Portuguese Real Estate

International Real Estate Institute

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Code of Professional Ethics

The purpose of this code is to establish clear and ethical parameters for the members of the International Real Estate Institute. Should a member violate these codes or standards of professionalism, their designation may be revoked for a period of time, and/or they may be expelled from the Association.

1 Members of the Institute must conduct themselves in a professional manner at all times.

2 Members must respect the professional reputation of other Institute members.

3 Members of the Institute must strive to maintain a public awareness that the Institute Members treat all assignments or projects fairly and impartially.

4 Members must strive to maintain and improve Professional Standards and be willing to assist the Institute to that end.

5 Members must respect a Confidential Relationship with other Institute members.

6 Members of the Institute must accept only those projects or assignments for which he/she has the ability to perform in a competent and professional manner.

7 Members of the Institute must not accept projects or assignments which involve a conflict of interest.

8 Members of the Institute must not engage in any practice which is in violation of the law of the land.


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SPAIN
Viana do Castelo
Braga
Leixoes
Porto
North Atlantic Ocean
Aveiro
Covilhã
Coimbra
Tagus
Portalegre
SPAIN
LISBON
Barreiro
Setúbal
Beja
Faro
Golfo de Cádiz
Azores and Madeira Islands are not shown

PORTUGUESE REAL ESTATE

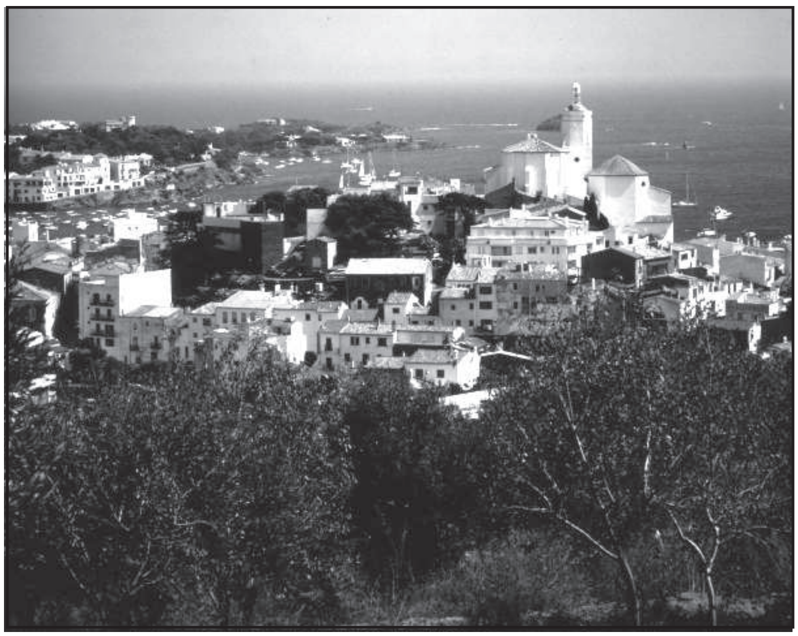
Table of Contents

By: Dr. M.A. Hines,
SCV, RIM, RPM

PORTUGUESE REAL ESTATE

Portugal is an up-and-coming European country that continues to attract Portuguese and foreign investors. The recent interest has been attributed to the preparation for, the offering of, and the aftermath of the 1998 World's Fair. The 11 million international and Portuguese visitors to the World's Fair viewed the investment potential of Portugal. Now more visitors to Portugal are anticipated as preparations are being made for the 2004 World Soccer Games to be held in Portugal. Many other major international events are scheduled in Lisbon and Oporto between the present and the major soccer event in 2004.

The continuing economic growth, that has recently surpassed the average European Union economic growth rate, encourages new real estate and infrastructure development. The economic growth of both Portugal and the other European Union countries has slowed in the new millennium due to the general global economic slowdown. But the very low vacancy rates among good investment properties - a quoted average of two percent - rising rents, relatively low inflation, favorable foreign exchange rates, and stable political and economic environments still encourage real estate development and investment.



The Portuguese Investment Environment

Portugal lies on the southwest corner of Europe as it is bounded on the west and south by the Atlantic Ocean and on the north and east by Spain. The Azores and Madeira islands that are located off shore in the Atlantic Ocean are parts of the country. Portugal and Spain jointly occupy the Iberian Peninsula and share similar long economic and political histories even though the citizens of Portugal generally speak Portuguese and French while the citizens of Spain speak Spanish, which is also a Romance language derived from Latin in earlier centuries. Both Iberian Peninsula countries feel closely associated with the other countries of Europe - particularly Western Europe - and with Latin American countries that speak the same languages. Many residents of both countries speak the English language. The Portuguese language has been adopted by Brazil.

