Bryce Holdaway is a director of Empower Wealth, which helps investors develop detailed multiple property investment plans that model cashflow, equity, debt management, investment performance, future provisioning and retirement outcomes. He is also co-host of *Location, Location, Location Australia* and *Relocation Relocation Australia*, which both screen on The Lifestyle Channel, available on Foxtel nationally.

EARN $2500 A WEEK

BY BUILDING A PROPERTY PORTFOLIO

PLUS HOTSPOTS YIELDING OVER 6%

It's never too late to start building a property portfolio to fund your later years. **Bryce Holdaway** shows how, with careful planning and commitment, three different households can realise their retirement dreams without taking a big risk

HOW OFTEN HAVE YOU found yourself picturing a retirement where you're enjoying regular overseas holidays, spending your spare time with your grandkids and leisurely filling up your days doing all the things you love?

We all have but we're brought down to earth quickly by reports suggesting there won't be enough money for a comfortable retirement. Perhaps even worse, some of us will have to work much longer than planned.

So the idea of creating a $2500-a-week passive income for a life in retirement free of debt ($130,000pa in today's money) could be thought a stretch of the imagination. This would put you in the highest bracket of retirement earnings in the country and, according to the latest census (2011), would provide you with more than double the average total household income of $63,960.

The goal is achievable

Nevertheless, after looking at three typical households – a late-20s single, a mid-30s couple with two young children and a mid-40s couple with two teenagers – that have never invested in property, and carefully considering if it's possible to achieve this passive income of $2500 a week, it's exciting to know it can be done with low to moderate risk and potentially minimal impact on their current standard of living.

The big question is, how?

For me, the preferred vehicle is residential property. I have used it as the cornerstone of each plan. I believe shares and business play their part in investment but I think most Australians see residential property as a tangible and easy-to-understand investment.

And the banks are fond of it – they lend the highest amount – 80% of the value and up to 95% – for mortgages, of all the investment classes. What's more, government has a huge incentive to make sure residential property is underpinned – to keep voters happy and ensure the economy is not at risk if the market were to collapse and force every borrower out on the streets. Importantly, it will never be worth nothing, as it's solid bricks and mortar and land.

It's my view, after dealing with clients' financial affairs over 14-plus years that anyone with a "material" income generally looks to store money in their principal place of residence before considering alternatives.

But the factor that appeals to me most is leverage: the ability through borrowing to get the compounding benefits of the large asset is by far the biggest drawcard.

All this leads me to the view that residential property is Australia's leading wealth creator.

Given what's at stake – a comfortable retirement versus one with less than adequate income – it's important any plan makes a priority of two things: protecting the capital base; and managing household cash flow to make sure you don't run out of money.

So I've adopted what I would consider relatively conservative strategies for each scenario: no mortgage insurance; all properties purchased would be within the bank's comfort zone with regards to size (nothing under 50sqm); practical and achievable capital growth rates; and realistic rental yields. The portfolios would consist of a spread of houses or apartments and a mix of capital growth-focused properties and yield properties. Three properties are necessary for two of the scenarios and five for the third.

It's crucial to arrange an optimal lending structure, making use of 100% offset accounts to minimise the interest being paid, the key to paying off the debt in the years approaching retirement; eliminate any high-interest debt such as credit cards or store cards; and to put in place simple and effective money management systems to ensure minimal slippage in the area where we all struggle – lifestyle and discretionary spending.

All of this will enable eliminating the mortgage on your principal place of residence promptly and efficiently, before a switch in attention to eliminate all the portfolio debt by retirement, leaving you in the highly desirable position of having a passive income to fund your retirement lifestyle while also having the assets as legacy for your family.

Property is the means

So given the residential property preference, can we be confident in the market in 2013 as well as in the medium to long term. I think there are plenty of reasons to be optimistic, including:

- We're enjoying historically low interest rates that make property more affordable, and borrowers reap the benefits.
- In support of the door being open to further interest rate cuts, inflation is under control in the RBA's preferred 2-3% target range.
- We have a housing shortage (with the exception of a few minority markets) that looks set to continue, so demand will exceed supply in an improving market for sellers.
- Rents will continue to rise as a result of the excess demand, providing enticement to investors chasing increasing yields.
- Self-managed super fund (SMSF) investment in residential property is helping to underpin the market and the trend under the current rules is only likely to increase

An important point is that Australia is not just one big property market but hundreds of submarkets in different cycles, providing great diversity. While property values don't grow in a straight line, the detailed plan in each of the three scenarios has been built with a horizon of more than 10 years and opportunities will exist during this time frame to build a portfolio across multiple submarkets to give your portfolio the best chance of outperforming the national averages.

