PropertyInvesting.com Reload original page

Home

PropertyInvesting.com 'Insider'

Discover proven tips, strategies and techniques to dramatically increase your property investing profits

Issue 8, Volume 6 - October 2007

By Steve McKnight

11:25am, Wednesday 31th October 2007

Hi,

Can you believe it? There are only 55 more sleeps until Christmas!

Okay, now that the friendly Santa reminder is behind us, I'm touching base with you today to have a quick chat about interest rates. There's quite a lot happening on world financial markets that savvy property investors need to know about.

In a nutshell, events are conspiring that cause me to be absolutely convinced...

...that interest rates are on target to crash through 10%, thereby triggering a massive credit squeeze!

No, this is not alarmist nonsense. Give me a few minutes of your time and I'll explain why 10%+ interest rates are as good as certain.

It's not all bad news though. The pending economic correction will create a buyer's market for property, the likes of which we haven't seen for over 16 years.

With this in mind, be sure to read on as I've given you three critical points that I recommend you immediately implement to ensure you're not wiped out, but rather well positioned to profit in the months ahead. Let's get started.

WARNING: US Recession On the Cards!

Don't believe the spin. Things are far from rosy for the US economy. In fact, many well credentialed independent economic observers are predicting a substantial recession. And I'm here to tell you that if the US economy gets the sniffles, then world financial markets will catch a nasty cold.

Think about this. The US Congressional Budget Office currently estimates their YEARLY spending on the Iraq and Afghanistan conflicts totals $132,000,000,000 (that's 132 billion dollars). Surely that's an amount that would make even Bill Gates blush!

Where's all this money coming from? The answer is debt, debt and more debt! In fact, the US government is so desperate for money that they're borrowing from China, Russia... even Mexico.

Of course, countries aren't charities and they don't lend interest-free, and given the increasing debt burden and massive budget deficits, currency experts are now starting to question the true worth of the once all mighty US dollar, especially as the domestic US economy suffers reflux as it chews through their sub-prime housing problems.

The response from the US Fed is to keep dropping their cash lending rate in the hope that lower interest rates entice consumers to borrow more, and then use that money to keep spending so that their economy grows rather than stalls.

Rates Set To Rocket Up!

Hopefully you're still with me, as I'm about to tie it all together and explain how a higher Aussie dollar will naturally and surely cause our home loan interest rates to keep rising.

Consider this. You're an investor with the following two investment options:

A. You can buy US government bonds and get 4.75% return. Remember that the greenback is presently weighed down with massive debt and is looking pretty ordinary by even the most optimistic observers.

OR

B. You can buy Aussie bonds and receive a 6.75% return. Remember, the Aussie economy is backed by a resources boom and forward orders for metals and resources which we simply can't meet due to antiquated infrastructure.

Unless you've got rocks in your head, you'd buy Aussie bonds because the return is higher and the underlying investment more reliable. And that's exactly what foreign investors are doing. For instance, a current popular FX trade that high rollers are using is to borrow money in Asia at low interest rates (say 1%) and convert that borrowed money into Aussie dollars to buy Aussie bonds paying 6.75% interest, thereby making (hopefully) enough of a margin to bank a nice profit.

Clearly, this is a strategy that only professionals should try since there's more risk in what I've described above than driving down a major freeway at top speed with your eyes shut.

The essential message is this - the more the US dollar drops, the better the Aussie currency looks, both in terms of return and reliability. And as investors convert their foreign pounds, pence and pesos to buy Aussie dollars, buyer demand will keep putting upwards pressure on the value of our currency.

On the plus side, a trip to Disneyland hasn't been as financially attractive on the currency exchange since the mid 1980's. On the downside, as our dollar heads into territory not seen in two generations, we're more likely to buy cheap imports and blow out our own trading account as exports become more expensive and less competitive on world markets. That is, our spending on purchases will go up, but our income from export sales down.

It's a little cruel that the US is trying to stimulate their economy at the exact same moment the RBA is trying to cool ours. But cool it they must if they want to keep inflation in check.

Conservative channels like the ANZ Bank have published the following glib forecast:

> "It now looks as though the Reserve Bank has considerably more work to do in order to dampen medium-term inflationary pressures. We now expect three more 25bp rate hikes in the current tightening cycle - once in November and two more in the first half of 2008."

If this happens then home loan interest rates are at 9% before the end of March next year.

Except for pork barrelling, there may be a glimmer of hope that the RBA could steer us into safe fiscal territory. Sadly though, it seems that dumb and dumber is the name of the election game since each party seems hell bent on trying to out do each other in the amount of money they're promising to put in the hands of consumers to spend.

Here's the newsflash... tax cuts win elections, but our country desperately needs money spent on infrastructure, not iPods!

Sadly, no one seems to be listening, so what the tax man giveth in the way of tax cuts, the RBA will surely taketh away through higher interest rates.

