HOW IMPORTANT IS TIMING THE PROPERTY MARKET?

by Michael Yardney

Timing is one of the most misunderstood concepts with regard to investing.
The truth is successful investors know how to create wealth at any point in a cycle.

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Michael Yardney's propertyupdate

ABOUT THE AUTHOR

Michael Yardney is Australia's leading expect in the psychology of success and wealth creation.

Michael is a #1 bestselling author of 8 books and frequently challenges traditional finance advice with innovative ideas on property investment, personal finance and wealth creation.

His wisdom stems from his personal experience and from mentoring over 2,000 business people, investors and entrepreneurs over the last decade and over the years Michael has probably educated more successful property investors than anyone else in Australia.

Michael is Australia's most trusted property commentator and his opinions are frequently quoted in the media and he has been featured in all major newspapers, finance and property magazines throughout Australia and in his regular segments on Sky TV as well as on commercial radio.

Michael also writes regular columns for Yahoo Finance, Smart Company, Your Investment Property Magazine, New Zealand Property Investor Magazine and Your Mortgage.

He was recently *once again* voted Australia's leading property investment advisor – that's the fifth time he has won a similar award in the last seven years

Michael Yardney has been featured in:

Is it a bad time to get into property investment?

The news of falling house prices and the prospect of further falls to come is leaving many investors wondering if it is a bad time to get involved in property investment.

I understand why they're thinking this way. No one wants to buy near the top of the market and see the value of their properties fall and then wait a number of years for the market rise again.

It's often said that timing is everything when investing, but I'll let you in on a little secret – that's not really the case.

I know when I first started investing I understood little about market cycles, yet I made some great investments. Then I learned about the concept of ...

COUNTERCYCLICAL INVESTING

I was told that smart investors aim to acquire assets counter-cyclically. In other words, they follow Warren Buffet's advice:

BE FEARFUL WHEN OTHERS ARE GREEDY
AND BE GREEDY WHEN OTHERS ARE FEARFUL!

I read that understanding the recurring relationship between the different stages in the market cycle was critical to maximising the returns on my investment dollar, while at the same time exposing myself to minimum risk.

And it seemed to make sense – if you know where things are heading and buy before the crowd does – before prices start to rise strongly – you were likely to make big profits!

But over time I realised that that was **not always the case. In fact, if you wait for the right opportunity counter cyclically, you'll often be left behind.**

So I'm no longer a big believer in countercyclical investing because I realised that...

TIMING IS ONE OF THE MOST MISUNDERSTOOD CONCEPTS WITH REGARD TO INVESTING

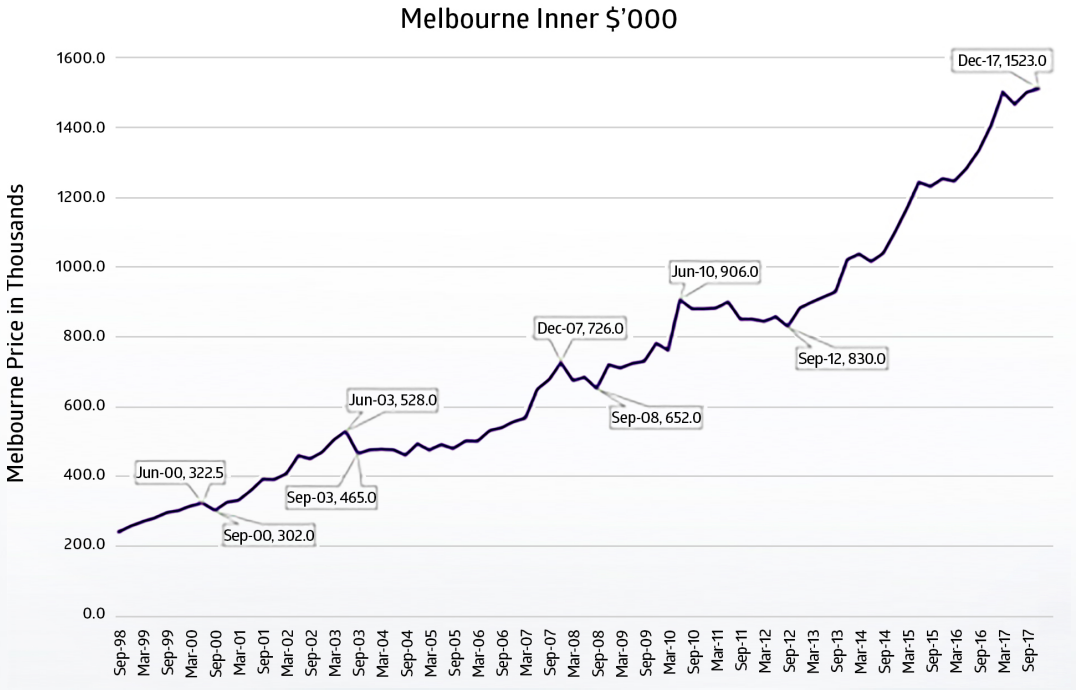
The truth is successful investors know how to create wealth at any point in a cycle.