We have factored in "future values" to make the plans realistic but we will talk about the purchases of property and the retirement income goal in today's dollars. An important point to highlight is that for every portfolio suggested, it is currently possible to find properties that satisfy the requirements and in a lot of cases our buyer's agency team is achieving this for our clients, which gives us confidence that it will be possible in the future also.

THE GOAL: THREE INVESTMENT PROPERTIES WORTH $10 MILLION

The youngest of our three households

Stepping onto the property ladder

THE FIRST CASE STUDY is Rachel, who lives in Sydney and rents a property for $500 a week. Typical of her generation, she is enjoying the "here and now" and is not so focused on retirement, given she has yet to reach even half the popular retirement age of 60.

Rachel has no major assets, a credit card debt of $5000 and savings of $30,000. (See the table below.) And she has time on her side. Given compound growth, the longer you have, the better the results and the more comfortable you will be. But at this age you are often just establishing your career, your income is still growing and the equity reserves that you can draw on are often limited.

Rachel is likely to meet someone and possibly start a family in the future, and there will be subsequent claims on her cash flow. It is also likely that this would bring an additional income into the mix.

The plan for Rachel is to get her into her own home so that she can lay the foundation for her portfolio. Although she has time as a strength, she has no personal equity to draw on; but she will eventually achieve this by being on the property ladder.

In terms of finance structure, a tool for each household is an offset account with interest-only mortgages. This goes against the traditional model of having a principal and interest (P&I) loan but, by using a 100% offset account, the outcome is similar to having a P&I loan, only you have improved flexibility and cash flow to let you build the portfolio, with paying off the mortgage still an important part of the plan. This is possible with the majority of lenders.

As Rachel lives in Sydney, the first step is to take advantage of the NSW first home owners grant (FHOG) and NSW stamp duty concessions for first-home buyers. I'd suggest she purchase a new one-bedroom apartment for $330,000, which would mean that she has access to $15,000 FHOG (for any new build purchased before December 31, 2013). Along with this, she would save $10,340 in stamp duty concessions. All up this means a significant incentive of $25,340 is available to encourage Rachel to buy her first home.

While these are significant bonuses, Rachel still needs to consider how she will provide the balance of the deposit as the concessions alone will not be enough. There are a number of ways to do this, including paying mortgage insurance for a loan of up to 95% of the purchase price. But in the interests of protecting Rachel's cash flow, we want to place her savings of $30,000 into her offset account and take advantage of her parents' kind offer to go guarantor for the purchase.

This way she won't need to borrow more than 80% of the purchase price secured against the one-bedroom apartment, thus avoiding a significant mortgage insurance premium. Rachel would simply use the FHOG and her parents' security to provide the required funds to settle and service a loan equivalent to 100% of the purchase price plus settlement costs, as well as eliminate her high-interest credit card debt.

Rachel's investment foundation would be set and all surplus money she accumulates should now be directed into her offset account, with the view to minimising the interest on her mortgage and effectively reducing it as quickly as possible.

A first investment property

Because cash flow is so important, we don't want to consider buying the first investment property until the impact of doing so won't place a huge strain on the household cash position. The impact of leaving Rachel's savings in offset, along with trapping additional surplus cash flow, means that in two years Rachel will be in a position to consider purchasing her first investment property. If Rachel is like most first-time investors, she will want to buy her first investment property in her own state. But ultimately we would be looking for Rachel's first purchase to be a property with a growth focus, given that equity is the major deficiency in her portfolio at present and building this up as quickly as possible should be the focus. That being said, income is important to protect her cash flow.

We suggest a property worth $350,000 in today's dollars in a suburb with a history of 8%pa growth and a yield of 5.5%pa ($370 a week).

