

Residential Property Investor Report

From Irish Mortgage Brokers in association with PropertyWeek.ie

HEADLINE FINDINGS

1. Based solely on rental incomes versus deposit returns over a five-year period, investment property is overvalued by 43% in Dublin, and by just under 50% in Cork and Galway
2. Current rents would need to be 70% higher in Dublin, 91% higher in Cork and 89% in Galway for an investor to see any kind of return over five years based on the current average asking prices of property
3. Target prices to pay for 2-bed apartments as investments based on matching deposit yields would be on average: €201,000 in Dublin, €150,000 in Cork and €141,000 in Galway; or with rents continuing to fall: €128,000, €94,000 and €86,000 respectively

FOREWORD

Residential property does not look good as an investment option in the current market. Jack Fagan of *The Irish Times* put it like this recently: "The banking climate for private investors could hardly be worse." (*The Irish Times*, 23/04/2009). Falling rents, declining property prices and changes in both lending and taxation policies have combined to bring enthusiasm and confidence in this sector to all-time lows.

Irish Mortgage Brokers is pleased to present its first Property Investor Report in which we establish a measure of the current situation and present a sense of where the market needs to get to in the near future. In association with research company PropertyWeek, we have brought together a range of different data, including property prices, rents, latest taxation, and deposit rates, to provide you with factual information on the state of the residential investment property market in Ireland in 2009.

Any investment carries with it a risk, and in order to justify that risk there needs to be the possibility of a return on it above that of lower risk options, otherwise why would anyone take it? We have chosen to benchmark against money on deposit, which as a low-to-no risk option would, under optimum conditions, produce lower returns than property, which is medium risk.

The point of presenting this information is to enable people to see for themselves, based on independent analysis, the rental prices that would have to be achieved today in order for property returns to match deposit returns, and on the other side of the same coin, the 'target' prices that would have to be paid for a property given the current rental market in order for it to match deposits. We have also considered the prevailing scenario of falling rent and presented what that target price would have to be.

Capital appreciation/depreciation has been omitted because we have chosen to evaluate the property proposition on the basis of a pure 'return on investment' similar to, say, share dividends, and because capital appreciation can only be realised by a sale we do not factor this in. But it is important to point out that some people view property investment very differently and see long-term capital gain rather than shorter-term return on investment as the true appeal of bricks and mortar. Promoters of property would argue that you can assume (at some point in the future) at least some capital appreciation, but taking a five-year view, especially under current conditions, this would be a moot point.

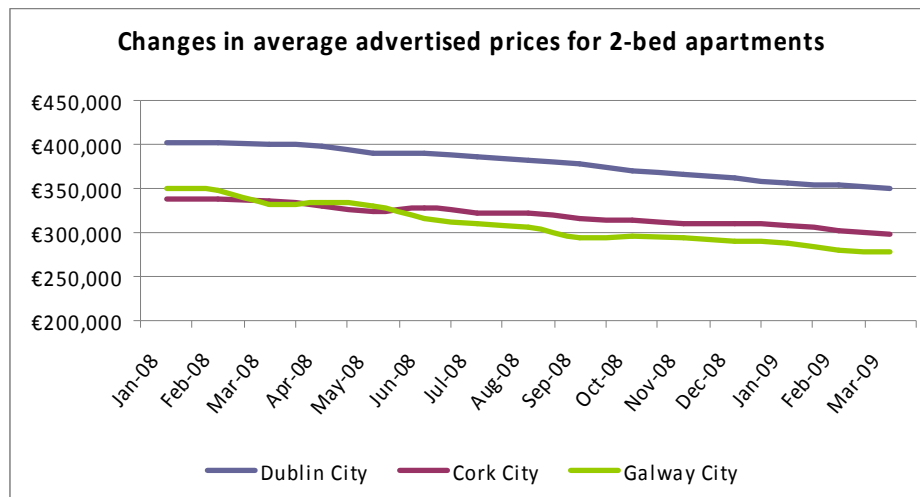
While Irish people have traditionally been keen to own their own home, there seems to be growing numbers interested in long-term renting. This report is not intended to influence people in that regard (although some of the information contained in it may be relevant and we will be producing reports on that matter in the future). Rather, we are interested in property investment as a separate matter from where people make their home, and in its pure form as an option for anyone with spare capital.

As a long term proposition property is still a perfectly good asset class. In the same way that the dotcom crash didn't put an end to the internet, the recent property crash does not mean the market for housing is gone. However, the sensible view would be for home buyers to make long-term location-based decisions about where they want to live and in what type of property; and for investors to run the numbers themselves for their own particular circumstances to determine their target buying prices rather than hoping an investment within the framework of current asking prices will work out at some point in the future.