Timing definitely matters, but successful investors find that timing isn't really that important. Have you noticed how some investors seem to do well in good times and do even better in bad times? Market timing isn't really important to them.

On the other hand, others do poorly in good times and even worse in bad times? Market timing seems to have very little effect on them either. Interesting isn't it?

So how important is timing the market?

Let's look at some real figures to work this out. Below is a graph of the median house price for Melbourne inner ring properties over a 20 year period from 1998.



It's interesting to note that our current downturn is the fifth downturn over this 20 year period.

Now, wouldn't it be interesting to know how much difference it would have made if a property investor managed to buy right at the bottom of the market of each of these downturns as opposed to them getting it terribly wrong and buying right at the peak of the cycle?

The following table shows the difference in equity as well as the overall difference in capital growth if you could get your market timing perfect.

Year of Downturn	Holding Period	% Fall in Price from Peak to Trough	Extra Equity Today	Difference in Compound Capital Growth
2000	17-18 years	6.67%	$21.500	0.58%
2003	14-15 years	11.93%	$63.000	1.11%
2007-8	9-10 years	10.19%	$74.000	1.91%
2010-12	5-7 years	8.39%	$76.000	5.04%

A couple of conclusions can be drawn from this:

1. "Perfect" timing has little impact if you hold your investment over the long-term.

The investor who bought at the very worst time in 2000 is only $21,500 (or 0.58%) worse off than the investor who got the timing right by buying at the very bottom of the market.

In fact, the difference is statistically irrelevant if you hold your property over the long-term – say 20 years.

Even the investor who bought in 2007 just before the Global Financial Crisis hit, is only 1.91% worse off than if they would have bought just before the property market started to pick up in 2008 when the RBA dropped interest rates to stimulate our markets.

Of course, if our hypothetical investor had held off buying while waiting for the ideal time to get into the market after the GFC, it is unlikely they would have bought at the "perfect time" as they would have been waiting for market signals that the property market had moved on to the next phase of the cycle.

And these would only have come to light well after the bottom when prices started rising, auction clearance rates rose, and other investors had moved the market to the next level.