Rachel would have two properties in her portfolio – her principal place of residence (PPR) and first investment property (IP) – and she can take a break from investing for a few years to get used to having the responsibility of an investment property. She can continue to trap any surplus cash flow and place it in the offset account so the portfolio builds up equity through growth of the properties along with debt reduction on her PPR.

Rachel can consider adding to her portfolio three years after the purchase of the first investment – but this time looking for a property with a stronger income to do some heavy lifting with cash flow and to make more headway in her PPR mortgage.

For this, we will look outside the capital cities for a property in a suburb that has a history of moderate growth, 6%, but with strong cash flow, which in this case is 6.5% gross yield: a $220,000 property getting $275 a week. This is the value in today's dollars, but at the time of purchase this property would cost Rachel $294,410, taking into account that the value will have grown.

The final purchase would be a growth-focused property in 2024 – just less than a decade after she purchased her first investment property. In a significant milestone, Rachel's purchase would be achievable for her in her own right as the portfolio would now be worth enough for her to release her parents as guarantors.

In today's dollars, it would be a property worth $380,000 in a suburb that is likely to achieve 8% capital growth and 5.5% gross rental return. All that's left now is for time and compounding to kick in.

So Rachel would have three investment properties and her own home, be on track to pay off the loan on her principal place of residence by 2033, and be in a position to retire 12 years later – in 2045 at 60 with the equivalent in today's dollars of $2500 a week.

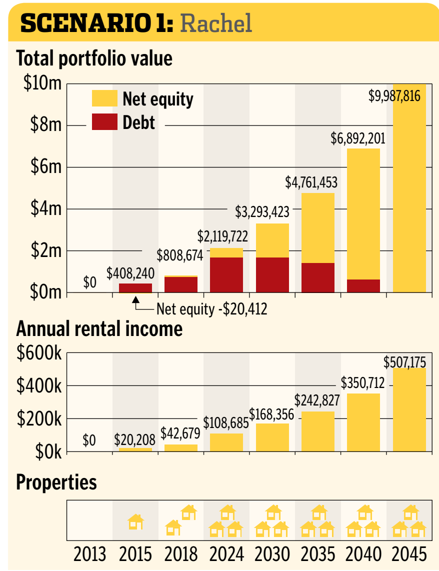
RACHEL'S PROFILE

Annual income	$65,000pa
Monthly income after tax	$4282pm
Bill payments (including rent)	$2594pm
Lifestyle and discretionary spending	$1276pm
Credit card payment	$133pm
Total expenditure	$4003pm
Monthly surplus	**$279pm**

INVESTMENT PLAN

PROPERTY	PRICE IN 2013	YEAR BOUGHT	TARGET GROWTH	PRICE WHEN BOUGHT	LOAN	TARGET YIELD	CUMULATIVE LVR[2]		
							TOTAL	RACHEL	PARENTS
PPR[1]	$330,000	2013	6.0%	$330,000	$333,300	NAp	101.0%	80.0%	21.0%
1	$350,000	2015	8.0%	$408,240	$428,652	5.5%	97.8%	80.0%	17.8%
2	$220,000	2018	6.0%	$294,410	$309,130	6.5%	85.7%	80.0%	5.7%
3	$380,000	2024	8.0%	$886,023	$930,324	5.5%	72.9%	72.9%	nil

[1]Principal place of residence; assumes first-home owner grant and NSW stamp duty concessions. [2]Loan to value ratio.



THE GOAL : THREE INVESTMENT PROPERTIES WORTH $7.8 MILLION

SCENARIO 2
Mid- 30s married couple with two young kids

Unlocking the equity in your home

THE SECOND HOUSEHOLD is in the box seat when it comes to setting up this retirement goal. They have time on their side and growing incomes. And as well, they've had time in their principal place of residence to create some equity through reducing their loan and benefiting from any improved capital value.

Daniel, 38, and Rebecca, 36, are married with two young children. Their home is worth $575,000, they have a mortgage of $300,000, $10,000 in savings and credit card debt of $5000.

Unlike Rachel, who is more interested in her career and enjoying her social life, for Daniel and Rebecca the focus is well and truly on their young family. Household cash flow needs to not only juggle the basics of survival but include basics such as childcare and school fees. A family holiday is needed each year to get away from the pressures that come with juggling family and career.

It's important any financial modelling makes allowances and provisions for "real life", not just simply the costs associated with maintaining the property portfolio.

