

## Strata: Capital Works and Value

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We are sometimes asked about the affect of borrowing by the strata corporation on the value of units.

We'll try and keep things simple! Of course, in the context of this answer we can't say anything about the demographic or economic factors that play a role in the value of your unit.

First, let's consider a slightly different question: Why do capital work on a strata property?

There are two reasons: First, because you have to. You need to comply with specific matter such as a fire order or you need to comply with the general requirement of strata legislation that you must maintain the common property.

The second reason is: Because you want to. You believe your property will be improved, your lifestyle enhanced and your investment increased if you do certain works.

Both of these have a value component. The works you do should either increase the value of your unit or restore it to the value that it had.

Presumably, you wouldn't do the work unless the increase in value you expect exceeds the cost of the work.

This brings us to an important point: How do you measure value? It's easy to be confused by the dollars, but the real way to measure it is be Return On Investment. This is a percentage. If you invest a dollar in your property, what percentage return will you get?

Now let's talk about funding.

When you're considering the ROI you get from the capital works, the important thing is to take this after you've factored in the cost of funds. If your "pre-funding" return is 5%, but your cost of funds 10%, then your real return is loss of 5% and you wouldn't do the work.

Lannock's experience is that, most of the time, for most strata properties and most strata unit owners, borrowing by the corporation is the cheapest form of funding. If borrowing is cheapest most of the time, then it follows that in most cases, your return will be greater if the corporation borrows.

Finally, let's consider a practical situation.

If you sell your unit for \$500,000 and you've had a \$10,000 special levy to fund capital works, then your net return is \$490,000.

However, if the corporation has borrowed to fund the capital works, a prospective purchaser is likely to say: "I would have paid \$500,000, but I see that there is a loan in the strata corporation and my notional share is \$10,000, so I'm only going to pay you \$490,000".

Same result, different way of getting there.