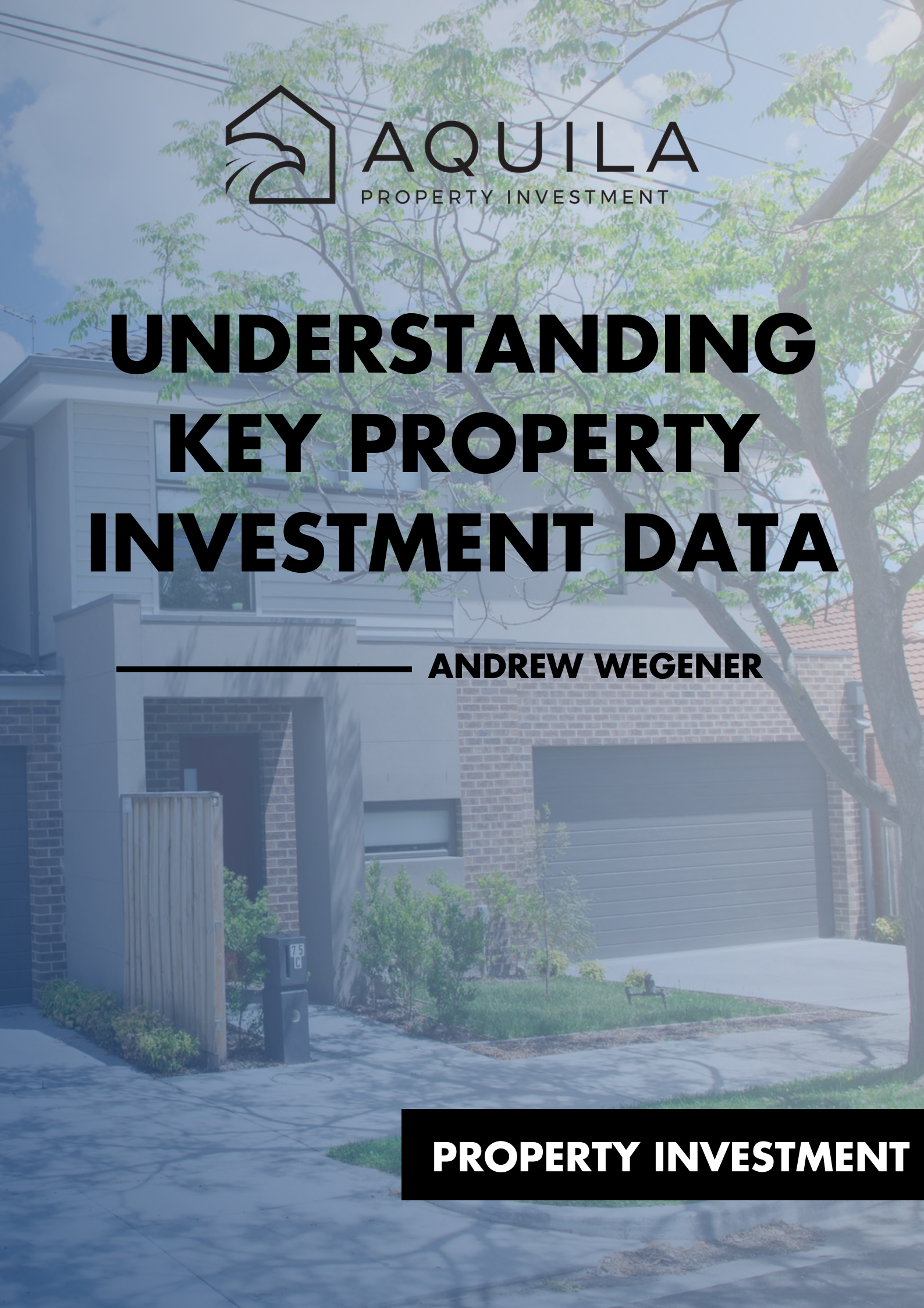


AQUILA
PROPERTY INVESTMENT

UNDERSTANDING KEY PROPERTY INVESTMENT DATA

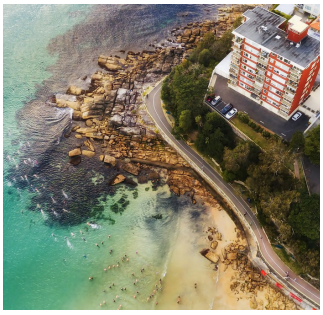
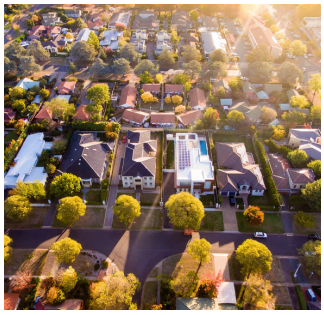
ANDREW WEGENER

PROPERTY INVESTMENT

WHY READ THIS REPORT?