Cutting interest costs

The most obvious place to start is to reconfigure their debt to help improve their cash flow. First priority is to release equity in their family home, which will be used as a buffer as well as covering the deposit and costs associated with buying the property. Second, for the same reasons outlined in relation to Rachel's plan, we will change the mortgage on their principal place of residence to interest-only instead of principal and interest repayments. Finally, they would use their buffer to pay off their high-interest credit card debt to free up further monthly cash flow.

Given they have solid equity and, under the reconfigured lending they have strong cash flow, they are in a position to buy their first investment property. Focus for the first one is on capital growth, so this purchase would be a $500,000 property within a 10km radius of a major capital city and be looking for a yield of 4% (about $385 a week in rent). Importantly, all rent received would go into the offset account to take maximum advantage interest being calculated daily and paid monthly. The higher the offset account is for as long as possible during the month, the better it is for reducing the amount of interest on non-tax-deductible debt – ie, the mortgage on the PPR.

We would give Daniel and Rebecca a few years before considering another purchase. To truly succeed in this plan of "multiple property" purchasing, it must be a conservative and considered approach with household cash flow and liquidity a priority. Three years allow this couple to get used to managing a busy home, a young family, careers and an investment property without responsibilities becoming overwhelming.

MONEY COMES ALIVE

WATCH Bryce Holdaway share the tops things to look for when buying an investment property

Download the free *viewa* app, select the *Money* channel and hold your phone or tablet over this page to watch what Holdaway from Empower Wealth says about what you should know about investing.

The second purchase would also focus on capital growth given they still have time on their side. This would be today's equivalent of a $400,000 purchase in 2016, again looking for a suburb with a history of growth at 8% with a rental income of 4% ($310 a week).

The final purchase would be in 2020 and, given the focus is on reducing the overall portfolio debt by retirement, a higher-yielding property is required here. This purchase would be worth the equivalent of $250,000 in today's dollars and have a yield of 5.5% ($265 a week).

Daniel and Rebecca would have three investment properties and their own home with a plan to pay off the loan on their PPR by 2031. They would be in a position to retire six years earlier than Rachel, in 2039, at ages 64 and 63 with no debt and with the equivalent of $2500 a week in today's dollars.

DANIEL & REBECCA

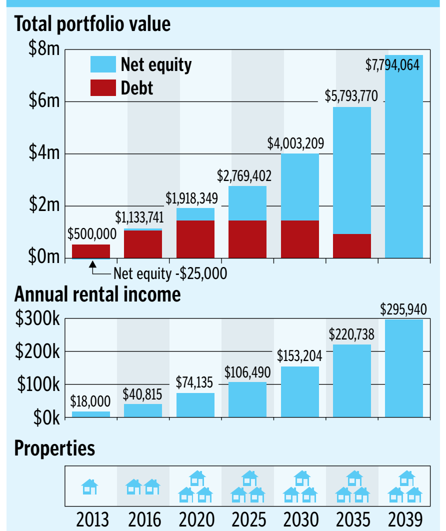
Daniel: income	$80,000pa
Rebecca: income	$40,000pa
Joint income after tax	$8042pm
Bill payments	$2156pm
Lifestyle and discretionary spending	$2750pm
Loan payments	$2712pm
Total expenditure	$7618pm
Monthly surplus	**$424pm**

INVESTMENT PLAN

PROPERTY	PRICE IN 2013	YEAR BOUGHT	TARGET GROWTH	PRICE WHEN BOUGHT	LOAN	TARGET YIELD	CUMULATIVE LVR[2]
PPR[1]	$575,000	existing family home	7.0%	NAp	NAp	NAp	53.9%
1	$500,000	2013	8.0%	$500,000	$525,000	4.0%	77.7%
2	$400,000	2016	8.0%	$503,885	$529,079	4.0%	74.2%
3	$250,000	2020	6.0%	$375,908	$394,703	5.5%	61.9%

[1]Principal place of residence. [2]Loan to value ratio.

SCENARIO 2: Daniel & Rebecca



Tips

- Get on the property ladder sooner by using parents' equity for a guarantor loan.
- Start as early as possible – compounding works best with time on your side.
- Hold property for the long term and never sell.
- Invest across multiple states to save on land tax.
- Buy existing properties for investment rather than new.
- First-home owners should buy a new principal place of residence for the FHOG and stamp duty exemptions.

