

Making more of your rent roll

By Mark Lipson & Robert Lissauer, Sothertons

Don't take your rent roll for granted – in current market conditions property management is more valuable than ever to your business.

We know that a well-managed rent roll division smooths cash flow for your business. Whether residential or commercial, the reliable and predictable income from rent offsets the commission income volatility from property sales.

If your property management division is performing well, your rental portfolio should also provide an ongoing source of property listings. Property owners with a high level of trust are more likely to choose the agent who manages their rental property when the time comes to sell.

A well-managed rent roll is a valuable asset and you can release its value either by selling all or part of the portfolio of properties that make up the rent roll, or borrowing sensibly against the rent roll to invest in business expansion.

How your rent roll is valued

The value of your rent roll is determined by the expected required rate of return generated by the rent roll asset. There are two sets of valuation factors that influence the expected rate of return.

1. Specific business risks attributable to the management of the rent roll (Micro economic factors). These include:

- Size and quality of properties in the portfolio.
- Geographic spread of the properties.
- Ownership concentration – the number of landlords relative to the number of properties in the portfolio.
- The investment in quality staff to manage and operate the property portfolio.

2. The factors effecting supply and demand of rental properties in the market (Macro economic factors). Changes in economic conditions have a profound influence on the value of your rent roll.

In periods of sustained economic growth, rising housing prices and easy access to finance, owner-occupiers tend to dominate the housing market. These periods are usually associated with falling rental yields for the investor. The rental cycle is no different to any

other investment cycle. There are always pressures and influences in the market to drive the cycle back to higher rental yields.

Trends in supply and demand

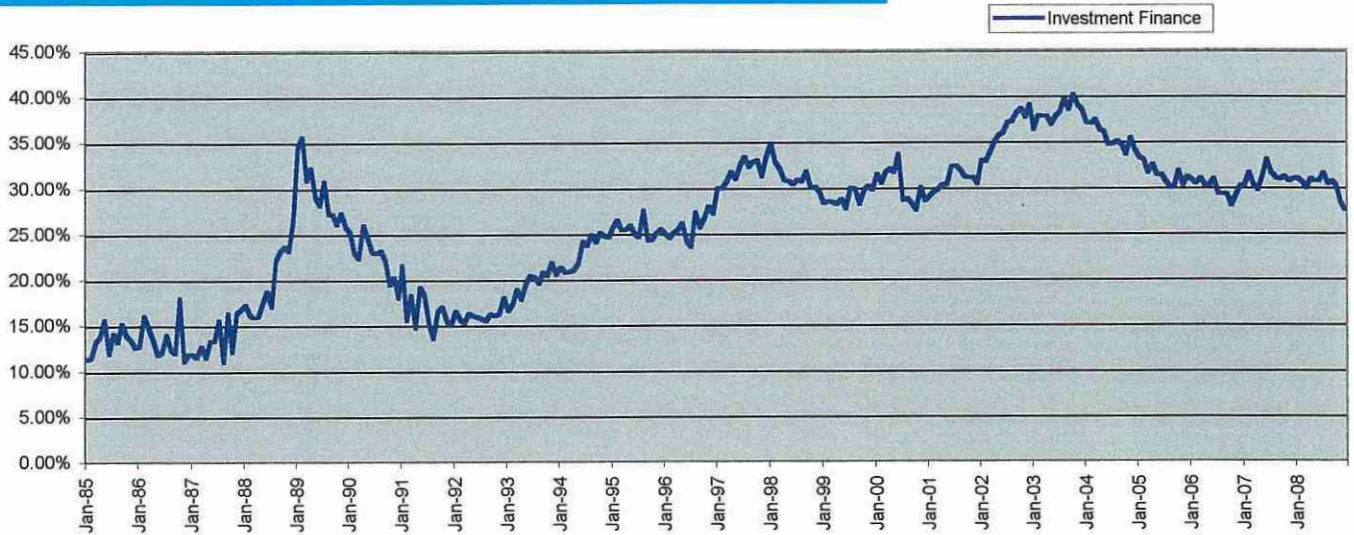
Crucially, access to mortgage finance and the level of interest rates on borrowed funds affects the supply and demand of properties. We know that owner occupation is boosted by access to mortgage finance, regardless of income and saving levels.

Added to these factors, Government support for first time homebuyers also influences whether younger individuals and families will leave the private rental market to seek home ownership. This means fewer investment properties and fewer tenants in the rental market.

The landlord's choice

When the influences on demand create increases in residential housing prices, growth in rents can lag well behind housing prices – causing the rate of return on rental investments to fall substantially.

Percentage of investment finance of total housing finance *seasonally adjusted*



Landlords are faced with the choice to retain their investment or capitalise on the higher housing prices. If a landlord sells their investment, that property is then transferred out of the rental stock, potentially on a permanent basis. Rental apartments are often refurbished and sold into a rising housing market, while older rental properties may be demolished and town houses and other multi-dwelling developments constructed and sold for owner occupation.

In recent years there has been a trend of landlords shifting their investments

out of the rental market, creating a diminished level of investors in the housing rental market. The chart below shows that according to the Australian Bureau of Statistics, since October 2003 the level of housing finance commitments for investment activity has decreased from a high of 40% in 2004 down to 27% in December 2008. This is a fall of over 30% of total housing finance dedicated to housing investment activity.

