



Gone are the days when it was common practice to buy an owner-occupied home as your first property. In today's environment of high rental demand and short supply, buying your first home as an investor might place you on stronger ground

Like many things in life, property is personal. And like many things in life, it can also be calculated.

Of the many decisions a first homebuyer has to make, deciding whether to be an owner-occupier or an investor could be the most crucial. The appropriate research and calculations must be combined with your personal preferences and priorities to choose the best option for you.

To allow a more informed choice, *Your Mortgage* has compiled a scenario-based comparison between two first homebuyers – one owner-occupier and one investor. The detailed comparison can be used as a

guide to the financial part of being a first-time buyer (during the first five years).

Rich Harvey, director of propertybuyer, says that although the final calculations might conclude that one type of first homebuyer is more financially viable than the other, your final decision must be based on your individual needs and wants: "First homebuyers need to decide based on what's going to work for them best, because you can get so carried away and analytical about the numbers, and, I guess, don't enjoy the process of moving forward and being a first homebuyer."

The verdict must be based on whether you would like to begin your property

career early, or whether you simply want to enjoy a sense of ownership.

"If you don't have a personal need to live in a property you own, you can rent somewhere else but still get into the market as a landlord. This way, not only do you still get to own that rising equity, you have a tenant and tax breaks to help you manage the costs," says Margaret Lomas, founder of Destiny Financial Solutions. "It comes down to whether the margin between the income and the expenses on an investment property (after your tax breaks), plus the rent you pay elsewhere, is less – or more – than what you would pay if you owner-occupied."

The financials

The process of applying for and obtaining a mortgage as a first homebuyer is usually the same for owner-occupiers and investors. All fees and charges should be similar, and the features offered to you as a borrower will simply differ according to the product you choose.

Your product selection will differ according to what's best suited to you as an individual borrower. Owner-occupiers will opt for an owner-occupied home loan, and investors will opt for an investment loan.

Most lenders will lend up to and above 100% loan to value ratio (LVR) for first-time owner-occupiers and first-time buyers as investors. "The LVR shouldn't differ from investors to owner-occupiers," explains Michael Lee, consumer advocate, Mates Rates Mortgages. "You can even get lenders who offer 106% for investors. This enables borrowers to capitalise their fees and lenders mortgage insurance (LMI) into the loan."

If you're an investor applying for a mortgage, make sure you have a rental estimate letter completed before visiting your lender or mortgage broker, as this amount can usually be added to your income to add strength to your application. You can obtain this from the current real estate agent of the property.

If you are an investor, you can't apply for the First Home Owner Grant (FHOG) and will therefore have \$7,000 less than a first-time owner-occupier when it comes to financing the initial fees and costs associated with buying your home and establishing your mortgage.

This could significantly affect your financial position, particularly if you're very close to being able to afford the property on your current income. For

details visit your state or territory's website, eg www.osr.nsw.gov.au/

The scenario

In order to calculate a well-rounded and level comparison of two first homebuyers – one owner-occupier and one investor – we've assumed the following:

The buyers

- Both are first-time (single) buyers
- One is opting to buy as an owner-occupier and one as an investor
- Both are currently renting for \$200 per week in NSW
- Both are taxed at a 30% tax rate (income not entering the equation)

The property

- Property price = \$300,000
- Tenant secured for next five years = \$260 per week in rent
- Two-bedroom unit in a block of eight
- Property is located in NSW
- Unit block has stairs (no elevator), minimal landscaping needs and no air-conditioning
- The unit management has no sinking funds or special levies
- Strata and management fees = \$2,000 per year
- Building and pest inspection = \$500 (before purchasing)
- No maintenance or repair costs in first five years of ownership

The mortgage

- Lender: A bank
- Loan product: Fixed rate 8.39% for five years (owner-occupier or investment loan), reverts to 8.57% variable after five years (rate as at 16/1/08)
- Loan amount: \$270,000 (which each buyer can afford)

- LVR: 90%
- Deposit: 10%
- Term: 30 years
- Financial advice = \$1,000 (solicitor or accountant)
- No assistance from guarantor or family pledge
- Only the owner-occupier is able to apply for the FHOG = \$7,000 (may be higher in Victoria)

Both buyers calculate their expenses versus costs at the end of the first five years of owning the home to determine their financial positions. This can be used as a guide to decide whether to consider owning their first home as an owner-occupier or an investor.