Traps

- Failing to see the time opportunity in younger years and thinking it is too late to start in later years.
- By not saving your own initial deposit, you may not have a proven track record of being disciplined in spending your money. This requires focus and sacrifice – delayed gratification.
- Wasting money through discretionary spending on consumer items
- Putting all your eggs in one basket as a first-time investor – not diversifying across states or types of property.

Basic principles

It's never too late to start investing with a goal in mind, the earlier you start the better. You don't need to manage 10-plus properties to achieve a healthy retirement. The three case studies show it is possible to achieve a comfortable retirement using residential property, provided each person involved is diligent about managing their money correctly through adopting some basic principles.

It's not as simple as just picking any property. Each scenario requires a tailored solution including time frames, individual cash flows, property selections and performance targets along with lending and taxation impacts unique to each household. Seek out experienced professionals to bring it all together. It really is all about mastering the principles of ABCD: asset selection, borrowing power, cash flow management and defence. Get all four components right and in sync and you might just get to spend that time with your grandkids, going on holidays and doing what you love in retirement.

THE GOAL : FIVE INVESTMENT PROPERTIES WORTH $7.2 MILLION

Where there's a will

Don't give up if you're struggling for a deposit, advises Jane Slack-Smith

Many first-home buyers do not have the 20% deposit that lenders prefer. This, however, does not mean they can't buy now. As I tell my clients, "where there is a will there is a way". In fact, there are three ways you buy if you are in this situation:

- Use a smaller deposit, as little as 5%. However, you will need to pay the one-off lender's mortgage insurance premium.
- Have a family member with equity in their property go as guarantor. Often parents do this to help their kids. It is not without risks and responsibility, so you need to be aware of these.
- Get a gift. This is often from your parents - it might be cash they have or they may take out a loan and give you those funds. This is similar to the family guarantee but your parents are not exposed as much in terms of being a legal guarantor for your loan in case you default.

Rachel

In Rachel's case, we have gone for the second option, so she is responsible for paying the interest on both loans. Rachel will need to make sure that she can service her lifestyle and the interest on these two loans as well as ongoing costs of property ownership.

The couples

For those with your own homes, you are truly sitting on a goldmine that you can utilise straight away. However, you need to do this in a structured way and make sure you can afford the new debt. I often set up a buffer as well when releasing these funds – a safety net of sorts. Often when you try to access the funds you may have accumulated in your home, lenders will want you to secure your home and your new property together. This is called cross-collaterisation. Although it might suit the investor buying one property, for both couples in these case studies it is an inflexible finance structure that will prevent them from expanding their portfolio. At Investors Choice Mortgages, we often find ourselves fixing up this structure for our clients so they can keep buying properties after their bank says they can't.

When setting up finance for these couples, I would concentrate on lenders that have offset accounts as part of their offering. Surprisingly, there are many lenders these days who offer these for their basic loans without the expense of professional packages. The offset account against an interest-only loan is one of the golden keys of success for property investors. As the interest-only loan is fundamental to the offset account being workable for all three case studies, I would also look at lenders who have interest-only periods longer than five years or those who have an easy interest-only period extension. We don't want to have to be making new applications to lenders in the future if it is not necessary.

My top tips for our couples:

- Tap equity from your home and leave some as a buffer for those "just in case" situations.
- Don't cross-collaterise your home and investment properties.
- Use interest-only loans and offset accounts.
- Consider fixing some of your loans. You can even hedge your fixed and variable loans by being with one of the very few lenders that will allow you to have an offset account against a fixed loan. Then, depending on the interest rate of the day, you can move money between your offset accounts.
- Target lenders that have long interest-only periods, such as 10 years, and simple extension processes.

Jane Slack-Smith recently won Australian mortgage broker of the year. She is the director of Investors Choice Mortgages and founder of Your Property Success online education. See www.yourpropertysuccessnow.com.au or www.investorschoice.com.au

Making up for a time handicap

Michael and Jennifer are to be envied on paper: a strong combined income, having hit their peak earning years, and a mortgage of only $110,000, resulting in a comfortable equity position. But they have the least time before they reach retirement age so their strategy will need to be tailored to missing out on some of the benefits of compounding. They need to be a bit more aggressive in when they buy and also find the fine balance between chasing capital growth – to expand their capital base – and yield – as they need the income and resulting cash flow to reduce the debt by retirement.

