



**AQUILA**  
PROPERTY INVESTMENT

# WHAT IS THE RIGHT PROPERTY TO INVEST IN?

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**PROPERTY INVESTMENT**



# INTRODUCTION

It's one of the age-old questions for property investors; should you buy a house, a townhouse or an apartment? Which will produce better returns for you? You'll have no doubt heard plenty of arguments in both directions; for example, 'Houses are better because you get more land' or 'Apartments are better because they're lower maintenance'.

The short answer is that any of these property types can make a good investment, and that most of the contributions to the 'houses versus apartments' debate are shallow and simplistic. All property types can be effective investments if you understand and apply the basics of supply and demand, and buy a property type that will be in high demand but low supply in the future.

So how do we figure this out?

## PROPERTY TYPES

Firstly, we need to understand the fundamentals of each property type. There are three main residential property types: houses, townhouses and apartments. Each have specific strengths and weaknesses. If you're familiar with these, then skip down to the next section.



WHAT IS THE RIGHT PROPERTY TO INVEST IN?

# HOUSES

A house is considered a detached properties, which means it does not adjoin any other buildings. It sits on its own block of land, which means that as the owner you own the house and land without having to share ownership with anybody (this is known as Torrens Title). This makes houses the most flexible property type, in that you can do as you wish with the building and land without the agreement of others, as long as it conforms with council regulations. You can renovate internally and externally, and extend the building to better suit living requirements as they change. Houses are the most common property type, and have traditionally have been the most popular. The construction of houses in the future is also limited by the supply of land. This provides a level of safety and predictability in terms of both the supply and demand of houses, making them a consistently attractive option for investors.

Houses do have their downsides, however. They are bigger and have more surface area than a townhouse or apartment, making them costlier to maintain. Houses also make relatively inefficient use of land which has made them increasingly expensive over time. This means that you will generally not be able to buy a house in as good a location as a townhouse or an apartment. It also means that you are likely to receive a lower rental yield.

The size and flexibility of houses make them appealing to almost all demographic groups, and particularly to families and other larger households. Modern houses are traditionally 4 bedrooms, 2+ Bathrooms and 2 Car Spaces.





# APARTMENTS

Apartments are considered to be attached properties, as they are inextricably attached to other buildings. Apartments are built adjoining each other and on top of each other on a single block of land. Because there is no single owner of this land, and access to each apartment requires common areas such as driveways, hallways and stairways, apartments come under a different title scheme known as Strata Title. Strata titled properties require a body corporate which administers common areas, insurance and also looks after the external aspects of the building to maintain consistency across the complex. As an owner, you will contribute money to the body corporate and have a say in its decisions.

The strata title aspect of apartments is considered by many investors to be the biggest drawback to owning one, as it reduces your flexibility and may lead to you being forced to pay high body corporate levies to maintain the complex and its facilities. You will also have very limited scope to modify the apartment once it is built; you can renovate it internally but you can't change the externals or extend the building. Also, because apartments can be built on top of one another, they are not as limited by the supply of land. This can lead to rapid oversupply within an area if too many buildings commence at once.



Nonetheless, apartments are becoming more popular in Australia. Our households have become smaller over time, and as less physical space is required, apartments offer an easy, low-maintenance option. Apartments can offer common facilities, such as pools, gyms, and rooftop areas that would be unaffordable to maintain by one property owner alone. Additionally, while body corporates can be costly, a well-administered one can save time and money by professionally managing the complex and sharing costs between owners. Apartments can also offer views that are simply not achievable with a house. Finally, by using land more efficiently, apartments are cheaper to buy than a house in an equivalent location, which enables owners to either save money or choose a better location to live in.

For investors, the combination of lower maintenance costs, a higher rental yield and a superior location for the price can make them a strong investment option. This needs to be balanced against the lack of flexibility and the risk of oversupply.

Most apartments are 1 or 2 bedrooms in size, so are most appealing to singles and couples. The accessibility and ease of maintenance makes them particularly attractive to downsizers and retirees, as well as young people.

## TOWNHOUSES

Townhouses sit in the middle of houses and apartments, sharing characteristics of both. They are known as semi-detached properties, as they will generally adjoin another townhouse, but won't be built on top of one another, and usually have a backyard or courtyard area of their own.

