

Portfolio

Borrowed funds generate biggest investment gains

People who borrowed to invest in either shares or property a decade ago are wealthier than they would otherwise be, according to a report by the Australian Securities Exchange and asset consultancy Russell.

The report found that those on the top marginal tax rate who borrowed 50 per cent of an investment for shares a decade ago have generated an annual return of 13.9 per cent compared with the annual 10.6 per cent return garnered by those who did not borrow. Residential prop-

erty investors who borrowed gained an annual 12 per cent gain, versus the annual 8.8 per cent gain recorded by ungeared investors.

In calculating the after-tax returns, it was assumed that all loans were interest only and that home loan rates are on average 1 per cent a year lower than margin lending rates for Australian shares. The calculations allowed for the tax deductibility of interest costs.

"The results reflect that the performance of the two asset classes has more than offset the borrowing costs

over the 10 year period," according to the report. Those on the lowest marginal tax rate did even better in both cases. Such an investor would

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have produced an annual 16.2 per cent gain by borrowing 50 per cent of an investment in shares, rather than a 13.2 per cent gain.

A residential property investor on the lowest marginal tax rate would have gained an annual 13.4 per cent from a geared investment, versus 10.6 per cent from an ungeared investor.

The better performance from shares was due to the fact that they provided the best real returns for local investors over the past two decades, according to the report.

It found that Australian shares outperformed all other sectors, delivering the best after-tax and after-cost returns at both the lowest and

highest marginal rates, and also at the superannuation tax rate, across the past 10 and 20 year periods.

"The latest results also reinforce that super remains one of the most tax-effective environments in which to invest, and that super should be considered as an important part of an individual investor's overall investment strategy, alongside their owner-occupied property investment," said the director of investment strategy for Russell Investment Group, Andrew Lill.

Staff reporter