

SPECIAL REPORT

Bali leasehold



“ LEASEHOLD TITLES, PARTICULARLY IN THE SOUTHERN PARTS OF BALI, OFFER BETTER LAND OPTIONS WITH LESS MONEY DOWN. ”

SOMETHING BORROWED, SOMETHING NEW

FREEHOLD TITLES IN SOUTH BALI HAVE BECOME PROHIBITIVELY EXPENSIVE LEADING TO AN INCREASE IN THE DESIRABILITY OF LEASEHOLD OPTIONS. NOT ONLY FOR FOREIGNERS, BUT ALSO FOR INCREASING NUMBERS OF INDONESIAN BUYERS.

| by **THOMAS JONES**

The merits of freehold property are obvious. It allows the security of owning of a piece of land, safe in the knowledge that it is yours to enjoy, build upon and pass on as you see fit; and most importantly, to enjoy the capital appreciation on the land, which in Bali has been very dramatic in recent years, leading to vast profits being made by early investors.

Ironically, as freehold land prices in the most popular areas of southern Bali have increased almost beyond comprehension, many new investors now find themselves priced out of the market. In an environment like Seminyak, where freehold land titles are limited as Balinese landowners have realised that by leasing the land they can hold onto it as their birthright and still enjoy an income, leasehold titles are definitely becoming a more attractive investment for commercial developments, such as hotels, entertainment venues or rental villas.

Domestic investment flows

With the rapidly increasing amount of domestic money flowing into the Bali market, an interesting phenomena is developing; Indonesian citizens are now buying leasehold titles, something unheard of in the past. Unlike foreigners, Indonesians have full rights to buy freehold, but with freehold land plots becoming extremely rare, opening the mind to leasehold titles provides the commercial buyer with better and more affordable options for more attractive land packages.

“Leasehold titles, particularly in the southern parts of Bali, offer better land

LAYAR
SEMINYAK

SPECIAL REPORT

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options with less money down," according to Dominique Gallmann, founder and CEO of Exotiq Property in Bali. "In the past there was no way an Indonesian buyer would even consider buying leasehold. But now, for the first time in the history of this office we are selling leasehold titles to Indonesian citizens," he says. "In the past we would never have thought about approaching an Indonesian client with a leasehold investment proposition. We have just sold our first big piece of investment land to an Indonesian buyer."

Indonesian investor, Widi Ariwibowo purchased a villa in Seminyak through Exotiq Property to operate as a rental investment, and was more than happy to take it on leasehold title. "The property was a great short-to-medium term investment alternative to freehold and was much simpler than buying freehold, especially beneficial for on-selling," he says. "I bought it with a 25-year lease and a 25-year extension at a pre-agreed price, plus 25 further years at market price and I was able to make a tidy profit on the resale, which helped in the purchase of bigger property. Of course, as the book value of the lease decreases, you need to closely watch the stream of income and the market value of the lease. Being in a prime, fast-growing area with a great management programme already in place and a strong turnover in guest rentals was a deciding factor in the buying and then reselling of the property. I also had the added luxury of enjoying staying in a beautiful villa when I wanted."

Other leasehold opportunities attracting foreign buyers

PRIVATE VILLA PETITENGET

are those offered in larger developments such as Double-Six, Seminyak by PT Paradise Investasti (Made / Kadek Wiranath), a low density development consisting of five levels, with 146 one- and two- bedroom units of varying sizes and layouts. The development includes eight penthouses and all units are available to purchase for an exclusive lease period of 47 years, bank backed with guaranteed ROI of 6 percent for three years, six years and 10 years respectively. The development also offers buyers the option to enter a rental pool from the beginning of the term and not take guaranteed returns with prices ranging from US\$295,000 to US\$3 million.

Key considerations

The benefits of leasehold on Bali are simple. Apart from opening up a wider selection of land choices, it also allows for a less expensive outlay. If an investor were to purchase a freehold plot in Seminyak they would have likely put down IR2 billion (US\$206,186) up front to build a hotel. But if they were to lease the land for IR20 million (US\$2,061) a year and pay 25 years with two extensions of 25 years taking it to 75, or even 100 years, then they would not have to deposit so much money up front. They then have the ability to look at cash flow options and future values and see which is a smarter option. This also allows them to consider devaluation of the asset: no hotel is built to last beyond a 30 years lifespan without a major refit. This also gives them flexibility in choosing the pieces of land they want. If the leasehold plot is better located they can easily, and

SPECIAL REPORT

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safely, take the leasehold.

