Considering commercial

By Paul Stevens

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Investing in property has always been about location, whether the purchase is commercial, industrial or residential. However, getting value from the estate agent or broker and securing the best return on investment means knowing and asking the right questions, and pushing to get them.

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Investors who seek a commercial property investment must initially establish the potential rental income as well as lease terms and conditions, and the strength of the tenants currently holding the lease (if applicable). From here you need to identify property expenses to establish a market related purchase price and look at is a property is zoned for business. Often records reflect a property is zoned for business, but the owner has failed to pay the transportation development levy to the municipality. Check that is all in order, but to avoid this pitfall ensure that you state in the deeds of sale that any outstanding transportation development levies are the seller's responsibility.

Do your homework

Checking paper work is a bore but it needs to be done to save headaches later on: examine municipal plans and the surveyor general's diagrams of the property to ensure there are no servitudes, and scrutinise existing lease agreements to ensure the details provided are correct.

Many commercial buildings are leased sometimes to more than one party. Potential buyers should ask their broker for a rent roll and copies of current leases, particularly if the purchase is for a building with multiple store fronts.

The rent roll reflects the leases, how much rent each unit pays, whether they contribute to the common area expenses, what the lease terms are and when they expire and rental increases. For reference, commercial lease increases either linked to the consumer price index (CPI) or as a set percentage.

Another gauge of a good commercial property investment is prospective developments within the area. And, if an airport is going to be built locally, consider the impact on your investment. If you are leasing to a spa or outdoor café, for example, the value will likely decrease because of noise pollution. But, if your investment is for warehousing and logistics, locality to the airport could be the x-factor in its value.

Understanding building grades

Determining a realistic return on investment is difficult and depends on the strength of the tenant occupying the property, the location (that word again) and the length of the lease. A rule of thumb is a 10% return on investment, but there are always variations.

Part of the variation can be attributed to the building grading. A-grade buildings are generally those less than 10 years old; B-grade ones are between 10 and 20 years and C-grade buildings are over 20 years old.

However, upgrading a C-grade building could raise rental levels to being roughly in the bracket typically expected of a B-grade property. While allowing a B-grade building to deteriorate could cost the owner in terms of rentals tenants are prepared to pay.

Generally, A-grade industrial premises command rentals of R45-55/m2; B-grade industrial premises are in the region of R25-35/m2 and C-grade between R15 and R20/m2 - but every one of these rates will depend on the yard availability to the specific units, so these become further key areas potential investors should investigate.

One key benefit to owning commercial property, particularly as an investment, remains the return on investment. Typically these commercial property investments are paid off more swiftly than residential property investments, and the commercial property market is more stable: leases are based on longer periods and have steady escalations.

Purchasing a property in the right position offers investors good returns for years, and once the property is bond-free and fully tenanted, it also places the owner in a position to acquire additional commercial property through leveraging previous investment capital. It requires patience, insight and experience to get there, but it can be done.

ABOUT PAUL STEVENS

Since 2013, Paul Stevens has been the CEO of Just Property Group Holding (Pty) Ltd which controls an international group of property franchises specialising in residential sales, rentals and management. He joined as a franchisee in 2003 and now, as CEO, drives the strategic direction of the Just Property brand with his charismatic optimism. He is also actively involved in the evolution of the South African property landscape, working closely with high-level industry stakeholders.

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