

# The Motivations of Rental Investors

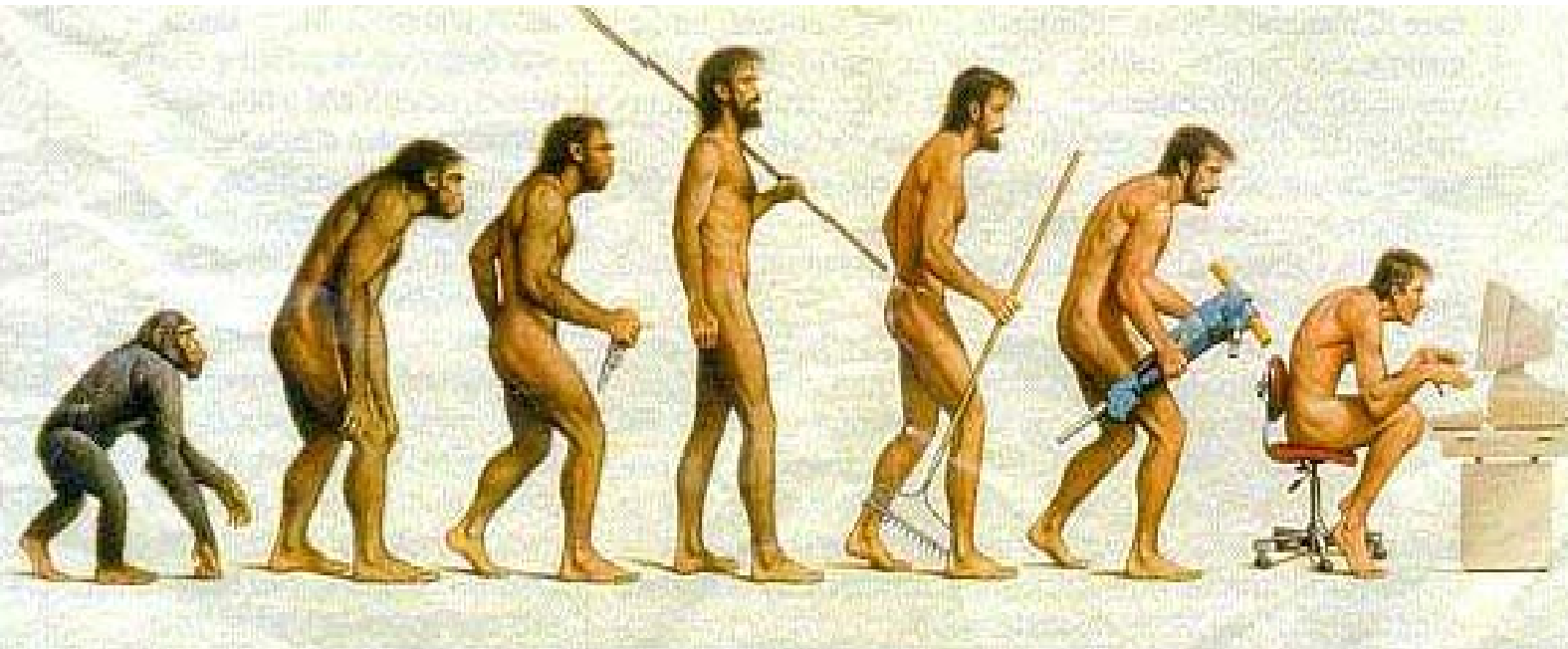
**Dr Tim Seelig**

Housing Policy Research Program, University of Queensland  
Australian Housing and Urban Research Institute

Queensland Research Centre

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# The evolution of Property *Homo A Economicus?*



FOR  
SALE



“Economic activity is human behavior ... The essence of property is human behavior”

Julian Diaz \*

\* Diaz J (1999) ‘The first decade of behavioral research in the discipline of property’, *Journal of Property Investment and Finance*, Vol. 17, No. 6, pp 326-332

# Overview of presentation



- Background to the recent AHURI study
- What we know of investors from previous analysis
- What the recent study suggests about investors:
  - ➔ characteristics
  - ➔ motivations
  - ➔ experiences
  - ➔ behaviour
- Potential policy implications

# Background to the AHURI study



- Some existing knowledge of rental investors
- Mostly informed by ABS surveys (no longer operating) or special one-off studies
- Past emphasis largely on either categorising investors or on developing their profiles in terms of the ‘average investor’
- Some sense of how investors have rationalised their investment decisions, but little focus to date on what motivates and drives investment behaviour, and the circumstances in which investment occurs
- Interest in investors waxes and wanes ... allowing for subtle and more dramatic changes to occur under the radar

