Can you run a business inside your SMSF? **Monica Rule** lays down the law in **WEALTH on TUESDAY**

Richard Hemming tells us what to look for as small caps reporting season takes off in **WEALTH on TUESDAY**

Dangers lurking in the bank of mum and dad

A parental guarantee is one way to get in the market but it comes with its own set of risks

JAMES GERRARD
PROPERTY

Average house prices in Australia fell by 0.5 per cent in the December quarter with Sydney suffering the largest decline of 3.1 per cent. So what does this mean for parents who have, or are thinking about guaranteeing their children's home loans?

With a peaking property market and deteriorating housing affordability, Ramon Mitchell, Director of Acquisitions at Performance Property Advisory, has noticed an increasing trend of parents helping their children enter the property market via family guarantees. "We're particularly noticing an increase in younger, first-home buyers who are making the most of this to get on to the increasingly difficult to reach first rung of the property ladder" says Mitchell.

Under normal lending circumstances, where a borrower does not have enough savings to meet a 20 per cent deposit plus stamp duty, the bank will either decline the loan or impose Lenders Mortgage Insurance, which can cost thousands of dollars. Sydney mortgage broker Elaine Lam explains "a family guarantee can be a useful tool that allows borrowers to finance property with little or no deposit, where their parents are willing to assist by providing a limited security guarantee secured against their home, an investment property or another financial assets such as a term deposit".

But the procedure can be a risky strategy as it allows borrowers to buy property with no cash and no evidence of genuine savings, as long as the bank is satisfied the borrower can meet the ongoing loan repayments, says Lam. In the event the borrower defaults on the loan, the bank will come after the parents for any losses and costs that the bank incurs.

The benefit of a family guarantee lie solely with the borrower, not the guarantor, says Joseph Alam, head of retail business at finance broker Lendfin. "It can take upwards of 10 years to save for a deposit in some areas of Australia and during this time the property market is likely to have lifted substantially, meaning the borrower keeps chasing ever shifting goalposts".

DANIEL WILKINS

A parental guarantee can be a risky strategy as it allows borrowers to buy property with no cash and no evidence of genuine savings

Mitchell has also witnessed the use of family guarantees to help children "buy into aspirational suburbs and avoid having to buy at a lower price then sell and upgrade a few years later, triggering a round of real estate agent fees, stamp duty and legal costs".

Sydney couple Daniel and Alyssa James recently bought a house-and-land package in Sydney's northwest with the help of a family guarantee from Alyssa's parent. The couple noted that "the family guarantee meant that we could upgrade homes sooner and allow us to be closer to Sydney then we currently are".

For parents who already have a guarantee in place, Alam suggests a few pointers:

- The property is revalued every two years. If there is enough equity, the bank will release the parents from any liability of the original loan.
- If there isn't enough equity to release the parents, Alam advises the parents and children have a frank talk on how long the guarantee is to remain in place and agree on an increased loan repayment schedule so that the children can reduce the debt to the point where the parents can exit the guarantee arrangement with the bank.
- For parents looking to provide a family guarantee to their children for a property purchase, Lam advises that each party understand their obligations under the contract, and in particular, the parents should seek legal advice on the repercussions if the children's marriage dissolves.

North Shore Property Sales principal Trevor Chan recommends "that an agreement should be drawn up between the parents and children to handle any potential situations that could arise in the future to avoid future disputes". Alam of Lendfin adds that "parents should speak with their children about the large responsibilities involved and ask how stable their employment situation is."

Not all banks allow parental guarantees, while others have strict rules. Lam recommends that prospective borrowers thinking about a family guarantee first seek advice from a mortgage broker to find out their options and then discuss the potential scenarios with their parents.

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Energy market fears feed into bonds, equities

STIRLING LARKIN
GLOBAL INVESTOR

ment, as after all, it is typically the role of equity not bond markets to separate the wheat from the chaff.

Also remembering that fixed-income investments are traditionally seen as a shelter during volatile times, it has become unsettling to many to now accept that this asset class, in particular, is the actual eye of the global storm.

As the graph highlights, the

Colour of money: blue chips end in the red

ROGER MONTGOMERY

May I suggest that conventional or traditional blue-chip companies — those big stalwarts that have been around forever and are believed to have reliable dividends — aren't blue-chip companies at all.

Your goal as an investor should simply be to purchase, at a rational price, a part interest in an easily understandable business where crease in value. Think of a special bank account with $10 million deposited and ready to earn its owner 20 per cent per annum in interest forever.

Assume this obviously special bank account retains all of its interest and is allowed to compound for a decade or more.

If we auctioned it today, I suspect that 20 per cent interest 10 years, it may still trade for quadruple the amount deposited ($240m) and the buyer who paid $40m would be satisfied with their return.

We can replace the bank account analogy with a company and by renaming the money in the account "equity" and the interest rate "return on equity" we have the ingredients for a true blue-