

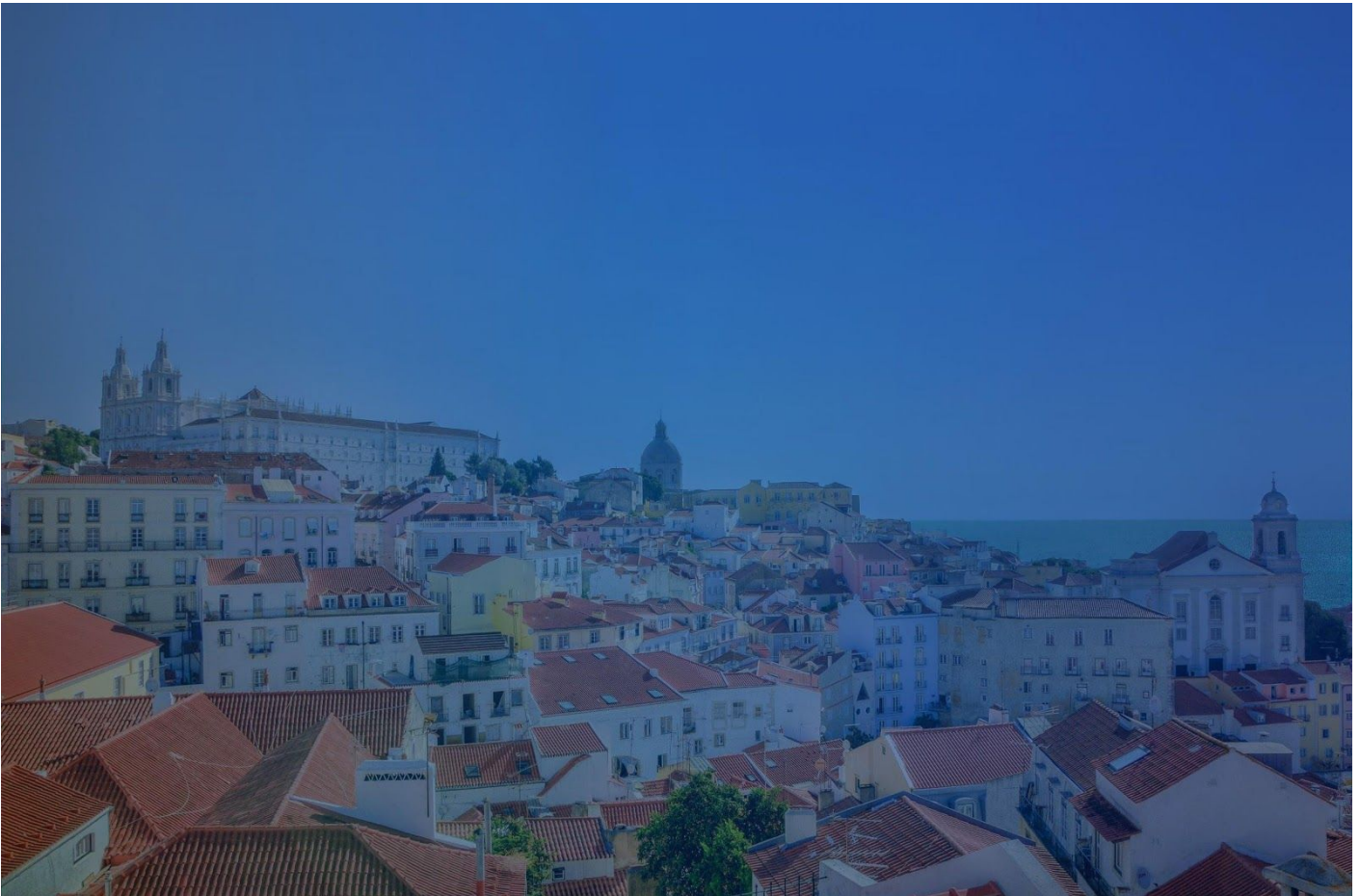


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# Complete Guide to Real Estate Investment in Portugal

Marcio Fenelon  
March/2019



1. The cruise flight to the Portuguese market
2. The potential earnings for real estate business
3. Financing
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5. Documents and legal security

## To the Reader,

There is nothing more satisfying than investing in a market with liquidity and where prices are increasing, just like Portugal in recent years. It increases the confidence of investors and entrepreneurs, who can cash their assets quickly and profitably.

Portugal has become an extremely attractive country to invest in and develop new business or services. There is a lot of money rolling between commissions, salaries, fees, rents, and sales.

