# Advanced Property Analysis (MMP321)

## Topic 1, Part 1: PRE as an investment class

### Introduction
Investment objectives can be divided in to 2 parts:
1. **Growth:** relatively long time horizon with no immediate need for the investment funds.
    - accumulation phase, may be higher risk.
2. **Income:** short term horizon and on-going need to use the cash generated from the investment.
    - yield phase, usually lower risk.

Investment Constraints
1. **Risk:** Possibility of returns varying over time.
2. **Liquidity:** Ability to buy/sell quickly at full value and without affecting the price.
3. **Time Horizon:** Period over which objectives & constraints are relevant.
4. **Expertise:** How much ability & desire the investor has to manage investments.
5. **Size:** Amount of capital invested.
6. **Capital Constraint:** Ability to obtain additional capital if new opportunities arise.

### Asset Class Relationships

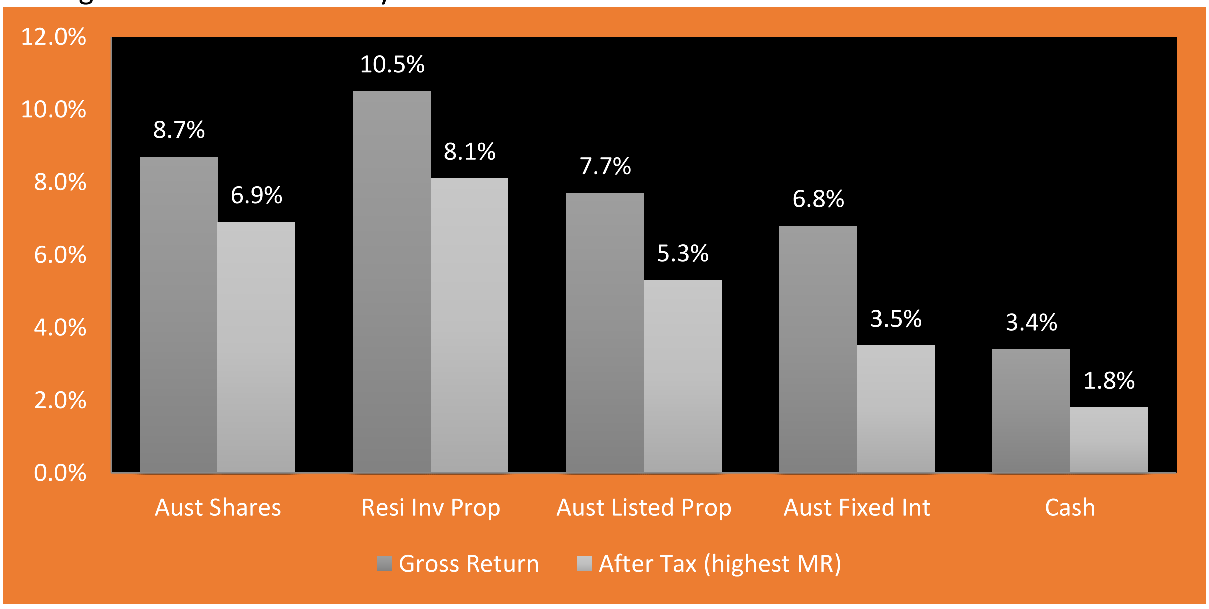
| | Equities | Property | Fixed Interest | Cash |
|---|---|---|---|---|
| Risk | High | Medium | Low | Very low |
| Total Return | High | Moderate | Low | Lowest |
| Long-term Growth | High | Low/Moderate | None | None |
| Inflation Protection | Long-run good | Good | Poor | Very poor |
| Correlation with other asset classes | Low with cash & fixed int. moderate with property | Low with cash & fixed int. moderate with equities | Low | Low |

### Why Invest in Real Estate?
1. **Diversification** - counter-cyclical to general equities exposure.
    – Expanding economy – strong forecast GDP/employment growth benefits general equities → share prices appreciate, interest rates rise. Property, often with cash flows locked in medium to long term leases, doesn't benefit in the short term, and investors find property investments less attractive relative to general equities.
    – Contracting economy – forecast declining GDP/employment growth means general equities are less attractive, while property investment cash flows remain stable. Investors shift to property investments for secure cash flows and out of general equities.

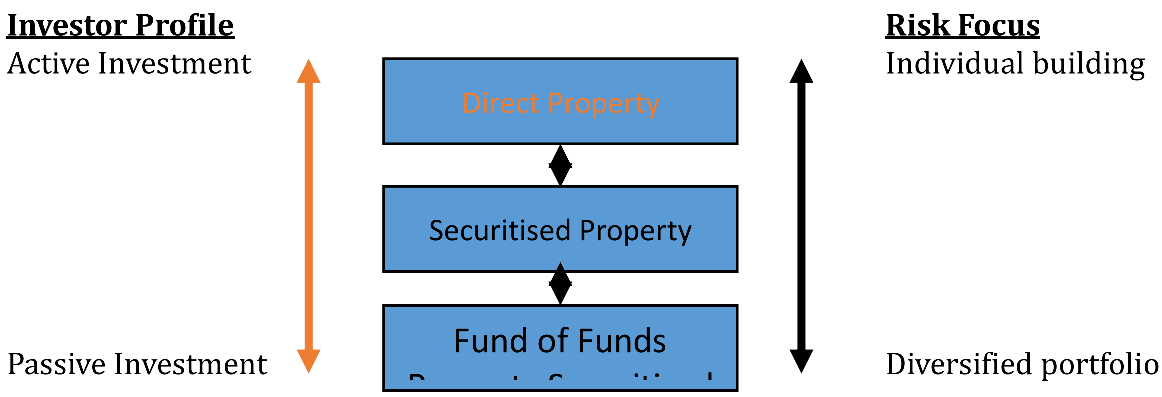
2. **Yield** - large proportion of commercial property returns (75%) come from income, with an average income yield of approximately 2.9% above the average yield on equities over the last 5 years.
3. **Perceived lower risk** – long lease terms, contracted income streams, “bricks & mortar” idea of property. Stability and income security is the rationale of approx. 70% Aust. institutional property investors.
4. **Capital growth** – appreciation in land values.
5. **Ability to tailor real estate exposure to investment objectives** – for example one strategy might be higher growth, higher risk, lower yield (value-add or property development).
6. **Ability to add leverage**.
7. **Tax advantages** (negative gearing, depreciation, CGT).

**Why Invest in Real Estate**

Average annual returns – 20 years to 2015




**Property Market Investment Structure**



**Trends in Australian Real Estate**

- Foreign investment in Australian property continues to rise. Over the past 7 years (to 2015) China has invested $24B in Australian property, with a majority in commercial
- Approximately 70% of Australia commercial property is securitised
- The decline in the resources sector continues to impact property markets in QLD and WA
- Prime real estate stock has seen significant yield tightening over the past three years – investors looking at secondary/non-CDB assets
- Australian major banks exposure to Australian commercial property has grown from approx. $60b in 2005 to $176b in 2016