We're Trapped In a Gloom Cycle!

I'm sorry to have to tell you that we're trapped in the beginnings of a gloom cycle. Last year I was almost laughed out of town when I predicted interest rates would be a percent higher within 12 months. Sadly, I've been proven right.

Now, I'm updating my forecast to conclude that - unless there is a substantial shift in economic policy and a marked move towards good governance - Aussie interest rates will be at, or slightly above, 10% on or before the 30th June 2009. And this is regardless of who wins the election.

Pushing political spin to one side, the truth is we're heavily in debt (just like the US), but it's businesses and consumers (rather than the government) who are to blame. Home prices are, frankly, at ridiculous levels. The 1 in 100 year drought is pushing up the price of food, oil prices have never been higher, and both sides of government are handing out billion dollar election promises like candy.

It's all spend, spend, spend... and this will only result in inflation. In response, the RBA has no option but to keep bumping up interest rates in the hope that, sooner or later, people put away their credit cards.

Your Homework - Here's What To Do...

First of all, don't waste your time, or breath, trying to change the system.

Federal Treasurer Peter Costello was right last week when he said "I don't believe the business cycle is defeated. At some point the business cycle will turn down. No doubts about it."

Hallelujah! That's the most honest statement I think I've ever heard out of the mouth of a politician!

Accepting financial markets for what they are is essential in deciding how to position yourself to capitalise on cyclical changes. It seems we're now at the dusk of the easy money phase, so I suggest you ready the heavily sails in preparation for choppier financial seas.

Specifically, here are three absolutely essential things that I've recommended my closest family and friends do as soon as possible:

1. Exit Marginal Property Deals While You Can

Honestly, a property deal that's floundering in the current climate is going to be a bigger dud as interest rates rise and the real estate values soften. I'm telling friends and family to bite the bullet - sell while you can and live to fight another day.

2. It's Time To Get Educated

The next market correction will trigger the biggest redistribution of wealth in two decades.

As interest rates continue to climb, we will enter a true buyer's market where those who know what, where, when and how to buy will make more money in five years than others will in several lifetimes.

Of course, just like the good times don't last forever, neither do the bad times either. For instance, when the currency correction happened in Asia in the early 1990's, people who snagged good quality property for cents in the dollar came out the other side with literally millons of dollars in easy equity. On the other hand, people forced to sell will lose a lifetime of wealth in seconds.

The writing is on the economic wall. If you don't know how to read it then get educated fast.

3. Prepare And Be Patient

I'm no Chicken Little. I'm simply letting you know what I'm doing.

At the moment I'm sitting on a pile of cash and waiting patiently for the financial sun to set. In the meantime I'm cherry-picking great property deals as I see them, but I'm not risking the bank on a speculative project that will flop when money dries up and banks stop lending as freely.

Already I notice that many financiers have tightened their lending policy on building projects - down to 65% LVRs. This is the first of many similar moves.

Super Deal - If You're Quick...

Changing to happier topics for a minute, did you see Elise Jackson featured on Hot Property recently? Of course, Elise was a R.E.S.U.L.T.S. Mentoring Coach, and together with her husband to be Dean, have been busy renovating and developing property. They're A-Grade quality people who have worked hard and deserve all their tremendous success.

You may be aware that Dean and Elise have published an excellent product called Renovation Toolbox, which is currently available for sale at PropertyInvesting.com. (see http://www.propertyinvesting.com/go/215).

Renovation Toolbox comprises Dean and Elise's complete system for doing successful and profitable renovations from start to finish. It is the most comprehensive, logical and sensible product of its type I've come across, which is why I'm happy to sell it on the website. In short, if you are interested in renovating then this is a must-have resource. You'd be mad to try renovating without it.

Renovation Toolbox is currently selling for $495. And I'm here to tell you it's worth every cent and more.

However, for the remainder of this week ONLY, Dean and Elise have agreed to cut the price by a very generous $100 as a goodwill gesture in the hope that investors who need help to start, push through or finish reno projects can do so profitably and before the economic climate turns.

Make sure you get in quick though, the offer is only available for the first 50 buyers. Head to http://www.propertyinvesting.com/go/215 for more information.

Final Thoughts

In what may be his last month as Treasurer, I thought we'd end with a timely quote from Peter Costello as it ties up our entire discussion well:

> "China is very strong but you can't just grow an economy in double figures on a long-term basis. All flows of capital they have been sending to the US might reverse, and you will get a major realignment on major currency markets. That will be a wild ride when that happens (as it) will set off a huge tsunami that will go through world financial markets."

Indeed Mr Costello. We've all been warned. The question is... who will take notice?

Until next time, remember that success comes from doing things differently.

Warm regards,

Steve McKnight

P.S. Don't forget to check out the $100 off special on Renovation Toolbox. It is only available THIS WEEK, so get in quick. Find out more at: http://www.propertyinvesting.com/go/215