The amount of data that is available to you as a property investor can be overwhelming. With so many different statistics and data points to consider, how do you make sense of it all? This report has been made to help you come to grips with some of the main property investment data topics that you'll come across, and give you an independent insight into what they mean for you as an investor. It will also help you avoid making key mistakes that many investors make when assessing such data.

Enjoy the report!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OWNER OCCUPIER TO RENTER RATIO

The Owner Occupier to Renter shows you what percentage of properties in the suburb are owned by people who reside in the property, versus the percentage of those owned by investors (and thus are rented). It is generally used to assess the quality of a suburb, with a higher percentage of owners signaling a higher quality of suburb.

This is because owners will generally take care of their properties better, improve the value of their properties over time, and be more actively in the local community than tenants. Additionally, as an area grows more attractive, owner-occupiers will pay a premium to live there and over time start crowding out investors. This theory is broadly correct, but its important to understand what is driving this statistic before you assess suburbs on this basis.

There are two main factors here which will create a higher percentage of renters in a suburb:

1. The type of housing within the suburb.

Houses are favoured by owner-occupiers to a much greater degree than other property types. Owner-Occupiers predominantly favour houses, townhouses are distributed relatively evenly between owner-occupiers and investors, while apartments are skewed heavily to investors. As such, suburbs that have a higher percentage of apartments and townhouses will have a higher ratio of investor ownership.

2. The age of the suburb.

New properties are heavily marketed to investors, and so suburbs with a high percentage of new properties will have a higher percentage of investors. At the same time, these locations are unattractive to owner-occupiers; in the case of housing estates, because of their distance from employment centres and amenity, and in the case of medium-high density apartments, these areas are noisy and congested, and the new apartments are too expensive. Housing estates change over the next 10-20 years, as development within an area slows down and new estates move further out. Investors will start to sell up, and are bought out by owner-occupiers, who are attracted to the suburb due to its relative proximity to the CBD compared to new developments. High-density suburbs rarely change, although suburbs with lower-density townhouses and apartments will become more owner-occupier heavy over time.

What are some examples in South-East Queensland? On the new estate side, we have suburbs such as Redbank Plains, which has doubled in size in the past 10 years, and despite being 90% detached houses has a very high 55% renter ratio. Springfield Lakes, which has almost tripled in size in that period, has 93% detached housing, and a high rent ratio of 49%. Pimpama, which has grown six-fold in 10 years, and has an 80/20 split between houses and townhouses, has a whopping 69% renter ratio. Compare this to the Ferny/Arana Hills, an established area in Brisbane's inner north-west, which has 92% detached houses and only 16.3% of renters.

