COMMERCIAL PROPERTY NEWS

SCOPE PROPERTY GROUP

Partnering YOU in wealth creation through commercial property

ISSUE 6

NEWSLETTER | SPRING 2012

A MORE BALANCED LOCAL ECONOMY IN THE YEAR AHEAD

Welcome to the Spring edition of the Scope Property Group newsletter. Looking back over the last quarter here in Australia it appears as though we are weathering this worldwide economic storm better than most, with the economy growing by a strong 1.3% in the first quarter of 2012, with annual growth coming in at 4.3%.

Now whilst these figures lead us to believe that the economy is being run like a well oiled machine, caution needs to be exercised as there are still signs of future problems looming on the horizon. Jobs growth has slowed turning negative recently, commodity prices have fallen between 20-30% and asset prices in Australia have also fallen (house prices down around 8% and share market down 7% for the financial year end). In addition, there are daily stories of patchy business conditions, even here in the West, with many companies cutting staff, while consumer and business confidence remains fragile.

But it's not all bad news, there is some good news.
"Inflation has retreated to below 2%
"The RBA has again cut interest rates.
"Sydney Swans won the Grand Final

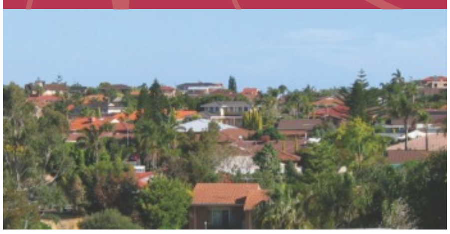
Interest rates are probably the most topical when it comes to investing and it is important to note that since November 2011 we have seen the cash rate fall by 150 basis points, of which the banks have only passed on 98 basis points. Irrespective of the levels of these reductions passed on, conditions bode well for all of Scopes investors who directly benefit from these cuts with lower interest costs for those on variable rates improving the cash positive aspects of your investments.

Now given that there is always talk of WA seceding from the rest of Australia given that we seem to be supporting the rest of the nation on the back of our resource rich state, how is the local economy faring? This last quarter saw a bit of a slowing, with a significant pullback by many of the major mining companies on large projects in response to falling commodity prices. Some referred to this pullback as the end of the resources boom. Not so. Now whilst this fall in commodities has seen many projects (mainly iron ore here in WA) be deferred or scaled back, resulting in retrenchments and laying off of contractors, what many people don't realise is that many of these were actually "pushed" forward by the companies as a result of previously high commodity prices and this situation is simply a realigning of the project time-frames back to within original plans.

This has resulted in tightening of general business conditions, and now sees those businesses directly exposed to the mining industry also needing to carefully manage their businesses.

The end result, a return to more balanced local economy, rather than the dichotomy we have seen here over the last three or four years. This too also results in an increasing number of opportunities becoming available for Scope, as local businesses and individuals start tightening their belts. We are confident that in the very near future we will be able to present our investors a number of these opportunities.

How to make that untapped equity work for you!



Now whilst many of our existing investors have already discovered the benefit of unlocking the equity in their homes as a means to invest with Scope, there are still many people out there who are yet to discover this.

I am sure that many people will remember the Commonwealth Bank advertisement "Equity Mate!" whereby the bank was promoting the ability to draw back on you housing loan and using the "Equity" for a holiday, boat, new car renovation. What about investment?

Over the years we have all worked hard, focused on repaying the mortgage and in the process built up a considerable amount of equity as a result of the amortization (repayment) of the loan and general market appreciation. But many are still unaware of their ability to leverage it and use this to achieve their financial goals.

from page 1

Unfortunately though, some people have a reluctance to tap into this equity in their homes, as there is the perception that they will be putting everything on the line.

"What if something goes wrong?"
"We could lose the home."

The same could also be said if they choose to do nothing. What opportunities are they missing out on by thinking that they don't have the funds to invest??? I am sure we have all heard "should have, could have, would have...", unfortunately after the opportunity has passed.

So how does it all work? In simple terms, equity is the unrealized value in an asset. Let's assume that your house is presently valued at say $850,000 and your mortgage is $200,000, you have equity of $650,000. Now provided that your income can support any additional borrowings, most banks will lend you up to 80% of the value of your property. This scenario will therefore provide you with $480,000 of geared equity to invest.

So now we have access to this equity, what can we invest in? Traditionally people looking to invest into property would look at buying a "rental". This investment started to take off in the early 80's when people used this equity to buy a negatively geared, residential investment property. So what is negative gearing and how does it work?

Negative gearing is a mechanism whereby the government allowed investors to write off the interest costs of any borrowings used to acquire an investment property, along with other holding costs, against all income - not just that generated by the investment.

Now, up until about 2000, the net rental incomes generated by these investment properties were generally enough to cover most costs including interest and maintenance, but after this the losses started to grow, to the point that in 2007-08 Australia's negatively geared property investors claimed aggregate losses in excess of $9.0 billion.

Unfortunately though, with changes in tax rates, interest rates and the general value of houses nowadays, the benefits of negative gearing are not as effective as they were say 15 years ago.

So with negative gearing ceasing to be an effective tax minimization strategy, the smart investors are looking for "cash positive" investments. Something where the income generated by the investment more than supports the holding costs (interest) on borrowings used to invest. These investments provide investors with the ability to make a self-supporting investment (not a drain on your day-to-day income) that also has capital appreciation, making your equity really work for you.

So how do you take this next step in your investment journey to wealth creation and get comfortable releasing that equity for investment? First and foremost it is vital to educate yourself about the risks involved, so that you can get comfortable with your fears and invest with an open mind.

