Mary Holm: Low rates no reason to buy property

By Mary Holm
5:00 AM Saturday Feb 20, 2016

Photo / iStock

Q: My query is one you've talked about many times -- investing in property versus shares.

We are mortgage-free and looking at saving more aggressively towards our retirement. We've read your column over the years and have come to realise that property is perhaps a lot more trouble than it's worth, and we like the concept of not having our eggs all in one basket. So we set up a managed fund with the long term in mind, and all is well.

The trouble is that everyone we talk to tells us we are absolutely crazy not to be buying property, with mortgage rates at such a historic low.

We were so sure at first on the managed fund, but now there's all this talk about shares going down (driven by the Chinese economy), and my confidence is wavering. I know it's impossible to know what's around the corner, but any advice would be appreciated.

A: President John Kennedy's father Joseph sold shares shortly before the 1929 sharemarket crash because, "I knew it was time to sell when my shoeshine boy gave me a stock tip." If everyone is making a certain investment -- and suggesting that you do -- it's usually wise not to join them.

I'm not saying property prices, in Auckland or elsewhere, will fall. I wouldn't be surprised if they do, but they might not.

What I am saying is that historically low interest rates -- particularly given they've been low for some time now -- are not a good reason to invest in property.

Sure, the low rates have made property investment more attractive. But that, along with high immigration and other factors, have contributed to growing demand for property and hence rising prices. If you buy property now, the advantage of low interest will be offset by higher entry prices than would otherwise be the case -- even outside Auckland.

Furthermore, the fact that interest is at historical lows suggests that rates are more likely to rise than fall in the medium term. That will inevitably lead to financially stretched people selling properties, which will soften prices.

Counting on a decent gain if you buy property now feels pretty risky to me.

Mind you, investing in a share fund -- assuming your fund mainly holds shares -- is risky too. Who knows where the current market wobbles will lead us?

But you said you've made your investment "with the long term in mind". That means holding your course when the seas look choppy.

To quote another American, hugely successful share investor Warren Buffett, "Unless you can watch your stock holding decline by 50 per cent without becoming panic-stricken you should not be in the stock market."

Do you pass that test?

If so, hang in there. If you're making regular contributions and the markets slump, you'll benefit from buying at low prices. And the markets always rise again. Also, as you say, a share fund is less hassle than property and gives you diversification from your home.

But if you don't pass the Warren Buffett test, I suggest you move not into property but into a lower-risk managed fund -- perhaps one that holds lots of high-quality bonds as well as some shares. It will probably grow less in the long run but give you a smoother ride.