Townhouses are mostly strata-titled, as they require common areas such as driveways, and generally require shared building insurance. In some cases, however, they can have torrens title. Because townhouse complexes usually require fewer common areas than apartments, the body corporate levies are often lower.

Townhouses offer a balance between the size and privacy of a detached house, and the low maintenance and efficient use of land offered by apartments. They still require land to be built on, so the supply of townhouses in a location is naturally constrained.

However, a number of townhouses can be built on the same block as one house, which decreases their cost. They will usually be smaller in size than a house but bigger than an apartment, with the most popular configuration being 3 Bedrooms/2 Bathrooms/1 Car.



This configuration is quite flexible and can appeal to singles, couples, smaller families and downsizers/retirees, although because most townhouses have stairs, they become less appealing to the aged. Like apartments, they are difficult to substantially modify once built. For investors, townhouses balance the advantages and disadvantages of the other two property types, including flexibility, maintenance, location and rental returns.



So now that we understand the different types of property we can buy, what's next?

## **PROPERTY SUPPLY AND DEMAND - THE BIG PICTURE**

The value of everything is determined by the laws of supply and demand, and properties are no exception. In a perfect market, the future supply of property would match the future demand of buyers and renters perfectly, leading to price equilibrium and consistent performance across all locations and property types.

However, the property market is far from perfect. Developers of new property only have limited land available for them to build their product, and they are restricted by government as to how the land can be used. Property development also has long lead times between start and finish, sometimes many years, and cannot easily change to meet changing demand. Ultimately, this stops developers from meeting the market with the right kind of property supply. The resulting mismatch between demand and supply creates wealth for some and destroys wealth for others. We want to be on the right side of this equation.





# FUTURE DEMAND

Knowing exactly what people will want in the future is not a simple task, and if we all knew perfectly what the future would bring, we'd all be rich! There are, however, some key trends which we can take note of:

- People are living longer and having less children. This means more time as a percentage of people's lives are spent without children in their homes, which is making more compact properties in better locations more popular.
- People are getting wealthier, and their property expectations are higher. Regardless of our stage of life, we are expecting bigger, more luxurious properties with better design and more features.
- Smaller households mean that the number of bedrooms are becoming less important in a property. Instead, property buyers and renters are prioritizing other parts of the property - kitchens, bathrooms, living areas, and outdoor entertainment areas. There is also a growing expectation for extras such as pools that would have been considered a luxury item previously.

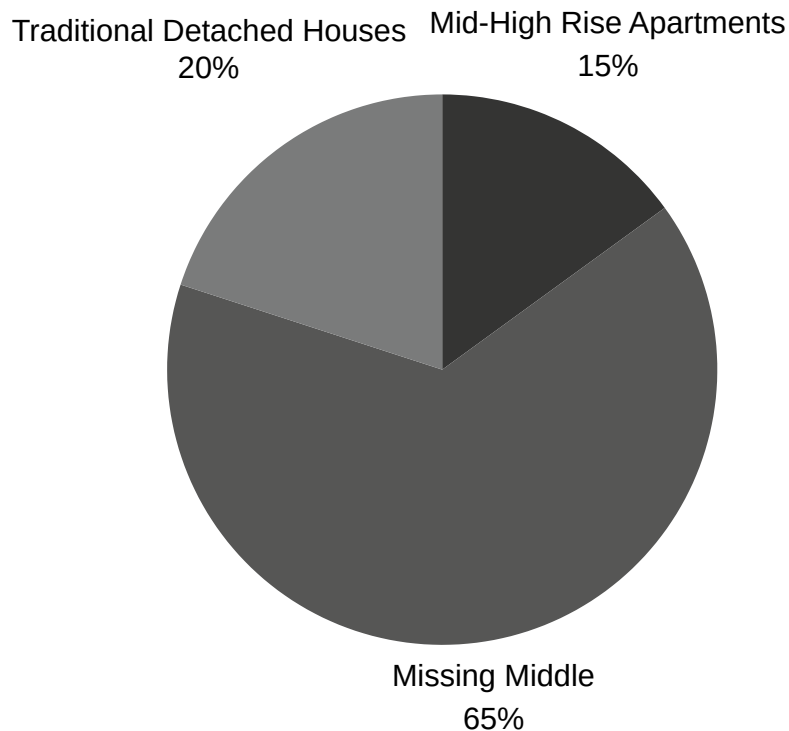
How will these trends flow through into future housing decisions? Here I'm indebted to the work of Michael Matusik - one of the best analysts of this topic in Australia. He breaks down properties into three different types. Firstly there are traditional detached homes on a standard block of land. Secondly, we have mid-high rise apartments - built in large complexes and usually at least 5 storeys in height.

