Property Investment Matters

Capital Growth Vs Cash Flow

Investors have to weigh up the pros and cons when determining whether to chase capital growth or high rental yields when buying properties. Property investors commonly fall into one of two camps – those who are disciples of capital growth, and those who think cash flow is king. So which is better?

Going for growth

Capital growth should be seen as part of a medium to long-term strategy, with properties being held for up to a decade or more. The aim should be to achieve an annual increase in the property's value of about seven per cent to 10 per cent.

Rental yields on such properties are likely to be a modest five per cent or lower because they are often in highly desirable areas in and around capital cities or regional centres. They usually come with a high price tag as a result of strong demand from buyers.

However, this high cost/low yield scenario plays into one of the biggest strengths of capital-growth properties: negative gearing. In simple terms, this situation means the interest you are paying on a loan is more than the income from rent.

Cash flow-positive property

Investors who buy cash flow-positive properties draw comfort from knowing they will usually get a monthly return.

This strategy is based on finding reasonably-priced properties that have high rental yields. They are usually found in smaller regional towns, or developments such as student accommodation.

Positively-geared properties often appeal to new or younger investors who have not yet built up a lot of equity in their property portfolio or who are on lower incomes. Some of the disadvantages with cash-flow positive properties are that they usually don't grow anywhere near as well or as consistently as capital city property, and can require a relatively larger deposit as they are often considered to be a higher risk by lenders.

Best of both worlds?

Clearly, it would be great if a property could deliver high capital growth and a strong cash flow, but finding such a gem is difficult.

In the past decade, some mining towns experiencing a boom have defied the norm – delivering soaring rents and phenomenal capital growth. However, such cases are the exception to the rule.

The verdict

So how do the two philosophies stack up? That will depend on your risk profile, but it is worth remembering it requires high cash flow to pay down a mortgage and create a situation whereby you have sufficient equity to buy again.

Contrast this with the power of capital growth. With only five to seven per cent capital growth, just one property worth $500,000 will grow by $500 to $700 per week, plus this growth is essentially not taxable until the property is sold a long time later and any capital gain is taxed at half the rate of income tax. Rental yields of cash flow-positive property can almost never hope to match such a gain, especially after they are taxed.

Happy Flats Barcelona = Best of Both Worlds!

Capital Growth - We are purchasing discounted property in a Capital Cosmopolitan City with a fantastic climate located on the Mediterranean Sea, geographically central to Asia and North America, with easy access from the entire E.U. Barcelona is considered a trendy and fashionable city and is growing in popularity. Top analysts predict prices are bottoming out and current numbers are showing stabilisation in the property market. Barcelona is projected to be one of the top growth cities in the world over the next 20 years making it both an excellent short term and long term investment market. Barcelona is just recovering from its worst economic crisis In its recent history (based off the real estate market) so not only is the property at a value, but all inputs including the materials, labour, offices and employees are all at a discount making this the perfect time for an early stage company to capitalise on a “first mover advantage” and become a market leader.

Cash Flow – We are dedicating the rental to student housing which is in high demand. There is a significant supply/demand imbalance in the Barcelona student housing market with more than 250,000 registered university students and only 20,000 official university dormitories available. Barcelona is the #1 destination for Erasmus International students and €15 billion to be awarded now through 2020 to modernise higher education. Spain has also initiated a mandate for Barcelona universities to offer 1 out of every 3 courses taught in English by 2020. This gives HFB a perfect fit, synchronising with the corporations predicted “vintage year”.

This strategy provides HFB the rare opportunity for long term Capital Growth on the properties and short term Income from rentals for improved liquidity.