Choosing a path: Invest in Stocks or Property?

Should I put my hard-earned savings into owning a piece of multiple companies at once? Or channel them into bricks and mortar? Both have their attractions, and understanding which combination will work for you is key.

In all honesty, most of us probably decide which route to take based on hearing successful decisions others have made, and what feels comfortable to us. So which way should you choose?

Directly comparing these two investment choices is almost like comparing apples and oranges. When you decide to go with an investment property, you're usually purchasing a single asset. The equivalent with shares would be purchasing shares in a single company, which is not something most people would do.

When investing in shares, we generally build a portfolio that comprises of different companies doing different things and at different stages in their business. This diversification means that share investments can hold considerably less risk than a single property investment. Why? When we talk about risk, most people generally assume this as a negative. A better way to think about "risk" in this context is what are the potential outcomes?

For a single property, the upside could include, gentrification, rezoning or even long-term low interest rates which inflate prices, resulting in substantial upside capital return. On the other hand, you may be unable to lease the property, constant property maintenance issues, rising interest rates or even rotten neighbours moving in next door. This broad range of influences, arguably means a single investment property is considered a "high risk" investment.

On top of this you most certainly borrowed (leveraged) to undertake the investment. Leverage magnifies an outcome, so when things go well, leveraging will amplify the positive, but by the same token, when things go wrong, leveraging can amplify the negative.

Share investors will typically invest in a portfolio that is made up of a range of different companies that are likely at different stages in their business, and service different needs. Some may be experiencing fantastic growth, some maybe mature and some inevitably will not be doing as well. It is this mixture and offsetting of winners and losers that reduces the range of potential outcomes in a share portfolio. Therefore, making this arguably a lower risk investment versus a single investment property.

Rather than focusing on which will give you a better outcome, a better approach would be to consider which option suits your circumstances.

If you're a tradie or an aficionado of property markets, property may be a better option as you can add value by using your skills and knowledge, albeit at the expense of your time. Property is also easier to leverage, so if you have a secure income, and are willing to tolerate higher risk for higher potential return, there are ways to use leverage to your advantage.

Building a share portfolio however might suit someone with less certainty in their income or future plans. This is because you don't need to borrow (leverage), there are lower barriers to get started, and there is also a higher level of flexibility. The flexibility comes from having the option to add as little or as much funds as you please, and if things do get challenging, shares can be sold down to cash quickly.

Ask yourself;

- Do you have a long-term outlook?
- Do you want to diversify your investments?
- Can you tolerate low liquidity, or do you require high liquidity?
- Are you comfortable with the value of your investments changing daily?
- How much do you have to invest?
- Are you prepared to pay upfront and ongoing costs of owning property and do you have time for regular management?
- Do you have a steady income or reserve funds if you are unable to rent your investment property?

Ultimately, you will need to consider the strategy that works best for your circumstances. Maybe shares, maybe property or maybe both. It's not a binary decision and many investors own both at some stage in their journey. Many investors find success with mixing and matching as their circumstance allow (diversifying). You could start with shares to build a solid financial foundation and then venture into direct property once you've gained confidence and financial stability.

There are alternative ways to invest in real estate. These alternatives can provide diversification without the commitment and responsibilities of directly owning property, albeit at the expense of agency.

Below is a continuum on the different property investing options by level of personal involvement and responsibility.

Source: Morningstar.

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