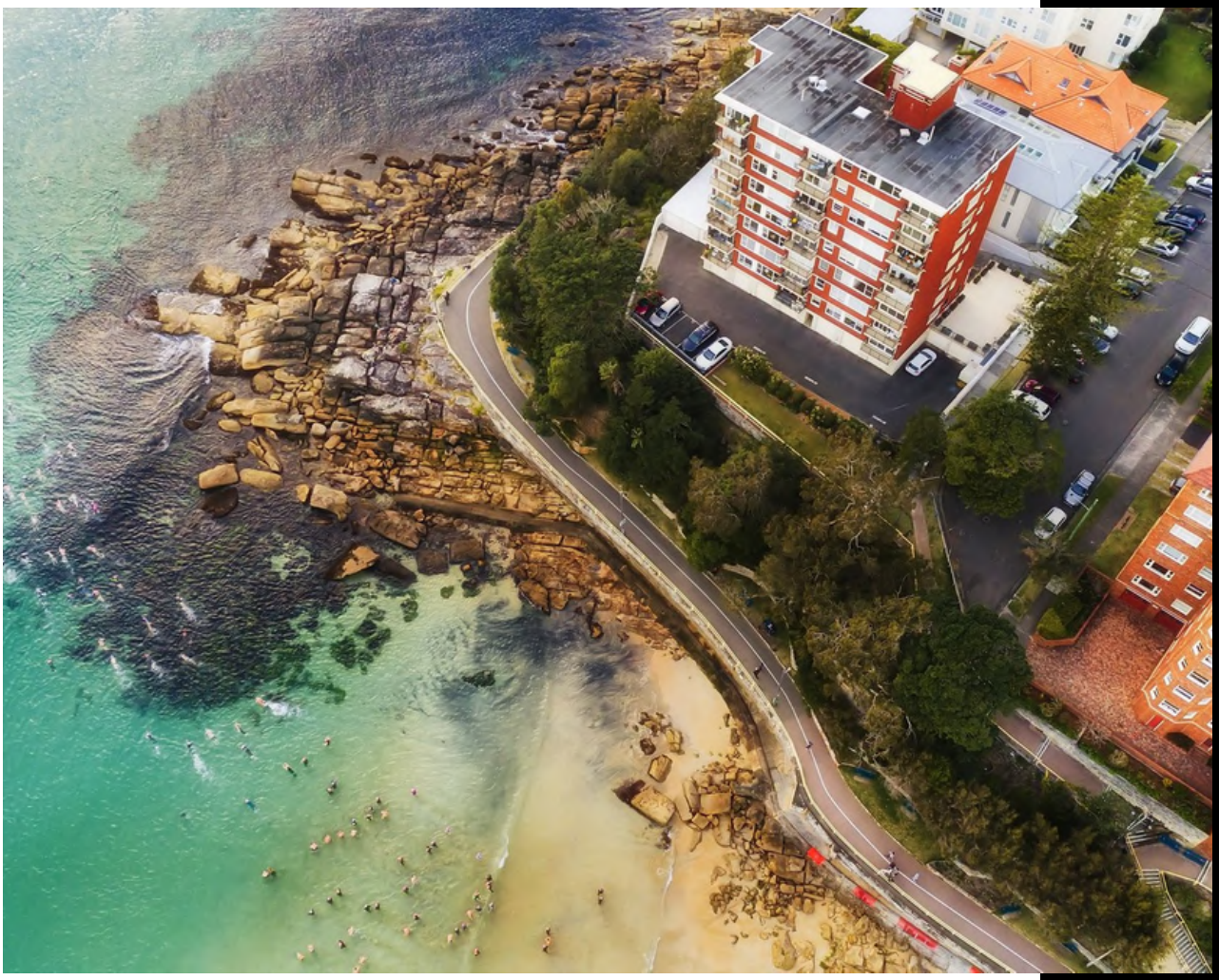
If we look at the inner city, we can see this effect again. In the Newstead-Bowen Hills area, the housing stock is predominantly apartments (90%), and the population has almost doubled in the past 10 years. As we'd expect, the ratio of renters is very high at 64%, although tempered down a little by the demand for riverside apartments amongst wealthy downsizers. Just over the river, the suburb of Bulimba has seen much less growth and has a more diverse range of housing, made up of 50% detached houses, 13% townhouses and 37% apartments. It has a lower percentage of renters (41%) to both Newstead-Bowen Hills and the new housing estate suburbs mentioned above, but significantly higher than Ferny/Arana Hills.

New Estates tend to have a higher percentage of investors, as these types of properties are marketed heavily to investors.

So what this mean for you as an investor?

Owner-occupier/renter ratio is a useful consideration and often does provide a good indicator for the quality and attractiveness of a suburb. However, you must take the age and stock type of a suburb into account, so you can use it as a valid basis for comparison. If a suburb with many new estates has a ratio of <30% of renters, then this is likely to be a positive, while above 50% should be ringing warning bells. Equally, don't expect popular established suburbs with a reasonable proportion of attached housing to match more suburban established suburbs. You could make the assessment that buying in Ferny/Arana Hills is better than buying in Bulimba because it has a lower proportion of renters, yet Bulimba has been the best performing suburb in Brisbane over the past 25 years. Everything needs to be viewed in context.

RENTAL YIELDS



Rental Yield is the return generated from rental income, as a percentage of a property's overall value. At the suburb level, it is averaged out across all of the properties rented in that suburb. A strong rental yield means higher income and is often the basis for 'cashflow positive' investments, making it a popular statistic to cite when selecting a location to invest in. So how should we use this statistic to help us?