Karl Deeter, Operations Manager, Irish Mortgage Brokers



PROPERTY PRICE OVERVIEW



Source: The Property Week

Dublin

Having fallen below the €400,000 mark in March last year, the average asking price for 2-bed apartments in Dublin has now fallen below the €350,000 mark for the first time since October 2005. The asking price for 2-bed apartments in Dublin fell in March by 1 per cent to now stand at €349,736, down over 3 per cent already this year, and down over 12 per cent on March 2008, when the average was €399,588. Monthly price drops for 2-bed apartments have been smaller than for 3-bed semi-detached, but they too have been recorded nearly every month since the start of 2008.

The average asking price for a 3-bed semi-detached property in Dublin fell in March by 1.5 per cent to €422,828, 5.6 per cent down for the year so far, and 14.8 per cent down on March 2008, when the average stood at €503,925. That's a drop of just over €81,000 in one year. Going on asking prices, the peak for the Dublin market was seen in mid-2007, reaching just over €510,000 for 3-bed semi-detached properties. That equates to about a 20 per cent drop to date from the peak. The rate of inflation had begun to fall much earlier, back in late-2006 in fact, but the confidence of sellers took a lot longer to be eroded and so asking prices themselves remained stubbornly high right through 2007. Since then, we have registered drops every month, bar two, in the asking prices for 3-bed semi properties in Dublin. Recent drops (-1.4 in November, -0.7 in December, -2.4 in January, and -1.5 in February) suggest that the bottom has still not been reached.

Cork

Asking prices for 2-bed apartments in Cork fell below the €300,000 mark for the first time since 2006. The drop for the month was 1.8 per cent to average out at €297,242, down about 4 per cent since the start of the year, and down 11 per cent in twelve months, with only two months in that period not showing price drops. The average asking price in March 2008 was €335,098.

The average advertised price for 3-bed townhouses (semi-detached plus terraced) in Cork City fell in March by 1 per cent to €308,487, a 1.5 per cent fall since the beginning of the year, and 10 per cent down on March last year when the price stood at €347,369. This is a fall of about 16 per cent from the peak average of about €362,000.

Galway

The average asking price of a 2-bed apartment in Galway city now stands at €277,078, down already this year by 4 per cent, and down by a dramatic 15 per cent on March 2008 when the figure stood at €331,974 – over €10,000 more than a Galway 3-bed house.

In Galway city, asking prices for 3-bed townhouses fell further below the €300,000 mark to €287,553 for March, a 2.7 per cent drop for the month, a 5.4 per cent drop in 2009 already and like Cork down 10 per cent on March 2008 when the average was €321,435. The peak price in mid-2007 reached nearly €335,000. The Galway market is exceptional in terms of property types in that 2-bed apartments have at times been more expensive on average than 3-bed houses. Also a finding in other property price reports, it is probably because the majority of the apartments in the Galway city market are so new and also quite large in comparison to some of the 3-bed housing stock. However, the harsh realities of the current market have corrected this "glitch" in the figures.

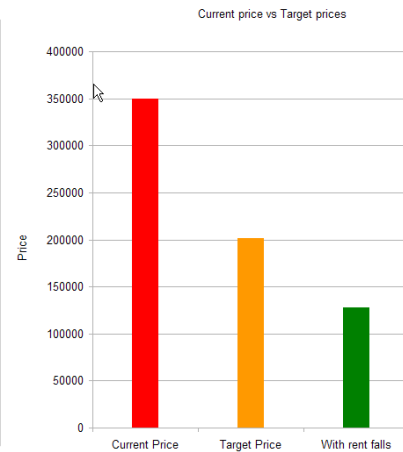
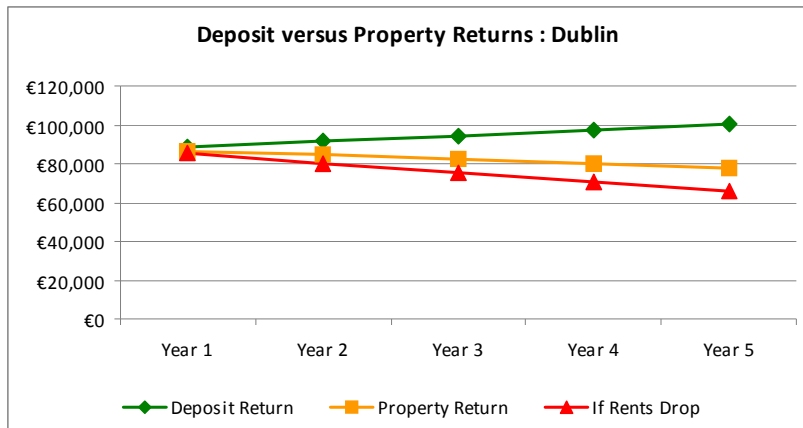
Paul O'Connor, MD of The Property Week & MyHat.ie