Finally, we have the so-called 'missing middle'. These properties usually live in the inner and middle-ring suburbs of our major cities, and consist of small-lot homes, duplexes, townhouses and boutique apartments. From here, his team has forecast how demographic changes will shape the demand for new properties over the next decade.



The graph below shows the results:

## HOUSING DEMAND - NEXT TEN YEARS



*Source: Matusik*

The results, based off the trends we've already discussed, are pretty clear. We will increasingly favour properties that offer a balance between location, flexibility, space, design, and of course, price. This will be best met by the 'missing middle' - well-located smaller homes, duplexes, townhouses and apartments in smaller complexes.

There will still be a market for high density apartments in the inner city and new homes built in the outer suburbs, but this will not be what the majority of buyers or renters want.

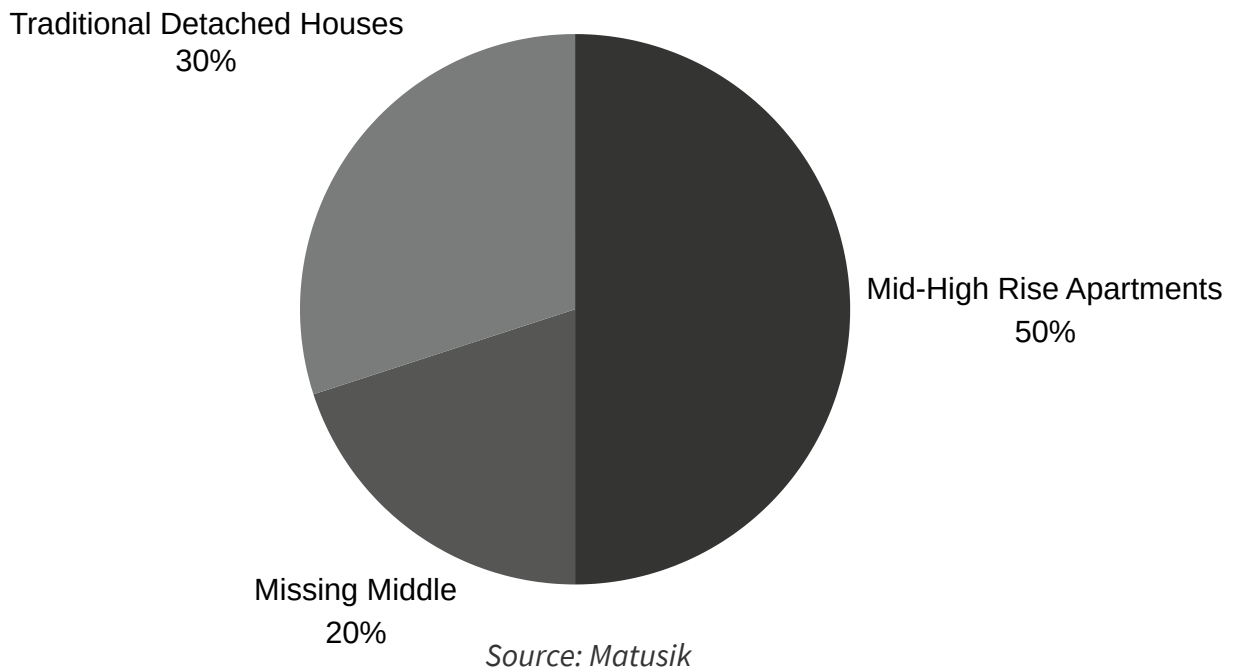




# FUTURE SUPPLY

So what is the market building to meet this demand? This is where the problems start arising, and for investors, where the opportunities and dangers really open up. Firstly, Matusik provides us with a summary of what has been constructed in the Australian property market over the last five years:

## HOUSING SUPPLY - LAST FIVE YEARS



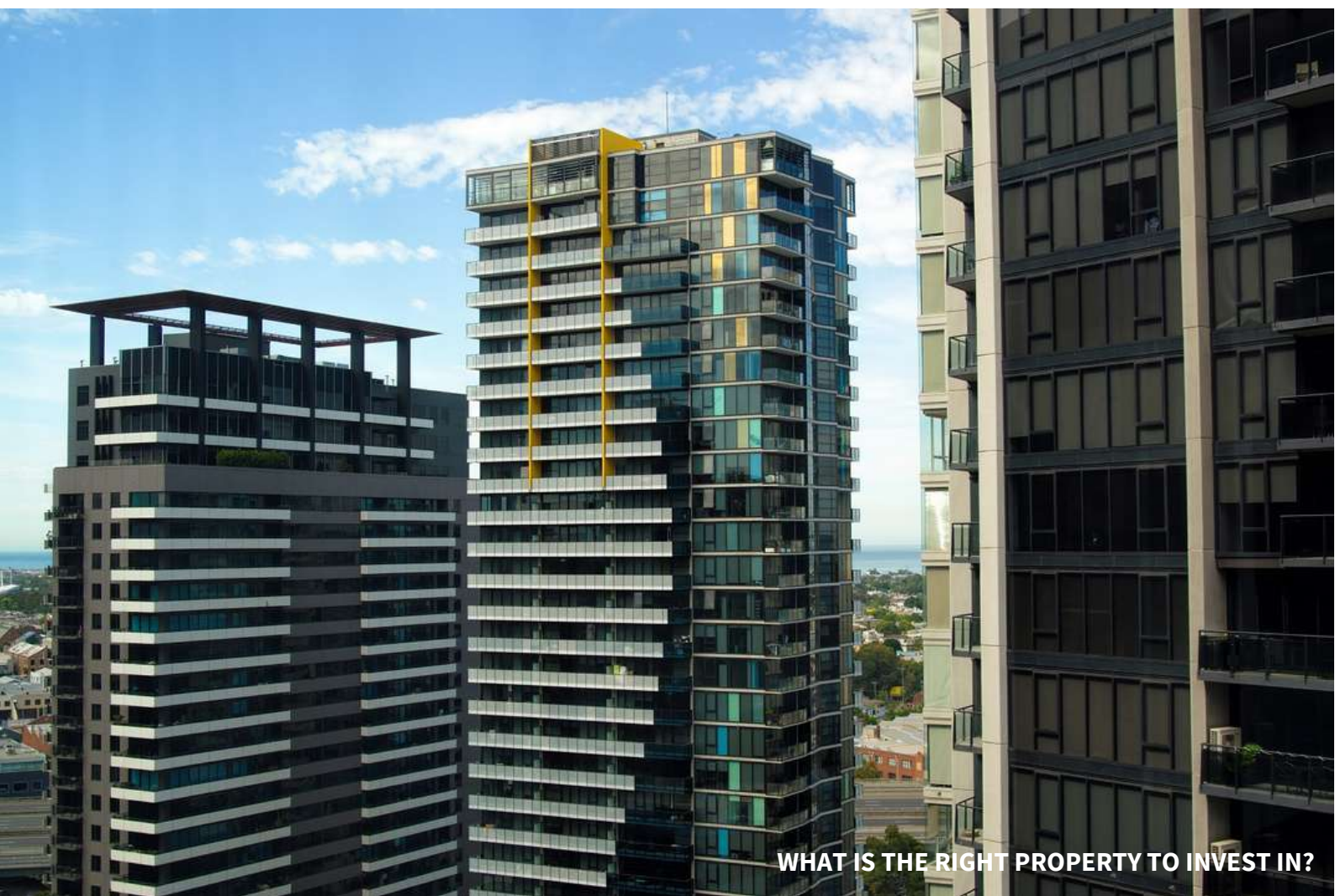
As you can see, supply is not meeting demand. If you want the simplest answer for the apartment oversupply and price falls in Australia's capital cities, here it is.



