

Buy-to-let or buy-to-fret?

BEWARE THE BUY-TO-LET residential property market. You may just be entering the buy-to-fret market, Gavin Opperman, the managing executive of Absa Home Loans, says.

Opperman says he is not contradicting Absa Home Loans' view that property is a good investment. "We still believe that bricks and mortar is a good home for a portion of investment assets."

But he says that if, in the current economic climate, you are involved in speculative investing in residential property for the rental income it provides, you could be heading for financial difficulties, particularly if you don't have sufficient cash flows to deal with predictable and unforeseen hiccups.

Opperman says the buy-to-let market received a big kickstart when interest rates started falling in 1999. The interest rate cuts sparked a latter-day gold rush, with property developers building tens of thousands of new homes across the country, effectively flooding the market, particularly in the mid-priced rental range.

Opperman says the people who bought second homes for speculative purposes in this now saturated sector and who rely heavily on that rental income "may well find themselves in a very sticky situation because the projected returns are not materialising".

Interest rates are now rising and can be expected to continue to rise, Opperman says. A rising interest rate environment puts pressure on anyone with a mortgage bond, but particularly those in the buy-to-let market.

And he says you should remember that higher interest rates affect all borrowings, not only home loans, and there are knock-on effects into other aspects of the economy. So all costs will go up.

On top of this, owners of buy-to-let properties face a never-ending and often grinding quest to keep their properties occupied. The problem is that South

In the current economic climate, there are dangers in buying a residential property for the rental income it can provide.

PERSONAL FINANCE looks at why it is risky.

Africans prefer buying to renting, and we currently have a glut of rental properties.

"This has led to a buyers' market for tenants. If a situation of over-supply exists, prices come under pressure. Many property experts, including economists and estate agents, say that yields on rental properties have come down, in

some cases quite dramatically," he says.

"Some bondholders are finding that their mortgage obligations are not being covered by their rental income. And then, over and above that, the owner is still responsible for levies, rates and taxes, insurance, and the upkeep of the property. These can amount to significant monthly costs."

And remember the taxman is also waiting in the wings to take a share of any rental profits.

THEN THERE ARE OTHER HASSLE FACTORS facing landlords, such as the law protecting tenants.

Opperman says it can be a difficult and an expensive process to have recalcitrant tenants removed, even if they have reneged on the terms of the lease, such as vandalising the property or not paying the rent. This can cause unexpected loss of income and mounting bills, not to mention stress.

It is not that property is a bad investment, Opperman says, but that an ill-planned property decision could be a bad investment.

A wise investor injects sufficient equity into a buy-to-let property and sees the return in terms of the growth of the asset – in other words, an escalation in the value of the property – rather than the yield it can generate, such as rental income. The same wise investor will also know that no mortgage product can, ultimately, resolve the problem of a poor investment decision.

Rental income, for a prospective owner, should really be only the icing on the cake. So if you can't afford the cake, there's little point in even thinking about icing. □



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