Why we chose fixed rate scenario

Staying in touch with your financial situation can be tough work for a first homebuyer. If you're on a tight budget this can make it even harder to stay on target.

For this reason it can often be a more sensible decision for first homebuyers to opt for a fixed rate home loan to keep mortgage repayments stable each month. This way you know exactly what your mortgage will cost you every month for a set number of years.

"I'd recommend many first homebuyers fix their interest rates for two or three years. This gives you some peace of mind and security," says Martin Castilla, lecturer for The Property School.

The final verdict (disclaimer)

According to our basic five-year calculations, it's worth considering investor ownership over the traditional owner-occupier option as a first-time buyer.

In saying this, our calculations don't take into consideration any inflationary measures, Capital Gains Tax or the individual circumstances of our readers. These elements may sway our final calculations significantly.

While the information and broad investment strategies outlined in this article are believed to be accurate and valid, the journalist has no knowledge of the individual financial and other circumstances of the readers

of this magazine.

Readers should seek their own investment advice from a suitably qualified expert before undertaking any investment. YFM

Handy websites

- www.osr.nsw.gov.au/benefits/first_home/
- www.yourmortgage.com.au
- www.yipmag.com.au

Property websites

- www.reports.rpdata.com.au/
- www.prdnationwide.com.au/research
- www.realestate.com.au
- www.domain.com.au
- www.propertybuyer.com.au



Owner-occupier now, investor later



Sharon Masson, 32, had been renting in Sydney's Northern Beaches for five years before she decided it was time to buy a place to call her own.

After spending every Saturday for eight months searching for

the perfect home, Sharon found a large one-bedroom property at Queenscliff she felt was too good to let go. As a first homebuyer, Sharon says she'll live in the unit initially and may consider using it as an investment property later on.

"In an ideal world, if I could buy something else, something bigger or better by the time I'm ready to settle and have a family, I'd love to keep this property as an investment property – given the location and the size. At this point in my life I guess I just wanted something for me," Sharon explains.

"If you have the luxury of buying an investment property and living somewhere else rent-free, go for it," she says. "If you're paying rent you could be putting that (or less) towards your mortgage repayments. For me, currently, my mortgage repayments are less than my rent and saving combined, so it was a no brainer to buy and live in the home."

Sharon suggests taking a trial-and-error approach to see if you want to be an investor first then homeowner later. "You've got six months before you have to move in and still claim the FHOG. Rent it out for six months and see what it feels like. Take advantage of that time."

Loan details

Lender: Virgin Money

Loan product: Split 50:50 variable and fixed

Loan amount: 95% of purchase price

Unit price: High \$300,000s

Interest rates: 7.84% (variable); 8.44% (fixed)

Deposit: 10%

Loan term: 30 years



Once-off government fees

- Transfer registration: \$90 – fee charged by state government to cover the transfer of the title of your new property
- Stamp duty on mortgage: \$0 (exempt)
- Stamp duty on property purchase: \$0 (exempt)

TOTAL = \$90

Once-off home financing fees

- Mortgage registration: \$90
- Loan establishment fee: \$600
- Settlement attendance fee: \$100
- Lenders mortgage insurance arrangement fee: \$20
- Lenders mortgage insurance (LMI): \$2,813
- Rate lock fee: \$395

TOTAL = \$4,018

Once-off property costs (once in five years)

- Property valuation: \$200
- Conveyance fee (or solicitor): \$1,000
- Research and property advice: \$6,000
- Removalist costs: \$1,000
- Building inspection report: \$300
- Pest inspection report: \$200
- Connecting telephone and internet: \$100

