy in, but they can create fast equity. Generally, you have to sacrifice location and price.

Mostly in these markets you are not buying position and areas, you are simply buying equity. The market may actually be moving so fast that properties that are sub-$500,000 are rising at $3,000 a week, or $156,000 a year. If you time it perfectly, you can get some fast equity and still make money. I helped many people buy in Sydney in 2013 with the market running hot. They were pushed out to Liverpool, which is a working-class area of Sydney some 32km from the city, but people made fast money; well over $150,000. Now that the boom is slowing they have equity, which is great, but they don't have a property in a premier location because they bought growth over position. Hot markets come under attack from laggard investors who chase an equity grab. There is nothing wrong with buying for equity; it is what it is.

Hot markets are better for selling than buying, so if your plan is to consolidate your portfolio you need to learn when markets are hot and try to time the peak and sell. Getting over market value for your property generally happens when the market is hot and there is a lot of fear around missing out.

The six key macro drivers of growth

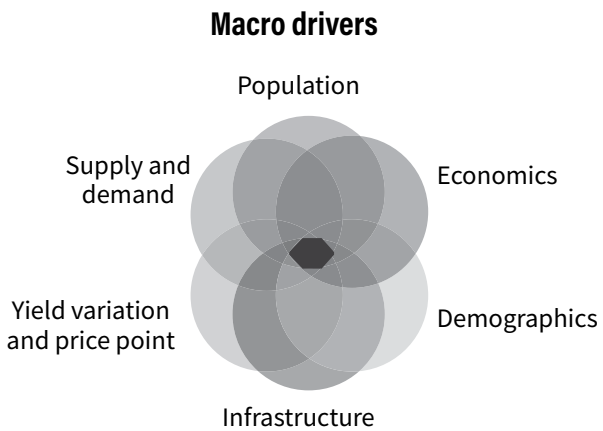
Bigger cities are such good investment zones because they often see growth drivers occur inherently within them. Conversely, regional areas are always trying to attract growth, which can be hit and miss.

Governments spend money to grow cities and meet the demands of Australia's exciting future. If these drivers start to impact your market or even your area, you will see growth. Sometimes growth is slow and minimal, for example 1%, but occasionally it is fast, like 25%.

At the time of writing, Brisbane, Perth, Sydney and Melbourne are spending up to $30 billion on their cities to improve living standards, which can lead to growth in pockets in the suburbs and hubs within cities themselves. Where? Well, that requires some investigation. However, overall the drivers bring stability and consistent growth to cities, hence properties within capital cities are growing steadily and doubling in 13 years. Conversely, many areas that are lacking drivers and stability have not grown, and/or are struggling to grow, or have been boom to bust areas and may be dying today.

Let's delve into the drivers that make real estate and the economy tick. The macro drivers are:

- population
- economics
- demographics
- infrastructure
- yield variation
- supply and demand.



Population

As we know, Australia is on track for a much larger population by 2051; as such, areas of high population growth are smart investment areas to focus on. Increased population translates to demand and taxpayers that activate the economy.

Our big cities will dominate our future. If we were to drill down to what makes up the forecast, it is essentially the following:

- One birth every 1 minute and 46 seconds.
- One death every 3 minutes and 27 seconds.
- A net gain of one person due to international migration every 2 minutes and 39 seconds.

This leads to an overall population increase of one person every 92 seconds within Australia (ABS Population Clock, January 2017). This is fast by world standards, and is great news for property investors.

According to the ABS population projections by Australian city, the following is a realistic scenario. At 30 June 2056, the population of Australia's largest cities will be:

- Sydney: 7,649,000
- Melbourne: 7,970,700
- Perth: 4,164,400
- Brisbane: 4,955,100
- Adelaide: 1,848,500.

Economics

Remember, high wages mean low unemployment and low unemployment means more disposable income. Where there is wage growth, you will often find property price growth. The reasons why wages are very important will be discussed in more detail later in the book, but for now just remember that wage booms create property booms.

Today our economy is changing, and these changes act as a guide for investors. In the recent mining boom, wages grew based on the high demand for and shortage of labour, and property values followed. This was most notable in areas highly exposed to the resources boom. We also saw that when wages slowed and demand eased, these areas had a property correction that was in many cases heavy.

Cities are centres of diversification and hubs for many industries; all forms of work drive them. Hence they are less likely to fail in a downturn, and will have a soft landing when compared to elsewhere. Cities may fall 5% in value from time to time, but more volatile areas can lose up to 50% in value.

Of course, some economies are growing faster than others, but major cities generally have a diverse range of economic influences and job choices, and attract more job growth as new ideas and businesses are spawned. Governments work with businesses to push innovation in our economy, and cities provide a launch pad for skills and knowledge.

House prices are linked to wages, and the easiest way to explain this element of economics is by considering average income versus average house price. The two main economic markets to consider within property are the bearable and equitable markets:

- **Bearable markets** are markets where incomes can cater to the property prices, and they exist all over Australia. If people are struggling to pay the mortgage or just meeting their mortgage repayments, these areas can still *bear the price* – hence the name 'bearable'! However, it is often very hard for these areas to grow internally until wages grow or interest rates fall. Most of Australia is made up of bearable markets, and they are fine and will grow with inflation. But many areas are below bearable, and we call these places 'mortgage belt markets'. They are suburbs that are exposed to the pressures of daily life; they often have the least wealthy inhabitants of our cities. If mortgage rates climb or the cost of living rises

too much, these areas slow as the incomes are not high; they can be volatile areas. Today the average Australian income versus debt ratio is 168%. That means people are borrowing more than they earn. This is alarming, and in mortgage belt markets it can lead to house prices that are soft as there simply isn't room for expansion based on the inability to meet the cost of growth.

- **Equitable markets** in property terms are suburbs where wages are growing. The economy may be rewarding certain skills at a particular time. Within suburbs where you find improving incomes you can often see a corresponding rise in property values, aligned to the wage growth index. Also, if the debt ratio is lower in these areas as people do not have to borrow or gear highly, you can see that there is more room for equity growth, hence the term 'equitable market'. In simple terms, if incomes rise property follows suit, as people will spend more on housing since it is high on their list of wants and needs.

Within property economics, we also want to study job and wage growth, as this links directly to where to buy property that will perform. This formula of the future will be discussed later in the book as we explore the 'knowledge economy'.

Demographics

The greatest gauge for a market is the consumption habits of people: what they're buying, where they want to live, and where they're shopping. Let's explore inner-city demographics and the outcomes for property.

The world's population – currently 7.3 billion – is expected to reach 8.5 billion by 2030, 9.7 billion in 2050, and 11.2 billion in 2100, according to a new UN DESA report, 'World Population Prospects: The 2015 Revision'. It's fair to say that with a growing population and

ongoing job competition within CBDs, there will be a rise of younger people who want to live close to the economic heartbeat. This competitive pressure means there is a natural inherent tension for some areas to become lucrative over others.

We looked at the different buying groups earlier and you will remember that they are first homebuyers, investors, upgraders, downsizers, industry and superannuation funds, retirees and overseas investors. Within these groups there are subcultures; for example, students, hipsters and 'DINKs' (double income no kids). All these groups are consumers and they behave differently. For example, today downsizers are actually getting to the age where they want a smaller home. It was meant to happen in 2011 and didn't! The downsizers retired, and it was thought they were going to sell down their family home and move into an apartment, but it did not happen! Five years on, the downsizers are now actively buying smaller properties. Was it those extra five years of house upkeep that pushed them to apartments? Or perhaps dwindling cash in the bank? Either way, it is time to cash up and sell down. The important thing is, now that it has started, it will continue.

My belief is that suburbs that are driven by a demographic that is university-educated and within the workforce are going to be the next growth areas, from family zones to inner urban areas. These people are going to rule society, wages and wants. I'll discuss this in more detail later.

Infrastructure

Private enterprises and governments spend billions of dollars on infrastructure each year. If you can locate the new and upcoming infrastructure, you will find the growth. Cities need to ensure they replenish their systems to maintain relevance in a global economy, and new infrastructure can change the market landscape of a suburb. It is sad, but Australia's plan for the bush is less sophisticated than our plan for our top 10 cities. Regional infrastructure is bad in

many areas, and in some cases it is even closing down – for example, airports and rail connections – while money is being poured into bigger cities to make them more competitive. It is what it is!

Be sure infrastructure is actually forthcoming. We have all heard of a bridge that may 'one day be built' and what it would do for an area. The question for investors is, has it started? The Infrastructure Australia website is a good source for what is on the radar for upgrades across the nation.

