Property as part of a diversified portfolio

Unless you have only invested in term deposits, you have probably had some experience or knowledge that most non-bank investments provide higher returns over time with the trade-off being occasional swings in value. The degree of variation depends on the type and mix of your investments. The key to achieving more consistent growth is by holding a diversified portfolio of assets, such as fixed-income investments, shares and property.

STORY
Will Roberts
FANZ Private Wealth

The concept behind a diversified investment portfolio is that each type of asset will perform slightly differently at a single point in time helping to smooth returns. Further to this, diversification within each type of asset is important as different industries or properties can perform differently over the same period of time. A classic example given by investment advisers is that of the ice cream seller and the umbrella seller. One prefers sunny days, while the other rainy days. By owning shares in both, you have lowered the influence that weather has on the performance of your investments.

Property is one of those investments that adds value to an investment portfolio, although it's important to understand the different ways you can gain exposure to the New Zealand property market, and what those options mean for you in terms of the risk and returns.

The most well-known form of investment in property is via direct investment in residential property. For larger investors, they may also hold commercial property. The attraction of direct property investment for many people is that it's a physical thing that can be viewed and utilised, i.e. you own 'bricks and mortar'. Equally, property is an asset that can be borrowed against and in times when it's appreciating, your returns are enhanced (both positive and negative) by using the bank's money to finance your ownership. What few people appreciate is that you can gain high-quality exposure to commercial and industrial property through the share market and managed funds in both large and small quantities, although the ability to borrow against these types of investments may be less than with direct investments.

The New Zealand share market includes a number of property investment opportunities covering a range of property types. The characteristics are very similar to direct property ownership, i.e. income through rents and leases (paid as dividends or other distribution), and returns are equally enhanced by a degree of bank debt within the investment vehicle. The key difference is the liquidity of these investments as your 'share' of ownership can be sold at any point in time for a minimal brokerage cost. Most of the options are also structured to be tax-efficient for investors through a PIE structure. The risks remain similar though; mainly from low occupancy and rising interest rates.

This is where the merits of diversification come in. It is not currently possible to get direct exposure to the residential property market through the share market, and the Auckland residential property market in 2019 has been sluggish as best. Contrast this with share market listed property companies where the average increase in 2019 has been over 20%! Without doubt, this has been an exceptional year so far and property investment hasn't always favoured listed property, but those who were exposed to both residential investment and listed stocks will have benefitted from a more consistent result.

By extending this idea of being diversified beyond property, we can construct portfolios of investments that contain a degree of consistency and resilience, regardless of the economic environment. The key to a successful strategy is determining a level of return that reflects your ability to accept the risks that might exist. By engaging an adviser, investors develop a strategy with the appropriate level of risk and are more likely to achieve their objectives around long term investments, a comfortable retirement, and estate plans.

will.roberts@sraminvest.co.nz

FANZ Private Wealth is a boutique investment advisory service who specialise in providing personalised and impartial investment solutions for individuals and trusts. Call 0800 727 2265 to contact an adviser.

FANZ Private Wealth is an operating division of Funds Administration New Zealand Limited (FANZ). FANZ is a subsidiary of SBS Bank which is a registered bank. Neither FANZ nor FANZ Private Wealth is a registered bank.