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4 December 2003

Review of Rental for Domestic
Waterfront Tenancies in NSW
Independent Pricing and
Regularity Tribunal
PO Box Q290
QVB Post Office NSW 1230

Dear Sir/Madam,

Re: Rental of Domestic Waterfront Tenancies

I wish to make a submission in respect of the review into rentals for waterfront tenancies on crown land in NSW.

Having read the information available on the website and in particular the proposal put forward by the Department of Lands and the Waterways Authority, I would like to comment as follows,

1. The formula starts with a supposed value for the leased area being 50% of the rate per square metre of the adjoining freehold land (as determined by the valuer generals statutory land value). Here we are being asked to determine a value for the leased area based on a proportion of the value of very different commodity. Some of the differences include,
 - a. Ownership of the adjoining freehold land gives the owner the right (subject to Council approval) to erect housing.
 - b. Freehold land can be sold into a large market of potential purchasers.
 - c. Owning Freehold land allows the owner to choose the term that he wishes to hold the property.
 - d. There is no restriction on transfer of title.
 - e. In almost all cases freehold land has street frontage allowing the owner to easily access the land and any improvements.

In all cases the Crown Land leased or licensed to the adjoining owner is substantially inferior to the adjoining freehold land that is being suggested be used as a benchmark.

Department of Lands and the Waterways Authority comments that "remnants" (eg, lane closures) are often sold at a 50% discount to adjoining freehold land. Comparing leased/licensed Crown land to these Remnants, we still find that Remnants can create substantial advantages to the adjoining freehold owner.

- a. Incorporating Remnants into the adjoining property, allows the purchaser to potentially increase housing that may be allowed on the property. Lessees/License holders are specifically prohibited from erecting a habitable structure.
- b. The now larger freehold property can be sold to a large potential market.

- c. Once again freehold ownership allows the owner to chose how long they wish to retain property.
- d. There are no restrictions on transferring the property.

Consequently once again “Remnants” that are priced at 50% of the adjoining freehold land is shown to be superior to the appeal of the leased/licensed area. To get a more realistic appraisal of the Crown Land, a discount should be applied compared to sale of Remnant land. Rather than using 50% of the adjoining freehold, the better comparison may be 50% of the value of “Remnant” land which has already been suggested should be at a 50% discount. Following this logic, we arrive at the first part of the formula –Crown Land should in these circumstances be valued at 25% of the value (on a square metre rate) of adjoining freehold land.

- 2. Once the appropriate value (per square metre) is determined, the Department of Lands and Waterways Authority suggests an equitable rate of return of six percent is appropriate.

Firstly this inquiry relates to residential users so of course we should look at returns commensurate with residential investments especially of similar properties.

Before we investigate the appropriate return, perhaps reading a very current article in the Australian Financial Review of Tuesday the 2nd December 2003 would be appropriate. It shows the rental return of a possible residential investment in Sydney as being one percent net and furthermore states that “AMP’s chief economist Shane Oliver, says this is the average net yield on residential property”

Some comments on Sydney Residential property investment,

- a. Most investors in residential property are mainly looking to the capital growth of the asset. In this case Crown Land would also increase in value as the adjoining land increase in value.
- b. Generally speaking the greater the land component in the residential investment and the more prime the property, the lower the return the investor will generally accept as they would have greater expectation of capital growth.
- c. Normal residential leases do not impose on the lessee the following obligations that waterfront leases/licenses impose – the lessee to erect the improvements, the lessee to maintain the improvements at their cost, the lessee to demolish the improvements at the conclusion of the lease.
- d. Normal residential leases do not charge the lessee GST on top of the rent.
- e. Normal residential rents have been shown to increase at a far lower rate that the increase in value of Sydney land prices, yet this is part of the formula proposed.

Consequently given that it has been shown that the terms imposed by the lease/license of the waterfront land on the lessees is far more onerous and costly to the lessee and that the increase in future rents should be more substantial than the increases on normal residential property investment, it is only reasonable that the returns should be lower than cash returns on normal Sydney Residential Property Investment. Given the above and the comments by Shane Oliver, two percent per annum should be more than equitable.

Some final points,

1. Department of Land and Waterways says the formula produces an effective return of three percent but they do not show that they should be entitled to take the value of the adjoining freehold land (per square metre) as the commencing base.
2. Many owners of waterfront land are already paying very substantial amounts of land tax. The massive increase the proposed formula would impose once again be a huge impact on these owners.
3. If section 6A of the valuation of Land Act 1916 results in increased values for waterfront land when there is a leased/licensed area involved, this would result in double taxation as not only would the freehold owner pay for the lease area but its presence resulting in a higher statutory valuation would lead to great land tax payments.

