Market Report

Colliers and PwC release an Eastern Europe Report

Colliers International in association with PwC publishes latest tactical investment report that analyses the impact that Latent Capital Gains Tax (LCGT) can have on yield pricing in a property transaction.

Numerous factors play their part in defining the ?gross yield' in any given real estate transaction. In the ?Yields and Capital Gains Tax' report, Colliers draws attention to the importance of understanding Latent Capital Gains Tax (LCGT) - and the impact this can have on a quoted gross yield. The report highlights that even if you see a deal being reported at 6.5%, the actual net yield can, and most likely will, vary significantly around that number depending on the deal structure ? existing market reporting of yields doesn't reflect this.

The report shows that when LCGT is factored into the equation, the net yield could vary by up to 70 basis points around this 6.5% figure quoted. This yield spread is based on a hypothetical, but very realistic transaction, where a sizeable capital gain has been made on a property deal ? based on the current purchase value relative to the book value.

"As Eastern Europe continues to mature as an investment market, we are likely to see more deals with a longer tax history come to market. Getting the right advice on how best to negotiate the LCGT position will be critical in driving value and returns for both parties" commented Damian Harrington, Colliers International's Regional Director of Research & Consulting for Eastern Europe.

Two factors are considerable in determining how LCGT is negotiated between buyer and seller and thus the overall impact on a yield:

? the type of deal structure used i.e. share or asset deal, and

? the balance of the market i.e. is it a buyers' market or is it a sellers' market.

For example, in the Czech Republic the market norm for 2011 was to split the LCGT 50/50 between buyer and seller. So, if the LCGT amounts to 3.2 million Euros, this translates into the purchaser receiving a 1.6 million Euros discount to the purchase price. In yield terms this equates to a 20 basis point discount, so the yield paid is actually 6.7% and not the 6.5% quoted.

If the balance of the market shifts in favour of the buyer, allowing them to negotiate a discount of say 80%, the equivalent yield discount would be 32 basis points on the same deal i.e. the yield would be 6.82%. On an asset priced at 54 million Euros, that's a significant saving.

In a sellers' market we would anticipate that no LCGT discount is made available to the purchaser i.e. the purchaser pays the gross yield of 6.5%. It is worth considering, however, that in such circumstances the purchaser may have inherited a ?hidden premium' of up to 3.2 million. The size of this premium will be partly determined by the balance of the market in the future. For example, if the sale takes place during a buyers' market, the worst case scenario is that the vendor has to

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offer the new buyer a full LCGT discount. In effect, this means that their original purchase was closer to an effective net yield of 6.14%.

Datum: 10.02.2012

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