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PROPERTY INVESTMENT ANALYSIS (DESCRIPTIVE)

08-Dec-2006

Property: 25 Kowarra Crescent Merimbula
Description: 2 Bedroom

SUMMARY

Assumptions		Projected results over	5 yrs
Property value	\$275,000	Property value	\$334,580
Initial investment	\$0	Equity	\$44,703
Gross rental yield	4.08%	After-tax return /yr	42.26%
Net rental yield	3.10%	Net present value	\$25,511
Cap. growth rate	4.00%	IF SOLD	
Inflation rate	2.00%	Selling costs & CGT	\$22,375
Interest rate	6.32%	Equity	\$22,328
Taxable income	\$92,110	After-tax return /yr	12.99%

COMPUTER PROJECTIONS

Investment Analysis	Projections over 5 years					
End of year	2002	1yr	2yr	3yr	4yr	5yr
Property value	\$275,000	286,000	297,440	309,338	321,711	334,580
Purchase costs	\$9,915					
Investments	\$0					
Loan amount	\$289,876	289,876	289,876	289,876	289,876	289,876
Equity	\$-14,876	-3,876	7,564	19,461	31,835	44,703
Capital growth rate	4.00%	4.00%	4.00%	4.00%	4.00%	4.00%
Inflation rate (CPI)	2.00%	2.00%	2.00%	2.00%	2.00%	2.00%
Gross rent /week	\$220	11,211	11,548	11,894	12,251	12,618
Cash deductions						
Interest (I/O)	6.32%	18,320	18,320	18,320	18,320	18,320
Rental expenses	23.36%	2,673	2,726	2,781	2,837	2,893
Pre-tax cash flow	\$0	-9,782	-9,499	-9,207	-8,906	-8,595
Non-cash deductions						
Deprec.of building	2.50%					
Deprec.of fittings	\$16,500	2,372	3,256	2,239	1,583	1,155
Loan costs	\$4,961	992	992	992	992	992
Total deductions		24,357	25,295	24,333	23,732	23,361
Tax credit (single)	\$92,110	6,376	6,638	6,033	5,569	5,210
After-tax cash flow	\$0	-3,406	-2,861	-3,174	-3,337	-3,385
Rate of return (IRR)	42.26%					
Pre-tax equivalent	82.06%	65	55	61	64	65

Note that the computer projections listed above simply illustrate the outcome calculated from the input values and the assumptions contained in the model. Hence the figures can be varied as required and are in no way intended to be a guarantee of future performance.

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Detailed Notes on Spreadsheet Items

PROPERTY VALUE

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

Property price (\$):	275,000
Renovation costs (\$):	0
Total book value (\$):	275,000
Property market value (\$):	275,000

PURCHASE COSTS

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

Conveyancing costs (\$):	800
Stamp duty (\$):	8,115
Other costs (\$):	1,000
Total Purchase costs (\$):	9,915

INVESTMENT & LOAN

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

	Investments	Loan	Total Cost
Property costs (\$):	0	275,000	275,000
Renovation costs (\$):	0	0	0
Purchase costs (\$):	0	9,915	9,915
Furniture costs (\$):	0	0	0
Loan costs (\$):	0	4,961	4,961
Totals (\$):	0	289,876	289,876

CAPITAL GROWTH & INFLATION RATES

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

Average rate of inflation (%):	2.00
Average rate of capital growth (%):	4.00

EQUITY

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

Projected values over	5 yrs	10 yrs	15 yrs	20 yrs
Property value (\$)	334,580	407,067	495,259	602,559
Loan (\$)	289,876	289,876	289,876	289,876
EQUITY (\$)	44,703	117,191	205,383	312,683
Approximate costs if sold.....				
Capital Gains Tax (\$)	12,131	29,943	51,471	76,791
Solicitor's fees (\$)	1,673	2,035	2,476	3,013
Sales commission (\$)	8,571	10,165	12,106	14,466
EQUITY (after sale) (\$)	22,328	75,047	139,330	218,413

INTEREST COSTS & TYPE OF LOAN

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

Loan type:	I/O Yrs 1-40
Interest rate (yr 1) (%)	6.32
Loan (\$):	289,876
Loan costs (written off over 5 yrs):	4,961
Monthly payment (\$):	1,527
Annual payment (\$):	18,320

RENT

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

Rent per week (\$):	220
Potential annual rent (\$):	11,440
Vacancy rate (%):	2.00
Actual annual rent (\$):	11,211