TOTAL = \$8,800

Yearly property and mortgage costs

- Mortgage repayments: \$24,720/year (\$2,060/month)
- Contents insurance: \$100
- Strata fees/body corporate (incl. building insurance, garden maintenance) = \$2,000/year
- Council costs and rates: \$1,000/year

TOTAL = \$27,820

TOTAL EXPENSES 1 YEAR: \$40,728 (excl. property price)

Yearly earnings (from the property)

Once-off earnings

- First Home Owner Grant (eligible): \$7,000

Yearly earnings

- Capital growth: \$24,000 (based on \$300,000 x 8%/year gross capital growth)

(Note: \$24,000 is unrealised and will be realised at the point of sale and hence is not included in yearly calculations)

TOTAL YEARLY EARNINGS: \$7,000 (1st year only & excl. capital growth)

Final yearly costs after first year = \$27,820 (yearly property costs – yearly earnings)

Total cost first year: \$33,728

(total expenses first year – total earnings first year)

Total cost after second year: \$61,548

Total cost after third year: \$89,368

Total cost after fourth year: \$117,188

**TOTAL COST AFTER
FIRST FIVE YEARS:**

\$145,000

(Note: there would be \$120,000 of capital growth realised after five years if the

owner decided to sell the property. None of the \$120,000 would be eligible for CGT. Calculations have not taken inflation into account)



Once-off government fees

- Registration: \$90 – fee charged by state government to cover title transfer of your new property
- Stamp duty on mortgage: \$1,021 (claimed as an investor deduction)
- Stamp duty on property purchase: \$8,992

TOTAL = \$10,103

Once-off home financing fees

- Mortgage registration: \$90
- Loan establishment fee: \$600
- Settlement attendance fee: \$100
- Lenders mortgage insurance arrangement fee: \$20
- Lenders mortgage insurance (LMI): \$2,813 (claimed as an investor deduction)
- Rate lock fee: \$395

TOTAL = \$4,018

Once-off property costs

- Property valuation: \$200
- Conveyance fee (or solicitor): \$1,000
- Research and property advice: \$6,000
- Building inspection report: \$300
- Pest inspection report: \$200
- No land tax as the NSW 2008 threshold is \$359,000
- Advertising for tenants (assuming tenants stay from year 1 to year 5): \$48

TOTAL = \$7,248

Yearly property and mortgage costs

- Mortgage repayments: \$24,720/year (\$2,060/month)
- Rent: \$10,400 (\$200/week)
- Contents insurance: \$100
- Travel expenses: \$400
- Rental manager: \$810/year (6% (average of 5–7%) x \$13,500/year (gross rent))
- Strata fees/body corporate (incl. building insurance, garden maintenance): \$2,000/year
- Council costs and rates: \$1,000/year
- Sundry rental expenses: \$95/year
- Depreciation: \$8,000/year (included in yearly costs for tax deductions but not in cash outlay calculations)

TOTAL = \$39,525

TOTAL EXPENSES 1st YEAR: \$60,894 (excl. property price)

Yearly earnings (from the property)

- Gross rental: \$13,500/year (\$260/week)
- Tax deductions on property (from setup + first year costs): \$5,296.38 (full explanation of calculation on ATO website <http://www.ato.gov.au/>)
- Capital growth: \$24,000 (based on \$300,000 x 8%/year gross capital growth)

(Note: \$24,000 is unrealised and will be realised at the point of sale and hence is not included in yearly calculations)

TOTAL YEARLY EARNINGS (incl. 1st year): TOTAL = \$18,796.38

Total cost first year: \$42,097.62

(total expenses first year – total earnings first year)

Total cost after second year: \$62,826.24

Total cost after third year: \$83,554.86

Total cost after fourth year: \$104,283.48

**TOTAL COST AFTER
FIRST FIVE YEARS:**

(Note: there would be \$120,000 of capital growth realised after five years if the owner decided to sell the property. There would be CGT payable on this amount.)