# Past studies of investors

- Previous studies have emphasised certain characteristics of rental investors
- Tendency to be:
  - ➔ small scale (one or two properties in the main)
  - ➔ household based ('mum-and-dad' investors)
  - ➔ Wage-earning workers ('amateur' investors)
  - ➔ Middle aged, middle income, couples, home owners (those with the means and opportunity)
  - ➔ attracted by the potential for longer term capital gains
  - ➔ Investing in same city or state as resident in
- Low cost investor features:
  - ➔ Older, lower income, more reliant on rental income, seek to exit

# Overview of AHURI study



- Focus on the motivations, expectations and investment behaviour of rental investors
- Trying to understand the contexts and circumstances in which rental investment occurs
- Qualitative study, based on semi-structured interviews across several cities and regions
- Sociological (social-behavioural) approach
- Many challenges in recruitment etc

# AHURI study: critical questions

- Why are people investing?
- Why in property?
- What attracts them to specific dwellings?
- What are their expectations?
- What are their experiences?
- How does all of this impact on rental investor behaviour?
- What the implications re supply and policy?

# AHURI study: investor snapshot

Study participants seem fairly typical of investors from past studies:

- Largely similar to the erstwhile traditional picture
- Still relatively small scale but av. holdings slightly larger (may be indicative of the wider picture?)
- Higher av. Incomes (indicative of the wider picture?)
- Most (80%) bought existing dwellings (split evenly on houses and flats/apartments)
- Used specific loan from bank (interest only or 'I & P')
- Most put in less than 20% equity
- 3/4s: use negative gearing, agents to manage, expect to invest for more than 5 years

# Critical issues from new study: Why become an investor?

## **The motivators for (property) investing decisions include:**

- financial factors
- personal goals
- personal and family circumstances
- several other influences.
- market conditions are important, but are often linked to these other factors
- some did not have strong motivations – but they had the financial capability.

# Critical issues from new study: But why property?

## Attraction of property over other areas of investment:

- Binary is misleading - a number of property investors also currently investing in other areas, mainly shares.
- However, shares were seen as being of a different order and scale to property, and were treated accordingly.
- Many investors had previously lost money in shares; not keen to repeat the experience
- Shares or no, there were several reasons behind investors' choice to invest in property over other forms of investment.
- The most crucial was that it represented a good (long term) investment ...with a sense of 'low risk' and 'guaranteed' return
- Most investors identified 'long term investment' or 'capital gains' as having been seen as the most important 'reason for having invested in property'

# Critical issues from new study: But why property?

- Rental income and negative gearing had been seen as largely unimportant, but these can become more significant with the more properties owned / the higher the income
- Capital growth trends were seen as the most crucial ‘factor considered’ when investing, but interest rates, rent levels and negative gearing also seen as being of importance
- Tenancy law simply does not rate as a factor impacting on investors’ decision-making
- Residential property seen as something which allows for other potential benefits (eg future residential or holiday home for them, or their kids).
- Other benefits of familiarity with property, its tangibility and sense of control

# Critical issues from new study: Sentimentality and informality

- property widely regarded by investors as something relatively easy to invest in – not seen as mysterious or complex
- the general impression is that ‘lots of people do it’
- personal experience and intuition reported as the dominant sources of information for investors in making property investment decisions.
- accountants, estate agents and specialist advisors were much less commonly used (if at all).
- housing market information readily accessible now (internet, etc) – no longer reliant on property or investment professionals
- Investors’ sentimental feelings about properties are significant
- influence of advice from friends, books and investment seminars in shaping investment decisions also important
- information/sources used by investors objective or reliable?

# Critical issues from new study: when, what, where of investing

- some investors had been highly mindful of property market cycles - critical factor which impacted on investment decisions
- with others, awareness of the cycle led to reflections about whether they had in fact bought at a 'good' or 'bad' time, but housing market conditions had not been all that important.
- for many, market timing issues are countered by the greater significance of personal circumstances, and capacity to invest.
- competing priorities in terms of location
- Most investors said they aimed towards the 'middle of the market' (not many target low cost, but high cost not seen as attractive either!)
- personal, intuitive and emotional factors strongly evident in the process for dwelling selection.

# Critical issues from new study: investor expectations

- investor motivations also linked to expectations
- Investors measure their success in different ways, but most commonly, capital gains over the longer term are what they are expecting
- for most, this is in effect how their sense of the success or otherwise of property investment is assessed
- The expectations (for the long term) were high but also often rather broad and general
- investors generally accept that positive returns were not going to be made until a number of years down the track, that costs may well outweigh returns initially.
- significance of negative gearing – for most not a deliberate strategy, and for many not a crucial factor in investment decisions, but for nearly all a ‘welcome and generous tool’ or ‘added bonus’

# Critical issues from new study: The 'succour of success'



- Previous and current experience of property kept investors in the property investment market.
- Nearly all who had been in the property investment market for several years, and many more recent investors had experienced what they regarded as 'success'.
- This success provided an ongoing incentive for investors to remain in the property market, to increase their portfolio, to consolidate, or to start realising their assets as part of their investment strategy.
- Indeed, investors, new and seasoned alike, reported very high rates of satisfaction with various aspects of their property investment: yield, capital gain, property and tenancy management