Population, Per Capita Income, and Wage Comparisons and Trends

Even though the population and per capita income of Portugal is similar to that of Greece - a little more than 10 million people (as of July 2002 10,084,245 people) and roughly U. S. $11,000, as of 1999 - the average hourly wage of Portugal (U.S. $5.48 in 1998) tends to be far less than the average hourly wage of Greece (U.S. $8.91 in 1998). Inflation is tending to rise due to the continuing increase in wages and salaries that are approaching the average for the European Union. Portugal experiences an overall trade deficit just as Spain and Greece do. While the Gross Domestic Products of Portugal (U.S.$111 billion) and of Greece (U.S. $125 billion) are relatively close, the Gross Domestic Product of Spain (U.S. $596 billion) is much higher than either Portugal or Greece. Another general comparison might be made about Portugal: Ireland with only about one third the number of citizens of Portugal has only a U.S. $90 billion Gross Domestic Product but its average per capita income is U.S. $24,000, that compares favorably with France and the United Kingdom. The average hourly wages of Spain and Ireland were more than twice as high as that of Portugal in 1998. The hourly wages of all these countries have risen since 1998.

Exchange Rates, Trends, and Implications for Real Estate Investors

As Portugal applied to join the European Community (often abbreviated "EC") on March 28, 1977, it used the escudo as its currency. Portugal and Spain joined the EC on January 1, 1986. For the first time Portugal held the six-month rotating presidency of the European Union (often abbreviated "EU") - the title given the evolving central government of some of the Western European countries - starting on January 1, 1992. As the EU presidency was held by Portugal, the escudo became a part of the European Monetary System (often abbreviated "EMS") and was subject to limited fluctuations around an established target rate for the escudo. In spite of these restrictions, both the Portuguese escudo and the Spanish peseta were devalued by six percent on November 23, 1992 shortly after the Portuguese presidency of the EU ended. The escudo was again devalued by 6.5 percent on May 14, 1993. The European Rate Mechanism currency bands restricting the fluctuations of the various European currencies were widened to 15 percent. Again the escudo was devalued by 3.5 percent on March 6, 1995. At the end of that year, 1995, the single European currency was given the name "euro."

On March 25, 1998, Portugal became one of the eleven countries to qualify for the European Monetary Union. Bilateral exchange rates were established for the escudo. For example, one Deutschemark (often abbreviated DM) was set equal to 102.505 escudos. At the end of 1998, one euro was set equal to 200.482 escudos. As the year 1999 opened, the European Central Bank assumed the monetary policy function for the countries using the euro as their currency. On January 1, 2002 euro banknotes and coins were introduced to Portugal and the other EU countries. By July 1, 2002 the escudo disappeared; the euro became currency of the EU countries. The U.S. Dollar strengthened against the euro at the first of the decade and then weakened in 2003 to 1.15 U.S. Dollar to one Euro in May.

The foreign real estate investor may encounter a favorable currency situation as the property investments are made. If the currency of the foreign investor is stronger than the euro, the foreign currency will buy more euro-denominated assets in Portugal than if the foreign currency were weaker than the euro. The foreign investor may wish to finance the property acquisition in the weaker currency, the euro, with in Portugal. In contrast, if the euro weakens against the U. S. Dollar, the mortgage payments on the Portuguese property financing would be easier to make. Making mortgage payments using a weaker currency is financially favorable to a foreign investor- particularly one from the United States-may wish to finance the Portuguese property investment in the home country, in this case, in the U.S.

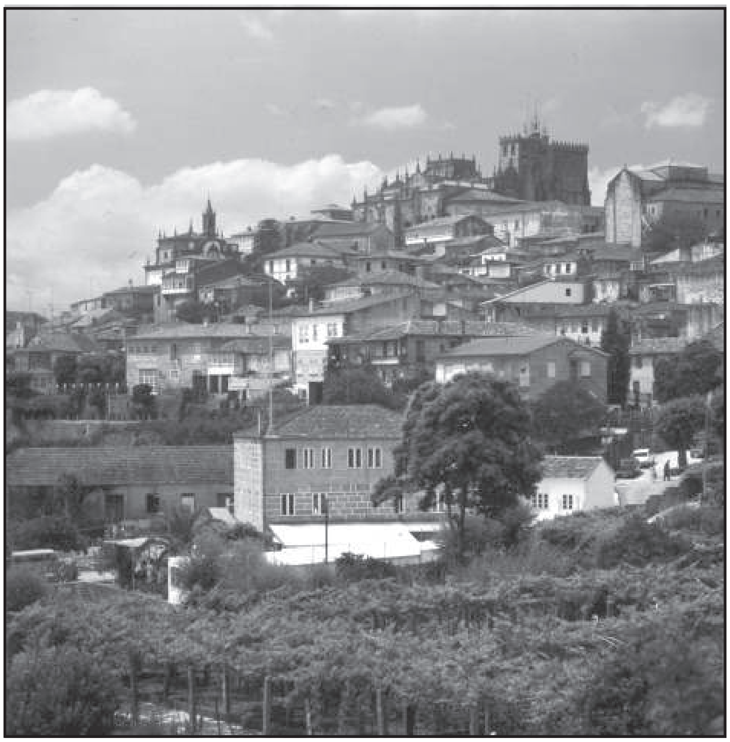
The real estate investor could consider hedging any currency risk by using euro or escudo forward or futures contracts or euro forward or futures contracts or euro option contracts for shorter term exposure. For longer term currency exposure, currency swaps might be arranged by the investors international bank. The investor could anticipate the amount of funds in euros or escudos that would be received periodically from the investment property operation and the amount of funds that would be remitted to the home country from the eventual sale proceeds from the property. If a decline in the value of the escudo or euro receipts is anticipated, part or all of the cash receipts might be hedged. Most real estate investors wish to receive, ultimately, property receipts in their home currencies.