The reason infrastructure is so important to look at as an investor is that it brings demand to an area. Demand and infrastructure work side by side. Imagine a rail line opening in an area that means the journey to the city now takes not 50 minutes but only 25. That is a significant change. People will see value in that and demand will follow – a potential windfall for property investors.

Yield variation

A rental return or yield is the cash flow your property can produce. It is fairly normal for a landlord in a city to receive 4% to 6% rent cover. This is known as the property's rental yield. It is the property's income measured against its value.

Understanding gross yields is imperative, as they are indicators as to where the market is. For example, at the bottom of the most recent Sydney cycle in 2008, yields were 6.5%; today – at the top – they are closer to 3%. This is a significant difference.

Rental variation is a big factor in the success of many areas. At the peak of the market a yield will be lower than at the start. If you buy at the peak it can mean you have a low-yielding property that will impact your potential to buy more properties and reach your portfolio goal. Yields compress and expand with interest rates and the supply of real estate, so if interest rates are going down, yields tend to follow. Yields can tell us a lot.

When we have good rent, owning property is simple as you often don't have to pay for it from your wage because the rent covers the mortgage costs! When the economy is suffering, this puts more pressure on businesses to make profits and stifles wage growth. For property, you may see that rents don't grow for a while and, in some cases, will actually also deflate moderately.

Supply and demand

Supply comes with planning and development, and I have already devoted a whole chapter to this as it is so important. The world's number one driver within property is supply and demand. And this book is devoted to beating it! Everything I have shared about area growth is driven by supply and demand, and every city has areas where you can avoid mainstream supply challenges. The key is to unlock the winners and losers within the future town plan.

The absorption rate of the supply is another important factor. You may see lots of supply, but if there is demand to match it – if sales rates and volumes are high – the properties are absorbed. Supply is not a risk. Conversely, if the rate of absorption is low then an area may have a few years of adjustment as properties linger on the market.

So what does it all mean for investors?

As an investor, the market cycle is important, as are the six growth drivers. True long-term wealth comes from having your assets grow in well-chosen areas. Parking your money in solid, safe cities and suburbs is prudent. Cities are growing again and are the best bet for your personal game of Monopoly. Real estate is often slow but is rewarding; with the huge population growth we are experiencing, even if we have to wait the current 13 years of the real estate cycle, it is better than many other alternative investments.

One day you will want to retire from your investments. I cannot stress enough to make sure you purchase near growth drivers, in bigger cities and in the best locations possible. And if you can take advantage of how property cycles work you can then buy low and revalue or sell high!



Want to know how?

Come and see how we do it at a Property Investor Night.
If you want to learn about strategies like these, we invite you to join us at your local investor night. It's free and anyone can join us. We'll give you some great investing tips as well as info on how to reduce your tax, pay your home off faster and where to invest. You'll also have the chance to talk to one of our expert coaches and have your questions answered.

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CHAPTER 14

ACHIEVING AN ABOVE-MARKET SALE

If you own a property, odds are one day you will want to sell it! So you need property that can fetch a good resale price. Today, for example, there are properties that are worth $800,000 but sell for $700,000 because they are fundamentally the wrong property and don't hit what society wants. Conversely, there are properties that are worth $800,000 but actually fetch $900,000 at market. In this example, that's $100,000 above market value – but $200,000 above the wrong asset's value. A huge amount of money!

If you unfortunately buy the incorrect property in a less desirable location, it is then very hard to get this form of growth. As the saying goes, 'You cannot fatten a pig on market day.' People often don't factor in that one day they have to sell. They buy investments with little regard to the wider resale market.

Achieving a resale result above what you are expecting is extremely rewarding and if you have done the right planning should form part of the 4 × Plan. Competition is the key. It is worth remembering that the more interest you can generate from buyers, the more your property will sell for. So if you buy a property that is not the target of mass

interest, one day it will be hard to sell and you won't reach more than market value.

Buying and owning to sell

You do need to look at buying knowing someday you will sell. If something about a property catches your eye for the wrong reason and irritates you, odds are it will do the same for the next person.

Have in the back of your mind when you are choosing a property that there is often an opportunity to rectify irritations over time. For example, you may have a neighbour too close to you when you buy a property, making it feel less private, but if you plant a tree in the right place, ten years later you don't have a problem; you may have now created privacy with a mature tree. This can add value, as you bought a problem but are selling a solution.

Some investors will hold a property for 7 to 15 years and never spend a cent on it during this time. They expect to sell the investment at a premium price just because 'property always goes up', but often they can't achieve the price they want due to depreciation and poor upkeep. Landlords will often overdramatise the cost of improvements and see maintenance as a fuss and an irritant rather than as a way to keep up with buyers' needs in the market. This means investors often have to do a major renovation before reselling. I prefer small improvements over time, and then property styling when I sell.

You need a good agent to get a good price

So how does a property advertised for $800,000 reach a sale figure of $900,000? Particularly when it is only ever worth $800,000? It's a pretty simple formula: the right property, the right location and the right market. But there is a fourth ingredient: a good sales agent! The best in the business create competition and make buyers fight for something they may not even know they want.

As a buyer, I often get frustrated at good agents' methods of selling property. But as a seller I love a good agent who knows how to push up prices. But an agent is not a miracle worker – they do need a good property to begin with to get the best result.

Have you ever wondered why agents open homes for only 20 minutes? They want you to feel uneasy. They want to create a bottleneck of people by having as many people in the home at once as possible. That way buyers know there are many other people focusing on that property, creating a sense of urgency. Competition is the fuel to higher values, even if it is very much fabricated.

Agents today are also very frugal with information, so that they can lure you to the property to stir your emotions when you see it. Price guides and a lack of data bring both the qualified and unqualified to visit a property. It is all part of the agent's plan to build up a fear of missing the moment.

You need a good plan to get a good price

Selling above market value is a process. For example, many investor landlords who sell still have tenants in place in the home upon sale. How can that affect sale prices? Dramatically. Often it detracts from the sale, rather than assisting. What if the tenants are not desirable to potential buyers?

There are many keys to selling for over market value, and designing a plan that works is essential to make it happen. Things you may need to look into further to assist you include:

- confirming the attributes of a great agent over a mediocre agent
- finding the best agent who knows your property and the area well
- using the best method of sale of your property (which is usually auction rather than private treaty)

- presenting your property for sale with punch
- marketing your property well to a wide audience.

Preparing the property for sale

The main thing when you are selling is that you want a real estate agent who knows how human beings behave. An agent at the top of their game connects with and feels a home and translates that to the buyers.

Making the property look good

If you make your property a beautiful visual experience people often pay more as it makes them feel good and helps them visualise themselves in the property. People are visual, so a buyer needs to become attracted to what they see. For example, the colour of the home, the cleanliness and its space all need to be monitored by an agent. Good agents open properties but also do a nearby inspection in the street and yard for problems, well before opening the home. Perhaps a stolen shopping trolley was left in the street, or a dog has knocked over a nearby bin. A good agent is prepared to do the dirty work and tidy up before the viewers arrive. It's amazing how big an impact these things can have on a buyer's first impression.

For an agent to achieve a high price for your property and make you a small fortune, you also need to ensure that you do not fill the property with your personal items or your tenant's items. You need to transform the property to appeal to the demographic who will buy it. This is why homes often have staged furnishings to match the target buyers. This connects people to the property's benefits: to the buyer 'it just feels right'!

Making the property sound good

People are also auditory, so individuals like hearing your property. Yes, *hearing* it. A property that is in a good urban area has sounds.

For example, hearing a nearby café and just how fun it is can make people want to buy your property. Again, this helps buyers imagine themselves living in the area. A good agent may not just show the property but show people nearby enjoyable elements like the café. As for a property in suburbia where buyers will want quiet, making sure the neighbours know when the home is open and ensuring they don't have the leaf blower out is important. If you have a garden, it may be hearing the garden and birds that appeals to prospective buyers. A quality agent may even put some bird food out to show the home's natural appeal.

Choosing the best time to sell

A flat market is not an excuse for not beating the market, it just means you have to pick your time carefully. As a seller you need to monitor absorption rates, which is the rate that property is bought and sold, because if there is too much stock on the market it is hard to get over market value as buyers have a lot of choice.

