

Residential property remains a good bet in the long term

Cooling market indicates high growth may be a thing of the past but there's no need to panic

By **Fergus Muirhead**

HOW lucky is it for those of us that have been unconvinced by the government's attempts to "simplify" pensions that the property market seems to be continuing its inexorable drive upwards, making more of us millionaires, at least on paper, than ever before.

On top of the continuing rise in the value of the homes in which we live, more and more of us are dipping our toes into property investment. "How many properties do you have in your portfolio?" has replaced questions about the car you drive or the school your kids attend in some fashionable restaurants and wine bars and it seems that those investing in property to let can't do anything wrong.

Buy-to-let mortgages for second homes are commonplace and for some it is de rigueur to have a third or fourth mortgage. And all this on top of what was an already growing market in people buying properties either here or abroad to use as a holiday home or to let to friends and family in that twilight world where "rental income" and "tax" are never uttered in the same breath.

Douglas Robertson, head of the department of applied social science at Stirling University, reckons that homeowners need to be careful, especially those who see the house they live in as an income earner at retirement.

He says: "Housing is a peculiar commodity, in that like all goods it has a use value, but unlike most others it also has an investment value. The investment

value only exists in a rising market, but fortunately that has been a long-standing pattern.

"The big problem is that many people talk of a house being their core investment, but unless they sell and downsize, then this asset is effectively frozen. So the reality for many is that the investment passes on to children, as inheritance, and the government gets its take through inheritance tax."

So effectively those who talk of the home they live in being their pension may be deluding themselves, since the only way an income can be provided is for the house to be sold and replaced with a smaller model and the cash left over spent or invested elsewhere to provide an income.

Those of us who have bought property in addition to the ones we live in and see that purchase purely as an investment should continue to benefit from a healthy market, according to Martin Smith, financial services director at Clyde Property. "The buy-to-let market has grown incredibly over the last 10 years with a period of sustained increases in house prices and the emergence of innovative buy-to-let mortgages. Our experience is that tenancy occupancy rates remain high with virtually no void periods for most properties in good locations."

Having said that it may be that the market is now beginning to slow. It is fair to say that the yield, or rate of return, has tightened for many investors as interest rates have risen 1% since August last year, and interest payments on mortgages are rising faster than rental income.

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For many in the buy-to-let market, however, it is not the short-term income that is important, rather the fact that there is still an expectation of long-term capital growth. Also the fact that borrowing-to-buy allows an element of gearing that cannot be found in other investments, as Smith explains. "If you have £50,000 to invest on the stock market then fine, but your growth is based on that initial investment. With property you can borrow another £150,000 and buy a property at £200,000 which is currently increasing in value by around £20,000 per annum."

While this may have been the case in recent years, it's unlikely that this level of growth can be sustained over the next 10-20 years, or even the next 12 months, according to some commentators.

At the same time, many new purchasers are arranging interest-only mortgages where the monthly rental payments merely service the monthly interest payments and the original debt is not reduced. If that happens then the gearing is ineffective and a period of slower growth in the housing market may mean that greater returns could have been obtained, without the hassle of dealing with tenants and loans and tax, by investing in more traditional areas such as unit or investment trusts, or indeed directly into the stock market.

So while residential property, either in the shape of our homes or as an investment vehicle, may have made many rich in the last 10 years it may be that the best is past and a more balanced view is needed in the next 10 for investors who do not yet have a foot on the ladder.