2. Owning the right assets is critical.

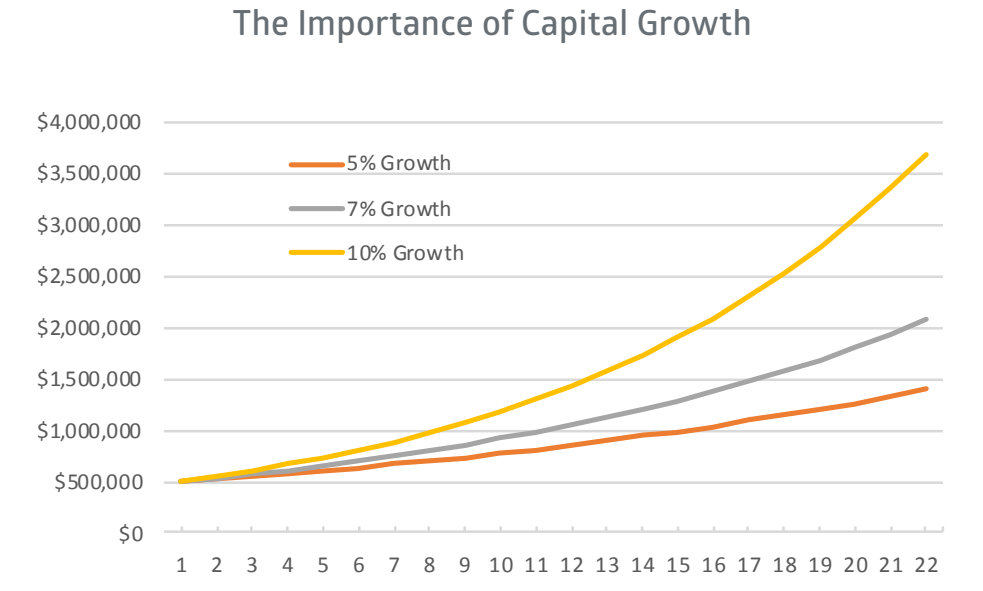
The property market is very forgiving. The longer you hold your investment property, the less important perfect timing of your purchase becomes.

More important than timing is the quality of the asset you own, because investment-grade properties will outperform the averages with regard to capital growth.

Currently many would be investors are holding off, waiting to get their timing right after the market bottoms.

My experience is those who are procrastinating now are highly unlikely to be able to pick the bottom.

When the market turns they'll still sit around waiting for the right signals and will most likely be worse off than those who made a poorly timed decision but took action and bought a property.



The graph above shows that if you own the right property – one that grows at "wealth producing" rates of return over the long term, your asset base will grow more substantially and give you the cash flow you require to develop financial freedom.

Correct asset selection is more important than correct timing, but this brings us to our next point...

3. Time in the market is important.

If you want to become wealthy, you will need to understand the power of compounding.

It's the very root of making money work for you and happens when you let the earnings of an investment compound instead of withdrawing them and spending them.

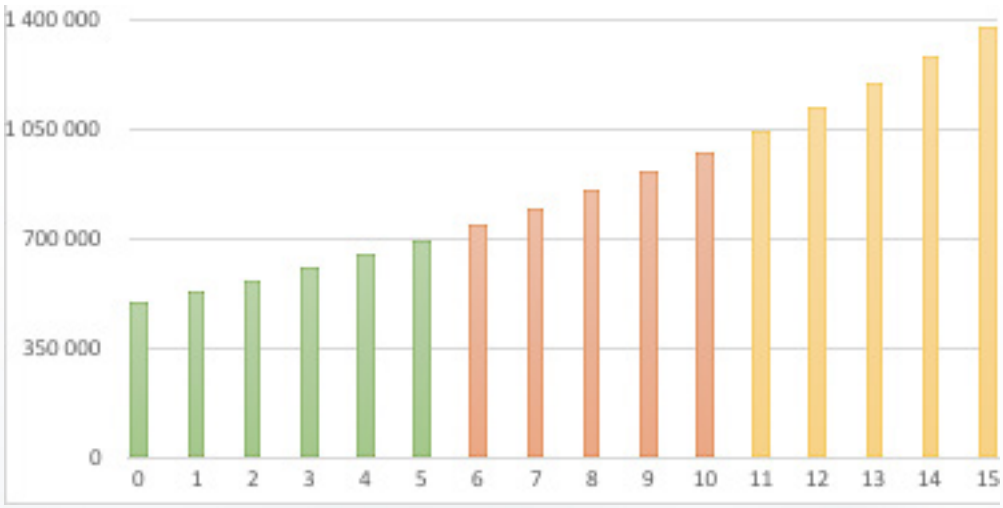
For example, if you had $10 000 in an interest-bearing account and it earned 3 per cent interest ($300), you would be practising compounding if you left the interest in the account to grow further. This means you'd now be earning interest on $10,300, not just the original $10 000.

