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Investment Property Loan

Investment Property loan is not that different from regular home loan. However the property ownership and loan structure is crucial for investment property. For this reason and because borrowing to invest is high risk strategy, you should seek financial advice to make sure that this is right strategy for you. More often this will mean that you will need to have conversation with your accountant and financial adviser before deciding what ownership structure is the best for you.

Can I use the equity of my home to pay for deposit?
Yes you can use the equity of your home to pay for deposit. The amount of equity available can be calculated by subtracting the loan of the property from the value of the property. However the amount of equity you can access will depend on your ability to service the loan.

For example if your home is valued at $500,000 and the loan balance is $200,000. Your equity is $300,000. Please note that because the maximum amount of Loan to Value ratio (LVR) without incurring lenders mortgage insurance premium is 80%. If you have no issue with your ability to service additional loan, you are able to access to your equity at maximum $200,000 ((80%x$500,000)-$200,000)).

How does interest rate on investment loan compare to owner occupier loan?
As investment loan represent higher risk for the lender, the interest rate on investment property loan is higher than owner occupier home loan interest rate. Due to APRA restriction on interest only loan, the interest rate on investment loan with interest only repayment is higher. Depending on the lender this can be about 0.50% higher.

Should I choose principal and interest or interest only loan?
Deciding to choose between principal and interest or interest only loan will depend on few aspects such as the lender interest rate, tax implication, and your objectives. However it is apparent that the attractiveness of having interest only loan has been diminished due to raising cost associated with interest only loan. The following example show comparison between interest only loan and principal and interest.

	Interest Only Loan	Principal and Interest (P&I)
Loan Balance	$500,000	$500,000
Interest Rate	5%	4.5%
Monthly repayment	$2,083	$2,533
1st year Interest Cost	$25,000	$22,335

From the table above we can see that although the minimum monthly loan repayment of principal and interest loan is about $450 or 21.60% higher than that of interest only loan. It will provide interest cost saving of approximately $2,665 in the first year and more in the subsequent year. This cost saving however is gradually diminished as individual move up the higher tax tier.

Marginal Tax Rates	Net interest saving on P&I loan taking into account tax implication
19%	$2,159
32.5%	$1,799
37%	$1,679
45%	$1,466

For this reason, we recommend that you seek advice from tax specialist before making decision about the type of loan repayment you should have. Interest only loan is now more expensive and carries higher risk while providing diminishing tax advantages. Principal and interest loan on the other hand provides lower interest rate and as your loan principal is paid off overtime this will translate to reduction on the overall investment risk.

What expenses are tax deductible with regard to investment property?

The Australian Taxation Office (ATO) website provide some guidance about this however we recommend that you seek advice from tax professional. In summary the following expenses are tax deductible according to ATO website:

- advertising for tenants
- body corporate fees and charges
- council rates
- water charges
- land tax
- cleaning
- gardening and lawn mowing
- pest control
- insurance (building, contents, public liability)
- interest expenses
- property agent's fees and commission etc

For more information please visit ATO website:

https://www.ato.gov.au/General/Property/Residential-rental-properties/

Disclaimer: Please note that this guide is developed without taking into account your objectives, financial situation or needs. It should not be used, relied upon, or treated as a substitute for specific professional advice.