Property or money market: Which is the better investment?

By Adrian Goslett

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For some time now, house prices have grown at a rate slightly below inflation. This continued house price decline in real terms has caused investors to take stock of their options. Real estate is, and always will be, one of the highest yielding long-term investments. However, if undertaken as a short-term investment, you might as well roll a dice and hope for the best.

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It is possible to make a profit off the sale of a property in the short-term, but this is dependent on market fluctuations and other factors that are out of your control. But, if you look at the statistics on house price growth over time, you will notice that, in virtually every instance, the homeowner will stand to make a substantial profit off the sale of their property if they choose to sell after at around the ten year mark or later. This is because the ebbs and flows of the market even out over time to yield a more stable and substantial return.

Significantly lower ROI in money market

When weighing up investment options, investors should consider the returns of other reliable asset classes – money markets, for example – to the resale value of real estate over a ten-year period rather than over a five-year period or less. When you do these calculations, you will discover that if you were to make a lump sum investment into a money market and leave it to earn interest for ten years, your return on investment will be significantly lower than if you were to purchase a property for that same lump sum amount and sell in ten years' time. For example, according to Lightstone Property statistics, a R1.6m property purchased as a primary residence in Claremont in 2010 is now worth R3.5m. By comparison, if you had invested the R1.6m into a money market at a 10% interest rate for ten years, the value of the fund would amount to R3.38m after tax.

However, while these amounts are similar, in the investment scenario, you would still need to pay rent over this period, but in the property scenario, you would not. Assuming a 9% annual escalation in rent for a property of the same value, you would have paid roughly R1.4m in rent over ten years. This leaves you with a net return of R1.9m on your investment, which is a R32,000 profit on the original R1.6m. If you compare this to your house, which is worth R3.5m and will earn you a

R1.9m profit, it becomes clear which is the better long-term investment option.

Monthly contribution scenario

Even if you did not have a lump sum amount available and chose to make a monthly contribution towards an investment fund instead of making monthly repayments on a home loan, the accumulated value on the investment fund in ten years' time will still not match the return generated from the sale of the bonded property. Using the above scenario, if you were to sell the R1.6m property ten years into the home loan, you would generate roughly R2.3m profit after subtracting the R1.17m that was still owing. For the same amount you were paying in instalments on your bond (roughly R15,500 p/m), you could have continued to rent and invest whatever was left over into a money market instead. In this scenario, you would only generate roughly a R850,000 net return by the end of a ten-year period compared to the R2.3m profit you could have earned if you had invested in property instead.

In summary, the notion that property is an unstable investment is simply unsound. As the above scenarios prove, property does still generate the highest returns when viewed as a long-term investment. The bottom line is that it depends on your personal needs and situation. If you're looking at a return over the short term or you need to rent to build up some capital, a fiscal investment may be the better bet for you. But, over the medium to long term, a sound investment in property will likely yield you far better returns.

ABOUT ADRIAN GOSLETT

Adrian Goslett is CEO and regional director of RE/MAX Southern Africa. He joined RE/MAX Southern Africa in 2005 as a franchise development consultant, supporting various regions and offices. Throughout his career at RE/MAX he has held various positions. In 2010, after successfully leading 160 offices and over 1500 agents in six countries through the worst years real estate has ever seen in South Africa in 30 years, Goslett was appointed as CEO of RE/MAX Southern Africa.

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