If you are thinking of selling, give yourself time; monitor absorption rates in the area to try to find a selling window; that is, a period when there are more buyers than sellers. It could take 12 months to find the right window but it can mean you make a lot more money, which is the goal. If you sell in a rush, you usually get rushed results. A good agent will tell you when inventory is low and when it is time to strike. Too many investors tend to sell in frustration when their property hasn't performed as they expected, not understanding what they bought or the terrain they bought in, and they sell at the worst time possible.

Choosing the best method of sale

Trying to get the highest price for your property involves choosing the best method of sale. Auctions can produce some hot results as they allow an agent the ability to sell before, at auction or after

auction. It is a three-phase system that plays buyers off against each other in all aspects. The auction system is designed to get people to make offers prior to the auction which favours the seller, bid at auction which is an emotional roller coaster for the bidders and causes price surges, and if the property gets passed in (it does not reach the asking price) then it is still possible for the property to sell afterwards through private negotiations. I don't buy at auctions but I do love selling this way.

Sydney and Melbourne are great auction markets. If you buy in a suburb that sells well via the auction system, you are usually in a good location for future gains.

So what does it all mean for investors?

Selling property well is an artform; it is equally important as buying property. Don't be afraid to pay the right agent what they are worth. Most agents in Australia today are just passing through the real estate industry, having a go. They earn upwards of $50,000 a year, are not highly skilled, and should not run your sale. Sell with the best and odds are you will get the best result.

Fetching a high price at market can lead to a sizable amount of extra, unplanned gains, as much as 10% to 20% above the true value of your property. It begins with buying well, finding a good location and choosing a winning property with the right owner-occupier appeal. Things then build up when you find the right realtor to work for you. Outstanding agents will make buyers pay a premium for the right property.

Just remember, if the property doesn't pass muster it is harder to get this bonus growth factor and extra wealth. However, if you get it right, this extra windfall becomes the cream on top and goes a long way towards paying tax, costs and incidentals. It is a must of investing in property to try to hit this windfall through the resale market.

Remember, buy right and sell well!



Want to know how?

Come and see how we do it at a Property Investor Night.
If you want to learn about strategies like these, we invite you to join us at your local investor night. It's free and anyone can join us. We'll give you some great investing tips as well as info on how to reduce your tax, pay your home off faster and where to invest. You'll also have the chance to talk to one of our expert coaches and have your questions answered.

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CHAPTER 15

CREATING A CASH FLOW PLAN

Buying real estate well is a matter of really focusing on what will perform. Once upon a time many investors ran off to small mining towns to chase rents. Returns of 9% or 10% were common. With interest rates at 7%, they were the only properties that paid for themselves: positive cash flow properties! For a while it was a successful strategy, but in the end it failed. The fundamentals were not there to support the rents, and when the mining economy slowed, so did the rents. It wasn't a long-term or sustainable investment plan.

So what is going to be an investor's best hope for positive cash flow property into the future? Given the current deflation in the economy and Australia's record low cash rate, we can still shop in good areas and get medium yields. We don't have to take huge risks to get a sensible return.

Cash flow basics

Let us start with some cash flow basics. There are three parts to the cash flow puzzle: your wage, the taxman, and your tenant. If your tenant can pay the rent and it covers your mortgage, you are doing

well. Your own cash flow is freed up so you are not constantly forking out to hold your property. The longer you own real estate the more likely this is to occur.

Having a combination strategy that includes both cash flow and capital growth will provide you with serviceability and equity as a borrower, and will allow you to continue to move forward, so focusing only on yield is a flawed approach. Equity and servicing allows you to buy more properties, borrow more money and keep building your wealth.

Positive and negative

Often investors hear the terms 'positively geared' or 'positive cash flow' but are not sure exactly what they mean. The easiest way to understand these terms is that **positively geared properties** occur when the rental return and tax breaks cover your loan repayments and outgoings, leaving your wage or income unaffected. **Positive cash flow properties** are self-funding, and you do not need your tax deductions or your wage as the rent pays for everything. (However, many high-yielding properties at 10% can be in volatile small areas, which means they can be risky investments, so be wary and do deeper research. An investment that starts out as positive cash flow can turn negative over time.)

Conversely, **negatively geared properties** occur when the rental return and tax deductions are less than your loan repayments and outgoings, placing you in an income loss position on the property. There is, however, the underlying expectation that the accumulated losses will be more than offset by the capital growth on the property. In this circumstance, the rental return is not considered as important in the decision process, and you should also have a wage that you are happy to access to help cover the mortgage. Many people today find the right negatively geared property and ownership may only cost $50 per week.

The key benefit associated with negative gearing is that the loss associated with the property ownership can be offset against other income earned, reducing your assessable tax income, thereby reducing your tax payable. The result is that the cost of owning the property is being funded by your tenant (in the form of rent), the Tax Office (in the form of tax savings) and your surplus cash flow.

Ultimately, most investors will aim to be positively geared in the long run but start negative and hold property for a few cycles. Generally, people who pay high amounts of tax are advised by their accountants to choose the negatively geared investment option to maximise their tax returns and benefit from the long-term capital growth potential.

Some property portfolio cash flow options

A property portfolio can be cash flowed in various ways, and we will discuss the following methods:

- flight to quality cash flow
- tax for cash flow
- short stays and the new world of Airbnb
- dual income properties.

Flight to quality cash flow

I have already examined the fact that we are operating in a saturated property market. Beyond this problem, compounding the challenges we all face, regional markets that typically show investors good returns have now become speculative markets to invest in rather than investment markets. No-one likes to be a property speculator, so steer clear and stick to what I have said so far: major cities are the future.

The fact that any random person can develop and provide supply to the real estate market is scary. Good architecture, building, construction and design are without question what will make or break

real estate as an investment into the future. Good design is a telltale sign as to what will get the best future rents.

As we have all slowly become subject to the moving tides of the economy, less attractive designs have emerged within the property market. Older properties become redundant, and as buildings and landscapes are becoming more cookie cutter, planners have forgotten property is about people first. We are now polluted with many poor excuses for properties. The key to unlocking good rents is putting people first! So the property you buy needs to match this principle. The renting habits of previous cycles don't work anymore. The 'take it or leave it' market is over. In fact, many properties in the market today are going to see rents fall. Their owners would probably be better off negotiating with their tenants to pay less rather than losing them to the 'flight to quality' market we are in.

Development is essentially profit driven, not driven to benefit the public. Around 80% of the new market is driven via a labyrinth of incompetence, all the way from planning to delivery. No wonder so many people are fearful of new property; much of it is a sham!

People will pay more for what they worry they cannot have. In a 'flight to quality' market there are fewer of the best designed properties and those with superior amenities. These are achieving the best returns due to lack of supply and high demand. Conversely, as properties grow older and as more homogenous properties are also being supplied, neither category is effectively growing from a rental point of view. If anything, they are actually losing more rent than ever before. They are being pushed to the bottom. Tenants are paying less for them. A recent realestate.com.au survey found that 75% of tenants would pay more if the standard of property available was better. This is exactly what they are doing for the better properties within the marketplace, meaning investors are now yielding more, up to 1% above other properties if the design and property work well. Today you can have two new buildings or homes on the same street and one

will collect a 4% rental return and the other a 6% return based on its quality inclusions and design. A rental premium is available in the market, and is our new way to get better cash flow.

I recently had two clients buy a property on the same street. My first client paid about $600,000 and bought a high-pedigree piece of real estate and received $700 per week in rent, which is a pleasing return. My other client decided to pay less and bought an inferior property with inferior inclusions for $550,000, believing they were getting better value given the $50,000 price difference but not realising the fixtures, fittings and design matter. My second client is now only getting $450 per week. The difference in rent is huge. Yes, they were comparable properties in terms of price range, but one was superior and true value for money, while the other fell into the cheap category and is now in a race to the bottom.

And so what does getting it wrong now look like in cash flow terms? My first client is now renting their property for $250 a week more than my second client. Over the course of a year that is $13,000. Over 10 years that is $130,000. My second client needs to rejuvenate or renovate to catch up!

Rents are going backwards for the wrong dwelling, and then holding costs increase for the investor when they modify the property to try to catch up. Why would someone rent an old property with poor amenities when new property is offered at the same or a similar rate? That is what is happening now, and tenants are not silly – they fly from old to new, from poor design to quality design.

The design chapter (chapter 6) will help you gauge what people want and how to offer the market quality that they will pay more for. Make sure you re-read it, especially if you are currently in the market to buy. The flight to quality is relevant in most cities and in most suburbs across all dwelling types, from houses, units and townhouses to villas and penthouses. The market is starved of great properties, and in finding them you can find secure and high cash flow.