Brokers can close deals and receive good commissions, due to the high demand that makes sales very easy.

Architects have their agenda full of new projects, especially renovations of historic buildings. Interior designers and decorators are also very popular recently.

Contractors receive new quotes requests every day and are always looking for bricklayers, helpers, electricians, plumbers, tile workers, and painters.

Lawyers and accountants are very busy with opening new businesses, analyzing contracts and real estate documentation.

The touristic apartment managers receive good commissions to manage properties for short-term rental. This business triggers contracts for cleaning, maintenance, laundry, reception of guests and delivery of keys.

Investors have a higher probability of profit in Portugal than the average in the European and Brazilian markets with both the short-term and traditional long-term rentals.

Additionally, there is also the possibility of significant appreciation with the continuous attractiveness of real estate investment versus European financial applications.

Entrepreneurs are able to develop real estate projects with excellent profitability, both via sales or by keeping the portfolio of assets and their rents.

For Brazilian investors, the pressing market requires a tremendous capability of adjustment. Decisions need to be quick and accurate, among unrealistic and countless offers.

Good investments!

Marcio Fenelon

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# 1. The cruise flight to the Portuguese market

There is a combination of attributes that turn Portugal into an unbeatable opportunity for tourists, retirees, and real estate investors. Among the various reasons for the country's success, we highlight safety, hospitality, climate, taxes, touristic offer and low prices in general.

## Safety

It is a known fact that Portugal is much safer than Brazil, but it is surprising to find out that also the French, English, Dutch and Germans recognize Portugal as a safer place than their own countries.

In a world that worries about terrorism and violence, 99% of the planet's inhabitants should agree that Portugal is one of the safest places to live in. The only exceptions will be Iceland and Denmark, the two countries that were considered safer by **The Economist's** Global Peace Index.

## Willingness to welcome well

You can brag about your trip to Paris, but the best experience a tourist can have will always happen in Portugal. The waiter will try to speak your native language, make suggestions and wait with the most devoted patience for the meal order. Without rushing you. Plus, you will have to look hard to find a restaurant that serves bad food. And no one will be yelling at a tourist that does not understand the local language.

Hospitality is a matter of education and courtesy, which are important themes for the country. Portuguese are proud of its country, its food, traditions, architecture, monuments, and history. And they present these to foreigners with pleasure. It's like receiving a relative or a friend who is visiting your city for the first time. Portuguese might even get offended if you don't enjoy your stay. It is part of the culture that visitors must enjoy their experiences in this territory.

The chances of disaster are minimal. I repeat with a high degree of certainty that Portugal is an unbeatable place in what comes to hospitality and in the will to welcome people well, which are essential components to the success of tourism and to position Portugal as a destination for immigrants.

## There is no bad weather

Whether in winter or in summer, temperatures in Portugal are higher than in most European countries. The minimum temperatures are rarely below 10°C in winter and the maximum temperatures are usually around 30°C in summer.

Put yourself in the shoes of someone from northern Europe, where there are several months of rainy and cold weather. The sun goes down at 4 o'clock in the afternoon during winter. For these people, the most uncommon climatic event is a day of sun and heat, which is celebrated with long hours of strolls in the park.

Brazilians might find temperatures in Portugal very low in winter, but Europeans disagree. Living in a country with a hot, sunny climate is a blessing. It's something rare in their home country. And everything that is rare has a high value.

It is no wonder that there are legions of Englishmen living in Algarve, as well as French, Dutch and Germans in the streets of Lisbon, Oporto and Braga.

Portugal's climate is even more ideal from the point of view of all Europeans that come all the way from the north, with money on their pockets, to enjoy the south.

## The advantage of paying less taxes

Portugal took advantage of its severe crisis in 2009 to improve its competitiveness and positioning as an attractive country to live and to invest in.

One of the highlights was the Non-Habitual Resident Status. The name is horrible and confusing, but what matters is the result: tax exemption on all income earned abroad for a period of 10 years.

The impact regarding purchasing power and quality of life are overwhelming.

A French man can save up to 45% of his retirement in tax exemption. It represents a gain in purchasing power of up to 82%. A retirement of 3,000€ guarantees a middle-class lifestyle in Paris, whereas in Portugal, considering that a property was acquired and there are no rents to worry about, the € 3,000 monthly sum allows a life of walks by the river, restaurants, cafes, wine and much more. The same math can be applied to England, Germany, Sweden, Denmark, Belgium, Netherlands, Austria, Switzerland, and Norway, for example.

