Swimming *with* Sharks

a survival guide to international property investment

by Chris McGrath

On a recent visit to South Africa I witnessed a number of Irish holiday makers ignore a shark warning while swimming. They later said they didn't know that there were sharks in the water and joked that they regularly swim at home but have never been bitten by a Shark. As we holiday in more exotic locations, we are presented with new risks and cannot judge every beach by Irish standards. Similarly as we seek out property investments in far flung locations we will be presented with new risks. Overseas holiday homes, buy to lets and syndicated commercial investments are all in vogue, but one should not lose sight of the fact that International property investment is a risky business and should only be entered into after careful market research and evaluation. The following pointers may assist those interested in buying property abroad.

Investment Objective:

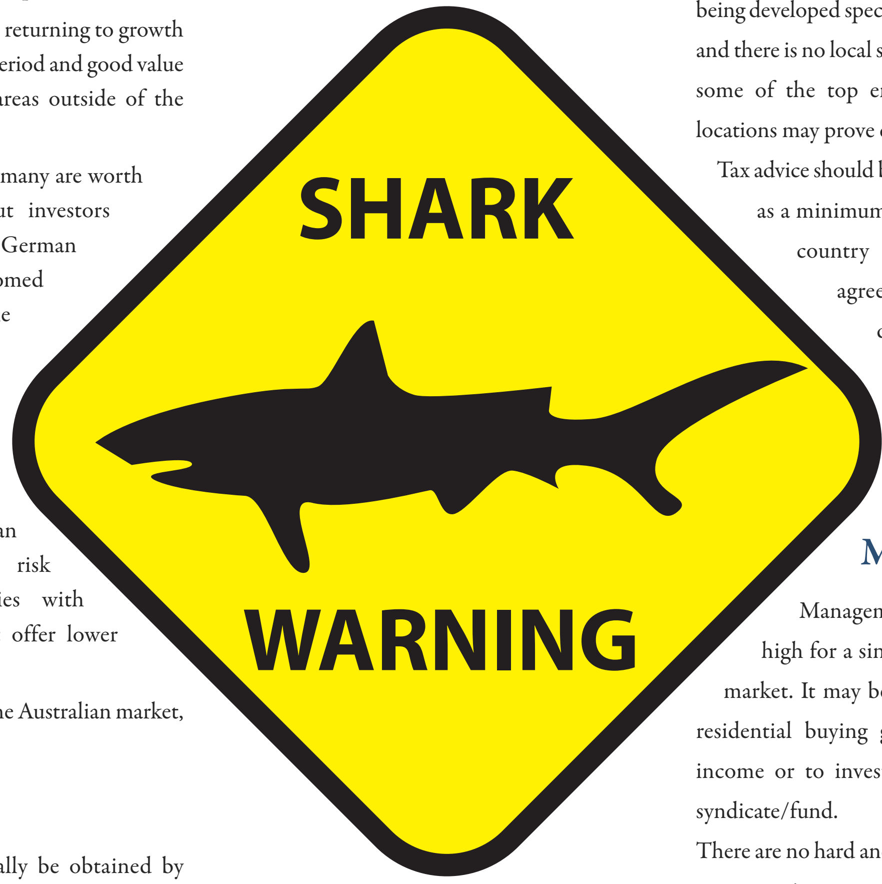
Your investment objective must be clear, do you want an investment property or a holiday home. People frequently answer this question with "a bit of both" however the criteria used to evaluate a holiday home and investment property are completely different. The selection of a holiday home is highly personal and is judged against a persons own taste and interests. On the other hand an investment should only be judged on a risk/return basis. Sellers frequently target product at this confused sector and offer developments packaged with rental guarantees for a number of years with provision for owner usage. These often prove not to be either good investments or holiday homes.

As a side note, I would always treat rental guarantees with great suspicion. The cost of the rental guarantee is usually built into the sales price of the property. The key considerations are who is offering the guarantee and what happens after it expires.