Example of old vs homogenous vs high-quality cash flow

Older properties are not winning the cash flow war. • They are losing rental demand • Rents are compressing in favour of better properties • They are not attracting the best tenants • They are not attracting the longest tenancies • They are suffering longer vacancies	**Homogenous properties are not winning the cash flow war.** • Winning low-end demand with older properties • However, homogenous rents are compressing in favour of new, better properties • They are doing better than older properties • They are not attracting average tenants • They are not attracting the longest tenancies • They are suffering longer vacancies	**High-quality properties are getting good returns.** • They are renting fast • Rents are expanding • They are attracting the best tenants • They are attracting long leases • There is a left over pool of tenants to choose from and re-let to
$500,000 property	$550,000 property	$600,000 property
Rent $380 per week	Rent $450 per week	Rent $700 per week
$19,760 per annum	$23,400 per annum	$36,400 per annum

Tax for cash flow

The next class of cash flow is tax for cash flow. This goes against the theory that there is no such thing as good tax because owning and providing real estate in Australia is very tax effective. Most people have some large costs in their life; one is tax. Does anyone like tax?

I don't mind paying it because if I am paying tax I am giving back to society, and it also means I must be earning well.

Negative gearing is an investment principle; the tax deductions can be a bonus of owning property. However, the deductions are just a by-product of owning investment properties. For example, a capital growth plan is a strategy and tax deductions are a great benefit that also helps people's cash flow situation.

So why do we receive a tax benefit? Investors provide property to the rental market, so to reward investors for providing these properties to the market the Australian Taxation Office (ATO) gives property investors a tax deduction.

Real estate is a fantastic vehicle because there are two portions to it: the land and the building. What goes up in value? The land. What goes down in value? The building. The government allows you to claim building depreciation; this is calculated on the building itself if it was built from 1984, and you can also claim all of its fixtures and fittings. Otherwise, if it was built before 1984 you can only deduct the property's chattels. When the building and its elements go down in value on paper, owners can claim that paper loss as a deduction. These deductions become cash flow.

Is this a bit complicated for you? Let me put it in a way that will make more sense. How many days per week might we work: five, six, or seven? Now, allow me to paint a picture. We go to work, eight to ten hours a day, and exchange our time for money. That process has been around forever. We need wealth magnets, right? Now, I don't encourage anyone to quit their job, especially if you want to become a property investor. Why? Because it's reasonably difficult to borrow money when you don't have an income! Beyond our income, property is also a magnet of wealth, but so is reducing our tax.

When we work, we get home at the end of the day after dealing with the boss, customers, the traffic and many other things, but we have

some money in our hands. Picture that cash in your hand for Monday's work. Do we get to take that money and do we get to put it in our pocket? Do we get to take it and deposit it in the bank? No, we don't get a cent! Every cent, every dollar, every second, every minute, every hour, every piece of effort you exert on Monday goes to the taxman! And it doesn't get any better for many people on Tuesday, or even into Wednesday. So here's the deal; if you have to pay income tax, you can offset that tax and claim much of it back by owning real estate.

For the average Australian, if they bought between three and five properties – the newer the better and the higher cash flow the better – they could legally claim back 70% to 80% of their tax for providing rental housing to the market. More simply put: some Australians could actually claim back the money they earned Monday, Tuesday and some of Wednesday. Now, that is solid cash flow!

According to the company Depreciator, who are experts in calculating depreciation, the ATO will often refund between $1,400 and $12,000 a year for owning a single standard property. So, be sure to provide a depreciation schedule to your accountant, because without this they will inaccurately estimate your tax return claim, not knowing the costings of your property's fixtures, fittings, furniture and common areas.

The tax system was thought out and created by wealthy people to be further embellished by other rich people, however the rules apply to everyone. There is indeed cash flow to be gained from the tax system. The current system is a daily mugging for those who don't use it to their advantage; most are unaware of the cash flow benefits that property brings. If you have five properties each offering you $10,000 in deductions, that's $50,000 per annum in your pocket, and it is all permitted. If you are paying $50,000 in tax every year with no losses, you are paying $50,000 too much. The advantage is you will reduce your tax to an extremely low amount and also get the upside of property and its ability to make you wealthy.

The negative gearing debate

You might be surprised to learn that all of the talk of negative gearing reform year in, year out is in reality a smokescreen to hide the real elephant in the room: tax reform. It's really as simple as that. Sure, negative gearing gets in the news, and why wouldn't it; it is a perk for the wealthy, right? It makes for a great political football while providing a mask for our real issues. Australia fundamentally needs tax reform, but it is such a politically sensitive issue that politicians are scared to talk about it. Essentially tax reform means fixing the Goods and Services Tax (GST), because Australia has a problem with this.

Australia is in the lowest percentile of performance of countries that have a goods and services–style tax. So, essentially, the major reform that needs to happen is to fix the GST. However, this presents a problem, especially for the politicians, because when you change the GST you're targeting the purse strings of everybody. This in turn becomes a scare campaign against the party in power. They seem to be deliberately avoiding the issue even though it's a major one, more so than negative gearing. Every year we hear about scrapping negative gearing, and one day it may go as a populist political move, perhaps even as I write this book in 2017! If it were to go, it would almost certainly be grandfathered, meaning if you have a property now it will still apply to that property for the time you own it, so I'm not too concerned.

The thing is, the tax gains that would come from scrapping negative gearing wouldn't amount to that much tax revenue for Australia. We're talking maybe a couple of billion dollars, as opposed to fixing the GST, which would be an astronomical amount of money. Not that a billion isn't astronomical … but you get the point. According to Treasury, if the GST were fixed, it would collect an extra $27 billion in revenue across the wider community.

In my opinion, the problem at hand is that fixing the GST is just too sensitive an issue for government to even contemplate. The Democrat

Party, which is no longer a political force in Australia, put some holes in the GST when it was originally adopted, given at the time they had control of Australia's upper house within parliament. Unlike other countries that placed GST – or its equivalent Value Added Tax (VAT) – on everything, we only put it on about half of items sold. So when you shop at a supermarket, buying your fruit and vegetables, you're not paying GST on them. In fact, from all the OECD countries that use a form of GST tax, Australia's revenue is the second worst worldwide from the tax.

The main shortfalls are in health which fails to collect $8.2 billion in revenue, food consumption that accounts for $7.3 billion, education that currently has a $5.2 billion exemption from tax, and finance which also is at $5.2 billion of forgone revenue. Two years of collecting these amounts and Australia could have a high-speed rail line from Cairns to Melbourne. That is how significant the loss is! As I said, this is much more than negative gearing's projected $2 billion savings.

The government doesn't provide housing for people, so they must be very careful about messing with the benefits of investment property ownership. We don't live in a country such as Sweden where a socialist government creates housing; we live in a capitalist country. Someone has to go out and risk their money, their reputation and their livelihood to develop property or even own it. If this was stopped, we would not supply the market with enough stock to house everyone and rents would soar, perhaps even values too.

Dr Julian Bolleter, a Professor at The Australian Urban Design Research Centre which monitors town planning and growth, said on the ABC *Catalyst* program that to keep up with our projected population growth, we need to build the equivalent of a new Sydney every 10 years for the next 90 years to house all these people. Think about that: we built Sydney as we know it today over 200-plus years, but now we need to build a new one every 10 years. To achieve this we need to encourage more investors into the market to pay for housing or we will have a property bubble.

Tax often gets recycled. If it comes back to property investors, it seems only fair. Let me talk you through this cycle. Let's start with the developer. They are buying a piece of property and paying stamp duty tax on that property. Then that new property comes under what is known as the margin scheme and the developer pays GST on the construction. Then that property is held for a period of time, and if the developer is over the threshold of owning land in the state the property is being built in, they pay land tax. Then the property is constructed, completed and passed on to the next person: the purchaser. That purchaser now pays stamp duty. The purchaser then owns the property and pays council rates, which is an additional form of tax. One day, the property could potentially sell. If the owner is an investor they're paying capital gains tax. They're also potentially paying land tax while they own the property. That's a lot of tax.

Let's say negative gearing was abolished, and that led to the withdrawal of 15% of stock from the market. This means you're then reducing tax revenue by 15% on all other property taxes. Within property, one tax offsets another. You're paying a tax, and then getting it back via negative gearing.

