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How to put property back in your portfolio

Identifying hot spots will be key for investors keen to return to the housing market, writes **Mark Channing**

BRYAN MEADE

Harencyk decided it didn't make sense to rent any more and, with his wife Anna, paid €220,000 for a three-bedroom mid-terrace house in north Dublin with a first-time mortgage from Permanent TSB

IRELAND has some of the world's best-value property, according to the Organisation for Economic Co-operation and Development (OECD) — yet soaring house prices have led to fears of a growing bubble in Dublin.

The OECD compared house prices with rents and wages and concluded that Ireland, alongside Germany, Greece, Portugal and Japan ,offered the best value. It added the Irish market had "bottomed out".

It is difficult to see value in some sectors, with a chronic shortage of supply causing house prices in Dublin to rise by €5,000 a month, according to estate agency Douglas Newman Good.

The Central Statistics Office (CSO) said last week that prices increased by 8.5% nationally in the past year, and were up 17.7% in Dublin.

With property again a hot topic, we look at how investors can cash in.

OUTLOOK

A two-speed market has developed here, with prices rising in areas where demand outstrips supply and stagnating elsewhere. Outside of Dublin, prices rose by just 1.3% in the past year, according to the CSO.

Experts say a lack of supply means the trend of rising prices in the capital is set to continue. Ronan Lyons, an economist with property website daft.ie, said: "It's difficult to see prices doing anything other than rise over the next five years in Dublin."

Prices are also expected to rise elsewhere, but unevenly. "Prices for the rest of Ireland are likely to rise at about the same rate as inflation, but property in the commuter counties such as Louth and Wicklow will probably rise faster," said Lyons

Carol Tallon, the author of the Irish Property Buyers' Handbook, believes that rental returns will be higher outside Dublin due to "low buy-in costs, higher rental yields and the chance for capital appreciations".

Commercial property is also tipped by many to do well, with commercial property agency CBRE saying 2014 will see "the return of the crane to the Dublin landscape".

SHOULD I INVEST?

Sarah Lord of Killik Chartered Financial Planners in London said there were a number of factors to consider before making a property investment.

"If the property is to be purchased as a home rather than an investment, it is a relatively simple decision," she said. "If the property is to be bought as an investment, such as a buy-to-let, other considerations apply. You must do the sums on whether the purchase is affordable, not just at the point of acquisition but on an ongoing basis."

Investors should look for income rather than capital gains, especially if relying on debt to finance the transaction. "Property would typically yield 5% or 6% gross," said Lyons. "If you're borrowing at 6% to get a 6% yield, that is a play on capital gains."

Unless you invest in a property fund or another tradable property investment, buying property requires effort and judgment.

Douglas McNeill, investment director with Charles Stanley Financial Solutions, said: "In property the best returns go to those who understand situations better than others. That could mean spotting a neighbourhood that's up and coming, or a scruffy property that would fetch a good price if it were nicely done up."

HOW TO INVEST

Property funds

Savers looking for a property investment do not have to buy a property and let it — they can buy units in a fund that invests in property.

David Quinn, the managing director of Investwise, a fee-based adviser in Dublin, said: "Property funds with a big diversified portfolio are the right way to invest in property. It is a much better option than a single buy-to-let where you're committing to one single location and asset."

He added: "You pay your annual management fee but you don't have legal fees, maintenance fees, advertising fees and all that goes with trying to find a tenant for a buy-to-let property."

Life companies such as Friends First, Standard Life, Irish Life and Aviva have a range of property funds open to retail investors. Gains are subject to an exit tax of 41%.

Goodbody has raised funds for IPUT, a property unit trust fund which owns property mainly in Dublin 2 and 4. The money was raised from high net worth clients, and minimum investment is €100,000. IPUT yielded an income return of 7.36% last year, making it an attractive component of a balanced pension fund.

According to Quinn, the current investor demand for property funds is "ferocious".

Reits

Another option is to buy shares in a real estate investment trust (Reit). A Reit is a public listed company which has as its main activity the ownership and management of property-related assets. Reits are relatively new to the investment landscape in Ireland. Green Reit and Hibernia Reit became the first domestic Reits to float on the Irish stock market last year. Both focus on commercial property. Goodbody Stockbrokers has "buy" recommendations on each.

In April, Irish Residential Properties Reit, which as its name suggests focuses on residential property, became Ireland's third domestic Reit. While Green is trading at a premium of 27% to its flotation price, Hibernia and IRP are just 3% and 1% ahead.

