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INSURANCE AND FINANCIAL PRACTITIONERS ASSOCIATION OF SINGAPORE

THE "ABCs" OF FINANCIAL PLANNING FOR PROPERTY PURCHASE

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Buying a property is among the biggest purchases a person may have in their life. It is a big financial commitment that needs careful planning. When buying property, there are many considerations, such as the type of property to purchase, affordability and financing, eligibility, as well as rules and regulations, of which most are often finance-related concerns. As such, it is good for an individual to do some financial planning first, before committing to a property purchase. This article provides some useful takeaways on the "ABC"s of financial planning for a property purchase, so that relevant issues can be considered in the course of taking the first steps towards this direction.

A- Analysis of one's own situation, goals & objectives

Every one of us are unique. We have different situations, concerns, goals, and objectives. Therefore, an analysis is needed to reach the right and optimal outcomes. How important is this? It may be compared to having a doctor check and assess our body to diagnose what's wrong, before prescribing the proper medication to treat the ailment. To further reinforce this, by piecing parts of the jigsaw together, such as one's objectives and financial situation, an analysis would go on to ultimately have the effects of producing a picture of one's vision and desired destination. This is no less different for financial planning in relation to a property purchase. Why? Because, it will give a good insight and understanding of what we have and where we are going, before mapping out the action plan.

Purpose of the purchase - The first thing to consider is the decision of whether to buy the property for one's own usage or for investment. With this objective cleared, one can then proceed to the evaluation of their options and plans before the execution.

If it is for own usage, the considerations that typically come to the forefront are residential properties like public housing (HDB flats), executive condominiums, private condominiums, or landed properties, as well as commercial spaces like factories, offices, shops, for business usage. If it is for investment purpose, the needle doesn't shift much either, as it will be either residential properties, or commercial ones (industrial, office, hotel).

Considerations for the purchase - It needs to be noted, the considerations for the purchase of property for these two purposes will differ. For example, in the case of an investment purpose, is their main objective to derive rental yield or, land a windfall through capital appreciation?

Therefore, depending on what this goal is, the considerations for the choice of properties will then vary too. Concerning time horizon, it may be useful to keep in mind a short term, such as within 5 years, or a mid to longer term (more than 5 years) planning.

This should also include consideration if they are going to upgrade, buy another property or exit as part of a risk management plan (more for investment purpose).

In addition, it will be also good for an individual to be aware and have an understanding of the various rules and regulations as well as eligibility for the different types of property purchases. For this, one can refer to the HDB website[1] and URA website[2] for HDB flats and private residential properties respectively.

For commercial property rules, the URA website[3] can be referred to for more information. This will include details such as guidelines and consideration for the usage of commercial properties, so that one may be sufficiently aware, before committing to a commercial property purchase for investment or own usage.

B- Budgeting

After an analysis of one's financial situation, goals and objectives, which will also uncover and help them understand what they want and what to buy, the next step of the planning will be budgeting. Buying a property is a big and long term financial commitment. The ability to finance the property is very important. It will be good for one to take note of their own asset/liabilities/income/expenses/cashflow and commence with some budgeting for their property purchase.

Two sources of funds - A good start would be to take a look at the amount of CPF savings (for residential properties only, not applicable to use for commercial properties) and cash that they have, and thereafter, plan and do some budgeting.

These two sources of funds can be used for initial down payment for the purchase of properties, the ongoing mortgage repayment, as well as some ongoing and one time cost.

For usage of CPF monies for property purchase, it is important to note that there will be accrued interest incurred and this needs to be paid back to CPF upon the sale of a residential property together with the amount that has been drawn out. This is an important consideration for people who are looking to sell their house and upgrade as this will affect how much cash, they can cash out. There are also other regulations concerning the use of CPF monies. This can be found at the CPF website[4].

C- Credit & Cost

In relation to budgeting, the next thing that one should look at will be the issue of credit and cost. A property purchase is a big financial commitment, hence, one may typically require credit and loan from a financial institution or HDB for the purchase of property.

Before committing to a purchase, it is prudent to find out how much loan can they take. It will be good to apply for a HDB Loan Eligibility (HLE) Letter (for HDB loan) or Approval in Principle (AIP) letter (for other property loan) before starting the property purchase journey.

This will help to minimise the possibility of forfeiting the option fee should the loan get disapproved, as well as minimise concerns during the loan application process due to any credit issue.

Together with budgeting, this will be an important consideration in terms of affordability, as it will help to streamline the choices of property that one can afford and purchase, and that way, help save valuable time too.

Credit - That said, the property chosen, one's income, credit worthiness, debt obligation, financial standing etc are factors affecting the amount of loan that one can take. On this note, it is needful to be aware of the various rules and regulations on the issue of credit.

These include things like mortgage servicing ratio (applies to loans for the purchase of an HDB flat, or an executive condominium where the minimum occupation period has not expired), total debt servicing ratio, loan to valuation (LTV) limit and loan tenure. For more information, you can refer to the MAS website[5] for these rules.

Cost - Apart from credit, cost is also an important aspect in financial planning for a property purchase. There are many different costs associated with it, which are typically classified into two main categories: upfront and ongoing costs. Some of these upfront costs includes stamp duties, conveyancing, valuation fees, commission, renovation (if applicable); while some ongoing costs include maintenance and property taxes.

We can see, from the two categories, it is paramount to consider this cost aspect during the financial planning process for a property purchase.

D- Do wealth protection & risk management

With the decision to commit to a property purchase, the next step to look into are areas such as wealth protection and risk management. For most cases, an individual will take a loan for the purchase of the property, which will necessitate the repayment through a monthly mortgage.

Premature death, disability or disease - As such, it is important to review one's insurance planning to ensure there are sufficient plans put in place for wealth protection, income replacement, debt cancellation or medical expense payment/reimbursement. In the absence of these safety nets, should unforeseen circumstances such as a premature death, disability or disease arise, it is possible they may not be able to financially cope with the continuity of the mortgage repayment. As a result, the financial situation may be negatively or even, severely impacted. To avert such a possibility, a person can consider additional insurance coverage to pay off this outstanding loan for debt cancellation.

External perils - On a separate note, there are risks associated with external perils like theft and fire, which can occur to a property. In this instance, a home insurance (for residential property) and/or a property and casualty insurance (for commercial properties under business) arrangement would be able to reinforce and ring-fence the owners from an array of such losses, accidents, and threats in relation to property and possessions, as well as liability claims from third parties. In many cases, the financial institution offering the loan will have this requirement as part of their loan offer.

CONCLUSION

I hope the “ABC”s pointers above may serve as a useful reference in your financial planning for a property purchase. However, it needs to be highlighted that there are more aspects and details concerning this subject matter, which are beyond the scope of this article. Every individual and their situation is unique, hence it will be good to enlist the expertise of a trusted and competent financial practitioner as well as a real estate practitioner. This is so that they can help navigate through the details of such planning and that way, ensure no stones are left unturned for something as paramount as the purchase of a property. With this, I wish you every success in your endeavours, be it for the pursuit of your ideal and personal accommodation, or for a property which gives you good returns for investment.

ABOUT THE AUTHOR

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Notes:

1. https://services2.hdb.gov.sg/webapp/BP13EligCheck/BP13SHome?strSystem=CHECK
2. https://www.ura.gov.sg/Corporate
3. https://www.ura.gov.sg/Corporate/Property/Business
4. https://www.cpf.gov.sg/member/home-ownership/using-your-cpf-to-buy-a-home
5. https://www.mas.gov.sg/regulation/explainers/new-housing-loans

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