Interest Rate Trends

The Portuguese prosperity of the last half of the 1990s and the early part of the new millennium has been prompted by relatively low interest rates, relatively low inflation, abundant loan monies, and high consumer and business confidence in the economic future of Portugal. Recently, for example, home mortgage interest rates have approximated six percent. Earlier interest rates were substantially higher. The countries of the European Union have been encouraged by the European Central Bank to harmonize their interest rates on a lower level than in earlier years.

Privatization

From an earlier period of nationalization of business and industry, Portugal is moving quickly back to a capitalistic system. Privatization is also being encouraged by the entry requirements into the European Union (often abbreviated "EU"). The government debt levels had to be reduced to a relatively low level as one of the EU requirements - approximately 3 percent. Many new EU entrants, including Italy, have had to pursue privatization programs to raise enough capital to reduce the earlier heavy level of government debt. In the case of Portugal, a high proportion of the government debt has been held by foreign institutions.



The continuing privatization program is benefiting the Lisbon and Oporto Stock Market. Some of the banks and other businesses have recently been privatized; their shares have added to the stock exchange volume. Shares of leading cement and paper pulp companies will be coming onto the exchange in coming months due to the privatization program. The government is selling about 25 percent of Portucel, the country's dominant pulp, paper and forestry group. The government is also selling its remaining share of Cimpor, Portugal's biggest cement producer. The small volume of the Portuguese stock exchange has included trading in Banco Commercial Portuguese and Electricidade de Portugal, the national power utility. The government is expected to sell about five percent of Brisa, the motorway operator, and a part of Galp Energia, Portugal's oil and gas utility.

What is the importance of the privatization program to the real estate industry? Liquidity is often needed by the mortgage lending institutions. Recently a high volume of mortgage loans have been underwritten for the expanded Portuguese real estate market in the prosperous period of the late 1990s and early 2000s. Much of the liquidity has been derived from the grants and loans from the various European agencies related to the European Union. Portugal has gained extensive funding for the country's development through their new membership in the European Union. In order to replace the exterior funding with internal funding, the sale of mortgage--backed securities to both domestic and foreign investors would add liquidity to the real estate finance sector. Investors have been attracted to the country due to the forecasted 2 2.5 percent economic growth of Portugal. This is lower than the economic growth experienced in 2000 (2.8 percent) but it is an attractive growth rate in light of the economic slowdown in the United States, East and Southeast Asia, and other parts of the world. Portugal is still considered an exception growth area within the European community.

How else is the privatization program related to the real estate industry? When the government sells off part or all of its holdings in major companies, the sell-off usually includes corporate real estate in the forms of office buildings, warehouses, manufacturing facilities, and company-owned housing. The placement on the market of such modern and depreciated properties usually attracts domestic and foreign real estate funds that have venture capital for short and perhaps medium-term investment. The real estate business is enhanced.

Another way the expansion of the Lisbon and Oporto Stock Exchange as well as the French and German Stock Exchanges in the near future affects the real estate business is the international expansion of the market mechanism for sale of shares of large Portuguese real estate companies. Investors of many countries may realize the opportunities of investment in Portuguese real estate.

Land Planning and Development

The central and provincial governments guide land development through their various planning and real estate-related ministries and departments. The land planning administration is similar to that of other European countries; the land development policies, patterns, and problems are similar to that of other European countries. Before one launches a real estate project, large or small, permission must be acquired from the planning authorities to embark on the anticipated project. Project plans may or may not fit the current goals and objectives of the planning authority. Plans may have to be revised and further readjusted before planning permission is received.

On the federal government level, the land development and redevelopment of the various provinces and the two autonomous regions are affected by the policies, regulations, and enforcement mechanisms of the Ministry of Planning, the Ministry of the Environment, and the Ministry of Infrastructure. The other ministries, including the Ministry of Home Affairs, the Ministry of Economy, the Ministry of Finance, and the Ministry of State Reform and Public Administration, also have roles to play in land planning and development.

Portugal is divided into eleven provinces and 18 districts which include Algarve and Baixo Alentejo in the south, Minho, Tras-of-Montes, and Douro Litoral in the north, and Alto Alentejo, Ribatejo, Estremadura, Beira Alta, Beira Litoral, and Beira Alta in the central section. Madeira and the Azores are autonomous island groupings that belong to Portugal; each has its own regional president. The Azores island grouping is located about 900 miles west of Portugal. The two islands of Madeira are located about 500 miles to the southwest of Portugal. Angola, Mozambique, and Macau have been autonomous colonies of Portugal. Indonesia, in southeast Asia, has long been closely associated with Portugal. In 1999 Macau was turned over to the People's Republic of China by Portugal.

The tourist regions, that include the entire country from the viewpoint of the government, are named Algarve in the south, Costa Verde and Montanhas in the north, and Costa da Prata, Planicies, and Costa de Lisboa in the central area. The government seeks to attract increasing numbers of tourists to the Algarve coast and to the key urban areas of Lisbon and Oporto. For many decades, the primary source of Portuguese tourists has been Spain; secondary primary source of Portuguese tourist has been Spain; secondary tourist sources have been the United Kingdom and Germany.