If we think about finances and quality of life, there is no better place to immigrate. So, I am glad to state that Portugal is an unbeatable place for those who want to make their earnings value more during their retirement.

Regarding real estate investments, the foreigner who arrives in Portugal will soon look for a house to live in. European retirees' money contributes a lot to the demand in the housing market, especially in the bigger Portuguese cities like Lisbon, Oporto, Braga, and Loulé.

## Low-cost flights

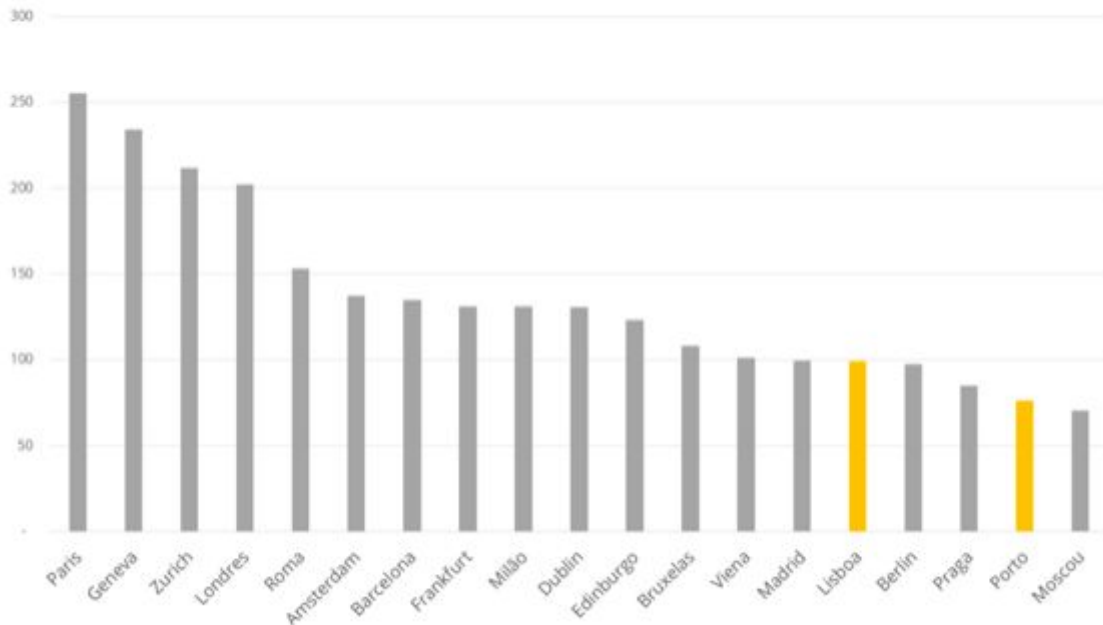
The phenomenon of low-cost airlines changed tourism. It is possible to travel between Oporto and Lisbon for 9€ (yes, you read it right, 9€ per trip) and also between Lisbon and Barcelona for only 30€.

The arrival of low-cost flights changed the entire dynamic of tourism in Portugal as well as in Europe, increasing the number of passengers.

At the same time, the cost of accommodation in Portugal is the cheapest in Europe.

## Hotels Daily Average Rates (€ / day)

Source: PwC



### Low cost of living

A complete meal at beautiful Salamanca (1 hour from the border of Portugal) will hardly cost less than 20€. In Oporto, I can list 20 different restaurants offering the same complete meal plus half a bottle of wine for only 5.50€.