Tax benefits or no tax benefits, it is my opinion that the smart thing for investors to do is to buy property in a great location with good, solid growth drivers, and think of tax as a benefit not a principle of Australian real estate investing. I have already mentioned this point but it's one that I wanted to reiterate. It does help your cash flow, but without it rents should increase so you would have a better cash flow profile in turn. Tax cash flow is about creating financial efficiencies in your life – a must for a savvy investor.

Short stays and the new world of Airbnb

Beyond cash flow from tax and the flight to quality, there are other, new ways to maximise and turbocharge your rental returns. Short stay accommodation using Airbnb or similar short stay accommodation

systems is a property investor's new high-risk and high-reward playbook. This effective strategy has been a regular contributor to my personal cash stream for a number of years. Short stay is here to stay, but there are rules and traps to be aware of.

Imagine building a property portfolio that you rent out on long leases in great areas close to the best parts of our major cities. Now imagine that in 2017, due to the nature of the disruptive world we live in, your rental property becomes a prized asset as a short-stay venue, meaning your longer lease can be replaced and you can double your income by renting your property out nightly or for short stays. Sound good? Well, welcome to the new age of property disruption and Airbnb returns! Disruption is everywhere, and our world is changing fast, not just in property.

The Yellow Cab Company recently went into liquidation in San Francisco; the market was completely disrupted by a new form of transport called Uber. Uber is the world's biggest personal transport company, but one that actually does not even own vehicles! The business model is based on efficient technology, checks and balances, and simple payment for speed of use. For a century, taxis were the incumbent form of personal automobile transport – now they are not. Things have changed; they always do. Uber's dominance has changed car travel forever. I recently took a trip across Brisbane – I stood on a corner hoping a taxi would come past and it didn't, so I pressed an app on my iPhone and booked an Uber. Within a couple of minutes, a mum going home from the gym picked me up and dropped me across the city where I needed to go. How can a taxi company with huge infrastructure costs compete with this part-time system? This mum was just making some extra money while she had another job and was using her time well – a serious threat to the taxi world.

Recently I travelled by taxi and the driver was crestfallen as he explained it was his last day on the job. He was leaving the industry after seven years. He explained that Uber had made his role

redundant. He asked me what I did. I mentioned real estate and that it too was developing a shared economy via technology like Airbnb. He went on to say that he used to wait outside hotels for 10 minutes for a passenger, but now due to Airbnb it was more like up to a 45-minute wait between guests, as fewer patrons were staying in hotels. The driver seemed to think that I was onto something, as travellers now preferred Airbnb. He speculated that Airbnb patrons probably used Uber for transport, and he is probably right! Hard times for many incumbent businesses, but opportunity for others. Today there are smart businesspeople taking over the role of anything the economy can share.

Like Uber and taxis, Airbnb and Stayz have caused a major disruption to the hotel industry. Combined, they now have the world's biggest stockpile of accommodation, far bigger than the biggest hoteliers, yet neither Airbnb nor Stayz own any real estate. They provide more places to stay than the world's biggest hotel chains but they don't have the costs. It's a business model that's difficult to compete with.

How can investors take advantage of this disruption?

The hotel industry will always be around, but if you buy suitable investment properties in the right areas you can create huge cash flow by competing with hotels and running your own short-stay cash flow plan. There have been many schemes for short stay over the years, such as buying in a hotel pool or a serviced apartment, but this is not what I am talking about. Those can be dangerous property investments. I suggest you do not ever buy a serviced apartment or hotel room. They will cripple you due to the zoning, lending, and the lack of liquidity they represent.

What I am talking about is your normal investment property bought because you foremost want to get wonderful growth from a superb property and area, and that will always attract long-term rentals if need be, meaning you can always revert back to traditional long-term

rentals should your circumstances change – and there will be a tipping point; there always is. But the new wrinkle in such a plan is that you can rent the property out as a short stay and the property can generate your own hotel-style return. This makes 2017 the year of the 'rentrepreneur'. Yes, a 'rent entrepreneur'.

Effectively becoming your own hotelier is not a passive investment plan like a rental property with a normal 12-month lease. Don't get me wrong: it takes a lot of work. Running your own little 'hotel' is more effort for more economic reward.

A decent single hotel room in a major city on average is $250 a night. However, depending on supply and demand this can be as high as $600 a night. All you have to do is work out how to rent your property out and compete. Sound simple? Well, it is a little bit harder than that. It is a very tactical game, one that most people are not successful at.

Choosing the right property for short-stay rentals

Choosing a short-stay property is about choosing a property that can rent well both normally and via Airbnb or Stayz, or other such companies. You never want to buy a property that is only suitable for short-term occupancy and leaves you high and dry as the world changes. What you want is a property that, if you cannot short-stay it 10 years from now due to whatever reason, you can revert the property back to a normal rental, and that rent would have grown because you are in an area that has active growth drivers because you purchased well.

The best properties are close to the features listed below because they create frequency of use by travellers:

- cultural precincts – weekend trade
- business areas – weekday trade
- tourism areas – all year round
- events and conventions – all year round.

If you have a property near a cultural precinct you should get good yields over weekends. If it is near the CBD, you will get business mid-week. If it's within a short walk of a convention centre or a sports arena you get more short-stay renters and a higher frequency. And if you can get all four elements you are in the right location!

Remember what short stay is *not*:

- buying a hotel room
- buying a serviced apartment in a motel pool
- a holiday letting pool rental.

Some short-stay examples

I have three properties I rent short-stay, all differently. Let me tell you about how it works for me.

The first is my own home. At Christmas I can house swap my home with a person who is in another part of the world – they can holiday in my home and me in theirs – or I can rent to holidaymakers who want to rent my home for a fixed rate over the peak season. I can then use that money to have a holiday somewhere around the world. In this situation I am a once-a-year holiday host. In doing this I never have to pay for a vacation; I effectively holiday for free, meaning my net wealth and spending remain the same. I have a holiday magnet in my life that saves me thousands per annum.

My second such property is a beachfront home in Cairns. I short-stay the property and receive a return over 5%, which is the normal long-term tenancy rate. It is the average for the area. However, because the property is not rented every day but is in a great holiday spot, I also get to use it for my own lifestyle. I love property that I can get a lifestyle reward from. I get the benefits of the days that it is not rented to use myself, and as a result I have a few holidays in that region each year when it is slow – a fantastic bonus. In this situation I am a short-stay holiday 'rentrepreneur'. This saves me around $10,000 a year in ad hoc vacations. More wealth magnets in my life!

My third such property is an inner-city apartment overlooking the Brisbane CBD. I work this property hard and rent it out to businesspeople as much as possible. In fact, I get twice the rent I would receive renting it out long term by running it as my own hotel. In this situation I am a 'rentrepreneur'. Working this property requires at least 20 minutes a day of my time, but the return is worth the effort.

Each of these properties provides me with good income or a way to harness opportunity. Not all properties can do that. Location is the key. If you are in an area that has no social, cultural or economic life, it just won't work.

Managing a short-stay rental

To rent properties as short stay you also need to be a good host, to both attract business and ensure positive reviews. This means having procedures in place to allow:

- timely responses to enquiries
- efficient check in and check out
- cleaning
- dealing with emergencies (such as lockouts or damage to the property)
- marketing your property online
- monitoring and evaluating the market and its seasonal changes
- monitoring and evaluation of the competition
- rapid and frequent price changes
- knowledge of special events that will affect demand.

If you want to consider being a 'rentrepreneur' and short-stay rent your property, you need to realise it's labour intensive. You must factor this into your planning.

Crunching the numbers

Not all properties are suitable for short stays, but some are fantastic. You can build a life around their economics. Today, a 5.2% return is a very good long-term rental starting return. For example, a $500,000 property renting for $500 a week is a 5.2% return. Over time, this will improve as rents tend to go up, meaning more cash flow the longer you own the property. Often as your gearing drops the rent goes up. For example, that property could go from $500 a week to $750. It may take 10 or 15 years but it will happen.

It is critical to understand which markets your property would appeal to, if any, in order to determine whether short-stay rentals is a feasible option for you and to correctly target your market.

Here is an example of a property I own:

> Normal long-term rent (12-month lease):
> $700 per week × 52 weeks = $36,400
>
> Rent through Airbnb for $350 a night (average 4 nights per week):
> $1,400 × 52 weeks = $72,800

Currently this property is yielding 11%. Not bad considering my mortgage is around $30,000 a year, and my gross rent is $72,800.