Planning permission has been given a number of office buildings, office complexes, and shopping centers in recent years as the country has prospered in the last half of the 1990s and in the early years of the new millennium. But most planning permissions have been given to prospective developers of sites in outlying areas of the major metropolitan areas of Lisbon and Oporto. Even with the recent additions of such commercial space, the low vacancy rates have prompted requests for planning permission for several projects that are currently underway.

The Park of Nations where the 1998 Expo was located and adjacent waterfront sites of earlier derelict buildings are being developed into modem apartment buildings, an entertainment-focused shopping center (Centro Vasco de Gama), and other structures. Part of the Expo buildings have been retained as part of the master plan for the newly redeveloped Park of Nations area.

Transportation Development

Part of the main transportation system was improved in advance of the 1998 World Expo. For example, a long-needed bridge over the Tejus River was built and financed on a toll bridge basis before the Expo opening. Now a third bridge is on the drawing board. The road system is most parts of the country needs major improvement according to the accident and fatality statistics that are recorded by the government. The unusually high roadway accident incidence is associated with inadequately banked curves, narrow roadways, inadequate drivers license requirements, poor driving habits, and driving at too high speeds for the roadway conditions. Modern rail equipment has been acquired for the less-than-exemplary rail system between Lisbon and Oporto, the main rail corridor, but the existing tracks are reportedly inadequate for use of the new equipment. Better rail systems are needed for international trade, particularly for trade associated with Madrid and Seville, Spain. Without an additional railway bridge over the Tagus River, a person trying to access the Algarve area from Lisbon cannot do so directly by train from Lisbon main stations. The person must travel from Lisbon to Setabul on the south side of the Tagus River by a non-train medium to climb aboard a train for the Algarve province. Then there is no train connection from the Algarve province eastward to Seville or Gibraltar, Spain.

Industrial Development

Many major industrial installations established by Portuguese and foreign companies operate in industrial areas of Portugal from the north through the central parts of the country. Years of industrial development promotion for Portugal by government and private enterprises have resulted in major industrial development that provides employment to a large Portuguese work force. Such major foreign companies as Ford-VW, General Motors, Mitsubishi, Toyota, Siemens, Texas Instruments/Samsung, ABB-Daimler Benz, and Procter & Gamble have invested large amounts in land, plant, equipment, and workforces. In order to encourage more new industrial activity and expansion of current industrial operations, better transportation and other infrastructure should be developed.

Retail Development

From the early history of Portugal, retail development has consisted of center city small shops housed by small, independent retailers primarily. Since the mid-1990s the country has entered a retail development era that favors large shopping center complexes at the edge of the metropolitan area or in the suburbs. The ten largest shopping centers, according to Healey & Baker of Lisbon, are listed below in terms of total square meters and their opening year (Exhibit 1, pg.10).

Chain stores, in particular, take space in all three locations of Lisbon, Oporto, and other cities, but the new, larger modern space of the major shopping centers tends to be preferred for efficient distribution of goods and services.

Exhibit 1

TEN LARGEST SHOPPING CENTER IN PORTUGAL

Source: Healey & Baker, Lisbon, 2001

Name and Location	Square Meters	Year of Opening
Colombo, Lisbon	122,000	1997
Forum Almada, Alomada	70,000	Opening 2001
Norte Shopping, Matosinhos	67,000	1998
Cascai Shopping, Cascais	63,500	1991
Arrabida Shopping, Vila Nova de Gala	56,500	1995
Gala Shopping, Vila Nova de Gala	56,500	1995
Centro Vasco de Gama, Lisbon	47,000	1999
Oeiras Parque, Oeiras	40,000	1998
Algarve Shopping, Guia (Albufeira)	40,000	Opening 2001
Forum Algarve, Faro	35,000	2000

Source: Eric van Leuven, Head, Healey & Baker Portugal, Lisbon, "Portugal," THE RETAIL GUIDE TO EUROPE AND THE MIDDLE EAST (London: Property Week, 2000), p. 82.

Some of the most prominent Portuguese food retailers are Continente, Modelo, Bonjour/Champion, Dia (Sonae Imobiliera), Feira Nova, Pingo Doce, Rechelo (Jeronimo Martins), Pao de Acucar, Jumbo (Auchan), and Carrefour. Major non-food Portuguese retailers include Sport Zone, Max Office (Sonae), Zara (Inditex), FNAC, Aki, Cortefiel, Benetton, and Mango. While many foreign retailers have entered the Portuguese market, some Portuguese retailers, including Sonae, Jeronimo Martins, and Throttleman, also operate stores abroad.

A relatively large number of foreign retailers, approximately 200 - that include chain stores - have been attracted to the expanding consumer market. The strongest foreign retailers, defined by number of outlets, include Multiopticas, 5-a-Sec, Benetton, Intermarche, Mango, 0 Boticario, Pingo Doce, Zara, and McDonald's. Close to one third of these foreign retailers have been seeking to expand their Portuguese business in recent years.