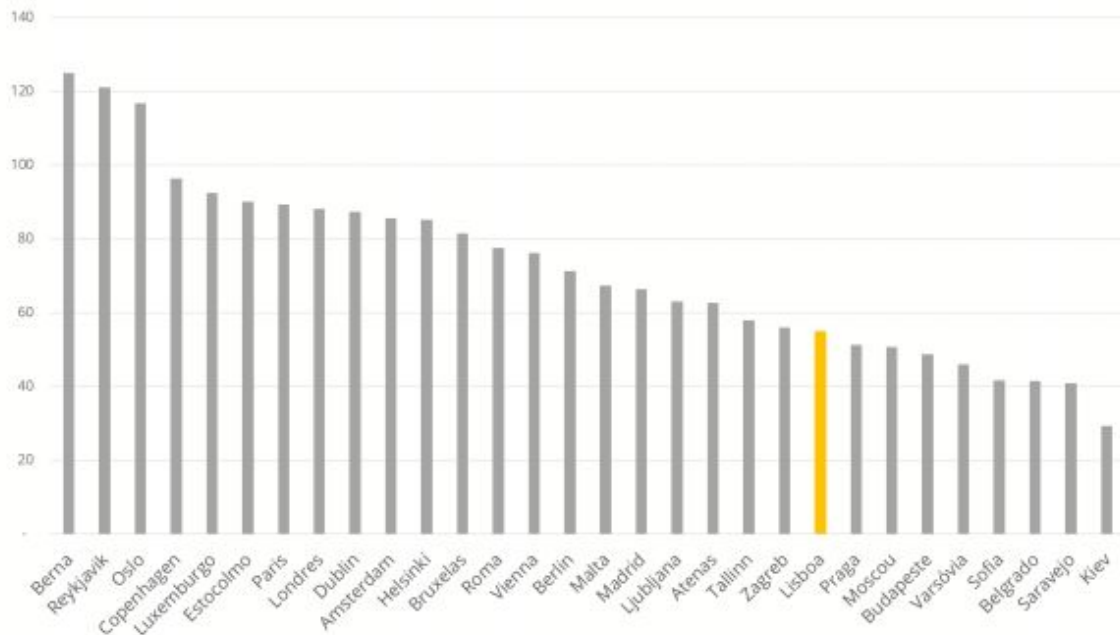
A couple with two children will spend 52€ more per day in beautiful Salamanca. The difference would be enough to pay for the flight ticket. It is very relevant. And it will always be like this when you compare other destinations to Portugal. The cost in Portugal is much lower than in other countries of the continent.

Buying a house in London is five times more expensive than in Lisbon. The beer is three times heavier in the pocket and the wine costs twice as much. For those who pay rent, London charges almost three times more.

It is true that you make a lot of money in London, which would justify a higher cost of living. But the ultimate best decision for a Londoner is to benefit from the English salary - through retirement - in the Portuguese cities, with its low cost of living.

The same assumptions are true for all the 21 out of 30 European capitals and for the residents of 99 other European cities that present a cost of living higher than the Portuguese capital.

### Cost of Living Index



Source: Numbeo

### Diversified touristic offer

Portugal is a country of history, architecture, and discoveries. Even for a European citizen, who is used to historic sites, the Portuguese cities are above average. The narrow streets, the countless hills, the unique architecture, the tram, and the Manel’s restaurant all together form a unique and original experience that everyone desires.

To top it all off, you are a few minutes away from the beach using a car or a train. And it is not a lousy one. White sand and all. Sceneries taken from northeastern Brazil’s beaches.

Just don’t expect hot water, that would be asking for too much. But from the north to the south, the coastline is a show of landscapes worth seeing.



And yes, some beaches are very good for surfing. Even too good in my opinion. Nazaré is the home of world championships for giant waves. Portugal also has many sites for wind-based sports such as windsurfing and kitesurfing. More, there are river beaches. Sand and clean, crystal clear water with space for everyone. In the countryside, there are mountains, plains and vineyards to enjoy.

To prove it is acting on all fronts, Portugal has snow as well. In the winter, you can go up the mountain to a ski resort in Serra da Estrela, which is also famous for its cheese.

Golfers are fanatic sportspeople. There is no middle ground. Either you play and you're a fanatic or you give up right away. To have the opportunity to play the entire year is a stroke of luck. Algarve's mild temperatures make it a dream come true for European golfers. Portugal was voted the best golf destination in the world in the last three years (Golf Awards).

Portugal is unbeatable, due to the combination of beach, countryside, golf, vineyards, mountain, history and architecture.

## Absurd competitiveness in real estate business

Find a country that offers the six conditions - safety, hospitality, good climate, favorable tax policy, low cost of living and broad touristic offer - and it is GUARANTEED the real estate market will be solid and active. Tourists will need beds to sleep in and immigrants will need homes to live in. As simple as that.

Portugal's value proposition, this is, the relationship between how much the country delivers and what it charges, is one of the best in the world. It is a high-level competitive positioning.