So in order to take those next steps in creating your personal wealth

1. Invest in your financial education.
2. Mingle with like-minded people
3. Have an exit strategy if the plan isn't working.

OUR LATEST SYNDICATE

ASPIRE BUSINESS PARK

In our last newsletter we profiled our latest acquisition, 231 Balcatta Road, now aptly named "Aspire Business Park". We are pleased to announce that Scope now have all of the necessary zoning, strata and building approvals in place, with refurbishment works now well underway. We expect that the refurbishment will be completed by late December and with marketing now well underway the first sales in early 2013.

Joint selling agents, Axia Corporate Realty and Raine & Horne Commercial, were appointed back in July with the marketing campaign to commence in early November.

Should you or any of your associates be interested in purchasing one of these attractive strata units please contact either Wayne Mitsikas from Axia on 0413 599 655 or Anthony Vulinovich from Raine & Horne on 0411 516 343 for further details.

Interest Rates

Like many companies exposed to interest rate risk, Scope receives commentary on the state of financial markets from a variety of sources, mainly banks, with differing perspectives on where the market is and where it is going to go. The following is a bit of a summary of where things presently sit in the world and here in Australia, and where things may go.

"As has been the way for the past several months/years, offshore events continue to dominate the economic landscape which has the effect of causing both confusion and opportunity, arguably in equal parts.

European economic woes continue to remain at the forefront, whilst in the US there have been signs of economic recovery, but it appears to be a case of two steps forward and one step back for them.

The main concern with the US is that they appear to have little in the way of stimulus measures available to them. With the cash rate at zero, recent measures have involved "Operation Twist", whereby they are selling short dated government bonds to finance the buying back of longer term bonds, which has the effect of lowering their long term rates.

The other measure, and probably most concerning measure, is "Quantitative Easing", aka printing money, to buy back govt bonds and increase money supply. As anyone with a passing interest in economics will know, printing money generally has inflationary impacts (think Zimbabwe or Germany circa early 1900's). Thankfully though, the inflationary problems haven't reared their head , but sure as the sun will rise tomorrow this may not remain the case if they keep firing up the printing presses.

So how does all of this impact on longer term interest rates here in Australia? If we take a look at the 3 Year Fixed Rate chart above, its had a very positive impact for borrowers. The 3 Year Fixed rate continues to remain below the lows of the GFC, and at levels not seen since the middle of last century. So can they go lower? Potentially, but history suggests this is unlikely.

So what is the rationale behind fixed rates at being at these "too good to be true" levels?

One explanation offered up is the amount of foreign ownership of Australian Commonwealth Government Bonds (ACGBs). Since the early part of this century, the amount of foreign ownership of ACGBs has jumped sharply as foreign investors chase our relatively high yield in a stable AAA rated environment. This increased demand has had the impact of pushing the price of ACGBs higher and pushing down yields (interest rates). As ACGB interest rates form the starting point for any commercial fixed rates this has a positive impact on fixed rates for borrowers but is also having a knock on effect to the value of the AUD. Basically, Australia is considered a nice safe place to invest.

But there is a risk for us here in Australia. Should these investors suddenly decide to unwind their ACGB holdings, they could so quickly which would see interest rates move higher, sharply higher, and the AUD quickly fall. Obviously, exporters would be rather keen for this event to occur, but those exposed to variable interest rates may feel some sharp pain.

In summary, so long as the uncertainty that prevails, particularly internationally, and this is expected to remain for some time, so will opportunities, no matter what side of the ledger you are on. However, risks are prevalent, and the key rationale behind interest rate hedging is risk mitigation. So, while it's never easy to get the timing right on any hedging decision, it's fair to say fixed interest rates, in particular, are at rather attractive levels right now.

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Market Pulse

Whilst in recent times there has been talk that the "mining boom" in WA has finished, there are many economists that disagree with this and say that WA is in a growth cycle, and not a "boom".

If we look at the state of the market based on the commentary from around town I don't know if we could say that this is the end of the "boom", more steady growth environment.

Office

* The ongoing tightening of Perth CBD/ West Perth office market is continuing to place upward pressure on rents and increasing the attractiveness of fringe suburban office space.
* Increasing construction costs and limited funding availability are restricting new office supply
* This tightening of availability and upward pressure on rents is seeing mid sized businesses looking for cheaper alternative accommodation outside of the CBD in precincts with good access to public transport infrastructure and main arterial routes.
* This move is seeing increased demand for suburban office space, subsequently forcing vacancy rates down and placing upward pressure on rental rates.

Industrial

* Industrial land values in Perth have been continually increasing over the past 12 months driven by demand outstripping supply for large industrial developments.
* This lack of available land and infrastructure for larger industrial developments has seen resulted in rents for prime warehouses rise by 3.5% over the past year.
* New supply of industrial property is subdued given the lack if available land and further impacted by the banks willingness to fund these projects in the current economic climate.

Access that Equity

With Scopes last offering there were unfortunately a number of disappointed people who missed their opportunity to invest due to delays in having finance facilities approved and in place to draw down.

We therefore encourage all of our existing and potential new investors to be prepared and have their facilities pre-approved and ready to go so you don't miss the boat.

Should anyone require assistance in getting these facilities in place we have an extensive network of brokers and bankers that are always happy to assist. Please feel free to contact Paul Mews at our offices for any assistance in this regard.

Scope Quote of the Quarter

In keeping with the theme of our opening story "How to make that untapped equity work for you" we have found another quote from Warren Buffett that epitomizes the concept of cash positive investments.

"Never depend on single income. Make investments to create a second source."
Warren Buffett

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