There are some broad themes in rental yield which apply quite consistently across the Australian property market. Firstly, rental yields will be weaker in the most expensive suburbs of a city, and stronger in the cheaper parts of the city. Secondly, rental yields will be weaker for detached houses, and stronger for townhouses and apartments.

This can be explained if we understand the economics of rental return. The rental return that a property will generate will be shaped by three main factors:

- **The location of the property** – this will include consideration such as access to employment, transport, services, lifestyle and amenity. This will be an immediate judgment of the location's quality, rather than a long-term assessment of the location's potential.

- **The amenity of the property itself** - Tenants will assess a property based on its internal and external space, design, condition and features, but again in an immediate sense rather than in its future potential. Tenants will not take into account the land or building's future use.

- **The availability of properties which offer similar locational and functional benefits** – the more similar properties available to the tenant, the less they will pay.

One of the keys here is that tenants will not pay for future potential, while buyers will. In the best suburbs of a city, land values will be higher because of the superior location, and also because land has the potential to be put to a more profitable use in the future. This might simply mean an extension of an existing house, or the conversion of an old house into a block of units. Such improvements will be more profitable in the best suburbs of a city than in the worst suburbs, and buyers and sellers of property within these suburbs will recognize this in terms of property value. Tenants don't care about this, however, and will only pay for immediate location and property benefits.

In the same vein, how effectively a block of land is utilised will have a large impact on rental yields. For example, a large block of land in a valuable location which only has an old, small house on it is a very poor utilization of the land, and would return a very low rental yield.

Only one tenant is utilising the benefits of the location, and are not doing it in very salubrious circumstances. However, if the owner demolished the house and build 4 townhouses, 4 tenants can make use of the location, and would enjoy the benefit of a new property to live in, albeit with a smaller backyard than the original tenant. The owner would significantly increase the income from the property, and only have to pay for the construction of the new townhouses, and so his/her yield would increase substantially.

There is also the effect of demographics on rental yields. Those with significant wealth are less inclined to rent as a permanent lifestyle arrangement, because it does not offer as much security, flexibility or prestige as owning. As people grow richer, they can afford to prioritise these needs, even if it does not seem economically rational to do so, As a result, demand from tenants is weaker in richer areas, while the demand from owners is stronger, which both work to reduce yield.

Conversely, in poorer areas, the cost of renting versus owning is a much more coldly rational equation, and in many cases people in these areas cannot afford to own property, which increases the demand for rental accommodation and pushes up rental yields, while reducing the growth in asset values. This is exacerbated by investor activity. Investors will generally pay a premium to invest in the best cities (i.e major capital cities) and the best suburbs of those cities, and will be prepared to sacrifice yield for safety and hopefully higher capital growth.

Suburbs with older housing will generally have lower rental yields than equivalent areas with newer housing. This is evident in a number of suburbs in Brisbane, including Stafford Heights, Salisbury and Keperra.

By definition, yields are tied to asset values, so it an increase or decrease of rental yield is not always as good or as bad as it seems. A increase in asset values but stagnation in rents will lead to a decrease in yield, but would be welcomed by property owners in the area. On the flip side, an increase in yield that came due to a fall in property values, would be equally unwelcome.

So what does this mean to you as an investor?

In South-East Queensland, we see these similar trends in action, with many different nuances specific to areas and property type. When evaluating the rental yields for specific suburbs in South-East Queensland, you'll need to understand the nature of each suburb and how this effects yield.