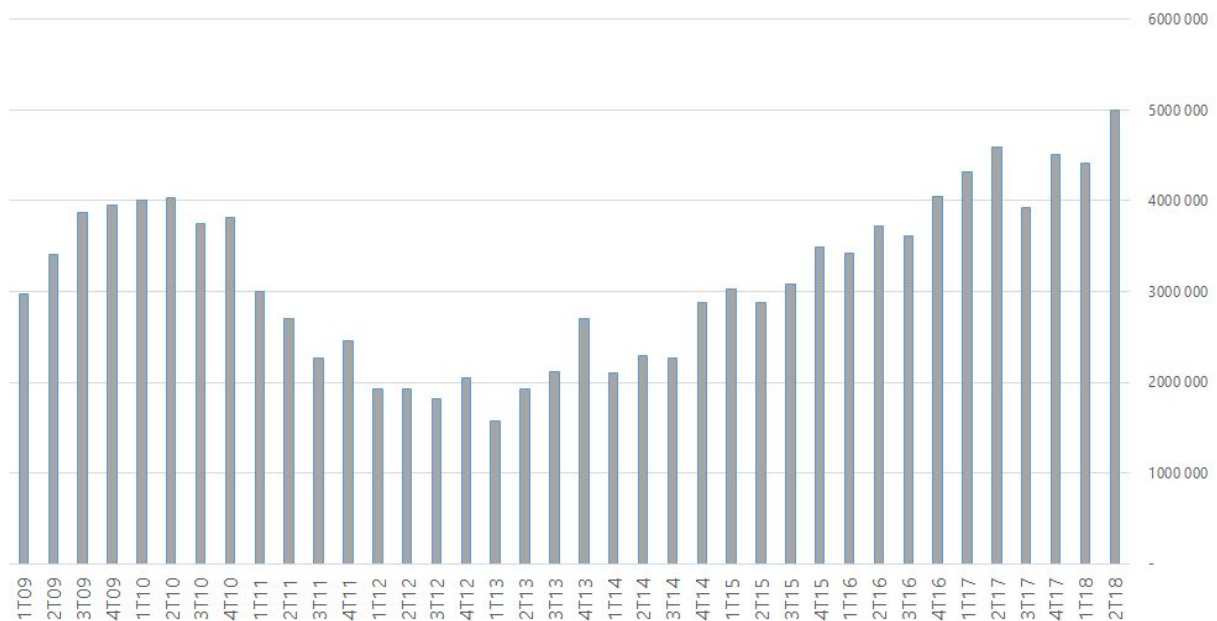
Denmark is safer, but the weather is quite hard, with very low average temperatures. The Swiss have better health, but the cost of living is one of the highest in Europe. Spain may have a similar climate, but it faces frequent problems with insecurity and terrorism. The Czech Republic has a slightly lower

cost of living, but it is not as great in terms of safety and climate. Malta has lower taxes but it doesn't have such a touristic offer.

## Real estate sales are growing like never before

There is nothing like a good volume of sales to motivate someone in the market. Portugal reported 5 billion euros in residential real estate transactions in one quarter of 2018, representing 2.5 times more than in 2012.

### Real Estate Transactions (€ millions)



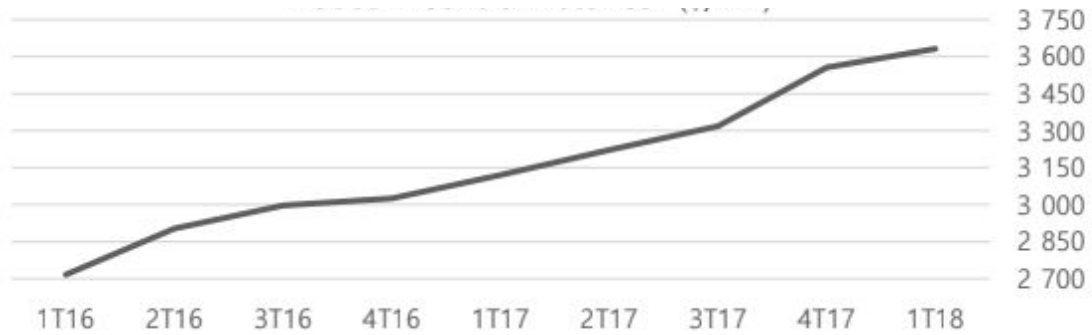
Source: National Statistics Institute

## Continuous price inflation

Real estate prices have understandably responded in a strong way. The city centers of Lisbon and Oporto have valued more than 46% since 2016.