Michael, 48, and Jennifer, 46, are married with two older teenagers. Their home is worth $750,000, mortgage $110,000, savings $30,000 and credit card debt $5000.

The focus initially is on reconfiguring debt – they need to release equity, establish their buffer, pay off high-interest credit card debt, trap all surplus cash flow to put into their offset account and change their mortgage to interest-only to free up additional cash flow.

They have the luxury of sufficient equity in their PPR to establish a single facility for all the money required for deposits, costs and funds for the entire portfolio.

The strategy requires them to make two purchases in the first year, not forgetting they are first-time investors. We don't want to be taking any huge risks or putting the capital base in jeopardy. We are not stretching them in terms of total value, as I'm suggesting a $350,000 purchase and a $220,000 purchase, making it a $570,000 outlay, plus costs, which is quite manageable.

MICHAEL & JENNIFER

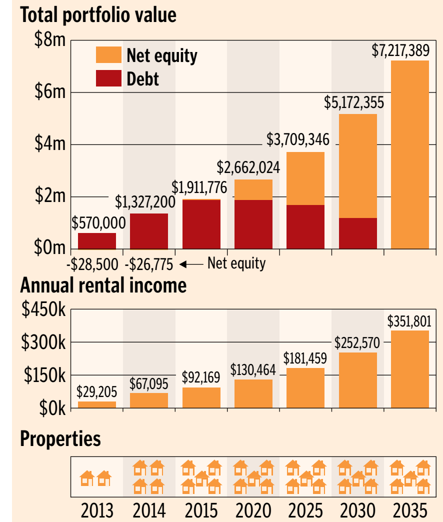
Michael income	$98,000pa
Jennifer income	$57,000pa
Joint income after tax	$9976pm
Bill payments	$2375pm
Lifestyle and discretionary spending	$4453pm
Loan payments	$2529pm
Total expenditure	$9357pm
Monthly surplus	**$619pm**

INVESTMENT PLAN

PROPERTY	PRICE IN 2013	YEAR BOUGHT	TARGET GROWTH	PRICE WHEN BOUGHT	LOAN	TARGET YIELD	CUMULATIVE LVR[2]
PPR[1]	$750,000	existing family home	7.0%	NAp	NAp	NAp	16.0%
1	$350,000	2013	7.0%	$350,000	$367,500	5.50%	44.3%
2	$220,000	2013	6.0%	$220,000	$231,000	6.00%	54.4%
3	$400,000	2014	7.0%	$428,000	$449,400	5.25%	63.5%
4	$275,000	2014	6.0%	$291,500	$306,075	6.00%	69.2%
5	$430,000	2015	7.5%	$496,919	$521,765	5.00%	72.0%

[1]Principal place of residence. [2]Loan to value ratio.

SCENARIO 3: Michael & Jennifer



By taking this approach, the price range enables us to look for a market that has solid growth for the first property – 7% growth and 5.5% yield (around $370 a week) – while getting some strong yield for cash flow with the second property – 6% growth and 6% yield ($255 a week). If we were to channel the same spend into one property, we wouldn't achieve the required growth and income objectives in this early part of their plan.

We can't sit on the sidelines for a few years after these purchases; time is of the essence. So in 2014, we would add two more purchases – one growth-focus property and one income focused – again boosting the capital base and adding to the cash flow. Here we would go for $400,000 property with 7% growth and 5.25% yield expectations and another for $275,000 with 6% growth and 6% yield expectations. The required rentals would be $405 and $320 respectively.

The fifth and final investment for Michael and Jennifer is a growth-focus property. Here we would add a $430,000 property with an expectation of 7.5% growth and 5% yield ($415 a week). This many properties this quickly means they can expect some periods of negative household cash flow (where expenses exceed income) but having created a "buffer" of cash in their offset account they can use this money to see through.

Michael and Jennifer would have five investment properties and their own home with a plan to pay off the loan on their principal place of residence by 2022 and retire with $2500 a week in 2030 at 67 and 65.