LOOKING CLOSER AT POSITIVE VERSUS NEGATIVE GEARING

When investing in property it is always important to ensure that the decision is aligned with your long-term wealth creation goals.

So when investing, you need to ensure that the property to be purchased is supported with sound market research to gain confidence for it to deliver financial returns over the investment period. It is also important to determine the gearing strategy that matches your goals.

Adopting either a positive geared or negative geared strategy depends on the remaining monthly cashflow available from owning the property.

Each strategy can be calculated by deducting the following costs from the monthly rental:

- loan repayments
- management fees
- strata fees
- council and water rates
- insurance, and
- repairs

with the resulting cashflow being either positive or negative.

***If it is positive,* the surplus can be utilised to either:**

- fund your lifestyle
- pay down your home loan
- pay down the investment debt or
- invest in further property.

***If it is negative,* then you will be required to utilise other income or assets to fund this shortfall.**

While there are a number of different factors influencing the gearing strategy to be adopted, you should also consider the positives and negatives of each strategy to ensure that it fits within your long term wealth creation goals.

Negative gearing

Pros

- The shortfall may be claimed as a tax deduction, with the associated tax saving or refund from the ATO part funding the shortfall.
- Potentially a lower deposit is required allowing you to enter the property market sooner.

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- Given you're largely investing for capital gains that generate equity, future gains may be used as security for additional property purchases.

Cons

- A longer-term investment horizon is generally required as the strategy is more dependent on capital gains from positive movements in property prices.
- What happens if your other income sources are reduced or lost? You may no longer be able to fund the property shortfall and then default on your loan.

Positive gearing

Pros

- Immediately following your purchase, you are receiving a financial return.
- You are less reliant on capital growth to receive a financial return.
- Provides a passive income stream.

Cons

- It's easier to achieve positive gearing with lower gearing, however this usually requires a larger deposit. This could potentially delay your entry into the property market and forego capital gains during this savings period.
- Increases your tax liability but this is not necessarily a bad thing because this means you are earning more!
- Generally, locations that deliver a higher income yield come at the cost of lower capital gains in the long term.