Above all, with any property, make sure you choose a property that is sustainable, with the right fundamentals, and aim for capital growth first. Everything else, like Airbnb yields, is a benefit. In today's world you can make a decision to aim for both.

According to the Airbnb website, on any given night, in 34,000 cities that Airbnb operates in across the globe, adventurous souls are opening up their spare rooms or rental properties to Airbnb. Amazing! If you have the right property, you will do very well. It will increase your daily cash flow. Today, there are even Airbnb managers who will promote and run your properties for you for a fee – a new real estate phenomenon.

Dual income properties

Dual income properties are a great way to extract extra rent. They follow the premise of making the highest and best use of real estate, lifting the overall rental return. Having two dwellings for two tenants using the property instead of one usually boosts the rent and ensures you maximise the property's overall yield.

Dual income properties can be in the form of two properties on one title, which is very common today under the affordable housing legislation in New South Wales and Queensland, which allows for two occupancies on one title for many properties. This may take the form of building a low-cost flat detached from the main house on an older property, or actually building a new property from scratch and designing it to have two income streams via two dwellings.

With all the talk in recent years about the growth of single-person households, here's a figure that may surprise you: domain.com.au recently noted that one in five Australian households has adults from two or more generations living under one roof. That's more than four million Aussies sharing a home with their parents, their adult children or other extended-family members, hence why this style of dwelling will be more popular over time.

How does a dual income boost yields?

Two properties or more can give you a superior yield and mean you don't end up losing too much income from your own back pocket. Let's have a look at some figures.

Let's use Sydney as an example. The broad gross rental return for a house in Sydney today is 3.1%, according to RP Data CoreLogic's 2016 market rental report. A $1.1 million home bought today may only rent for $660 per week, a total of $34,320 in rent collection. However, currently a home loan is around 4.5% and that's around $940 per week on such a property. The loss is $280 a week, and that's

a lot of weekly income to lose. In fact, that loss can actually make it very difficult to achieve your goals, and can even cripple you financially. The property may be great but its numbers aren't favourable for an investor. I find usually a $50 to $100 loss is manageable but much more can be trouble.

What about a dual income property? Today you can design and build your own dual income property for $1.1 million in Sydney, and the dwellings can produce a combined $1,100 per week in rent, a 5.2% return. This property would therefore produce $57,200 in rent. Remember, the average for a $1.1 million property in Sydney purchased today is $34,320 in rent collection in the housing sector. The extra $22,880 produced by a dual income property for the same price is $114,400 over five years in cold hard rent received. Not bad at all!

There are without doubt pros and cons to dual income properties. They do tend to suffer from valuation issues when buying and selling as there are just not enough of them traded on a regular basis in our suburbs for lenders to get good comparable data on. In comparison, one-bedroom apartments and four-bedroom houses – for instance – are sold often, hence there is good comparable data to support prices.

So what does it all mean for investors?

For most investors, securing cash flow is a sensible means of providing serviceability to their property portfolio. Similar to running a business, a well-managed property portfolio needs cash flow or your investing may run aground.



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CHAPTER 16

THE CULTURAL BELT

Before I finish, I want to discuss a fast-growing phenomenon in real estate today: the rise of the cultural property hot spot, also known as the 'cultural belt'.

Australia's population is growing rapidly in many different ways, from fertility rates to net migration intake. It is no question that we are a multicultural society. Multiculturalism is bringing global thinking to our country and consequently is affecting the future of property areas in Australia as we see cultural hubs emerge. We have seen and will continue to see the rise of the cultural hub.

So who makes up Australia today?

The ABS Migration Summary 2014–15 showed Australian citizens by country of birth. After being born in Australia, obviously, the next biggest population group was over one million new Australians who have come recently from the United Kingdom, over 617,000 new Australians from New Zealand, followed closely by China with 447,000, India with 397,000 and the Philippines with 225,000. Australia today is an Anglo–Mediterranean–Asian–Indian fusion culture, according to KPMG demographer Bernard Salt. All these newer cultures, their

ideas and wants are changing our communities and the real estate industry. Our property economics are becoming very different from years gone by.

The Sydney suburb of Chatswood was once a hub of commercial and residential property with transport links, but was less impressive than the nearby quaint, leafy suburb of Kallara. But today, Chatswood is equally expensive and may be more in demand. Why? Changing demographics and the gentrification of an area by a particular culture. The area is now a hot spot for Chinese Australians who will pay huge money to live there. While other Australian cultures scratch their heads as to what the Chatswood attraction is, the Chinese Australian community has built their own idea of happiness in that suburb. It simply comes down to different cultural preferences, a real estate phenomenon that is sure to happen again in the future. While real estate experts like myself were previously ignorant of these cultural opportunities, now we are asking ourselves why we didn't buy everything we could in Chatswood! The future is shaping up to be very different to the past.

Bernard Salt provides great insights into Australia's ever-changing human landscape. If you have a chance to hear him speak at one of his many events, I would highly recommend it; it will open your eyes.

Cultural hot spots have been relevant in our society for a long time. Bernard Salt has said: 'The Australian nation was changed forever when we welcomed the first boatload of post-war immigrants from the Baltic States in the late 1940s. It placed the nation on a pathway that has delivered economic prosperity, increased consumer demand and best of all sheer immigrant energy and determination.'

But unlike yesteryear, when they might have been considered low ranking or even outcast areas, today they are unique investment zones. They often have their own natural boundaries of supply and demand, which can rapidly change values within the suburb. Real estate is experiencing a new vibrancy that is altering the landscape of

people, lifestyles and housing, and picking these cultural gentrification hubs can be very lucrative for the early investor.

People from the same culture like to stick together. It was the same for the Greeks of Melbourne in the 1950s and for the Chinese in Box Hill in Melbourne today, and for other immigrant populations all over the world. Today, drive around inner Sydney and it's easy to notice the changes to the areas of Alexandria and Green Square, now heavily populated with Asian Australians who have battled over the real estate, leading to rises in values there.

In the past these spots may have been overlooked, but long-time locals are noticing the rapid price rises becoming a cultural hub can bring. Property values can be turbocharged. The inner west of Sydney has in recent times led the change through its new upper-middle-class housing gentrification, but these areas were originally cultural homes for the Italian, Portuguese and Greek communities. The wonderful cultural elements these communities have brought to these areas will always remain a legacy in Sydney and have contributed to the greater good of all. For example, I'm sure you have heard of Leichhardt, otherwise known as Little Italy, famous for its fine foods and Italian lifestyle.

Cultural areas are not new but what is new is that immigrants now have money. When the Greeks and Italians originally came, it was to start a new life with 'sweat equity'. Today, people of many nationalities, such as the Chinese and Indians, are coming to Australia with money and skills.

PIND – ever heard of it? Well, it is time to get out of your comfort zone and explore the new urbanisation the world is experiencing. The epicentre for the Indian community in Sydney is Harris Park. It has recently developed into a hub of Indian diaspora. Indians call Harris Park PIND or Little India. It is well known for its many Indian restaurants, music, merchandise shops and grocery stores. Housing in Harris Park ranges from the historic to the new unit market. It's so

close to the economic heartbeat that is Parramatta that it's a magnet for cultural investors seeking good rents, great growth and dynamic demographic drivers that are putting pressure on housing prices. The concept is simple: if more Indian Australians want to live in this spot than anywhere else, it will surely have supply issues. Indians are also finding communities in the north-west part of Sydney, in suburbs such as Rouse Hill, which is fast becoming Indian Australians' version of suburbia.

Fifty years ago no-one thought an area famous for Italians such as Leichardt would become such an aspirational suburb, but the momentum has shifted. Maybe Little India or Rouse Hill will be the next hot spot, with accelerated demand from more immigrants, a limited supply of land, and natural cultural boundaries (being the end of the suburb). With over one billion Indians on Earth there will be a fast-growing Indian migration rate. Don't be fooled; the cultural gentrification in these areas will lead to price growth.

So what does it all mean for investors?

For many years cultural belts were misunderstood in property circles. But lately they have reached their 'tipping point'. Everything has a tipping point: it is a time when significant change occurs and things are never the same again. No-one really knows when cultural areas become property investment zones, but they are now on the radar. What you are looking for is a community of migrants with money and aspirations and an area that will become the focal point of their lifestyle.



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CHAPTER 17

'MANHATTANISM' AND THE 'KNOWLEDGE WORKER'

The final real estate phenomena I'd like to discuss are the related concepts of 'Manhattanism' and the rise of the 'knowledge worker'.