This keeps building year after year and it's much the same with property.

Just look at the following graph which shows what would happen to the value of a property that grows in value at 7% per annual (of course this is an average – it doesn't happen each and every year.)

While this property doubles in value over 10 years, the power of compounding means that almost half (45%) of its increase in value over the 15 year period shown occurs in the last 5 years.

$500K property increases by 7% over 15 years



Once again, timing is nowhere near as important as owning the right type of asset and holding it in the long term.

4. No one really knows what's going to happen to the property markets.

In Australia we seem to have 25 million property experts – everyone has an opinion. You know what they say about opinions… there like belly buttons; everyone has one but they're basically useless.

Of course, even the property experts tend to get it wrong despite being armed with all the research available in today's information age. The reason is that market movements are far from an exact science.

The fundamentals are easy to monitor. Things like population growth, supply and demand, employment levels, interest rates, affordability and inflationary pressures.

However, one overriding factor that the experts have difficulty quantifying is investor sentiment. Currently investor sentiment is low, in fact the lowest it's been for decades, despite the economic fundamentals being quite solid. Unfortunately even the most rational of us tend to suffer lapses of logic when dealing with money and many of our investment decisions are driven by emotion.

Think about it…

When the media reports falling property prices or an impending housing crash, many investors become scared and sit on the sidelines, believing the end of property is nigh and things will never improve when, in reality, much of the risk has been removed from the market.

Conversely, when property markets are booming and stories of investors seemingly making large gains overnight abound, people want to jump on the bandwagon and cash in; often at a time when the market is near its peak.

You've heard me say it before, as supposedly rational being, humans tend to act irrationally when it comes to money.

Other emotional traps we experience include becoming overconfident, wishful thinking and ignoring information that conflicts with your current views.

In other words, many investors create their own "reality", but unfortunately I've come to realise that "the crowd" is always wrong.

When there is a general belief that property values can only keep rising and this spreads through a new generation of investors (as it does each cycle), driven by FOMO (the fear of missing out) they drive property values up even further, perpetuating the belief and helping make it a reality!

Similarly, when "the crowd" believes the real estate market is going to crash, FOBE (the fear of buying early) keeps them out of the market, and their negative sentiment gets reported in the media and then feeds on itself.

WHAT CAN AN INVESTOR LEARN FROM THIS?

#1

There are multiple property markets around Australia at the moment – some are still growing, others are poised for growth and some markets will experience falling prices over the next year.

#2

Rather than trying to time the market, buy the best assets you can. Timing your purchase well will give you a one-off bonus. However, owning the right property – an "investment grade asset" that grows at wealth producing rates of return will see your portfolio outperform over the long term.

#3

At times of poor or no capital growth, strategic property investors "manufacture" capital growth through property renovations or development.

#4

Booms never last forever, neither do busts. Don't be surprised when they come around and don't overreact. This will help you avoid being sucked into booms and spat out during busts.

#5

Our property markets are not only driven by fundamentals, but also by the often irrational and erratic behaviour of an unstable crowd of other investors. While the long-term performance of property is influenced by the fundamentals, its short term performance is much more affected by market sentiment.

#6

Treat your property investments like a business and stick to a proven strategy to take the emotions out of your investment decisions. Don't make 30 year investment decisions based on the last 30 minutes of news.

#7

Recognise that property is a long term play and set up financial buffers to help you ride the property cycles.

IF YOU ARE UNSURE WHAT TO DO NEXT IN OUR CURRENT PROPERTY MARKETS...

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That's why they won another award...

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Here's what the judges in the recent Your Investment Property Magazine awards had to say:

> "Metropole is at the forefront of property education, providing its expert advice and demystifying property investment through its industry leading blog, podcast and property advisory services. Its value offering is personalised and based on client's individual circumstances, with services delivered by a highly esteemed team of professionals."

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