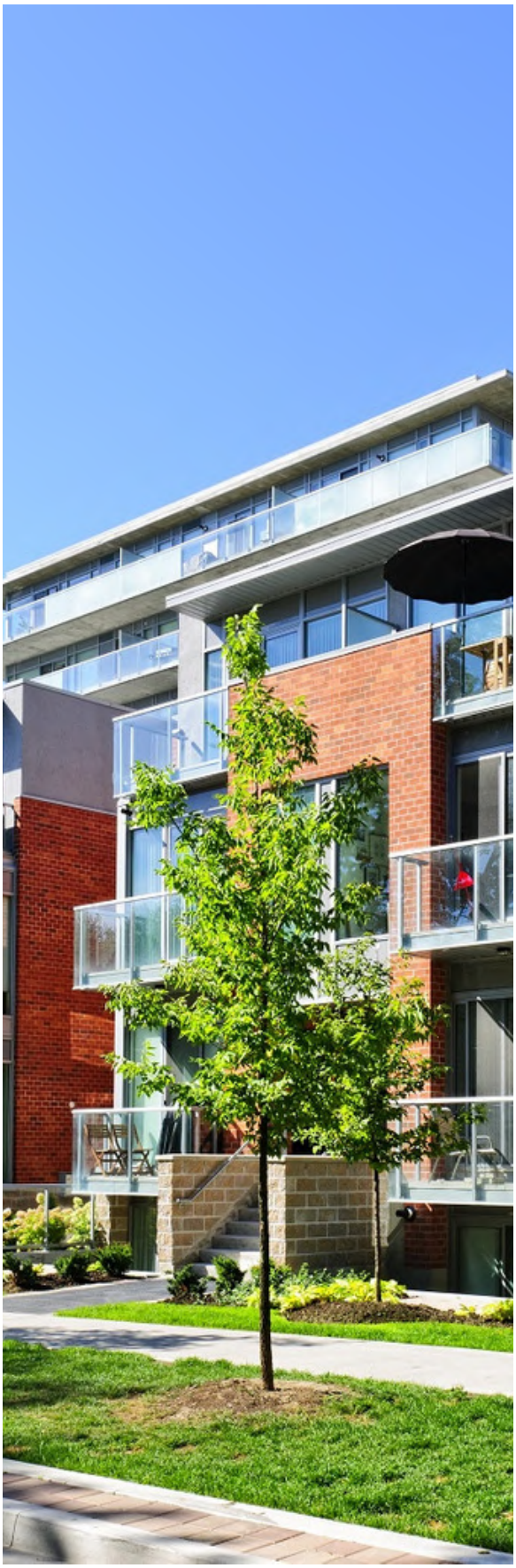
The most expensive suburbs in Brisbane, such as Ascot, Fig Tree Pocket, New Farm, Teneriffe, Bulimba, Hawthorne, Mermaid Beach and Sunshine Beach all have yields below 3% for houses, however, it is possible to find townhouses or units, which make much better utilization of the land, with rental yields from 4.5%+ upwards.

Suburbs such as Stafford Heights and Salisbury within 10km of Brisbane's CBD have poor yields relative to neighbouring areas, due to a high proportion of old housing stock. However, the land values are very similar, as these suburbs offer similar amenity and potential as their neighbours.

Most of Brisbane's outer suburbs have the highest rental yield, but due to future supply/demand have a high probability of achieving the poorest growth.

The recent oversupply of the Brisbane apartment market offer a number of lessons in this regard. Medium and high-density apartments should achieve higher rental yields, as they offer high location benefits as well as the most efficient use of land.

However, developers misjudged the level and type of demand, building too many apartments in certain areas, such as the West End, Woolloongabba, Newstead/Bowen Hills, and Chermside, and too many 1 & 2 bedroom apartments pitched to investors rather than larger apartments suited to downsizing owner-occupier demographic.



This has led to high vacancies and falling rents, as owners have been unable to find tenants and have been forced to discount heavily. Yields have fallen less, however, due to a corresponding drop in asset values. While higher-density apartments are an efficient use of land, the apartments have not been cheap to construct, due to high planning and labour costs.

This has proven to be substantial overcapitalization, and has made the reduction of rental income due to poor market research and design even more damaging. Investors have been lumped with expensive assets that have fallen in value, have little scarcity or land value, and are returning yields no better than many townhouses or units that have much greater prospects of capital growth.

Overall, rental yields need to be kept in the context of the location and property type you are investing in.

Just because a suburb has a low rental yield, you can still find properties within it that will produce a higher yield, which due to their location will make a strong investment. Conversely, if the pursuit of yield leads you to a marginal location, or an over capitalization of built value, then you should probably look elsewhere. There will be little future scarcity for your type of investment, and little capital and rental growth.

VACANCY RATES

The vacancy rate will tell you the number of properties currently available for rent in that suburb, as a percentage of the overall number of rental properties. It is a quick and effective way to check the health of a suburb's rental market. A low vacancy rate means very few properties are available for tenants, which translates into short or no vacancy time for landlords, and will often lead to rental increases. On the other hand a higher vacancy rate will lead to longer vacancy periods and lower rents, as there is more choice for tenants and less imperative to pay higher rents to secure a property.

