TIMING THE MARKET VS TIME IN THE MARKET

It's time, once again, to let the experts face off and champion their position on a contentious property-related subject. This time around, we're talking long-term strategies and whether you should be clever or just be patient. **ANGELA YOUNG [@DepEdAPI]**

It's another divisive topic, with plenty of experts on both sides.

We're talking about strategically buying at a particular time and moving a property on (again, at the right time) to make a profit, versus the idea that the longer you hold on to a property, the better it will be for you.

We've asked Property Investment Professionals of Australia chairman Ben Kingsley, and researcher and property educator John Lindeman to share their views on which offers the better advantages.

■ FIRST THINGS FIRST, LET'S TALK DEFINITIONS...

JOHN LINDEMAN: "Time in the market" is the term used by exponents of the "buy and hold" strategy. They tell us that we can't accurately predict where or when growth will occur, but it doesn't matter because price rises flow evenly and eventually almost anywhere – if we're patient. The market will perform in future in the same way as it has in the past and prices have always risen over time.

This notion has given rise to theories such as the "housing market cycle" and the "property clock", which not only rely on past performance but also state that prices double every eight years or so.

The facts tell a different story. Since we became a nation 115 years ago, there have only been four times when house prices doubled over eight years. Every other eight-year period has failed to meet this performance benchmark.

Not only have there been lengthy periods with little price growth, but house prices actually fell during the 1930s and failed to rise in the 1950s.

"Time in the market" is a safety-first strategy developed by those who either don't understand how the market works, or choose not to.

You'll hear the theory promoted by project marketers and sellers' agents as their "get out of jail free" card because if prices fall in the areas where they're selling, they can tell you not to worry, housing is a long-term investment.

"Timing the market" is based on the observation that the greatest growth in housing markets has always been achieved in the shortest time.

According to official Australian Bureau of Statistics (ABS) stats, Adelaide's house prices rose by more than 25 per cent in 2002, and Brisbane's shot up by more than 30 per cent the next year.

Not to be outdone, Perth's housing prices doubled in just two years from 2004 to 2006. In the last three years Sydney's house prices have boomed by 50 per cent.

This shows us that the biggest boom markets have not been speculative mining towns or ports, but our biggest cities. Every city has its time in the sun and when one is booming, another may be going backwards. This is why "timing

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the market" by buying where growth is about to occur and selling when it's about to stop is critical. Although booms are sweet, they're also short.

BEN KINGSLEY: Put simply, "time in the market" refers to taking a long-term investment position irrespective of the current market cycle – the investor's confident of the longer-term performance of the location… to deliver them solid to strong capital growth over a period of 15 years or more.

"Timing the market" refers to the investor believing that, based on their research, the market cycle for capital growth is placed at the bottom of the cycle or just starting on the upswing part of the cycle and that acting now will deliver them the solid to strong capital growth over the short term, say 12 to 24 months.

WHICH IS YOUR PREFERRED PERSONAL STRATEGY?

JL: I am at the stage where cash flow is more important than growth, so although I strongly support "timing the market" for investors wishing to grow their equity, for me personally a buy and hold, no-debt, high-cash flow investment portfolio is preferable.

BK: Personally I do try to invest for superior capital growth. I want to enjoy consistent and long-term capital growth because the asset value also plays a role in the rental income I can achieve over the long term. I don't want to invest in a location that my research tells me doesn't have great long-term upside.

I focus on properties that have very strong owner-occupier appeal, because they represent the true demand for an area. It's owner-occupiers and not investors that buy with their hearts, so I'm trying to jump on their coattails as their emotional interest drives the value of property higher in those locations.

I try to tap in to the owner-occupier psychology as this helps me avoid markets that don't pass the lifestyle test.

WHAT DO YOU THINK OF THE METHOD YOU'RE NOT ADVOCATING FOR TODAY?

JL: At some stage, when you've amassed considerable capital by buying, selling and then buying properties again in high price growth areas using a "timing the market" strategy, you'll want to change to a "buy and hold" cash flow "time in the market" strategy.

This is when you gradually swap your portfolio from those with growth potential to those that will assure you of a reliable income stream. In other words, you now use your equity to buy high rent-yield, buy-and-hold properties, which you own without any debt, in strong rental demand areas.

BK: When I'm researching locations, naturally I'm trying to assess where I believe that location is in terms of its market cycle in an attempt to determine the best time to buy.

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The idea that "timing the market" and "time in the market" are somehow mutually exclusive isn't correct. If you can identify an area that you think is about to start (or has just started) its upward cycle, you can sometimes enjoy the best of both worlds.

In my experience, this is what we call buying counter cyclical – you time your buying in quality areas when the overall market might not be performing as well at that time.

A good example of this is when a capital city's economy is a bit sluggish and the overall market sentiment and confidence is down, resulting in less buyer competition (buying at the bottom).

Yet, overall, the location has demonstrated consistent and long-term growth over the past 20 or 30 years.

IS YOUR PREFERRED STRATEGY SOMETHING THAT CAN WORK FOR ALL KINDS OF INVESTORS?