ANNUAL RENTAL EXPENSES

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

Normal Expenses:	
Agents commission (8.25%):	925
Letting fees:	220
Rates:	1,050
Insurance:	265
Maintenance:	213
Special expenses:	0
Total expenses (\$):	2,673
Normal expenses as % of annual rent (%):	23.36
Net yield or Capitalisation rate (%):	3.10

PRE-TAX CASH FLOW

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

Year		1yr	2yr	3yr	4yr	5yr
Rent		11,211	11,548	11,894	12,251	12,618
Cash invested	0	0	0	0	0	0
Principal		0	0	0	0	0
Interest		18,320	18,320	18,320	18,320	18,320
Expenses		2,673	2,726	2,781	2,837	2,893
Pre-tax cash flow	0	-9,782	-9,499	-9,207	-8,906	-8,595

DEPRECIATION ON THE BUILDING

This represents the capital allowance on the construction costs.

Property value (\$):	275,000
Construction costs (\$):	0
Depreciation allowance rate (%):	2.50
Depreciation allowance (\$):	0

DEPRECIATION OF FITTINGS (diminishing value method)

Item	Value (\$)	Effective Life (yrs)	Depreciation (\$)
General fittings	8,250	15.00	825
Low-value pool	8,250	4.00	1,547
Total	16,500		2,372

LOAN COSTS

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

Establishment fees (0.21% of loan):	600
Mortgagee stamp duty (0.40% of loan):	1,160
Mortgage insurance (0.32% of loan):	928
Mortgagee's solicitor's fees (\$):	1,000
Valuation fees (\$):	500
Registration of mortgage (\$):	57
Registration of title (\$):	72
Search fees (\$):	145
Other loan costs (\$):	500
Total loan costs (\$):	4,961

TOTAL TAX DEDUCTIONS (Cash & Non-Cash Deductions)

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

Year	1yr	2yr	3yr	4yr	5yr
Interest	18,320	18,320	18,320	18,320	18,320
Expenses	2,673	2,726	2,781	2,837	2,893
Deprec.-building	0	0	0	0	0
Deprec.-fittings	2,372	3,256	2,239	1,583	1,155
Loan costs	992	992	992	992	992
Purchase costs	0				
Total deductions	24,357	25,295	24,333	23,732	23,361

TAX CREDITS & AFTER-TAX CASH FLOW

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

Year	2002	1yr	2yr	3yr	4yr	5yr
Pre-tax cash flow	0	-9,782	-9,499	-9,207	-8,906	-8,595
Tax credits		6,376	6,638	6,033	5,569	5,210
After-tax cash flow	0	-3,406	-2,861	-3,174	-3,337	-3,385
Cost /(income) per week		65	55	61	64	65

INTERNAL RATE OF RETURN

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

Year	2002	1yr	2yr	3yr	4yr	5yr
After-tax cash flow	0	-3,406	-2,861	-3,174	-3,337	-3,385
Equity						44,703

The total amount in your "account" (including interest) at the end of the period is the equity (\$44,703) in the investment property. The IRR (42.26%) represents the effective "interest rate" that you have received, but with one important difference - because the interest remains in the property, it is not taxed. To receive an equivalent return from bank interest, you need to get 82.06% before tax.

TAX BENEFITS

These are shown below for the given taxable incomes and are based on current tax scales.

Number of properties: 2

	Investor	Partner	Total
Ownership: single name	100.00%	0.00%	100%
Present taxable income:	92,110	0	92,110
Rental income:	22,422	0	22,422
Total income:	114,533	0	114,533
Rental deductions:	48,714	0	48,714
New taxable income:	65,818	0	65,818
Present tax:	32,054	0	32,054
New tax:	19,302	0	19,302
Tax saving:	12,752	0	12,752

INVESTMENT CAPACITY

Buying 2 such properties (registered in single name), and taking into account current net incomes and living expenses as shown, the difference between total income and total committed expenses in the first year would be \$28,779. Total initial outlay would be \$0.

Number of Properties: 2 Registered: single name
 Ownership: Investor (100.00%) Partner (0.00%)

Income**Present net income**

Taxable income (investor) (\$):	92,110
Taxable income (partner) (\$):	0
Rebates & non-cash deductions:	6,703
Total net income	98,814
New rental income (\$):	22,422
Total income (\$):	121,236

Expenses

New tax (investor) (\$):	19,302
New tax (partner) (\$):	0
Rental expenses (\$):	5,346
Investment loan expenses(\$):	36,640
Home loan payments (\$):	10,200
Living expenses (\$):	20,970
Total expenses (\$):	92,458

Net surplus (first year of investment) (\$):	28,779
Total initial outlay required (\$):	0