What kind of vacancy rate should you look for? It's generally accepted that 2% or below is a good figure to aim for; in essence, this means that your property will be vacant on average for 1 week or less a year, and leaves you little risk of extended vacancy periods if the property is presented and priced correctly for tenants.

Does this mean you shouldn't consider markets with a higher vacancy rate? Not necessarily. Like with all property data, vacancy rates need to be interrogated further.

The headline vacancy rate for a suburb will give you the total percentage of vacancies, without telling you the specifics in terms of property type, price point or location within the suburb. For suburbs with a wide spread of property types and rental prices, the vacancy rate can be misleading. For example, properties at the low end of the market may be having very little trouble renting, while those at the high-end sit for some time. We have recently bought a number of apartments in Bulimba for clients at the bottom end of the price point (mid-$300s), and have had very little difficulty renting these out, despite the suburb's apparently dire vacancy rate of 4% - most of the available stock is at the higher-end, while entry-level property is relatively scarce.

Or perhaps there is a glut of apartments on the market in a suburb because of new development (these will always take some time to completely fill up) but very few houses available for rent. Hamilton, in Brisbane's inner-east, is experiencing this situation; 177 of its 1336 rental properties are currently available to rent – but only 22 of these are houses and townhouses (which make up 38% of the suburb). The problem lies with apartments.

The vacancy rate does not take into account the different types of housing stock. Therefore, suburbs with a high number of new apartments are likely to have a higher vacancy rate, even if houses to rent are in short supply.

A simple check that I use to dig deeper into the vacancy rate of a suburb is to look at the number of properties available for rent in a suburb on realestate.com.au or domain, and segment it by property type and price. This will give you a more accurate indication of what is available and what will potentially be competing with your investment.

Overall, vacancy rates need to be considered in the context of your wider investment decision, so I don't agree with hard and fast rules here. If the property makes a great investment in all other areas, but will have 2 weeks vacancy per year instead of 1, should you still consider it? Absolutely. Many of the best-performing suburbs in South-East Queensland have had high vacancy rates at times. You just need to factor this in to your returns. Also a suburb may have high vacancy rates now, but this may come down in the long-term due to limitations in future supply – which is why understanding future supply is so important!

Numbers that would genuinely alarm me are 5%+, particularly in areas with one predominant stock type. These kind of numbers are usually generated by areas with heavy development, and are best avoided anyway.

LOCATION SCORE/DEMAND TO SUPPLY SCORE

‘Buying Property Made Simple’ is the marketing claim of the website LocationScore (similar scores can be found at DSRData and BoomApp). Is this a realistic claim? Or is it just another flashy marketing tool in an industry riddled with them?

WHAT IS A DEMAND TO SUPPLY SCORE

A demand to supply score is generated for a suburb by aggregating data across 8 different property indicators, before an algorithm is used to produce a specific score. This score determines the current level of demand within a suburb versus its current level of supply, and ranks it against other suburbs, in the context of the entire Australian property market. In my experience it is an effective tool, that generally reflects the reality on the ground and is a useful predictor of short-term capital growth (or otherwise). However, it has considerable limitations as a predictor of long-term capital growth. Like all tools, it needs to be used in the appropriate context, and is just one of the many tools available to us to make sound investment decisions.

To use a demand to supply score properly, we need to understand exactly what it tells us. The raw data it uses are the 8 following property indicators:

- **STOCK ON MARKET**

The percentage of the overall number of properties in the suburb currently available for sale

- **ONLINE SEARCH INTEREST**

The average number of searches for a particular suburb on online portals, divided by the total number of properties for sale in that suburb.

- **VENDOR DISCOUNT**

The difference between the original listing price of properties and their final sale price

- **AUCTION CLEARANCE RATE**

The percentage of properties taken to auction, which sell at auction

- **RENTERS/OWNER OCCUPIERS SPLIT**

The percentage of renters within the suburb versus the percentage of owner-occupiers

- **DAYS ON MARKET**

The number of days on average properties take from listing through to a settled sale

- **VACANCY RATE**

The number of rental properties in a suburb which are currently available for rent

- **RENTAL YIELD**

The average gross income generated by rental properties across the suburb, expressed as a percentage of the median value of property within the suburb.

I explain some of these indicators in detail elsewhere – you can click on the links to find out more.