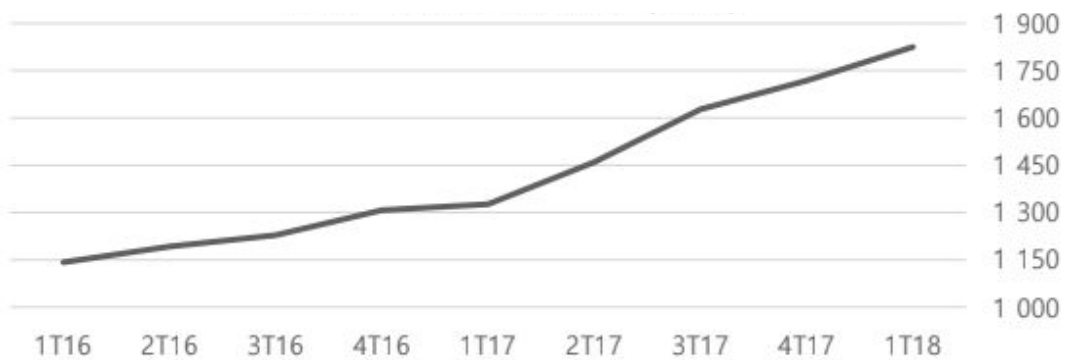
### Lisbon – City Center (\$/m<sup>2</sup>)

Source: National Statistics Institute



### Oporto – City Centre (\$/m<sup>2</sup>)

Source: National Statistics Institute



## 2. The potential gains in real estate business

A boiling market, filled with some good and some very good opportunities that depend on the investor's intelligence and capability to know where and how to act.

## Residential Properties for Rent

With the increasing demand of investors and foreigners and following several years without new property construction, Portugal is suffering a storm which is a perfect opportunity for those who are looking for a property to rent in the major city centers such as Oporto, Lisbon and Algarve.

Although the demand is huge, it is not explosive. But the fact is that the market has almost no offer. A property is often rented on the same exact day that it is put on an advertisement list. And no property in good conditions of conservation and with a reasonable price will take more than one month to rent.

It is a market with average yields (rent income divided by the investment) of 5.7% per year, being the minimum 4% and the maximum 10% per annum for the final purchaser of a ready-made property.

On the contrary, for the investor who wants to make changes or start a construction work, the property is even cheaper and the yield grows from 25% to 40% in comparison with a ready-made properties.

## Real Estate for Tourists (Local Accommodation)

Portugal underwent an economic transformation thanks to the growth of tourism. This growth was based on five major factors (i) low costs; (ii) safety; (iii) historical heritage; (iv) gastronomy and (v) diversified offer - beach, countryside and city.

With revenues growing 70% since 2011, tourism already accounts for 10% of the Portuguese GDP and is a major source of revenue for the real estate business.

The average Local Accommodation occupancy rate in main tourist centers is 78%, with average daily rates of 127 euros in Lisbon and 105 euros in Oporto. However, the potential return in Local Accommodation investments depends on the correlation between expected results and the investment made.

There are four major factors that will determine the profitability: location, management, taxation and conditions of the property.

Real estate in Oporto, for example, has a 40% higher expected return than Lisbon, since the square meter is much cheaper.

If you rely on a third party to manage a property, it will cost you, on average, 20% of total revenues. Those who don't have this expense and do the management on their own guarantee a return about 58% higher.

Regarding taxation, real estate properties located within urban rehabilitation areas (ARUs) can have a 40% reduction in income tax.

Finally, investing in a property that needs renovation will reduce the purchase price by approximately 20% when comparing to a new property.

The yields obtained are higher, around 8% to 14% per year, but also involves more expenses related to run a touristic property.

## Valuation Gains

The easiest strategy to take advantage of a vigorous market is to buy a property and wait for appreciation. It is a business of low complexity and with high probability of success nowadays in Portugal.

## Buying Properties Off-plan – 20% to 100% return

When someone buys a property off-plan, the goal is to capitalize the valuation gap resulting from the basic rule of real estate valuation - the closer to the delivery, the more valuable a property is.

The price difference between an empty lot and a ready and operating property is around 25% to 60% in Portugal.

In a dynamic market, a project with good quality that has been priced correctly will have a potential for valuation between 10% and 25% on delivery.

The advantage is that the investor can split the payment and give only 50% of the property to have access to 100% of the valuation. It is a way of leveraging the results.

## Rehabilitation and construction - 25% to 50%

Take a step forward in the real estate food chain and the prospect of return is even more interesting. Be a developer in Europe, buy buildings and lands, approve projects, enter the construction and sales business and capture even more value.

It is a more demanding activity in terms of capital and expertise, but with fantastic results in a strong currency market.

Buying some land or a building to renovate represents margins of 15% to 30%, which alone is already very good. To achieve even more attractive results, it is possible to obtain financing of 100% of the construction investment, although banks generally do not finance the investment for the land. This strategy can provide returns ranging from 35% to 90%.

## 3. Financing

Portuguese banks work very closely with foreign clients. The procedure for opening an account is extremely simple and the financing approval is frequently guaranteed to non-residents.

