Smart Money

A DIFFERENT PERSPECTIVE | **The money saved by not owning a home can be invested in growth assets such as shares**

Rent money isn't dead

Owning your home is not always a better financial option than renting, as Smart Money Editor **ANTHONY KEANE** reports.

WE'VE all heard the advertisements.

"Rent money is dead money," they claim. Or "don't pay off someone else's mortgage".

Most people view their home as their biggest investment, but is home ownership the best financial decision?

Are we financially better off renting, and channelling the money we save in stamp duties, council rates and maintenance costs into a high-growth investment such as the share market?

In many cases, the answer is yes.

The average growth of Adelaide property over the past 20 years is 7.1 per cent, well below the average growth of Australian shares of 10.2 per cent, says AMP financial planner Mark Borg.

Then there are the many thousands of dollars of costs involved with home ownership. Buying costs, renovations, rates and taxes all far outweigh the $30 or $50 it costs to buy and own a share in a blue chip company.

Fortunately for the real estate industry, home ownership is more than just a financial decision.

"Putting financials aside, there's no doubt that, for many people, owning their own home provides security, peace of mind and the chance to live out the great Australian dream," Mr Borg said.

"There are always other factors that will influence your decision to rent or buy your home, such as interest rates and whether or not you're prepared to take a bullish approach to investing."

Mr Borg said the common practice of buying a small home first, holding it for two or three years, then buying the home you want could often be a bad financial decision.

This is because owning a home for a short time still incurs costs such as stamp duty, mortgage guarantee insurance and buying and selling costs.

"Patience is a virtue when it comes to buying a home," Mr Borg said.

"If you only have a small deposit, chances are you will be better off investing your money wisely while you rent and save for a greater deposit."

Comparing the advantages and disadvantages is tricky, as there are so many variables. These include:

RENT money is dead money if you do nothing with the money saved by not owning a home.

Only if you invest it in growth assets such as shares will you benefit.

A HOME can be valuable as a base for other investments. People can borrow against the equity in their home to buy other investments, usually at a much lower interest rate than if they use margin lending to buy shares.

SHARES are much more volatile than property and attract capital gains tax when sold for a profit. There is no capital gains tax payable on the family home.

PEOPLE who rent and work from home may be able to claim a tax deduction on some of the rent they pay. This is not available for owner-occupiers.

Marinis Financial Group financial strategist Theo Marinis said there was a financial case for paying money into superannuation rather than off a mortgage. "When you own your own home you are servicing that debt with after-tax dollars. That's what we call bad debt," Mr Marinis said.

"You get a lot more money into super because your tax rate in super is lower than your personal tax rate in most cases." But owning a home was about emotion, he said.

"The reality is that most people want to buy their own home, even though they are financially better off not buying a home – myself included.

"Even though theory tells me I shouldn't own my home, I do.

"You don't just do things because it's financially the best thing to do. It's about balancing the lifestyle requirements."

Mr Marinis said many people were not comfortable putting all their money in the higher-growth alternative – shares.

He said the new superannuation rules – which come into effect on July 1 and make withdrawals from super tax-free for people over 60 – made super a more attractive place to put money rather than a mortgage.

Take the example of a 55-year-old on the top marginal tax rate of 45 per cent who pays $1500 a month off a mortgage.

The mortgage is paid in net income, or after-tax dollars.

If there was no mortgage, that $1500 would become $2800 if salary-sacrificed into superannuation because salary sacrifice works with pre-tax dollars.

It's a strategy that could be used for people nearing retirement who have a mortgage.

If possible, they could arrange to stop making mortgage payments and instead inject the money into their super, Mr Marinis said.

"Then, at 60, they can withdraw it tax-free and then pay the debt off.

"The higher the tax bracket, the better off you are."

BankSA general manager Chris Ward said investing in shares or managed funds instead of a home could be "an excellent way to build long-term personal wealth". "However, buying property remains the investment of choice for the majority of Australians, and with good reason," he said.

"It provides long-term security, leads to the ownership of collateral that can be used for future borrowing, and means you are able to make changes to the home." Mr Ward said buying a home introduced and strengthened financial discipline.

"In many families the home is seen as part of the children's inheritance and is virtually the only tax-free investment," he said.

Mr Ward said the desire for home ownership was strong, with BankSA research last year finding almost half of people aged 25-34 and one-third of 18-24 year olds planned to invest in property within five years.

"According to the United Nations, Australia has one of the highest home ownership rates in the world and it seems unlikely this will change," he said.

"While renting is the preferred option for some and a necessity for others, more than 70 per cent of Australians own or are buying a home."

Adelaide's median house price recently hit $300,000, making ownership a daunting prospect for many first home buyers.

"Fortunately there's now a wide range of options available to prospective borrowers," Mr Ward said.

These include no-deposit loans which allow the borrowing of up to 100 per cent of the purchase price, and family pledge loans where family members guarantee part of the loan using their own property as equity.

BIG DEPOSITS ARE BEST

SCENARIO ONE

Peter earns $50,000 a year and has saved $42,000 to buy a home worth $290,000.

He will pay $3000 in mortgage guarantee insurance and $10,000 in government stamp duty – leaving him with a deposit of $29,000.

If Peter was to make minimum repayments of $1626 a month on his home loan and simply maintain his property (as opposed to making any improvements), the equity in his home after seven years would be about $239,000.

However, if he chose to rent and, instead, invest his savings into stocks of the all ordinaries share market index, his share portfolio after seven years would be worth only $217,000 after capital gains tax.

SCENARIO TWO

If Peter saves only $30,000 to buy the $290,000 house, he will pay $5000 in mortgage guarantee insurance and stamp duty of $10,000, leaving him with a deposit of only $15,000.

His mortgage repayments would be higher ($2029 per month) and after seven years the equity in his home would be only $228,000. If Peter had invested his $30,000 in the all ordinaries index, his share portfolio would be worth $233,000 after the capital gains tax.

❑ Source: AMP financial planner Mark Borg. Assumes property growth of 7.1 per cent, all ordinaries growth of 10.2 per cent, weekly rent of $249 indexed by 3 per cent each year, dividend returns of 3 per cent franked at 50 per cent, council rates, maintenance and taxes of $3500 indexed at 3 per cent, stable interest rates.

Median house price history Adelaide now... NEWS.com.au/adelaidenow