WHAT ARE THE KEY INDICATORS OF THE DEMAND TO SUPPLY SCORE

From an asset value perspective, the key indicators are stock on market, days on market and vendor discounting. If there is limited stock on market and it is selling quickly without much discounting, this is a hot market, regardless of the other statistics, and will likely lead to price growth. Renter/Owner-Occupier split is a better long-term indicator than a short-term one, as it says more about the character of a suburb than short-term supply and demand. From a rental perspective, rental yield and vacancy rate will give you a good idea of the strength of a rental market, although rental yield can be ambiguous, as it is tied to asset values not just rental demand.

Auction clearance rate is problematic in Queensland, as auctions are an uncommon method of sale, due to historical preference and onerous government requirements around price disclosure. They are more common in high-end suburbs, and less common in lower-end markets, which means that the number of auctions in a suburb will often be too few to provide a meaningful indicator. Sometimes this can distort the results.

HOW DOES THE DEMAND TO SUPPLY SCORE PERFORM IN REAL LIFE?

So how does the DSR Score perform overall? I've found it to be very effective in determining immediate demand/supply in lower-end and mid-range suburbs, where there is plenty of data for each indicator, and where the rental market is aligned more closely with the owner-occupier market. Suburbs with a high demand to supply score will generally have large numbers of people at open homes, and properties, if well-priced, will frequently sell on the first weekend.

I've found it less effective in suburbs at the top end of the market, which will mostly achieve only an average or below average score, but still see the highest level of price growth. I believe this is because there are less buyers at the top end, which reduces the level of online search interest and increases the number of days on market, as deals take longer to reach. However, the sales prices will often be higher, because buyers have more capacity to pay and sellers can usually afford to hold out for the price they want. So don't necessarily be deterred from a high-end suburb because of a lower DSR Score – it's not necessarily a true guide of future price growth in the suburb.

The biggest limitation with LocationScore/Demand to Supply Score is in accurately predicting long-term growth.

The greater limitation with demand to supply scores is their predictive power over the longer term. The score only takes into account immediate, not long-term supply and demand.

An extreme but pertinent recent example is property in mining towns. You can be sure that many of the mining towns in Queensland, such as Moranbah, Dysart, Roma and Middlemount, and Western Australia, such as Karratha, Port Hedland and Newman, were achieving high demand to supply ratio scores during the peak of the mining boom. After all, buyer interest was very strong, properties were selling very quickly, stock on market was low and rental yields were exceptional. Those who bought at this time would have seen strong growth over the next two years, before experiencing a catastrophic plunge of up to 75% in value after that. The Demand to Supply Ratio score was accurate at the time. However, it couldn't predict the changes in the housing market wrought by the collapse in resource prices and the loss of jobs which followed (demand), and the big increase in housing stock driven by the boom in prices (supply).

So to return to the original point, does the score make property buying simple? Well, it does make it simpler – it's a tool which can save you a lot of time in aggregating data from a range of sources, and for the right suburbs, gives you a pretty accurate snapshot of the current state of the market. It's also helpful for checking on an area being spruiked as 'hot' by property marketers; take the cases of Ripley, Yarrabilba and Pimpama – all 'growth' locations according to marketers but all rank as 'poor' on the demand to supply score.

But should it be your prime decision-making tool for selecting a location? I don't think so. A high demand to supply score probably signals short-term price growth, but few of us are investing only for the short-term. Buying when the DSR score is high may mean buying at or near the peak of a market, which is a poor long-term investment strategy. On the other hand, If I can buy in a quality suburb with low future supply, but that currently has a low DSR Score, I will, because I have confidence in the location long-term, and because counter-cyclical buying can mean buying a property below its intrinsic value, rather than above its intrinsic value at the peak.

MEDIAN SALES PRICE

Median house and unit prices for a suburb will tell you what the ‘middle’ sales price has been over a period of time, such as a year. A suburb may have 100 sales in a year; the middle price is halfway between the 50th and 51st sale ranked in order of price. Changes in the median price data over time is used by many people to determine changes in asset values, and is often cited to justify why you should buy in a particular suburb (it has grown x % in the last 12 months).