Too many smaller, mid to high-rise, investor-focused apartments have been built and the market is not prepared to absorb them. The supply of new detached houses has been closer to demand, but almost all of this is being built on the outskirts of our cities, away from employment centres and services. The lack of housing supply in the inner and middle-rings of our cities has led to soaring house prices well above wage growth, particularly in Sydney and Melbourne, where demand has been strongest and land at its most scarce.

If we look to the future, this mismatch is unlikely to be solved. Unlike future demand, future supply is managed by governments and is easier to predict. The picture here is also stark. If we look at Brisbane, for example, almost all of the land supply for new detached housing is outside of a twenty kilometre radius of the CBD. Of the 240,000 detached houses planned to be built in Brisbane over the next 25 years, 95% are in the outer suburbs.

The situation with townhouses and apartments - the property types which make up most of the 'missing middle' - is similar. The Brisbane metro area is expecting to see 140,000 new units (townhouses and apartments) built in the next 25 years. While we don't know the exact nature of what these units will be, the suburb breakdown is a give-away: 70,000 of these units will be built in only eight suburbs. These will almost all be mid-high rise apartments - they simply can't be accommodated otherwise. Instead of spreading the supply of units across the city, where a mixture of types could be built, they'll be concentrated into high-density areas, leading to continued oversupply in these locations but shortages of the right property types elsewhere.





Too much of our future housing supply will be medium to high-density apartments and houses in the outer suburbs.

This is a problem created by physical land supply and compounded by government planning and restrictions. Land supply is at a premium in our major cities as the population grows and infrastructure struggles to keep up. Moreover, the zoning laws put in place by government restricts how the land in our cities can be used, and in many cases prevents outright the construction of the properties demanded by buyers and renters.

It is making it increasingly costly for developers to construct the types of property wanted by buyers, and this is compounded by government taxes and fees such as GST, stamp duty and infrastructure charges, which can add 20% or more to the cost of a new property.

The result? Developers are forced to continually increase density to make a profit. Detached house block sizes in the outer suburbs are diminishing relentlessly, while remaining unsustainably large in established areas. Townhouse complexes are moving further out of the city and are growing in size, and the builds are becoming narrower, with two adjoining walls instead of one, reducing space and natural light.

Meanwhile, apartment complexes are turning into large, soulless high-rises which crush their owners with high maintenance costs and body corporate levies as they age.

## WHAT TYPE OF PROPERTY SHOULD I BUY THEN?

This is a fairly grim picture of Australia's future housing supply. It does, however, create opportunities for the strategic investor. We know that certain types of properties, such as high-rise apartments and detached houses in the outer suburbs, are likely to be oversupplied. Other property types, such as strategically located detached houses, duplexes, and townhouses, and apartments in small complexes, are likely to be in high demand but short supply. These are the properties I would invest in.



# WHAT SHOULD I LOOK FOR IN ONE OF THESE PROPERTIES?

After choosing the right type of property, there are a number of key considerations we need to keep in mind when assessing the property itself. Other than the location itself, there are many different variables, including:

- Land Size
- Land Value
- Build Type and Quality
- Age
- Internal/External Space
- Configuration
- Design

How important each of these variables are will depend on the investment strategy you've chosen. For example, if you're buying a property to land-bank, the building will be relatively unimportant, but the land itself will be very important. If you're buying a new apartment, on the other hand, then the build quality, design and configuration will be very important, while the value of the land is unlikely to be relevant for a number of decades.

Nonetheless, there are a number of considerations for each property type that are consistent across different properties, and if achieved, will help to future proof your investment. They are built on the critical supply and demand trends that we've already analysed, and I've discussed some of the key ones for each property type in detail below:

## HOUSES

**Land Size** - For a simple buy and hold (i.e not a development or subdivision), you don't need a massive block size, but extra space on the block is becoming an increasing differentiator. Many new blocks have very small backyards, so an extra 100 sqm here can feel enormous. Side access and room for a pool, shed or even a granny flat will give your block more appeal to future buyers and gives you the opportunity to value add yourself and create extra rental income.