JL: The secret to a successful investment journey is to start from a high debt position and end with no debt at all.

"Timing the market" is more suited to this early stage, when you need to leverage your equity from high short-term growth.

BK: My theory of the perfect capital growth location and property that delivers decade after decade does have its limitations, because some of these locations are now priced out of the range of everyday mum-and-dad investors.

Higher end properties, which have amazing scarcity and owner-occupier appeal, are true diamonds but, like rare diamonds, not all of us can obtain them.

That said, there are secondary locations destined to join the elite locations over the decades to come that do offer more astute investors the opportunity to "play the long game".

WHAT METHODS OF INVESTING/ TYPES OF PROPERTIES DOES THIS CHOSEN STRATEGY BEST SUIT?

JL: "Timing the market" suits investors seeking a rapid increase in their equity, rather than investors who are after cash flow.

If you have just enough money for a deposit, your strategy should be to buy a property that's going to rise in price as quickly as possible, turning the growth in its value into profit (leveraging).

To work for you, the property must substantially grow in price during the time that you own it.

The cost of selling an investment property and then buying another (covering agents' fees, legal costs, inspections and stamp duty) is about 8 per cent of the sale price, so you need to buy in a suburb where the imminent price growth is likely to be much higher than this.

Timing is everything; not just buying, but also selling just before the growth comes to an end.

BK: It all comes down to location selection – no one property in isolation forms a marketplace.

You might buy the very best owner-occupier style property in the area, but without the marketplace of other great properties, your assets aren't going to thrive. That's why the area needs a lot of great properties that have status and appeal.

A rough rule of thumb is the area will deliver 80 per cent of your result and the property will deliver 20 per cent. The only exceptions to this rule are: if you buy into medium- or higher-density, which provides high levels of supply, yet limited owner-occupier appeal (demand) then your property will usually underperform when compared to the investment performance of other properties in that area; if you buy a rare property (say, a period home with high owner-occupier appeal), then the intrinsic value of this type of asset will deliver an outperform result.

Focus on buying "investment-grade" properties with strong owner-occupier appeal and not properties promoted as "investment stock".

HOW HAVE YOU SEEN THE ALTERNATIVE METHOD GO WRONG?

JL: There are countless examples where housing markets have gone nowhere, or even backwards in recent years.

Well-publicised crashes in mining towns such as Moranbah, Emerald, Dysart, and ports such as Port Hedland and Karratha easily demonstrate the futility of the "time in the market" strategy.

This buy-and-hold type of investment has also failed investors at some time in every capital city since 2003.

According to ABS stats, Sydney had no price growth from 2003 to 2013, Hobart none from 2005 to 2009 and Melbourne no growth from 2009 to 2012. Brisbane's housing market has experienced no price growth since 2009, while Adelaide, Perth and Darwin housing prices have gone backwards in the last six years.

BK: I've seen a lot of "hot-spotting" and timing the market prediction calls in my 20-plus years of researching and investing and in most cases these timing call predictions have been wrong far more often than right.

I'd also put my hand up to say that my own research over the journey hasn't yielded me with a perfect scorecard either, but as a true investor I'm all about investing and not speculating.

I'd much prefer to spend my money in areas and on properties that have great fundamentals and have stood the test of time and continue to deliver real dollar growth year on year, than to speculate on the next "hot spot".

It's pretty easy to do some simple and quick research to determine the real risk of oversupply or lack of true underlying demand from buyers.

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The classic example of this is any mining town story.

When the boom is on and demand is strong, you would think this is the easiest way to make money out of property with crazy growth percentages and rental incomes to die for.

Yet when the bust appears, the bottom falls out of the market since the true test and ultimate value of this marketplace is what an owner-occupier is willing to pay, once the circus leaves town.

SUMMING UP...

JL: The Tax Office tells us that three quarters of all housing investors lose money each year, yet if the "time in the market" strategy is correct and prices rise consistently over time, they should be making, not losing money.

This shows us that many investors discover to their cost that housing prices do not rise evenly and sufficiently in the future, no matter where and when they buy a property.

This doesn't mean that we should instead rely on hearsay, gut feeling or speculation but on "timing the market".

The secret to understanding the future of any housing market is that when people move they change the demand and supply of housing and if the changes are large enough they'll result in shortages or surpluses.

Buy in suburbs where the demand from prospective buyers is growing faster than the properties available – that's where prices are likely to rise quickly.

This is why timing, or predicting where and when these changes are likely to occur, is far more profitable than a buy-and-hold approach – or "hold and hope" as I call it.

BK: I think we can take some lessons from observing the world share markets and what some of the world's best investors advocate when they say that it's near impossible to always pick the timing of the bottom of the market.

That's why these great long-term investors concentrate more on investing in great companies with long-term fundamentals and upside, and they care very little about the share market itself.

Wise property investors could take a leaf out of their books and remember to invest in great areas and in high-demand low-supply properties in those areas with a long-term view.

READER Q/A

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