Office Buildings

Traditionally most major office buildings were located in central city areas such as the center city of Lisbon. Today, due to the difficulty of acquiring a central city site and then getting planning permission to proceed with building renovation or construction, most office buildings - like shopping centers - are being built on the edge of cities and in the suburbs.

Difficulties related to office building construction include earthquake-prone conditions and the multiple hills of the capital city, Lisbon. Hills often mean that rock is close to the surface and runs to great depths underground. Foundations are generally more costly as earthquake-resistant building methods must be used and as foundations must be dug through rocky terrains.On the positive side, Portugal has natural resources that favor local building construction. Marble, granite, and limestone which are key office building materials, are quarried in Portugal. Cement is produced in substantial quantities; cement is one of the key office building materials worldwide. The forests supply lumber as well as pulp wood for paper products.

Construction labor and management is generally available. Many engineers are graduated by the universities, colleges, and technical schools every year. One problem about the availability of unskilled construction labor is the ever-present temporary migration of unskilled Portuguese labor to central Europe for the many major building projects there. At the same time, immigrants from the former African colonies keep moving to Portugal, the country whose language they speak.

Marketing Real Property Interests

Groups of professional people, employer guilds, and employee unions were first recognized by the national government in 1956, but real estate associations were not recognized until 1962. The term, "mediadore" or "mediador autorizado" was introduced for an authorized agent in real estate transactions. No individual may represent another party in a real estate transaction unless he has qualified as a mediadore as defined by the Ministry of Finance. The *Gremio Nacional dos Mediadores*, the real estate guild or association, was organized. All authorized real estate agents were required to hold membership. A number of real estate offices in Portugal have qualified for membership. This group has been affiliated with the International Real Estate Federation, FIABCI, that is headquartered in Paris. Today, the licensed real estate agent may be a member of a professional association such as the Associacao de Mediadores Imobiliarios (known as "AMI"), Sociedade de Mediacao Imobiliaria or the Associacao dos Mediadores do Algarve (known as "AMA"). The client may also be better protected if the agent is a member of an international organization such as the European Federation of Estate Agents. Although real estate agents in Portugal are licensed, they generally are not regulated, they do not face requirements for holding professional indemnity insurance, and they are not bound by consumer protection legislation. The rules for estate agents also apply to foreigners, who cannot sell Portuguese property interests without a full Portuguese license. Additional individuals transact real estate business without meeting the government's requirements; in other words they are not licensed. They contend that they do not serve as an agent to either party to a transaction, but merely bring the parties together or sell their own properties. They may individually be listed in business directories as proprietors that buy and sell real properties.

The mediadore is authorized to serve as an agent in property transactions, in financing, and in appraising. Property management has not been a recognized real estate specialty business by the government and the public, but property management services are acquired particularly by those who keep a second home in a resort area in the Algarve district or to the east of Lisbon on the Atlantic shoreline. A few large real estate firms engage in construction, land development, and real estate agency. Real estate agent commissions associated with home sales range from five to ten percent of the sale price, according to David Hampshire, the author of BUYING A HOME IN PORTUGAL. Healey & Baker Portugal state that real estate commissions for commercial property sales run from one to 2.5 percent of the sale price. By tradition, most commissions are paid by the seller.

Quite often foreign buyers of Portuguese real property utilize the services of estate agents or real estate brokers and salespeople in their home countries who have Portuguese real estate affiliations. This particularly tends to be true of British purchasers of Portuguese second homes

Property Law and Leasing

A form of the civil code rather than common law is the basis for Portuguese law. Solicitors or attorneys are employed to carry out real estate transactions. But notaries public are particularly instrumental in the registration of new real property ownership. The registration of a new property title is required for legal conveyance of title. The notary system of Portugal is much like the notary systems of other countries of Europe. The Portuguese government has exercised its powers of involuntary acquisition of companies including their real estate holdings in past centuries. The compensation for the government's acquisitions has been questioned at times; the price paid the earlier owners may be relatively low in comparison to the going market value of the acquired properties.

Tenant Tenure, Rent Control, and Leases

Tenant tenure has been very strong until recent years. The government has enforced tenancy rights for tenants that has guaranteed long-term space use as long as the rent was paid. Rents were essentially frozen for about 50 years prior to the new era. Today some smaller tenants in center city rental units exercise considerable tenant tenure rights as they continue to occupy space that they occupied when the tenant tenure rights were liberalized immeasurably in favor of the landlord. Today lease terms run from three to five years with free rent possible up to three months. The landlord and tenant are permitted to negotiate the terms of the lease including rights to terminate the lease. No security of tenure tends to exist at the end of the initial term of the lease. The tenant can terminate the lease after giving 90 days' notice of vacation of the premises. Many foreign real estate market participants abhor the relatively short 90 days' notice period.

Rent Adjustment and Tenant and Landlord Lease Obligations

Rents are usually increased annually on the anniversary date of the initial lease signature, according to government legislation. The lease contract establishes the indexing system to be used in changing the rent for the coming term. The lease generally reflects 75 percent to 100 percent of the change in the agreed upon index. According to the lease, the tenant is usually obligated to take care of the internal repairs and insurance while the landlord is obligated to take care of the external repairs and maintenance and insurance.