Buying shares in a Reit carries many of the same advantages as buying units in a property fund.

Jim Clery, the head of real estate with accountants KPMG, said: "For a small investment you get an opportunity to access the performance of very big assets, very professionally managed and very big tenants."

Unlike buying units in a fund, where you invest directly with the fund company, you will need to go through a stockbroker to buy shares in a Reit. "You pay 1% stamp duty when buying or selling shares in Reits. Irish resident investors are liable to capital gains tax of 33% on any gain in the value on their investment," said Clery.

You can offset losses incurred on selling other assets against gains made on Reits for tax purposes, while losses on Reits can be used to reduce taxable gains on other assets. This facility is not available for gains and losses on property funds.

According to City Life Wealth Advisors there has been a surge in interest from clients looking to invest in Reits.

BUY TO LET

Buying a property and letting it typically requires more money — and, potentially, time and skill — than simply investing in a fund or buying shares in a Reit.

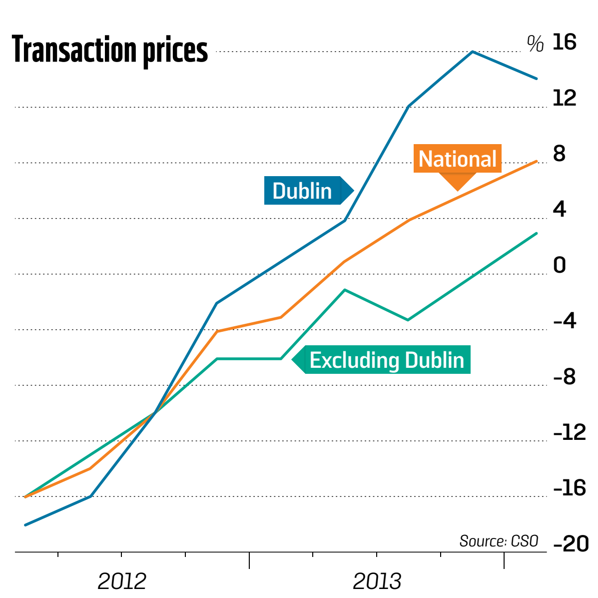
Investors who do not have the cash to buy a property outright can use a buy-to-let mortgage, which can substantially increase the returns on the amount you put down. However, it also increases risk.

According to Tallon, all eight main lenders offer buy-to-let mortgages. "I haven't seen any investors get more than 75% loan-to-value (LTV). Most of them are getting about 60% LTV but there is finance available," she said.

Permanent TSB launched new mortgages for buy-to-let investors last year, charging 5.25% for mortgages of less than 50% LTV.

Apart from mortgage costs, there will be purchase costs including survey fees, legal costs and stamp duty. You will also be taxed on rental income which could be up to 52% after universal social charge and pay-related social insurance. Only 75% of interest on buy-to-let mortgages can be claimed as a tax deduction. To get out of the investment there will, again, be legal costs and estate agent fees.

According to the latest rental report from daft.ie, the current rental market for Irish property is robust, with rents rising in every county except those in Connacht and Ulster. The biggest rises are in Dublin, where annual rents are up 14%.



First-time buyers make their move

AFTER months of house hunting, the wait is finally over for first-time buyers Lukasz Harencyk and his wife Anna. Originally from Poland, the couple have just received the keys to their newly bought three-bedroom mid-terrace house in Clongriffin, north Dublin. They paid €220,000 for the house that they financed with a first-time buyer mortgage from Permanent TSB.

"We have been renting for the past few years but financially it just didn't make sense any more. Our monthly mortgage repayment will be less than what we were paying in rent," said Harencyk.

The couple had considered buying an apartment but ended up buying a house as it was better value. The house they bought is a new build and was the last to be sold in the development. They only secured the property as a result of a cancellation. "We were very lucky. Someone else had gone sale agreed but had to cancel because their mortgage was refused," said Harencyk.

He believes that house prices in Dublin are going to continue to rise. Houses in Clongriffin are selling for €20,000 more than they were a few months ago.

"People are not afraid any more and banks are keen to give money to first-time buyers. The only way to get out of paying high rents is to get a mortgage so I think prices will keep going up," he said.