www.propertyweek.ie

Dublin city

Property position		Deposit position		
Property cost ¹	€349,736.00	Year	Capital	Interest
5-/10-year fixed rate for investors (average)	4.85%	Year 1	€88,678.72	€3,547.15
Mortgage required (to max. LTV of 80%)	€279,788.80	Year 2	€91,410.02	€3,656.40
		Year 3	€94,225.45	€3,769.02
Deposit required (20%)	€69,947.20	Year 4	€97,127.60	€3,885.10
Stamp required	€15,731.52	Year 5	€100,119.13	€4,004.77
Fit out	€3000.00	Total interest		€18,862.44
Total start up costs ²	€88,678.72	Less DIRT		€4338.36
		Total return		€14,452.08
Average rent ³	€1,250.00	<hr/>		
Annual rent (at average 11 months occupancy)	€13,750.00	Results after 5 years & target prices		
Interest-only mortgage cost per month	€1,130.81	Total profit/loss on deposit	€14,452.08	
Interest-only mortgage cost per annum	€13,569.76	Total profit/loss on property	-€10,698.31	
% of interest that can be offset	€10,177.32	Cash position of deposit over property	€25,222.39	
Sundry additional costs per annum	€1,200.00	Property price target (where it could match deposits at current rent)	€201,000.00	
Taxable income	€2372.68	Target price with rents falling	€128,000.00	
Tax due (41%+2% Levy+6% PRSI) = 49%	€1119.91	Monthly rent required to match deposit	€2,120.00	
Profit/loss per month	€15.02			
Profit/loss per annum	-€2139.66			
Total profit/loss after 5 years	-€10,698.31			



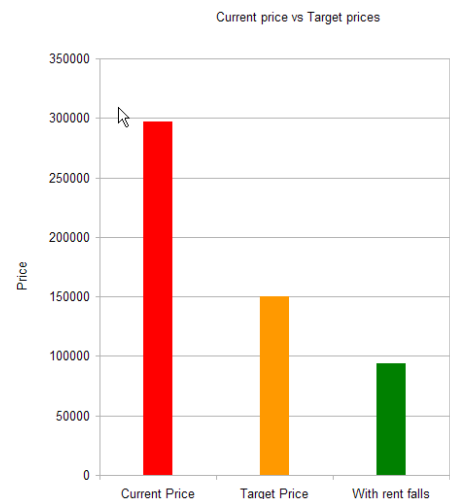
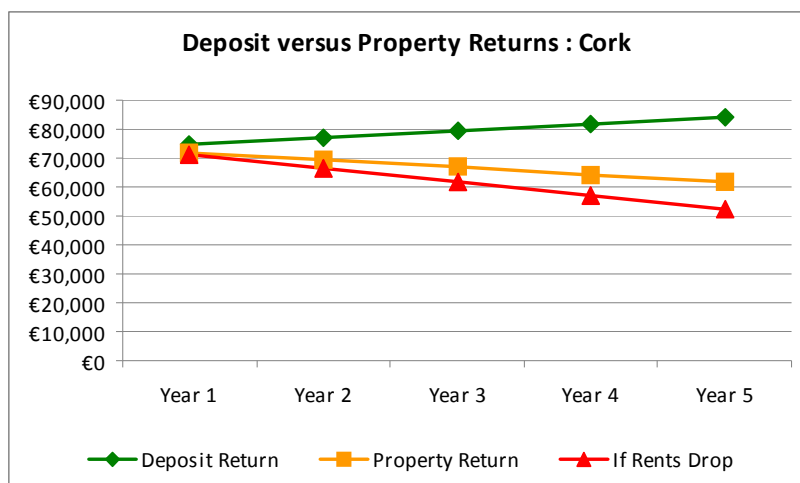
Notes:

1. Average asking price of a 2-bed apartment as of March 2009, according to PropertyWeek.ie data
2. Money required/available upfront is €88,678.72
3. Rental figure based on current advertised rates