Leaving aside the obvious point that past performance is not an indicator of future performance, there are some fundamental issues with median prices as a statistic which you should be aware of. Like any statistic, its usefulness is determined by

- The amount of data you have
- The time period you have the data over
- The level of variability in the input data

In the ideal world, we could track median sales prices with lots of data over an unlimited timeframe with no variability in the inputs. It would look something like this. We track the price of a suburb with a thousand sales per year, over a 50 year period of time. All of the properties in the suburb are identical in attributes, and no owner improves the value of their property in any way. This would give us an extremely accurate picture of median sales price movement.

The amount of sales data would exclude sales data which is misrepresentative, the length of time the data was acquired over would give us a true picture of performance over a genuine investment timeframe, and the consistent input data would allow us to make accurate deductions about what the data meant to all of the properties in the suburb.

Clearly though, this isn't the case. Some suburbs have very few sales, or sales fluctuate dramatically between years. Much of the median sales price data is given to you for a paltry 1,2 or 5 year timeframe – well below a true investment timeframe.

Finally, the data we have varies considerably; while some properties may have changed very little over a period of time, others will have been completely renovated and extended. In suburbs with high levels of development, new properties will often push up the median price without affecting (or in many cases reducing) the value of existing property.

There's a great article from Michal Matusik which highlights this - read it here.

Year	No. of Sales	Median	Growth	Low	High
1994	1	$156,000		$156,000	$156,000
1995	1	$26,000,000	16566.7%	$26,000,000	$26,000,000
1996	1	$332,000	-98.7%	$332,000	$332,000
1997	0				
1998	1	$357,000	7.5%	$357,000	$357,000
1999	3	$120,000	-66.4%	$48,500	$415,000
2000	22	$201,000	67.5%	$150,000	$7,037,000
2001	83	$185,000	-8.0%	$46,500	$460,000
2002	120	$216,000	16.8%	$40,000	$435,000
2003	205	$285,000	31.9%	$49,000	$550,000
2004	185	$350,000	22.8%	$178,000	$715,000
2005	220	$355,000	1.4%	$125,000	$730,000
2006	288	$370,000	4.2%	$134,000	$735,000
2007	482	$410,000	10.8%	$40,000	$810,000
2008	303	$449,000	9.5%	$174,500	$770,000
2009	483	$440,000	-2.0%	$147,000	$4,200,000
2010	431	$450,000	2.3%	$168,000	$892,500
2011	414	$437,750	-2.7%	$269,000	$800,000
2012	387	$430,000	-1.8%	$197,000	$850,000
2013	449	$438,500	2.0%	$224,880	$885,000
2014	502	$449,250	2.5%	$233,650	$1,200,000
2015	521	$460,000	2.4%	$234,800	$1,000,000
2016	479	$470,000	2.2%	$324,000	$1,050,000
2017	448	$492,500	4.8%	$235,000	$1,950,000
2018	288	$485,000	-1.5%	$235,000	$1,125,000

Median House Price and Sales Data for North Lakes, Queensland. 1994-2018

An example of North Lakes in northern Brisbane is a good one. We can see here that the suburb didn't have a meaningful number of sales until 2000-2001, which gives us 18 years of useful data. During this period there's been a big increase in sales as the suburb expanded, with a slight tail off lately as development has slowed. And what about price growth? There's some very strong growth from 2000-2008, which is too high to be purely written off as the increase in the cost of new housing. However, from 2008-2017 (the last full year of data), growth has been only $43,500, or just over 1% per year. In reality, property built 10 years ago is selling today for roughly what it cost to buy, and in many cases below this. So the small 1% per year gain is a reflection of newer housing pushing up the median, rather than a genuine gain for the unfortunate investors of 10 years ago.

ABOUT THE AUTHOR

Andrew Wegener is a qualified property investment adviser, buyers' agent and educator. He specialises in helping the next generation of investors master their money to build sustainable wealth so they can have less stress, more fun and find meaningful ways to help others.

In a largely unregulated industry that typically rewards conflict of interest and bad advice through undisclosed commissions, Andrew bats for his clients with independent analysis and recommendations. He's developed a reputation for detailed research and for speaking fearlessly and frankly on the property market and the property investment industry.

As the Director of Aquila Property Investment, he's kept busy working with clients to source quality investments in South East Queensland. He is particularly energised by working with younger investors buying their first property.

Considering taking the plunge and investing in property? Book in a free consultation with Andrew and get insightful and unbiased advice on your next move.

INSTANTLY BOOK YOUR FREE CONSULTATION