**Configuration** - A 3-4 Bedroom, 2+ Bathroom, 2 Living Area, 2 Car configuration is the best way to ensure your house remains in demand from buyers and tenants. Parents want a separate bathroom from their children, and also would prefer separate living areas from them as well. If you don't have this configuration, make sure you can achieve it with a renovation if you're planning on holding the property long-term.

**Internal/External Space** - Many new developments will squash you so good internal space will be a competitive advantage for your property. You want your main living area to be at least 6 meters in length or width to accommodate a dining area and a larger couch. A large kitchen is also critical for a bigger family. At least 3 Bedrooms should be 3 x 3 and the master should be bigger still. A covered outdoor area for entertaining is very important.

**Design** - Good flow between the kitchen, dining/living area and the outdoor area is a high priority. Bedrooms should be entered through corridors and not off the main living area to enhance privacy and reduce noise. Good natural light into the kitchen and main living area will completely change the feel of a home.



*Extra space on the block for outdoor living features will become more scarce, and will help your investment be more attractive to future owner-occupiers.*



# TOWNHOUSES & APARTMENTS

**Configuration** - A 3 Bed 2 Bath/1-2 Car townhouse is best option in most cases. This is flexible and fits most buyer and renter types. A separate laundry and powder room downstairs, with both bathrooms upstairs is the way to go.

2 Bed 2 Bath apartments are the minimum if you're going to hold the property long-term. A 3rd bedroom can give it a level of uniqueness and potentially attracted smaller families, but don't pay too much extra for one.

**Internal/External Space** - Clearly the more spacious the better here for both townhouses and apartments, but I would be looking for a minimum of 120 sqm of internal space (including garage) for a townhouse and 80 sqm (not including parking) for an apartment.

Townhouses should have a decent sized undercover courtyard and ideally some grass or gardens. Apartments should have a balcony large enough for an outdoor setting. The internal living area should fit a large couch comfortably and a small dining setting as well. At least 2 bedrooms should be 3m x 3m, and like with houses, a big master bedroom is increasingly important.

**Design** - Because space and light is at more of a premium for these property types, townhouses and apartments live or die by their design. The aspect of a property is critical as it will determine natural light. North is the best.

The number of aspects is also very important. For an apartment you should aim for two aspects, so a corner apartment is key. For townhouses, avoid row townhouses which give you only two aspects, unless they've compensated through extra light sources or higher ceilings.

Good use of space internally is critical. You don't want wasted space with corridors and stairways where you don't need them. Wider, fatter rooms are better than longer, narrower ones, as they feel more spacious. High ceilings transform townhouses and apartments and are well worth it.

**Land Value** - This might not seem like a factor in the short-term for a townhouse or apartment, but for those playing the long game, it can be very important. Eventually, the building itself will be worth nothing, and all you'll have is your share of the land it sits on. If your share of this land is very small (think high-rise apartments or sprawling townhouse complexes), then what you'll be left with will be small. As a result, you'll need to keep investing in the upkeep of the building in order to retain the value of your asset, which can become prohibitive.





**Build** - The build quality of a townhouse or apartment is a very important factor in the longevity and maintenance costs of the asset. A well-constructed brick townhouse or low-rise apartment is likely to stand the test of time and require little maintenance. In our experience, many newer builds have not been constructed to as high a quality, using cheaper materials and suffering from poorer workmanship.

This has been most pronounced in the high-density apartment market. Best case, a high-rise apartment will cost approx 50% more per sqm to maintain than a low-rise apartment, as there is both more built area to maintain and access is more difficult. Moreover, the last 20 years have seen very poor 'hygiene' across much of the high-rise construction sector, with low build quality, cheap materials and developer shortcuts a regular feature in new developments - not to mention ticking timebombs such as flammable cladding. You're a brave investor to purchase a medium-high rise apartment built over this period, and the regulation of the industry has not caught up enough yet to prevent similar problems in current developments.

Ultimately, if you heeded the message of this report, you'll realise that high-rise apartments should be avoided for a range of reasons. Build quality is one, a lack of land value another, and the consistent risk of oversupply the final nail in the coffin. High-rise apartments in Australia are a luxury item, not an investment, and should be treated as such by sensible investors.



*Well-located, low-rise apartments with good internal and external space and multiple aspects should remain in strong demand and short supply into the future.*



# 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 and around Australia. 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.

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