# Critical issues from new study: Management of property/tenants



- Investors pretty sanguine about who tenants their properties
- Not as keen on 'students', 'group households' (but OK with 'young people'!).
- Also less attracted to Centrelink clients and sole parents
- Spending on maintenance big issue: less than half spent more than \$500 pa on repairs/property
- Investors seemingly see repairs as discretionary and don't budget or plan for them:
  - have little understanding of tenancy law requirements
  - the need to is not stressed at time of purchase
  - can't adequately allow for reasonable maintenance costs
  - think of *themselves* living in the place (things can wait)
- A number of instances of investors indicating reluctance to increase rents when they have a stable long-term tenant
- Makes good sense; examples of genuine altruism too!

# Critical issues from new study: Changing motivations over time

- change in ongoing motivation commonly related to shifts between various wealth creation objectives;
  - ➔ shifts as a result of experience and increased level of knowledge
  - ➔ shifts resulting from changes in personal circumstances or objectives
  - ➔ shifts from wealth creation objectives to family concerns
- for those without strong initial motivations, esp in early investments, interests shifted over time to forward planning and consideration of how investments meet future needs
- for some, the rationale and objectives of being a rental investor became more nuanced or considered more broadly over time.
- These shifts often occurred as investors approached retirement and/or started thinking about financing their retirement.
- several described their transition from an 'inexperienced investor' to an 'experienced investor'

# Critical issues from new study: current and future outlook

When asked about their current thinking on their rental investment/s:

- The clear majority saw capital gains as more important than rental income over the next 5 yrs
- An even bigger majority saw capital gains as more important than rental income over the next 10 yrs
- Nearly all regarded property as the 'best investment'
- Some said they would still invest in property even if returns were clearly higher in other areas (eg shares)
- They were split 50/50 on whether they would have invested if negative gearing had not been available

# Critical issues from new study: drivers to sell property

- investors grouped into five categories in terms of future intentions about retaining or disposing of their rental dwelling/s:
  - ➔ those who had recently sold property/s
  - ➔ those either clearly considering or intending in the immediate future to sell
  - ➔ those who intended to sell in the longer term, as part of a planned long term strategy
  - ➔ those not intending to sell in the immediate or near future, but who had considered the factors or circumstances that might lead them to sell
  - ➔ those with no intention of selling a property at this stage.
- critical decision factors varied accordingly, but age and personal circumstances appeared to be the dominant considerations
- market conditions again less significant than expected?

# Potential explanations for understanding investors

- The picture of the sophisticated, well-informed and economically rational investor does not well-describe the norm among rental investors.
- A mix of ‘bounded rationality’ and ‘emotional opportunism’ is perhaps better descriptor of how people approach the housing market as prospective rental investors
- Overall limited research by investors ... but does this matter?
- Successful outcomes from property investment are only partially down to erudite financial decisions; also connected to serendipity and circumstance...but so what?
- Overwhelming ‘sense of success’ in the market is key!

# Potential implications for policy and research

- Investors coming in and out all the time, driven by a mix / array of financial incentives, situational circumstances, market conditions, personal goals and other influences
- They are not driven by economics alone, and so the capacity to shape their behaviour (and investment patterns) on that basis is often limited
- Investors also very clearly not driven by any sense of moral or social imperative to provide housing as a social service
- The ‘amateurism’ of many investors can be both problematic and a positive (in terms of supply)
- When the economics *are* paramount, investors usually have their eye on the long term capital growth picture

# Potential implications for policy and research

- Given investors' gains are mostly held in the long term (theoretical for now), recurrent costs through interest, land taxes etc may present a cash flow problem to investors.
- Negative gearing is not a critical driver for becoming an investor, but it is seen as an important component of the economics of property investment. Hard to remove?
- Aversion to low cost rental housing not necessarily by design – is an effect of housing markets, investor economics, and the broad availability of negative gearing without strings
- Relationship between investment and tenancy law reform continues to prove extremely weak, but don't let that ruin a good story!

# More information



Tim Seelig: [t.seelig@uq.edu.au](mailto:t.seelig@uq.edu.au) ph: 07 3365 1251

Tim Seelig, Terry Burke and Alan Morris (2006), *Motivations of investors in the private rental market*, AHURI Positioning Paper (published on AHURI website)

Tim Seelig, Terry Burke and Simon Pinnegar, with Alice Thompson, Alan Morris and Bill Randolph (forthcoming), *Motivations of investors in the private rental market*, AHURI Final report

“I personally think that the real estate market, whether it’s globally or in a regional sense, is as close to a perfect market as you can get. I mean people are very sensitive to supply and demand issues and the market responds accordingly, and usually responds quickly.”

A leading representative of the real estate industry (2006)