'Manhattanism'

New York City has some of the priciest real estate in the world. The average price of a home in the city is roughly $2 million, with lower priced homes going for around $1 million in places such as Williamsburg in Brooklyn. Of course, these are just median prices, and the sky is the limit for the most expensive properties in New York City. In January 2015, the city had the most expensive apartment sale in history when a midtown property sold for $100.5 million. And it's no surprise Manhattan tops the list with some of the most expensive neighbourhoods in New York City.

In property economics terms, '**Manhattanism**' is a principle of real estate growth. 'Manhattanism' represents a situation in which extraordinary things happen when metropolitan density becomes

extreme. In the case of Manhattan, there are more people living there per square metre than anywhere else in the US, meaning the world's number one growth driver is at work: supply versus demand.

'Manhattanism' occurs with an influx of residents and a lack of space. This is also seen in Hong Kong on a wider level. In cities around Australia, the phenomenon can also occur and push prices handsomely. The idea is to find a tightly held area where more people want to live: the top of a funnel of demand. These areas are mostly suburbs landlocked close to the city. They could be a peninsula such as Balmain in Sydney, or a preferred place to live such as Sydney's Potts Point or Elizabeth Bay, which are the densest suburbs in all of Australia, according to RP Data's *Top 20 Most Densely Populated Suburbs in Australia* study. The study showed that Elizabeth Bay covers about one quarter of a square kilometre of prime inner-Sydney real estate and is home to 5,093 people, which works out to be about two people per 50 sqm of land.

The article noted that 19 of Australia's top 20 most densely populated suburbs are located in Sydney. However, every city has areas that can be classed as 'Manhattanism' suburbs based on the metrics of people versus space. These areas are vibrant retail, living and entertainment precincts that are usually close to the CBD. Derelict warehouses have been transformed into stylish apartments and bike paths connect new public spaces. They are home to hipsters, entrepreneurs, millionaires – even billionaires – and some of the most expensive real estate in Australia. Most of the housing markets in these areas are now out of reach for investors, so often apartments are the last opportunity. But that is also changing.

At the time of writing, a Potts Point project by Greenland next door to Elizabeth Bay is ready for construction, with the penthouse prices at $11 million and one-bedroom apartments selling for over $1.5 million. That's how expensive areas that have more people clustering to live in them can become. Today, that area has the benchmark

of 'Manhattanism' pricing in Australia, with even a New York–like design to follow this sound property economics principle.

'Knowledge workers'

As an investor, it's worth knowing that these premier cosmopolitan commercial and entertainment precincts are the most sought-after urban living communities for a lot of the '**knowledge workers**' who are likely to be a dominant group seeking housing in the coming years.

'Knowledge workers' are those people whose job it is to 'think for a living'. This includes, but is not limited to, engineers, physicians, architects, engineers, scientists, accountants and lawyers. In the future, given their skills, this form of employment will dominate high wages and drive the economy. Their skill will drive ideas and more evolution among the shared economy of today. These higher incomes will be the catalyst for property price improvement in the areas they choose to live in. Regardless of market conditions these areas will always be in demand, so we will continue to see improvements in price even in flatter times, making them great areas to invest in for the long term. Because 'knowledge workers' earn more they can pay more for housing, and they are a growing demographic.

San Francisco in the US feeds Silicon Valley, where many global companies such as Microsoft and Google are located. Knowledge workers have long been blamed for helping to push families out of the suburbs, which now have skyrocketing property values and the highest cost of living in the US.

We have passed the mining boom, and now we are entering an exciting new phase of property: the 'knowledge property boom'! The knowledge boom has begun and is now spreading to Australia. This is important within our cities and for property investors because Australia is basing its future on becoming a 'knowledge economy' and leaving behind, although not forgetting, the old version of its

economy. The fact that this is the current business plan for Australia will have huge impacts in the coming decades for investors buying where knowledge workers will live: 'Manhattan-like markets'. These areas are now a smart buy for investors.

Today, controlling ideas creates more jobs; controlling new products and services creates growth. This is Australia's plan, and you now have to adapt your property purchasing to match the bigger picture.

Knowledge is unlimited and renewable, whereas natural resources and decaying natural features such as the Great Barrier Reef, which is sadly being destroyed day by day, are seen as part of Australia's old economy. The potential exists to create new knowledge every day, and that is what the government is aiming for. That new knowledge may just fix global warming and our planet and save the reef. That is the economy of tomorrow, not just showing tourists its beauty.

The Commonwealth Scientific and Industrial Research Organisation (CSIRO) invented wireless internet, a lucrative worldwide export, and that is just an idea. More ideas, more business, more people, more growth. Though we very much still live in a time where we mine and manufacture, where we have big agriculture areas and our economy is still built on strong tourism, the core of the economy is trying to expand out into areas that actually don't exist today. This is good news as Australia has a rich old economy and an exciting new economy. Overall, we have learned skills from our core. Now it is time to sell ideas from our farms, mines and beaches.

So what does it all mean for investors?

Imagine the possibilities for growth in owning real estate in an area where everyone wants to live and is home to people on the highest incomes. Just how expensive will your property become?

Cities have a food chain, and today's new-age apex predator is the 'knowledge worker' living in Manhattan-like areas. These places are

hotly contested property spots, year in and year out. They are great investment areas; for example, Brisbane's New Farm, Richmond in Melbourne, Cooks Hill in Newcastle, and peninsulas like East Perth. Every city has its unique version of Manhattan, where more people live per square metre and cluster together in tightly held locations, which are fast becoming premium areas, based on people, the environment and an inability to supply much more stock to those areas. They are areas where money climbs over money to belong.

Sydney's Manhattan-like markets are now very expensive for the average Australian investor. The boom began right under our noses but many investors didn't join the dots. Many other large cities are still affordable, even with a growing knowledge worker backbone, but if you wait too long to invest in these areas you may just miss out.

I like to look at the Australian property market – particularly in places such as Sydney, Melbourne, Brisbane and Perth – as though if you don't own real estate there right now and feel you have missed the boat, you actually still have an opportunity to buy and hold real estate there for another three to four strong decades. There will be good opportunities if you get in soon with the right property in the right location, as you will still be ahead of a huge number of people, despite the current prices. Remember, Melbourne is expecting to have growth of four million people, which would make it Australia's biggest city. Perth and Brisbane will also be doubling in population. Australia's business plan is to become a 'knowledge economy' and to virtually double its global and new world cities' output.

What will this do to these Manhattan suburbs in these cities? I'll let you be the judge.



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CHAPTER 18

ANYONE CAN INVEST IN REAL ESTATE

Cities have become victims of poor architecture. The fact that any random person can provide supply to the real estate market is scary. Good architecture, building, construction and design are without question what will make or break real estate as an investment into the future. Architecture and supply should begin and end with people in mind. Failure to recognise the community, the public interest and sustainability has troubled many new investments in recent times, and the expected returns for investors have not materialised. The market just has not responded to the wrong supply of properties, which represent a form of pollution rather than a home.

A big Australia is driving population growth and this is determining the types of new properties being built and creating two distinct markets. As discussed early in the book, we are in an oversupplied homogenous marketplace and an undersupplied owner-occupier–style marketplace. Following the owner-occupier market is where we find the flight to quality rental returns today.

Another issue is that too many properties are still being built today that add to – rather than help to reduce – our environmental problems. More property pollution!

But will the future of real estate be green? Well, it's already begun. Many socially responsible developers are designing and building smart homes: buildings that have their own energy produced by solar, and green living buildings with natural ways of creating energy that then power the complex and mean investors don't have to pay more. In Singapore, developers can build a taller building if they meet six-star energy efficiency ratings and add back to create a green public realm. This practice is evolving in Australia, and in the future buildings may just be judged on how they interact with the environment as much as how they look. Will tenants one day choose green? It certainly is looking that way, but I do believe we are one cycle away from that eventuality as well. A flight to a green market!

For now, we are in a cycle that is seeing consumer habits change to wanting the best properties of the day in the best location, even if they cost a little more than inferior properties. Consumers will pay to avoid bad design. Poorly designed and built dwellings, however, are still very common, which is a challenge for investors, who need a sharp eye. Development is profit driven, not driven to benefit society. As I mentioned before, around 80% of the new stock to hit the market is driven by incompetence from planning to delivery, and by the pursuit of overseas capital. No wonder so many people are fearful of property.

Property should begin and end with people in mind. The failure by officials to recognise the community, public interest and sustainability is ultimately making choosing the right investment property harder than ever before. Population growth is determining the types of new properties being built, as are low-pedigree developers.

