

A good day at the office with Resi back in demand

A market report by James Kersh, partner Sutton Kersh, 16th June 2005

When areas of blight begin to show gains in the commercial property market, you know that good times are around the corner.

Regeneration of an area usually begins with good quality housing stock and a corresponding demand following by the development of a commercial property infrastructure, usually of retail and leisure.

Seaforth in the north end of the city has this nearby in abundance in the form of Crosby and Waterloo and this is now helping to shape new good fortune in nearby L21.

In fact, L21 showed some of the biggest gains amongst the commercial lots in our most recent auction in June.

For example, offices in Seaforth Road comprising a mixed-use investment with a rent reserved of £11,440 gross per annum began the day with a reserve guide price of £70,000 eventually fetching £93,000.

Overall, whilst residential investors have become more cautious, interest in commercial property appears to be growing in line with national demand. Commercial property has shown returns of 18% in the past year. It's one of the most alluring investment stories around and the commercial property market shows few signs of overheating.

The case for investing in commercial property rests on a number of factors and whilst rental returns have fallen, they are still around 6%-6.5% a year, much higher than the yield on UK equities (3.2%), gilts (4.8%) and cash (5.4% at best). The flipside of falling yields has been raising capital values, but there's no sign of a bubble. While residential property values rose by 193% in the ten years to 2004, commercial property rose by a far more modest 38%.

In Liverpool, the economy has been strongly boosted by demand for new space by an increasing number of fledgling and flourishing businesses in the city. There is also counter on the horizon, however, to the cautious residential investor largely thanks to SIPPS with opportunities fast approaching.

The property market will receive a considerable boost from April 2006, following recent government proposals allowing investors to buy residential property, such as buy-to-lets, with a personal pension.

How does it work? Well, your property portfolio would be free from tax on rental income and capital gains and you will be able to put both new and existing properties in a pension.

It's potentially a great tax giveaway for higher earners, with savers who contribute to their pension schemes in order to buy property getting tax relief on the money.

For example, the government pays 22p for every 78p that you invest, taking the total contribution to 100p. Higher-rate taxpayers get a further 18p through their tax return. So someone who wants to purchase a £100,000 property would need to contribute only £78,000. Higher-rate taxpayers would get a further hand-out of £18,000.

Once a buy-to-let or holiday home is in your pension, the rent will have to be reinvested in the fund and used to pay off any mortgage, but it will be free from income tax at 40%, assuming you are a higher-rate taxpayer. Any capital gains when you sell will also escape tax.

Perks too could almost double returns from buy-to-lets.

For example, someone who bought a £150,000 property outside a pension with a 50% mortgage and sold it 10 years later might net a profit of about £75,000.

The figures do assume that any surplus rent after tax and mortgage interest is used to clear the debt and that house prices grow by 4.5% a year. If the property were held within a pension, however, the tax breaks would boost your profit to about £140,000.

All this is very good news and has come at just the right time following a plateau in the residential market.

It's certainly put a smile back on the face of our residential investor clients this summer who are now busy building their portfolios in anticipation of our next auction in July.