The competition between banks is intense, so it's worth checking which bank is offering the best conditions for your case.

Costs include the basic rate, known as Euribor - equivalent to Selic, an additional interest rate, known as spread, plus the costs of life insurance and property insurance and some administrative fees. In addition, banks include property and credit evaluation fees.

The APR is the mandatory disclosure rate in any financing offer and it takes into account all the mentioned costs. It is the best way to compare the different proposals.

Customers who have more than one service or product hired with the bank, such as salary domiciliation, credit cards, car insurance, and other applications have lower financing costs.

Banks analyze a credit based on three main criteria. First, the installments must represent a maximum of 33% of the income after taxes. Second, the higher the equity someone holds in Portugal, the safer the credit profile will be and the greater the chance of approval. Finally, chances of approval increase if there is one or more guarantors with equity and relevant income.

The maximum term of financing is set generally at 35 years, if the sum of the client's age and the term of the loan is below 80 years – in most cases.

The financed percentage varies from 60% to 90% of the property acquisition value, depending on the credit profile, the use of the property - investment, first, second or third home, place of residence and property evaluation.

Financing for non-residents is usually a bit more expensive, with a slightly lower term and a lower funded percentage.

The non-resident Brazilian can count on financing of 60% to 70% of the acquisition with spreads of 1.5% per year and a maximum term of 30 years in the current market conditions.

With such low costs, financing real estate in Portugal is a great investment. It is one recommended way of increasing the return on employed capital since the investments have a return that exceeds the cost of funding.

## 4. Taxes, fees, and other related

First, an alert: this text should not be considered as tax advice and does not replace a consultation with an accountant or a lawyer.

The nature of taxes and duties in real estate deals in Portugal is very similar to Brazil.

The IMT is dedicated to real estate purchase transactions just like ITBI does in Brazil. The tax rates vary from 0% to 8% depending on the use of the property and the value of the transaction.

There are several possibilities of tax exemption, and it is guaranteed that real estate companies can take advantage of exemption from the second year of

operation, if the company has made at least one transaction in the previous year.

The stamp duty is very similar to the Brazilian IOF, and is applicable to several financial transactions. In the acquisition transaction, the rate is 0.8%. And there will be an additional 0.6% tax levied on financed real estate, in case you have required this product.

All properties pay the IMI - the Portuguese version of IPTU - which rates are determined by each municipality. The average rate is 0.3% of the taxable patrimonial value, which is generally 30% to 50% below the market value.

There are cases where there is an additional IMI of 0.7% to 1% for assets exceeding 600,000 euros.

Upon receipt of long-term rent, an income tax of 28% is levied, while you may deduct IMI, stamp duty, condominium, real estate mediation, maintenance, and conservation of the tax base.

The taxpayer may also decide to be taxed for presumed profit - known as a simplified scheme - which assumes a 95% profit on long-term rental income. Non-residents pay a 25% rate in these cases. Therefore, the final rate will be 23.75% (95% x 25%) on revenue.

A property for tourism - known as local accommodation - can also be taxed under the simplified tax regime. In this case, the premise is a 35% profit, also with a 25% rate for Brazilians, resulting in 8.75% (35% x 25%) on revenue.

Alternatively, one can opt for organized accounting and pay taxes on business results, like any company does. Rates on profit will stay between 17.5% and 22.5% and it is mandatory to hire an accountant.

If the income from this activity exceeds 200,000 euros per year, it automatically falls under the organized accounting system.

All business activities pay a profit tax: 17.5% if profit does not exceed 15,000 euros and 22.5% on the other cases. In addition, unlike Brazil, a 28% tax is paid on distributed dividends.



It is required to pay VAT - equivalent to the ICMS - in the local accommodation activity at a reduced rate of 6%. To calculate the amount to pay, all the VAT already paid on purchases related to the operation is deducted, with a system of credits and debits very similar to the Brazilian ICMS. If you opt for the simplified scheme and you have annual incomes of less than 10,000 euros you can ask for VAT exemption.

The capital gains on real estate sales are subject to a rate of 28%. If the complete amount of a property sale is used to purchase another house (one's permanent home), to build a house or to purchase a building plot, there is an exemption of taxes. It is mandatory that the reinvestment of the earnings happens within 36 months after the transaction or 24 months before.

## 5. Documents and legal security

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### Reservation agreement

When parties reach an agreement, some sellers ask for a simple formalization which means signing a reservation agreement. This document contains a description of the property, the agreed purchase value and the identification of both sellers and buyers.