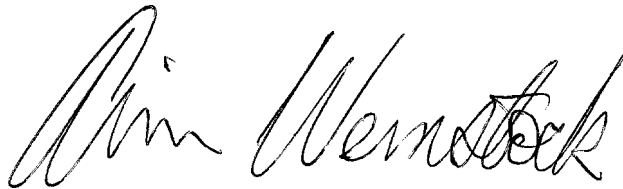
In summary I believe a far more appropriate formula would be as follows,

Rent (per square metre) = 25% x valuer general's statutory land value (per square metre) x 2%. If GST is required, this should not be borne by the lessee (as is the case in normal residential situation, the lessee does not pay GST).

If the government is looking at a greater but still equitable rental, I believe the only appropriate action is to increase the value of the lease to the lessee by substantially improving the terms and conditions (in the lessee's favour). Such a lease may then merit a higher price.

Regards,

Ami Weinstock

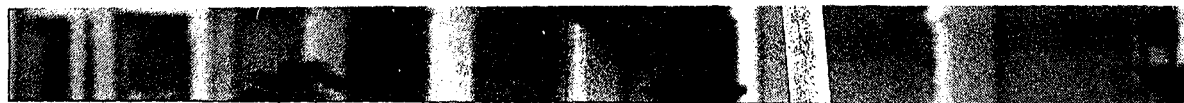
A handwritten signature in black ink, appearing to read 'Ami Weinstock', written in a cursive style.

the same result.

A HIA forecast estimated there would be a fall of about 7 per cent in new housing starts in the 2004 financial year compared with 2003.

Mr Tennent said the slowing market had been identified in two indicators used by the HIA. It surveys the top 100 builders about new housing construction, as well as monitoring the number of people **visiting** display homes. Both suggested there was a slowing in the market.

Mr Tennent also noted that high debt levels had made some people cautious about rises in interest rates.



Housing industry insiders say even a small rate increase will punish the already slowing property market.

Photo: VIRGINIA STAR

"In terms of employment, the building industry is still strong. But rate rises affect order books, so they dampen future rather than current activity," he said.

The president of the Real Estate Institute of Australia, Kareena Ballard, said the RBA should wait **until** the December **quarter** figures were out before announcing another rate rise.

That would mean any rise would be on hold until March. But Ms Ballard said the last rise had come when the market was already showing signs of a downturn.

"It was a softening market anyway but the rate rise stopped it even more," she said.

Ms Ballard said that, overall, the property market was healthy. But

there were indications that it was stabilising and so did not require another rise in the near future.

"There is an increase in the number of listings, which indicates buyers are waiting a bit more," she said.

However, there were still some vendors who had not adapted to the change. They would need to drop

But the OECD report was more worrying as it pointed to an overvalued property market. A handful of Mr Tobin's clients had already referred to it. However, it was still too early to judge its impact, or where house prices were heading in the new year.

Some buyers were **trimming** their expectations, though, he said. A property sold on the weekend for \$1.225 million, an increase of \$300,000 since it was last sold three years ago. But the vendors had reduced their target by \$150,000 just before the sale in recognition of a cooling market.

Rental yields close to the 'why bother?' mark

Tina Perinotto

A house in Sydney's inner-west is on the market right now for about \$760,000, but the agent says you could probably pick it up for \$700,000.

Ask what the rental proposition is and the agent will tell you about \$300 a week. That's a yield of 2 per cent. After you pay the insurance, rates, maintenance bill and agent's fees that's about 1 per cent net. And that is exactly what AMP's chief economist, Shane Oliver, says is the average net yield on residential property,

The big question right now for investors is: why bother? If you believe that the experts are right and the market will be flat for a while, the \$700,000 might be better off in the bank.

The low returns are simply a function of demand and supply, and in the past few years Australia's residential investment market has boomed like no other. According to the Reserve Bank of Australia, 40 per cent of all new lending for residential real estate is by investors, a figure the RBA says is unprecedented.

An article in *The Economist*, entitled "Shaky foundations, the higher house prices climb, the more they are likely to fall", says low yields worldwide will not worry investors if they believe there will be good capital gains on offer.

But if investors think the rising house prices are over, then other asset classes will start to look more attractive, which could stimulate more price corrections.

UBS chief economist Scott Haslem said residential investment returns typically tracked the 10-year bond

rate, now at 3.5 per cent. Bond rates "cycle around a bit", Mr Haslem said, and when the 10-year bond rate was 2 per cent recently housing didn't look overstretched. "Now ... clearly they do," he said.

The picture really hit home when you looked at the longer-term trend of housing yields falling from 6 per cent to 2 per cent, he said.

And although the 10-year bond yields were "fairly volatile", he said, now because of the improving world economic outlook, "we're in an environment where bond yields

aren't going to fall over the next six months".

Mr Haslem said there was a good chance that these factors would help stabilise the housing environment, if not through falling prices, then through rising rents.

"We think it is quite possible that if house prices were to stabilise we could grow our way out of this overvaluation."

In the absence of house price falls, rents would simply "grind higher in line with the CPI," he said.

AAR TUESDAY 2 DECEMBER
2003