The government continues to subsidize rents for lower income households. Young low-income couples have particularly benefited from this government program. But the elderly population of Portugal may be benefiting also. The elderly population is increasing in percentage of the total population.

Recent Comparative Occupancy Costs

Let us briefly review office, retail, and industrial rents as well as some total occupancy costs.

Office Rents and Total Occupancy Costs

At the beginning of the new millennium, rents rose 2 to 3 percent a year dure to the scarcity of modern, spacious office space for new domestic and foreign businesses and for the expansion of office space of existing businesses. The general worldwide economic slowdown has probably reduced the rent increase. The total office occupancy cost per square foot per year has been estimated around Euro 28 per square foot or nearly 300 Euro per square meter. In U.S. dollars, the total office occupancy cost per square foot in Lisbon has approximated $ 32 to $33 per annum or about $ 350 per square meter per annum. During the second quarter of 2000, various sources of global data quoted in <u>Global Real Estate News,</u> a newspaper published by the Internation Real Estate Institute, estimated Lisbon office rents per square meter per annum at Euro 251 or U.S. $223.

Retail and Industrial Rents

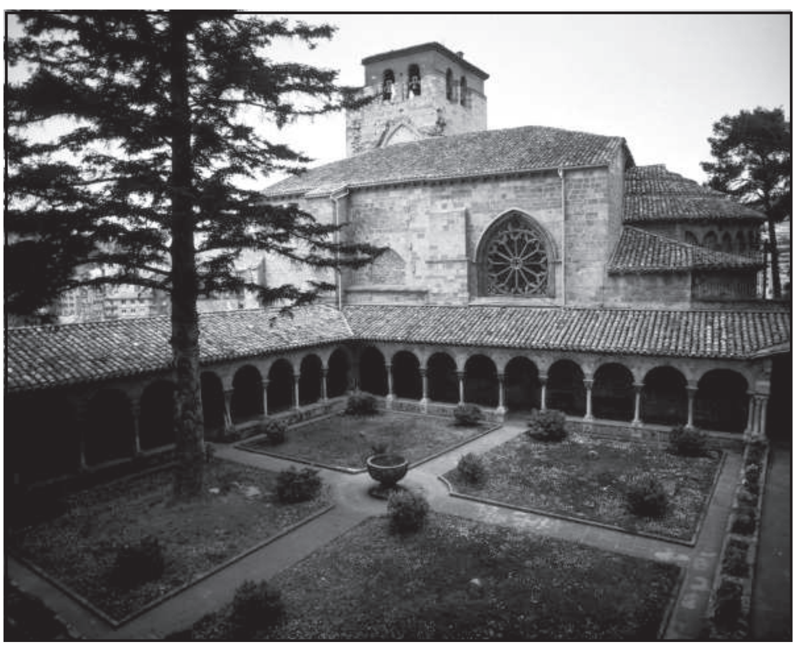
According to the recent <u>Global Real Estate News</u> source, rents for Lisbon shops in the second quarter of 2000 have been estimated at Euro 1,197 or U.S. $ 1,195. Industrial rents for the Lisbon area have been estimated Euro 75 or U.S. $65 per square meter per annum.

Real Estate Finance

As the demand for real estate finance in this economically prosperous period, an increased amount of funding for mortgages has been made available. The various types of banks are particularly strong sources of funds for commercial, industrial, and residential property finance. Even though pension assets have been rapidly increasing, the real estate sector may or may not be benefiting from this expansion. Pension fund assets are increasing due to the higher incomes received by employees and due to the continuing contributions as percentages of salaries and wages of both the employees and the employers into the Provident Fund for pension fund disbursement.

Principal Sources of Mortgage Funds

There are two main types of banks in Portugal: the clearing or commercial banks and the savings banks. The Banco Commercial Portuguese banking group owns Banco Portugues do Atiantico. The Champalimaud Group owns the Banco Totta e Acores and Banco Pinto e Sotto Mayor. The Banco Espirito Santo banking group owns Banco Espirito Santo e Comercial de Lisboa. The largest credit institution, measured by total assets is the government-owned savings bank, Caixa Geral de Depositos. A few foreign banks have competed with the domestic banking companies; more foreign banks are encouraged to enter the market due the recent changes in EU regulations that allow any bank trading in one EU country to trade in any other EU country.



From a history of inefficiency and slow transaction management, the banking industry has readily adopted electronic banking and customers have learned to use and appreciate automatic teller machines (often abbreviated "ATMs") Portugal has a well developed supermarket banking network. The banking outlets in supermarkets rely on telephone banking for personal banking services. Even though many ATM machines are well used, there are no drive-up banks in the country.

Off shore real estate ownership and financing is encouraged by the need of foreigners to avoid the withholding taxes on cash remittances, to reduce the incidence of business and personal income taxes including avoidance of payment of the Portuguese transfer tax (often abbreviated "SISA"), the inheritance tax, and the capital gains tax. Offshore banking centers are located in such tax havens as Gibraltar, the Channel Islands, and the Isle of Man.

