Should You Buy or Lease Your Business Premises?

The decision to buy or lease a commercial property can be a difficult one for the 2.4 million actively trading businesses in Australia[1]. Even online businesses can grapple with production and warehousing property decisions, however the challenge comes when considering your budget, the current needs of the business and your plans.

There are many considerations – both quantitative and qualitative. It is important to carefully consider each when deciding on the right option for your business.

Leasing a property means you are not locked into a fixed location and have the flexibility to move and change premises when the lease ends (to expand or downsize). The downside of that is you have less control over the property itself and your capacity to potentially adapt with your growing business needs. Plus, of course you do not own that asset and therefore are not able to borrow against it in the future.

Can owning your business premises be a more viable option?

If you consider that commercial property interest rates are currently well below commercial property rental yields, it is quite possible that buying may be cheaper than renting.

Current commercial property interest rates are generally around 4.5%-6% commercially secured (but significantly higher for no doc options).

Conversely, current commercial property rental yields are largely between 5%-10% and possibly higher depending on location.

Therefore, if your business requires a $1 million premise to operate from, the interest repayments are likely to be cheaper than possible rental payments.

There are however other considerations. You will be unable to borrow the full purchase price and will be required to contribute security of between 20% and 50% towards the purchase. Consequently, you need to have available capital. In addition, you're likely to also be required to repay the loan principal over the term of the loan.

Should you have the capital available, it's all in the maths. Will your principal and interest repayments for say 75% of the property's purchase price be roughly the same as lease repayments? Even if they are slightly more remember these payments are also paying off your loan principal and creating more equity in the property that may be realised when you sell sometime in the future.

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It is also essential to consider that if you qualify for a loan, buyers of commercial property cannot access lenders' mortgage insurance. Commercial loan terms are usually much shorter – around 15 or 20 years for loans under $1 million.

If you are still unsure which option is right for your business, read our tip sheet on the pros and cons of leasing and buying commercial property.

As with all things, it is not all black and white.

Other factors can influence your decision to buy or lease depending on the type of business and the use of the property. For example, a car mechanic may need to seek landlord approval to fit out and spend a considerable outlay to the premises to allow for vehicle hoists, washing facilities and grease traps.

The answer to the buy or lease question will differ for every business depending on what type of business it is, stage they are at, budget and plans.

Here are some other questions to ask yourself as a business owner:

- Do I want to stay in the same location long term?
- Is my business likely to grow and need more room?
- Can the business cover the maintenance and management costs of an owned property?
- Do I want to tie up capital in a commercial property?

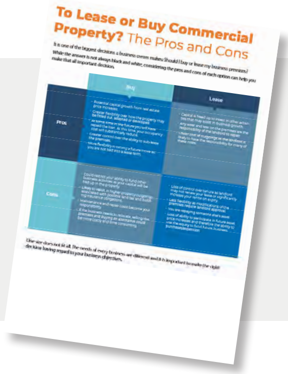
Non-property considerations

- It is also worth considering that when re-locating, be it to owned or leased premises, it can be quite costly to re-locate existing plant and equipment, particularly if these items are significant in scale.
- In many instances if these items are nearing the end of their useful life or becoming uneconomical to maintain relative to new equipment, it could be timely to update this equipment.
- The finance options for these items should also be factored into your plan to purchase or lease your next commercial premises.

Sources

1 Counts of Australian Businesses, including Entries and Exits, July 2016 – June 2020 | Australian Bureau of Statistics (abs.gov.au)

Remember to contact us to read our topic sheet on **'To Lease or Buy Commercial Property? The Pros and Cons'.**



To Lease or Buy Commercial Property? The Pros and Cons

It is one of the biggest decisions a business owner makes: Should I buy or lease my business premises?

While the answer is not always black and white, considering the pros and cons of each option can help you make that all important decision.

	Buy	Lease
Pros	· Potential capital growth from real estate price increases. · Greater flexibility over how the property may be fitted out, adapted or developed. · At some time in the future you will have repaid the loan. At this time, your occupancy cost will substantially reduce. · Greater control over the ability to sub-lease the premises. · More flexibility in timing a future move as you are not tied into a lease term.	· Capital is freed up to invest in other activities that may assist in business growth. · Any wear and tear on the premises are the responsibility of the landlord to repair. · Lower cost of outgoings as the landlord is likely to have the responsibility for many of these costs.
Cons	· Could restrict your ability to fund other business activities as your capital will be tied up in the property. · Likely to result in higher property outgoings associated with possible land tax and building insurance obligations. · Maintenance and repair costs become your responsibility. · If the business needs to relocate, selling the premises and buying an alternative could be more costly and time consuming.	· Loss of control over tenure as landlord may not renew your lease or significantly increase your rental on expiry. · Less flexibility as modifications of the premises require landlord approval. · You are repaying someone else's asset. · Loss of ability to participate in future asset price increases and therefore the ability to use the equity to fund future business purchases/expansion.

One size does not fit all. The needs of every business are different and it is important to make the right decision having regard to your business objectives.