Harencyk believes property is a good investment for both owner-occupiers and investors. "Property is definitely a good investment if you are going to live in it. At the same time, the interest you get for leaving your money in the bank is getting lower and lower," he said.

The couple have no plans to go back to Poland. "Ireland has been good to us. We see our futures here," he said.

MARK CHANNING

Mandatory schemes still won't fill the gaping pensions gap

COMMENT

NIALL BRADY

Could you get by on €8,500 a year, about half the minimum wage? That is what the average private sector worker can look forward to in retirement, according to the Irish Association of Pension Funds (IAPF). Its figures, published last week, are based on somebody earning €50,000 who joins a typical company pension scheme at 35 and retires 30 years later.

Such puny pensions should dispel any complacency about the adequacy of the defined contribution schemes that 230,000 private-sector workers are relying on to pay for retirement. They should also provide a wake-up call for social protection minister Joan Burton, although the contest for leadership of the Labour party is probably her top priority.

She is a champion of mandatory pensions, forcing all workers to save for retirement so that they have some security for old age. What is the point of being forced to divert €166,500 of your pay into a retirement fund over 30 years, though, if the result is a pension of €8,500?

To be fair, mandatory pensions would force you to start saving as soon as you start working, allowing you more time to build a retirement nest egg. Joining at 25 would yield a pension of €12,150 according to the IAPF's figures — a slight improvement but still not enough for even a subsistence existence.

The numbers do not take account of the bedrock of most people's retirement plans — the state pension of up to €12,000 a year. It could boost the €8,500 pension to €20,500, replacing close to half of a €50,000 salary in retirement. This comes closer to satisfying expectations, although they would invariably have hoped for more.

Banking your future on the state pension would be a mistake, however. It has been untouched through seven austerity budgets since 2008, as politicians ran scared of the power of the "grey" vote, while slashing welfare payments to the unemployed, the disabled and children. Pensioner power cannot defy the reality that the state pension is unsustainable in its current form. Without change, it is projected that by 2066 the state will face a shortfall of €324bn between what it pays in benefits, mainly pensions, and what it collects in pay-related social insurance.

The problems are enormous. Pretending they can be fixed with mandatory pensions is not a solution.

Cry for help

When bankers oppose plans that would boost lending, and therefore profits, it's safe to assume the plans are flawed.

The housing market monitor published by the Irish Banking Federation last week poured cold water on the government's proposals for a mortgage insurance scheme. The idea is to reduce the deposits required for first-time buyers, along the lines of Britain's Help to Buy scheme, easing their entry to the property market. The risk with easier credit is that desperate buyers will use it to drive prices higher, outbidding each other for the meagre stock of properties available for sale.

"The UK's recent experience provides a salutary warning on how not to address problems in the housing market," Conall Mac Coille of stockbroker Davy wrote in the IBF monitor. "Ireland needs a help to build scheme, not help to buy."

Other parts of his analysis show how poorly we understand what is happening in the property market, a knowledge gap that increases the risks of ill-judged meddling by government. Cash buyers have been calling the shots for some time, according to Mac Coille, accounting for half of house sales in the early months of this year. This makes a nonsense of the numbers published last week by the Central Statistics Office, reporting house prices rose 8.5% in the past year, because they ignore purchases by cash buyers. The omission means we can only guess at the full extent to which supply bottlenecks are inflating another bubble, at least in Dublin.

Another unknown is why cash-rich buyers are throwing so much money into property, especially when the best bargains were snapped up long ago. Mac Coille speculates they are fed up of seeing their money wither away on deposit and are lured by rising rents, which soared by 14% in Dublin city centre in the past year, according to Daft.ie, a property site.

Another attraction is a capital gains tax exemption for those who invest before the end of this year. The exemption made some sense when it was introduced in December 2011, at a time when the market was in free fall. It cannot be justified now that prices are rising across the country, and soaring in some parts. If government wants to be seen to be doing something useful, it should scrap the exemption immediately.

A slow burner

Gas prices are not an issue in summer — unless you are a heavy barbecue user. This is why the full deregulation of Bord Gais Energy from July 1 may pass unnoticed until the evenings grow chilly in autumn. By then, we will know what deregulation will mean for Bord Gais Energy's tariff. With more than 50% of the market, the danger is its priority will be to hold on to existing customers through loyalty rewards rather than compete on price. Its rewards club gives discounts at Tesco and priority access to shows at the Bord Gais Energy theatre. Consumers would prefer lower gas bills.