Which Market:

The big question is where to invest? There is no straight answer to this question. Each investor has a different risk profile, investment scale and borrowing capacity. In short different markets will suit different investors, but the following is a general guide for the average residential investor;

- Residential investments in markets such as Bulgaria, Romania, Turkey, Cape Verde, South America, Asia, Russia, The Ukraine or the Balkans (excluding Croatia) are not recommended.
- Some Eastern European markets, which were once attractive, such as the Czech Republic, Hungary, the Baltic States and Croatia no longer represent good value for money.
- The UAE (Dubai) is now overpriced with a huge supply pipeline. In addition its secondary and rental markets are largely untested.
- The US property market has been badly affected by defaults in the sub-prime mortgage market and prices are now stagnant or falling.
- Property prices are falling in Spain, particularly in the Costa Del Sol, following a 10 year property boom which saw prices rise by 270%.
- The Italian residential market has also stalled, following changes to vat on property and recent interest rate hikes.
- The UK and French markets are performing well but a recent report by Fitch Ratings ranked these markets as the most exposed to housing overvaluation out of 16 markets studied. In addition a lot of the French buy to let stock is significantly overpriced.
- The Portuguese market is returning to growth following a recessionary period and good value can be obtained in all areas outside of the Algarve.
- Poland, Slovakia and Germany are worth strong consideration but investors should be aware that German prices may not have bottomed out just yet and that the rate of growth witnessed in Poland in the recent past cannot be sustained.
- The mature markets of Benelux and Scandinavian countries provide low risk investment opportunities with good rental returns but offer lower capital growth prospects.
- The outlook is good for the Australian market, in particular Queensland.



Sourcing Tips:

The best value will generally be obtained by sourcing directly. If you are using an intermediary be careful as overpricing of between 5-200% is prevalent in the residential market. All information offered by the intermediaries should be independently verified and obtained in writing wherever possible. It might seem obvious but you should only sign documents translated into English after taking legal advice and avoid giving power of attorney to third parties. Public notaries used in many countries do not obviate the need for your own lawyer.

Identify all local property taxes and management charges before you buy as these can greatly erode rental income. Building standards vary considerably from country to country and the construction should be certified by an independent engineer. Fit-out standards also vary. In Lithuania for example it is common to sell apartments in a shell state, whereas in neighboring Estonia apartments are sold fully finished.

It is never advisable to borrow against your family home. 70%+ finance should be available in most developed countries, subject to your financial standing. If you cannot borrow in the local market then I would suggest that you do not invest there.

Syndicated property investments and property funds are an increasingly popular method of investing and are offered by many financial institutions and intermediaries. They provide an easy and affordable means of accessing international commercial property investments. They usually feature non recourse gearing of 60-70%, tax planning, a 5-7 year investment horizon and typically project an IRR of 13%+ per annum. Many syndicates have performed very well over the recent past but new providers are selling product of questionable quality. Before subscribing examine the underlying investment assets (buildings), fee structure, model growth assumptions and the promoters' track record. The sharks have now invaded these waters so be careful here too.

Exit Strategy:

You should plan your exit strategy prior to any purchase. Your objective should be to buy a property that will re-sell well and to do this you need to have a good insight into the local market. For example in Eastern Europe smaller apartments sell best, whereas in Portugal there is a greater demand for larger apartments. In some markets such as the Black Sea resorts, product is being developed specifically for overseas investors and there is no local secondary market. Therefore some of the top end developments in these locations may prove difficult to re-sell.

Tax advice should be obtained at the outset and as a minimum you should check that the country has a double taxation agreement with Ireland. If it doesn't you may end paying tax in both countries. Also investigate and make provisions under local inheritance laws.

Management:

Management costs will be relatively high for a single property in an overseas market. It may be better to buy as part of a residential buying group with pooled rental income or to invest as part of a commercial syndicate/fund.

There are no hard and fast rules when it comes to property investment. There will always be hotspots in depressed markets and black spots in appreciating markets. Information is the path to successful investment. Always research your market well, take independent advice and be slow to part with your cash, you may find it far easier to buy property than to sell it. Finally beware of sharks, they are slippery and can bite!

Note: This article is provided for general information purposes only. It is based on personal opinions of the writer and should not be relied upon, or form the basis of any investment decisions.

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