WHAT ARE PROPERTY BONDS?

A company that wants to finance the purchase of an existing property (office block, shopping complex, etc.) or a construction project, can issue property bonds.

- The **issuing company** is the legal owner of the property (shopping complex, office block, etc.); it is also responsible for its rental and maintenance.
- The **certificate holder** is the economic owner of a part of the property. In exchange for their investment, they receive an annual coupon and, on the maturity date of the certificate, a share of the sales price of the property.

A property bond is therefore a security that gives the holder an entitlement to a part of the income from the investment in the property (purchase of offices, shop premises, etc.). If you buy a property bond, you are therefore a creditor.

In contrast to what applies to regulated property companies (such as, for example, Cofinimmo and Befimmo), the exposure of a property bond is limited to one specific building or a limited number of buildings.

Features

- A certificate is issued for a specific **term** (usually 20 to 25 years). The certificate expires at the time that the property is sold.
- The certificate holder receives an annual **coupon**. This always includes the rental income (less the management costs) and a part of the reimbursement (repayment) of the invested capital.
- Given that the rental incomes are index-linked, the coupon will rise and fall with the **index**.
- On the final **maturity date** or on the sale of the property, the certificate holder will receive a share of the sales price of the property.

Risks

Liquidity risk: the liquidity of an exchange-listed security is determined by the number of marketable securities. For most property bonds, the number of marketable securities is relatively small. Investors who want to sell their property bonds may find it less easy to find a buyer, which has a negative effect on the price.

Market risk: the value on the secondary market depends on what happens to the underlying property. Interest rates also have a major impact on prices. A rise in market interest rates will generally lead to a fall in the value of the property bond.

Credit risk: a property bond is a debt instrument. If the company that issues the property bond starts to have financial problems or goes bankrupt, you may lose (some of) the capital you invested.

Yield risk: the coupon payment is uncertain. If vacant, or when renovation work is needed, the rental income falls; it is possible that a lower or even no coupon at all is paid out. And the sales price of the property on final maturity is also uncertain: property prices can stagnate or fall, which means that the property may finally have to be sold at a loss.

Costs and taxes

If you buy a property bond, then you also have to allow for the costs and taxes you need to pay. These also affect the return on your property bond.

COSTS

Brokers' fees: banks charge their costs for executing your orders on the secondary market.

Custody fee: to hold your certificates on a custody account, most banks will charge you a fee.

TAXES

Stamp duty on stock exchange transactions (TOB): if you buy or sell a property bond on the secondary market, you need to pay the exchange stamp duty.

Withholding tax on the coupon: The part of the coupon that matches the payment of a net rental profit is treated as interest. To the extent that this interest is higher than market rates, it can be reclassified as a dividend. Withholding tax will be taken on this part of the coupon.

The part of the coupon that corresponds to the partial repayment of capital remains untaxed.

Withholding tax on capital gains: when selling the property, withholding tax is paid on the part of the payment that exceeds the remaining balance of the invested capital. In other words, withholding tax is payable on the profits, but not on the capital repayments.

Want to know more about property bonds?

Read our *Financial Instruments information sheet* on our website www.bnpparibasfortis.be.

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