While large commercial and industrial project financing has long been available from the Development Bank of Portugal, home mortgage financing has become more available at more reasonable interest rates and on longer terms at the domestic and foreign banks, including the offshore banks. Sale lease-back financing is available for residential, commercial, and industrial property finance. Mortgage loans (hipotecas) are customary for home financing. Nonresidents may find mortgage financing available at domestic banks, but the terms may be more conservative than those terms offered residents. The length of mortgage loans may be shorter when the loans are acquired from offshore sources including foreign banks. Many nonresidents, therefore, often finance their Portuguese properties through home-country financial sources. It is recommended, though, that the Portuguese tax ramifications of external ownership and financing be explored before finalizing transactions.

Usual Home Mortgage Terms

The maximum percent of value for a home mortgage is normally 75 percent though loans representing 50 to 60 percent of value are more usual, particularly on mortgages acquired by nonresidents. The normal term of the home mortgage is 15 years, but the contract repayment period may vary from 5 to 20 years. The repayment period for nonresidents may be shorter. Standard repayment mortgages are the most common in Portugal, but endowment and pension-linked mortgages are also underwritten by the various lenders. Mortgage rates are declined recently to approximately seven percent.

Additional Costs Associated with Mortgage Financing

Additional expenses are associated with establishment of a mortgage for financing a residential property. If you are buying a property and obtain a 75 percent loan-to-value mortgage, you will pay 25 percent of the appraised value as a downpayment plus around 10 to 15 percent in fees, according to David Hampshire, the author of BUYING A HOME IN PORTUGAL. All lenders charge an “arrangement fee” of one to two percent. The lender may include a commitment fee and an administration fee, which may approximate one percent of the mortgage amount. Even though the Portuguese lender may not require a survey, foreign lenders on Portuguese property usually require a “valuation survery.” The fee for the valuation survey may be called an appraisal or caluation fee.

The legal fees are usually one to two percent of the purchase price for an average property. The actual amount depends on the work involved and the charge per hour for the needed work. Hiring a lawyer is an option, but is highly recommended.

Notary and Registration Fees

According to Healey & Baker Portugal, the notary and registration fees each run about one-half of one percent of the sale price. The notary fees are fixed by law and are based on a sliding scale that depends on the sale price. The notary fee may be around 1.25 to 1.5 percent of the value listed on the registry. A tax card with the taxpayer’s fiscal number on it must be presented to the notary before a property transfer is regisered. The notary will not proceed with his or her tax obligations. The notary accesses the taxpayer’s fiscal number that is displayed on a tax card. Before you can register a property in one’s name, a document must be issued by a notary. The fees payable to the Public Registry Office for property registration may amount to 0.3 percent of the value of the transaction.

Construction, Refinancing, and Foreign-Currency Loans

Lenders make construction loans for proposed properties, but usually require developer ownership of the land in advance of the financing. Typical construction financing usually entails lender payment to the builder in installments as various stages of the construction project are completed. Lenders usually require a life insurance policy and building insurance during the life of the mortgage. Mortgage refinancing is available as are foreign currency loans. The foreign-currency loan will carry with it exchange rate risk over time that may increase or reduce the cost of the financing depending on the exchange rate trend.

Important Aspects of Portuguese Property Taxation

The landlord pays the local government an annual occupancy tax that is 1.3 percent of the registered value of the property. The registered value is usually much lower than the market value of the property. The transfer tax runs 10 percent. For year 2001, the sliding scale for the residential property transfer tax called for no tax on property transactions valued at less than euro 61,216,000 and up to 10 percent on property transactions valued over euro 169,376,000.

If the value-added tax (often abbreviated “VAT or ”IVA”) is payable on any part of the property transaction, the current rate is 17 percent. In Portugal, the value-added tax is formally called *Imposto sobre o Valor* Acrescentado often abbreviated “IVA” in Portugal.Generally, the sale and lease of realestate is exempt from VAT. But the value-added tax is levied on new properties purchased from a land developer and on the properties that are being sold for the first time. The government expects the VAT (otherwise labeled the "IVA") to be invluded in the advertised or agreed sale price and not added after the closeing.

Depreciation of buildings is calculated on a straight-line basis. But the rate for Dwelling houses and commercial and administrative buildings is two percent while the rate applicable to industrial buildings is five percent.

Annual Property Taxes

Property taxes or rates (contribuicao autarquica/CA) are levied each year on the land and buildings by the local authority (camara municipal). As mentioned earlier, the landlord pays this tax, not the tenant. Of course, the rent may be established so that the tenant actually pays the annual property taxes. This tax is based on the value (valor tributdvel) of the property is recorded on the registry. Before the revaluations of real property during the 1990s, the register value might be far lower than the current market value. Due to the recent revaluations, the register value is closer to the current market value.

Property tax rates depend on the nature of the property owned as three local government classifications are applied: urban real estate, rural property and a mixture of the two. The rate for urban real estate falls between 0.7 and 1.3 percent of the property's register value as set annually by each municipality. The percent of the property's register value as set annually by each munivipality. The rate for rural property, that is assumed to be non-building land outside an urban site and houses and buildings used strictly for agrculture and rural activites, is a flat 0.8 [ercent of the registry value. Notification of the amount payable is made between January and April by th Direccao das Contribuicaes e Impostos of the Ministry of Finance in Lisbon. If the tax payable exceeds Euro 149.64, the payment may be allowed in two equal instalments, the first in April and the second in September. If you have purchased a property and paid the transfer taz (often labeled "SISA"), the buyer may be exempt from paying propery tax up to ten years, depending on the property's registry value.