As a confirmation of will, the buyer will pay an entry fee. It is important to understand that this should be a small amount since we do not know anything about the situation of the property yet.

In Portugal, it is very common for the buyer to give a cheque to the real estate agent who will keep it as a security deposit, but without deducting it.

## Due diligence

Due diligence is a fancy title for the process of verifying the regularity of a property. The process involves checking the physical space, the statements given by the seller, and the certificates and other documents that can be obtained from various public records.

The first step is to verify that the seller of the property is its rightful owner through the Registry Certificate issued by the Land Registry Office.

The property must be unoccupied and with no goods or possessions of other people, such as a relative, a landlord, a squatter or a tenant. It is also necessary to check if there are machines or equipment that can disturb or prevent the property of being used as desired.

In certain parts of the country, the buyer must announce his intention of buying the property, via Casa Pronta website, so that public entities with a legal right of preference can express their intention to buy or not.

To reduce the risk of losing your property, or being charged by creditors, it is important to carry out an extensive analysis of debts and/or obligations that have pending payments. You can find this information in the Registry Certificate obtained from the Land Registry Office, or from the official tax document (Caderneta Predial) requested at the Finance office. Additionally, there is the need to check for the existence of debts of condominium, electricity, water, telephone, and gas.

You will need to verify the dimensions and borders of the property or land too. These need to be the same as those presented in the Registry Certificate obtained in the Land Registry Office; in the Technical Housing Document (FTH) obtained in the City Hall (for buildings built after 2004), and in the Housing License (buildings built after 1951).

Check the Municipality Master Plan (PDM) and verify if there are any public works or projects that can affect the value of the property and possibly harm it.

All properties put up for sale in Portugal must disclose an energy certificate, which is a document that evaluates the energy efficiency of a property on an A + (very efficient) to F (inefficient) scale, issued by authorized technicians of the Energy Agency (ADENE).

The list of main documents includes:

- (i) Identification document and tax registration number
- (ii) Registry Certificate issued by the Land Registry Office
- (iii) Official tax document (Caderneta Predial) by the Finance office
- (iv) Amount of monthly quota and condominium debts
- (v) Bills for electricity, water, telephone and gas
- (vi) Technical Housing Document (FTH) obtained in the City Hall (for buildings built after 2004);
- (vii) Housing License (for buildings built after 1951)
- (viii) Energy certificate
- (ix) Other necessary documents requested by the lawyer

## Purchase agreement (CPCV)

Although it is not mandatory, it is more than usual to sign a contract of goodwill between the buyer and the seller, known as CPCV. This contract establishes the negotiation conditions of the property.

The seller must ask for a deposit, again a residual value but somewhat higher than a reservation. In Portugal, the common practice is to ask from 5% to 20%.

A good Purchase Agreement describes the property, the equipment, the deadlines for delivering documents and the date for signing the Public Deed. It may contain terms that suspend the deal for a certain period until a problem or implication that appeared is solved. For instance, until the property is vacated.

## Public Deed

Public Deed is the notarial act that grants definitive and public character to the transaction of purchase and sale of a property. In other words, it makes it official and concludes the contract that was previously an intention to buy and sell.

The deed will be signed in the presence of an official entity representative (notaries, solicitors, or other). This is usually the moment to delivery the keys and the ownership of the property.

## Registration

The transfer of a real estate only ends when there is a proper record of the transaction in the Land Registry Office. While this registration does not take place, for all intents and purposes, the property is still owned by the seller.

## Deadlines

The usual deadlines for carrying out the procedures of formalization of the purchase of a property are:

- 1-2 days to obtain the Registry Certificate and the Matrix Certificate.
- 1 week to 1 month to receive the Housing License if the seller does not own it.
- 1 to 2 weeks to negotiate the terms of the Purchase Agreement.
- 2 to 4 weeks to sign the Deed and pay the balance to the seller.
- 1 month to end the transaction by registering the property at the Land Registry Office on behalf of the buyer.

## The Author



Marcio Fenelon holds a bachelor's degree in Business Administration from EAESP-FGV and two postgraduate degrees from Insper and Fipecafi-USP. He acts as a developer, investor and consultant in Portugal for the last 2 years. Marcio has 25 years of experience in Financing departments of large Brazilian companies and during the last 10 years was dedicated to the analysis and fundraising of real estate investments.

Marcio is the author of two books, several courses and countless reports with investment recommendations. Through his work, he acquired a strategic vision on which are the potentiators of successful businesses in different areas. Marcio has been involved in dozens of real estate projects for offices, residential purposes, subdivisions, shopping centers, and hotels.