Cork city

Property position		Deposit position		
Property cost ¹	€297,242	Year	Capital	Interest
5-/10-year fixed rate for investors (average)	4.85%	Year 1	€74,505.34	€2,980.21
Mortgage required (to max LTV of 80%)	€237,793.60	Year 2	€76,800.10	€3,072.00
		Year 3	€79,165.55	€3,166.62
		Year 4	€81,603.85	€3,264.15
		Year 5	€84,117.25	€3,364.69
Deposit required (20%)	€59,448.40	Total interest		€15,847.68
Stamp required	€12,056.94	Less DIRT		€3,644.97
Fit out	€3000.00	Total return		€12,202.72
Total start up costs ²	€74,505.34			
Average rent ³	€950.00			
Annual rent (at average 11 months occupancy)	€10,450.00			
Interest-only mortgage cost per month	€961.08			
Interest-only mortgage cost per annum	€11,532.99			
% of interest that can be offset	€8,649.74			
Sundry additional costs per annum	€1,200.00			
Taxable income	€600.26			
Tax due (41%+2% Levy+6% PRSI) = 49%	€283.32			
Profit/loss per month	-€90.25			
Profit/loss per annum	-€2,566.31			
Total profit/loss after 5 years	-€12,831.56			

Results after 5 years & target prices	
Total profit/loss on deposit	€12,202.72
Total profit/loss on property	-€12,831.56
Cash position of deposit over property	€25,034.27
Property price target (where it could match deposits at current rent)	€150,000.00
Target price with rents falling	€94,000.00
Monthly rent required to match deposit	€1,810.00



Notes:

1. Average asking price of a 2-bed apartment as of March 2009, according to PropertyWeek.ie data
2. Money required/available upfront is €74,505.34
3. Rental figure based on current advertised rates

NOTES ON METHODOLOGIES & ASSUMPTIONS

Property prices: focusing on the classic residential investment property type of two-bed apartments, we look at Ireland's three main urban markets, Dublin, Cork, and Galway, and use a moving average calculation applied to the largest database of asking prices in the country (as maintained by The Property Week). Based on these asking prices we calculate an average amount of money required to purchase one of these properties in each market.

Rent: we take an average for the current rental rates in each market for a two-bed apartment, and set these figures against fixed-rate mortgages on interest-only terms to determine the gross cash-flow. The amount of rent taken is based on one month of vacancy per year to allow for the fact that there are often gaps in tenancy. Rent per annum is therefore 11/12ths.

Expenses and taxation: we factor in €100 per month to cover management fees, insurance and other landlord related costs. We take the 41% rate of taxation to calculate the tax due after expenses, assuming that if you were in the 20% tax band you would be less likely to have the income with which to obtain an investment mortgage, and while there will be exceptions we feel this has the broadest application.

One of the things which have changed is that of 75% allowance in Mortgage Interest against rent. Mortgage Interest is an expense to a landlord the way regular expenses are to any business, this is an oversight which will see many investors not only paying to support their investment property, but also being taxed in income they never made. We didn't consider a VAT reclaim in our calculations.

Capital appreciation: This is not factored into the figures as for the five-year perspective taken here it would be inappropriate.

Deposit rates: We take a market leading 5-year fixed deposit rate likely to be available to anybody who would have the amount of money required in each example to purchase the property in question. Dirt tax is applied at 23%.

Mortgage rates: We assume a general loan-to-value (LTV) of 80% for an investment property, with a rate which is an average of the best 5-year and 10-year fixed rates on the market. While this may skew the figures slightly for some, not every investor will get the best rate on the market and for that reason the middle figure is good for giving a fairly accurate picture of mortgage costs.

Target prices: These are the approximate prices that would need to be paid in order to match the current rental yields with the current deposit yields. Our target prices consider the 'break even' point under two scenarios: 'Target price at current rent' is the price you would need to buy at in order for the *current* rental yield to match deposits, while 'target prices with rents falling' assumes that with such a large oversupply of property for sale (both new and second hand) it is likely that rents will not hold up and therefore yields will be lower. We assume that drops in rents of 10% in year 1 and the same again in year 2 might be required in order to attract a tenant. In some areas it may be even more extreme, but as we are dealing only with urban markets in this report, we felt that 20% would give an indicative picture.

Start up costs: This is made up of the deposit required plus the stamp duty. Legal fees are omitted as they vary widely.

For more information on this report contact Karl Deeter of Irish Mortgage Brokers on 01-679-0990

For ongoing comment on financial matters visit www.mortgagebrokers.ie/blog

For more information on property prices in your local market contact Paul O'Connor of Property Week on 01-415-1228

For regular updates on property prices visit www.myhat.ie/blog

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