The central government imposes a stamp duty of 8 percent in general on the purchased and sale of real estate. Stamp duty is payable on a wide varietyh of items including records of movements of wealth, goods, or securites such as leases(6 to 10.56 percent) and morgages (5 percent.)

Capital Gains Tax

After January 31, 2002, capital gains taxes are payable on one half of the profit form the sale of real estate assets as well as certain other assets in Portugal. According to Ernst & Young in January, 2000, the capital gains rate in genral was 34 percent, the same as the corporate income tax rate. Capital gains realized by residents and nonresidents are taxed alike. Capital losses minus capital losses from the sle of shares and other transferable securities are taxed at a special raate of 10 percent. Capital gains from the sale of a principal home are exempt provided that the proceeds are invested in a new home, in a building, or in expanding a buiding, or in land for this purposes with th buying and selling of the propery and the costs for improvements and maintenance. Only 50 percent of the capital gain from the sale of real estate acquired since 1989 is taxable.

Corporate and Personal Income Taxes

As of January, 2000 the corporate income tax rate is generally 30 percent. In addition, corporations are faced with a municipal income tax surcharge of 3 percent. The withholding tax on dividends paid to nonresidents and residents is 30 percent, but subject to double tax treaties. By double tax treaty with the United States, the withholding rate applied to U.S. taxpayers is 50 percent of the regular rate or 15 percent. In like manner, the withholding tax rate applied to U.S. taxpayers is 15 percent for both interest and royalties paid.

Progressive rates that range from 12 to 40 percent applied to personal incomes as recently as 2002. The following table shows the chief personal income tax factors involved:

Taxable Income In Euros	Tax Rate (%)
Up to Euro 4,100.12	12
Euro 4,100.12 5to Euron 6,201.42	14
Euro 6201.42 to Euro 15,375.45	24
Euro 15,375.45 to Euro 35,363.52	34
Euro 35,363.52 to Euro 51,251.48	38
Over Euro 51,251.48	40

Real Estate Investment Considerations

Let us review Portugal's place in international country credit ratings, its foreign direct investment trends, and some evidence of real property yields in terms of prime office, high street retail, and shopping center space, shops in general, and industrial space.

Portugal's Place in the International Country Credit Ratings

In the 145 countries rated by Institutional Investors analysts, Portugal was ranked 20th in both 2000 and 1999 with a score of 79.7 of a possible 100 points in 2000. In comparison, the first ranked country in 2000, Switzerland, had a credit rating score of 93.8. Germany and the United States tied for second place with the score of 92.9. Spain, Portugal's companion country that also shares the Iberian Peninsula, ranked 19th in the group of 145 countries surveyed with a score of 80.4. Therefore, Portugal definitely earns an above-average credit rating in the competition with other advanced economies. Real estate investors may find this a significant indication of investment worthiness.

Foreign Direct Investment Trends

Portugal has received large inflows of foreign direct investment, part of which has involved real estate, direct investment, since 1990. The inflows have varied over the decade. In 1990 and 1997, Portugal received U.S.$ 2.5 billion or more direct investment funds. The year of the lowest flow of funds during the decade, 1995, represented only a little over U.S.$0.5 billion in foreign direct investment. The estimate for 2000 foreign direct investment has been U.S.$1.5 billion. In 2001 this flow of funds into Portugal is expected to be U.S.$1.7 billion.

Prime Office Yields: Recent Trends

From 1993 through 1999, prime office yields for Oporto exceeded those for Lisbon, according to DTZ estate management research. Lisbon, the capital, is the preferred city of the two urban places for major foreign investors. Therefore, we note that Lisbon prime office yields reached 10 percent or more from 1993 through 1998. Lisbon's office yields declined to approximately 9 percent in 1999. Generally Oporto's prime office yields exceed Lisbon's by approximately 2 percent. In year 2000 Lisbon's prime office yields ranged from 7 to 7.25 percent, according to several estate management company sources. The competition among domestic and foreign investors for Lisbon's prime office buildings while the vacancy rate was quite low probably forced the investment yields down from the 9 percent area of 1999.

Retail- and Industrial Investment Yields

Since shopping centers are relatively new developments in the prosperous Portugal economy, we are not surprised to note that shopping center yields (7.0 percent) in 2000 have been lower than retail high street property yields (7.50 percent), according to Jones Lang LaSalle Portugal. For example, Commerzbank of Germany invested in three Portuguese shopping centers recently. The domestic and foreign demand for the shopping centers has probably driven down the investment yields. A group of leading real estate consultants generalized for "shops in Portugal" the 2000 investment yields of 6.75 percent. As consumer spending as reached new heights in Portugal, retail space owners have raised rents and realized higher sale prices for their space.

Industrial space yields have been estimated for 2000 to range from 9 to 10 percent. The comparison of industrial space yields with office and retail investment yields often shows that industrial yields exceed those of the other two real estate sectors. We just noted that retail and office yields ranged from 6.75 to7.5 percent, significantly below the industrial yields at 9 to 10 percent.

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