

Where to find top yields for investment property

Duncan Hughes *Reporter*



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Real estate investors are getting gross yields of up to 7 per cent due to rental shortages and rising population growth, despite [falling property prices](#)

[\[https://www.afr.com/policy/economy/secret-rba-modelling-shows-20pc-drop-in-house-prices-20221022-p5bs13\]](https://www.afr.com/policy/economy/secret-rba-modelling-shows-20pc-drop-in-house-prices-20221022-p5bs13) and rising interest rates.

Rents are rising at record rates as vacancies hover at historic lows of about 1 per cent thanks to a sharp increase in overseas workers and students returning after the easing of COVID-19 restrictions.



Potential tenants queue to inspect a property. **Craig Sillitoe**

“High rents and low vacancies are boosting gross yields and net returns,” says Rich Harvey, chief executive of buyers’ agency Propertybuyer.

Chris Foster-Ramsay, principal of Foster Ramsay Finance, adds: “Investors ready to play the long-term game have been sitting on the sidelines with sizeable deposits and borrowing capacity for the right rental properties in the right locations. They are starting to move back into the market.”

Evidence of green shoots in the investment sector could begin to emerge next week when government numbers reveal the value of investment lending for September. In August, this fell nearly 5 per cent, or more than \$443 million. During the past 12 months investment lending has fallen more than 6 per cent, or by \$607 billion. Many investors could hold back if the Reserve Bank of Australia increases cash rates [<https://www.afr.com/policy/economy/annual-inflation-hits-7-3pc-exceeds-expectations-20221026-p5bsxt>] next Tuesday for the seventh successive month to curb inflation.

Where demand is strongest

Desperate potential tenants are offering to pay above market rents and up to 12 months of rent in advance to secure a property, according to Sydney leasing agents.

National vacancy rates are a record low 1.1 per cent, with listings across the combined capitals also at record lows and about 35 per cent below the previous five-year average, according to SQM Research.

Median weekly house rents in Sydney's harbourside Vaucluse are the most expensive, having increased by nearly 13 per cent during the past 12 months to \$2600, analysis by CoreLogic shows.

In Melbourne, the most expensive rental suburb is Brighton in the inner south (where the median weekly rent is about \$1300) and in Brisbane it is inner-city Ascot (with a median weekly rent of about \$1300).

Strong net overseas migration is expected next year in most Australian cities, according to the federal government's Centre for Population. The permanent migration cap has been lifted from 160,000 to 195,000 for the next 12 months, and more than 2 million applications have been processed since June.

Brisbane attracted more than 50,000 during COVID-19, and another 220,000 interstate migrants are expected over the next five years, according to the Property Council of Australia.

The gross yield equation

Darwin, where the property market is aligned to the fortunes of the mining industry, posted the strongest gross rental yields for houses during September of about 6 per cent, followed by Perth at 4.4 per cent, Hobart 3.8 per cent, Canberra 3.7 per cent and Adelaide 3.7 per cent, according to CoreLogic.

Gross yield is a percentage calculated by dividing the property's annual income by its market value and multiplying by 100. Falling property prices and rising rents mean gross yields are increasing.

Sydney and Melbourne are returning the smallest gross yields of 2.7 per cent and 3.1 per cent respectively for houses, but growth is underwritten because they are gateway cities for immigrants and overseas students, according to property specialists.

Apartment gross yields are higher than houses. Darwin is at more than 7 per cent, Perth 5.7 per cent, Canberra and Adelaide at 5 per cent, Hobart 4.4 per cent, Melbourne 4 per cent and Sydney 3.6 per cent.

CoreLogic economist Kaytlin Ezzy says: “Since August, national dwelling rents have surged by almost 20 per cent, equivalent to a weekly rent rise of about \$90 per week. The continued upswing in values is likely predominantly being driven by the strong return of overseas migration, coupled with extremely tight rental supply.”

She blames a slowdown in September’s rental rise to 0.6 percentage points on prospective tenants “coming up against affordability constraints”.

Apartment returns are more resilient because they are more affordable, Ezzy says.

Charter Keck Kramer, a property consultancy, says rental demand is increasing faster than anticipated, but supply is slowing because of rising interest rates, increasing construction costs and weak consumer sentiment.

“This creates significant development and investment opportunities across many apartment markets,” a recent report by the consultancy concludes.

Lending deals

Some lenders, such as Commonwealth Bank of Australia, have special offers for investors. The bank has cut its three-year fixed rate by 100 basis points to 5.59 per cent for principal-and-interest investors – that’s about 40 basis points lower than the same term for owner-occupiers.

Mortgage brokers say lenders will deeply discount headline rates for cashed-up investors.

Tax breaks

Mark Chapman, a director of H&R Block, says property investors are eligible for generous tax deductions for rental income, capital works improvements and capital gains.

Chapman says property investors should not be too concerned about losses from rental income due to rising interest rates. “You make a series of small annual losses on your rental income – for which you receive tax relief at your marginal rate – but

then at the end you make a potentially large capital profit on the disposal. The profit on disposal often outweighs the small, cumulative losses on rental income.”

Jeremy Goldschmidt, chief executive of RentBetter, a DIY platform for property investors seeking to cut out professional managers, says a typical rental property is losing more than \$14,000 a year despite negative gearing of loans, generous depreciation allowances and capacity to raise rents.

Goldschmidt says investors should be targeting expenses, such as management fees, advertising and maintenance, to reduce expenses and boost returns, rather than relying on tax deductions.

Red tape

Rental specialist Andrew Kent, president of the Australian Landlords Association, says onerous state government regulations and taxes are worsening shortages by forcing landlords to sell or repurpose rental properties.

Kent says many landlords have sold properties to owner-occupiers or converted to short-term leases to avoid new rules that increase owner costs for long-term tenants.

“The rental crisis is not caused by landlords, but a lack of landlords,” Kent says.

“Landlords are exiting due to government policies, which is putting pressure back on government.”



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Duncan Hughes is a Walkley award-winning personal finance reporter, based in our Melbourne newsroom. *Connect with Duncan on [Twitter](#). Email Duncan at duhughes@afr.com.au*