When acquiring a leasehold property it is imperative to carefully examine how a contract is written with careful considerations given to pricing and lease extensions. The strength of the lease, for both parties, all comes down to the wording in the contract.

"When some of the first leasehold agreements were made (in the 1980s) some of these leases were rented for as low as US\$100 per are, per year," says Gallmann, adding that many were written up very loosely with a small stock phrase that stated that the lessee had first right of refusal over the new contract; something called *hak prioritas*, with conditions to be decided later. "As these contracts have come up for extension some Balinese people have simply refused to extend or demanded over-inflated prices," Gallmann says. "As a result there are many stories of people being forced to simply walk away from their, sometimes quite substantial investment."

Some investors at that time, however, did see the writing on the wall and made sure contracts stipulated precisely that they would be renewed, including both the duration of the lease and extension, pegged to commodities like gold or to the fair market price. This strategy is now fully in place for new leasehold contracts.

Ingo Mueller of international advisory and law firm Limcharoen in Bali advises all his clients to leave nothing to question. "With all new contracts it is strongly advisable to have a

DISINI VILLA

specific reference to the duration of the contract and the number of permissible extensions and to either fixed at the time of signing or have a fixed mechanism in place to determine price," says Mueller. "Gold prices are a relatively strong indicator of price taking into account that market prices here are quite exceptional by international standards," he says. As for determining market price, there is no government agency doing valuation so it is best to include a clause where an independent agent will be brought in to value the property. "One way is to appoint an independent valuation expert or property agent who will work out current market prices based on what has sold in the area of a similar size and aspect," he advises. "If the two parties cannot agree then two agents will be appointed and the median price shall be taken."

Will these contracts stand up in court if challenged? "These are legal documents protected by the laws of Indonesia," says Mueller. "When the contract is silent then you are in a weak position and the landowner can refuse to cooperate. But as long as the contract is worded strongly then the land lessee is in a position where they can unilaterally exercise his or her rights to keep the use of the land."

Future proofing

On the whole, the property market on Bali is looking healthier than ever, particularly in the high demand areas of south Bali that are strongly performing. Infrastructure developments such

SPECIAL REPORT

Bali leasehold



as the airport expansion, the new underpass at the Simpang Siur roundabout linking Bali's main bypass roads, and the new elevated toll way, which is being built out through Benoa Harbour and linking both Nusa Dua and the main road to Sanur in the east are all underway. These are expected to have a great impact on easing entry to the island and the relentless traffic that can plague Bali's roads during high season. All are seen as strong indicators that the Indonesian government, both national and local, is serious about the needs of Bali in attracting foreign and domestic investment. Both will be finished before the APEC summit being held on the island in October 2013, which will be placing Bali firmly in the world spotlight.

The prevailing school of thought that leasehold land loses value with each passing year can be offset by the fact that the rising value of the land or improvements of any structures on the land can, in certain situations, offset time driven depreciation. Having a rock solid extension clause placed into the contract means the asset will not lose value and will remain an attractive proposition for future on-selling. ■

DOUBLE SIX
BALI

LEASEHOLD

Pros

1. It's cheaper — a 25 year lease is roughly 40 percent of the freehold price.
2. No tax on the transaction for the buyer of a leasehold.
3. No nominee needed. Straight deal between foreigner and land owner.
4. More selection in today's market.
5. Capital gains can be realised on a longer than standard lease term if resale is part of the strategy.

Cons

1. Resale can be tough if the lease ticks down below 18-20 years.
2. Little or no capital growth on a lease of less than 25 years.
3. Older leases do not guarantee a lease extension.
4. Risk that the landowner or his family will not extend if a guarantee is not written into the lease.

WHAT'S OUT THERE?

A few examples of leaseholds are on offer in the Oberoi Road area include at the large end of the scale, a 3,500 sqm plot offered at around US\$1.4 million, perfect for a hotel development, and a 700 sqm piece of land at around US\$280,000 — both for 28 years with a 25 year extension with certificates, access roads and utilities on site. These plots are selling at the same price of IDR14 million (US\$1,443) per 100 sqm, showing the consistency of the pricing in the area. As for villa investment a three-bedroom, 225 sqm dwelling on 650 sqm of land in Petitenget within a gated community is selling at US\$790,000 on a 44-year lease with a 40 year option, making for a great long-term rental investment. <http://exotiroperty.com>