Future change in real estate will occur fundamentally via population growth and technology. In Australia, distance and lack of water have

corralled our population into our bigger cities. The result is an arid country that has retained much of its natural landscape and beauty but is trying to grapple with an inability to fund itself, and it just can't yet connect its satellite cities adequately to lessen the burden on our bigger cities.

In Europe, living in a capital city or a secondary city is not an issue as transport connects you. In Japan you can live outside Tokyo in a smaller city that is more affordable and travel via bullet train to work in Tokyo in half an hour. Australia has a lack of options on where to live and work given its size, as most of its land is disconnected from its major areas or is agricultural or desert land. However, this makes investment easier. Our cities will grow and will be hotbeds of people. All we have to do is work out what property to buy and in which suburb. The rest should take care of itself.

Investing in our cities in a changing global landscape requires paying close attention and keeping up with trends. Once buying an investment property was a simple mathematical equation, now it's a game of patterns, place, discovery, questioning, refinement and choice.

As good as design is, it is always improving. New benchmarks are coming and the market is now forever competitive. Supply dominates an Australia that will grow in population very quickly. The fusion of many cultures means things are changing forever and traditional local logic is being surpassed by global ideas and results. Meanwhile, our economy is moving from muscle to knowledge, a significant transformation. Once upon a time our country was about selling coal; today it is about selling ideas on how to best mine coal to the world, from robotic trucks to automated mines.

To create something extraordinary in your own life you need to redefine your beliefs about property and the world. Successes of the past and lessons from yesteryear's property cycles, even if positive, are being left behind as our globe reaches over eight billion people and international free trade is everywhere.

We need to shift our thinking in life together with our knowledge and skills; ideas have to change to perform in the real estate of today and tomorrow. The real-life game of Monopoly has changed. To create a winning formula in your own investment plan, consider these new solutions and try to look at real estate through a different lens to break away from seeing an Australia with predictable homogenous dwellings. This is where imagination and creativity are required, where maybe you will need to redesign your old properties and chase success through renovating to be better than the market, or to just buy well from the get go. In the mid-1990s homes were as big as a quarter acre; now lots can be as small as 125 sqm, but with the right design both can make investors money. Valuable insights learned from across the globe are going to be the norm as the world competes in a pressure cooker of international real estate.

The fear of making a loss is often greater than the desire for a gain, but staying still and not investing is not a desirable option. It is hard to retire wealthy if you fail to try. The risk associated with poor ambition is far greater than missing the mark on a real estate transaction. Property bought unwisely can create a short-term misalignment in life, but in the long run property has proven to be a safe asset and time heals wounds in real estate mistakes.

But let's be better than that! Real estate can double in less than 13 years if you buy well. It is going to take some faith, action and knowledge to get there but it can happen. Investing is not for the faint-hearted and it can get scary at times, but truly all you need is a willingness to try. Real estate can be your vehicle to a longer, wealthier retirement.

Property prosperity is available to everyone, so learn the currency that is real estate and you can soon be enriched with its influence. You can provide certainty and enjoyment for yourself and your loved ones, and you can construct a steady means of prosperity that isn't

far fetched but real. Pick affordable and reachable goals, and try to use the fundamentals discussed in this book. Income can often be put on autopilot if you invest right, so strap in and enjoy the ride!

Learn real estate – it is a doorway to a productive and happy economic life.



Want to know how?

Come and see how we do it at a Property Investor Night.
If you want to learn about strategies like these, we invite you to join us at your local investor night. It's free and anyone can join us. We'll give you some great investing tips as well as info on how to reduce your tax, pay your home off faster and where to invest. You'll also have the chance to talk to one of our expert coaches and have your questions answered.

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GLOSSARY

Capital gain: the amount by which your property has increased relative to what you paid for it. Simply put, if you bought a property for $200,000 and it is now worth $350,000, you've made a capital gain of $150,000.

Cash rate/bank rate: the rate at which the Reserve Bank of Australia sets interest rates.

Cash flow positive: you have a cash flow positive investment if the incomings are more than your outgoings after tax-deductible items have been claimed. You receive more rent than your mortgage repayments, plus you are still ahead after taking into account items such as interest on the loan, maintenance, insurance, land tax and rates.

CGT (capital gains tax): the tax you pay when you sell an investment property if you've made a profit, based on the amount of capital gain.

Conveyancing: the process that legally transfers property ownership from one entity to another.

Cooling-off period: a period of time given to the purchaser to legally withdraw from buying a property. The conditions and length of time vary in each of the states and territories. (A cooling-off period does not usually apply to auctions.)

Cross-securitisation/cross-collaterisation: when a financial institution uses your property (whether owner-occupied or investment) as security for other property you purchase.

Density: the level of occupancy in a given area, or the number of people permitted to reside in an area. For example, inner-city areas are usually higher density than outer suburban areas.

Depreciation: the decrease in value of an item (such as a building) over time.

Equity: the difference between your mortgage and your property's value. If your home is worth $400,000 and you owe $150,000, then you have equity of $250,000.

Fixed rates: where a home loan is locked in at a specific interest rate for a specified term, usually one to five years.

Interest-only: only repaying the interest charged on your mortgage and not paying off any of the principal, usually for a fixed period of time.

LMI (lenders mortgage insurance): usually required by lenders when you're borrowing more than 80% of a property's value. It provides insurance to the lender in case the borrower defaults on the loan.

LVR (loan-to-value ratio): to calculate this, divide the loan amount by the value of the property, then multiply by 100 to get a percentage. Banks and financial institutions use this as a measure of whether you can afford the loan.

Median: the median house price is the middle price of all sales recorded in a particular area, suburb, postcode, city or state. If there were 100 sales in a particular suburb in ascending order, the median would be number 50 on the list. It's commonly assumed that the median price is the same as the average price but that's not the case. To calculate the average, you would add up the 100 sales and divide the total by 100 (the number of sales). This would usually result in a different amount to the median.

Negatively geared: this is where the incomings are less than your outgoings after all tax deductions have been claimed. For example, you receive rent on a property of $600 a month, but your mortgage repayments are $900 a month. Your shortfall is $300 a month, which

you claim as a loss when doing your tax return. Many people on high incomes use negative gearing to reduce their taxable income.

Off the plan: when you buy off the plan, you are buying a property before it is built, having only seen the plans. This is commonly done with apartments or units under construction or about to be built.

Portfolio (as in property portfolio): the number and type of investments you own.

Positively geared: this occurs when the investment income exceeds your interest expense and other costs. For example, the rent you receive may be $1,000 a month, but the monthly repayments are only $750 a month. You can also receive additional tax benefits on any income derived from a positively geared investment.

PPR: principal place of residence.

Property cycle: property values usually follow a cycle of growth, a slowdown, a counter cycle, and an upturn.

Refinance: to obtain new finance for something on different terms, usually involving the paying off of an existing loan by means of a new (and usually cheaper) loan.

Rental yields (and calculations): the return on an investment as a percentage of the amount invested. Gross rental yield can be calculated by multiplying the weekly rent by 52 (weeks in a year) and then dividing by the value of the property and multiplying this figure by 100 to get a percentage.

Serviceability: whether or not you can manage your mortgage payments, based on your income and expenses.

Stamp duty: a state government tax on the transfer of a property, calculated on the value of the property.

Strata title: also known as unit title. This title grants ownership of a section or a 'unit' of a larger building. This 'unit' can be sold or transferred by the owner.

Subdivision: the division of a parcel of land into two or more lots. This is commonly done when larger parcels of land are rezoned, allowing for smaller lots.

Supply and demand: the number of properties on the market at any given time determines the supply-and-demand equation. If there are lots of properties on the market, it's a buyers' market. If there are few properties on the market or those that come to the market sell quickly, then it's a sellers' market.

Vacancy rates: a measure of how many dwellings are available for rent over a specified period. A low vacancy rate means there are not very many dwellings available for rent, while a high vacancy rate means there is an ample supply of vacant properties.

Vendor: the seller.

Yield: the return to an investor on an investment, shown as a percentage of the amount invested.



Want to know how?

Come and see how we do it at a Property Investor Night.

If you want to learn about strategies like these, we invite you to join us at your local investor night. It's free and anyone can join us. We'll give you some great investing tips as well as info on how to reduce your tax, pay your home off faster and where to invest. You'll also have the chance to talk to one of our expert coaches and have your questions answered.

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