Construction slowing

Economic data from the Australian Bureau of Statistics also shows that

building and construction activity for total dwellings has trended downwards in recent years. The growth in total stock of dwellings to supply the housing demand has fallen since November 2003 and has crashed since 2007 (shown in the chart below).

The impact of a decline in building approvals and construction activity with the increase in demand by owner-occupiers has led to a shortage of rental stock with the resultant sharp increase in rents that we have experienced recently. The economic cycle for the investor has begun to turn again.

We understand your industry

Imagine working with a chartered accountant and business adviser who understands your industry? Sothertons has 30 years' experience working in property and real estate with architects, builders, developers, real estate agents, civil engineers and allied industries including renovators and product suppliers. So we do understand.

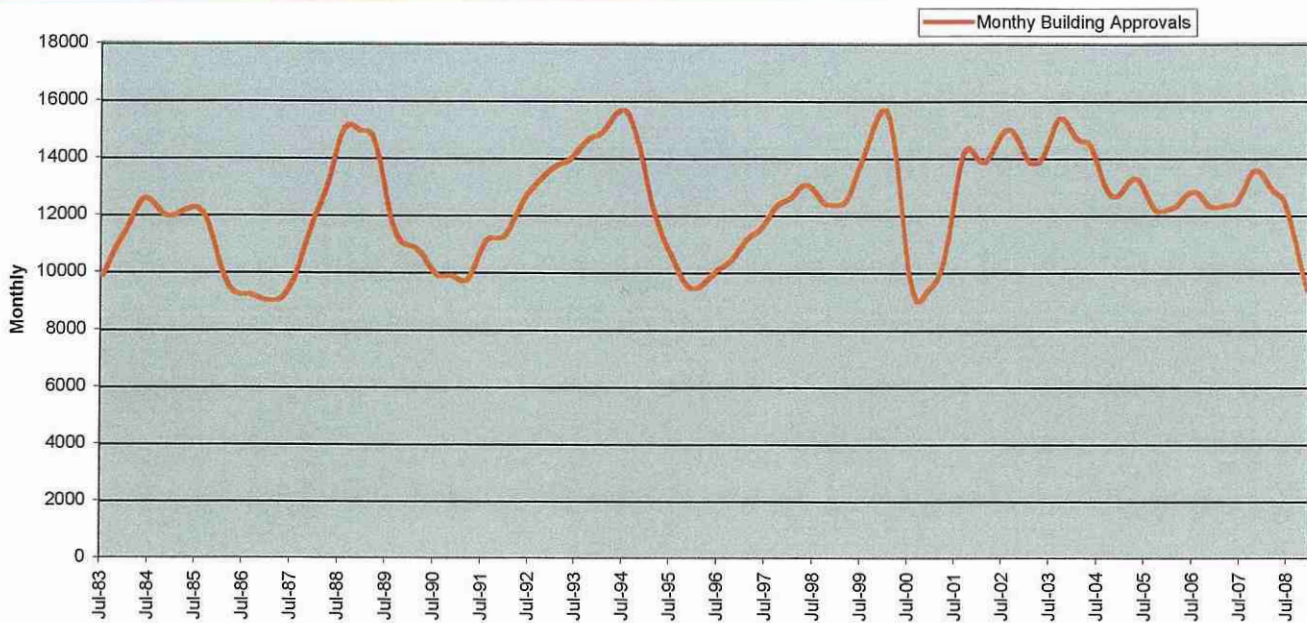
Contact Robert Lissauer or John Christopoulos on 03 9820 6400 to discuss your business needs

Sothertons chartered accountants Level 6, 468 St Kilda Road Melbourne Victoria 3004
www.sothertons.com.au

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Building approvals – monthly trend analysis



Where to next for your rent roll?

The current slowdown in the economy is associated with falling interest rates and a drop in median house prices in Victoria. These conditions, combined with the strong growth in rents in the latter part of 2008, indicate a strengthening recovery in rental yields. In fact these economic conditions will provide plenty of incentive for the residential investor to switch their investments from other, poorly performing asset classes back to bricks and mortar.

Economic conditions leading to the end of 2008 have greatly improved the revenue and profitability of quality rent rolls managed by real estate agents, making them of even greater value to your business.

With activity returning to the housing investment market, our view is that the value of rent rolls will continue to strengthen over 2009.

What should Real Estate Agents do now?

There has been a growing demand by agents to grow their property management fees through acquisitions and so the inevitable outcome has been an increase in the value of this asset. It is therefore essential that you invest the time and energy to maintain your rent roll in such a competitive marketplace.

Effective management is the key, partly because as we said the landlord who has a successful relationship with you when renting will choose your agency for selling. Stay in touch with owners on your rent roll, with up to date market information relevant to their investment. They will feel comfortable that your agency is in touch with their investment outcomes and with larger market forces. They will develop trust in your agency's skills in all areas of business. Giving owners an understanding of the value of their investment, and how to maximise that investment return, may also increase your turnover of rental stock and listings.

Call Robert Lissauer at Sothertons on (03) 9820 6400 on to discuss your business needs.