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Guard against property crash

HOMEOWNERS who are worried that property prices might fall are using complex schemes to protect the value of their homes, *writes David Budworth*.

The investments allow you to bet that house prices will drop and, if you are right, your profit from the bet can offset the fall in the value of your property.

They also let investors gamble on the housing market without having to own a property.

Last week, Goldman Sachs, an investment bank, launched a service that allows you to speculate on house-price movements using covered warrants and certificates.

Mark Valentine of Goldman Sachs says: “Covered warrants and certificates provide investors with a means of hedging their exposure to the residential-property market.”

Homeowners in London and the south of England are already suffering from house-price falls, and prices are slackening in the rest of the country. Hedging is a way to minimise losses caused by price swings.

Imagine you want to sell your house, but are worried that the value may fall in the next year. You could buy a warrant that goes up in value if house prices fall. Any money you make on the warrant would make up for what you had lost because your house had dropped in value.

The warrants and certificates are linked to two Halifax house-price indexes. Each warrant has a call and a put.

You buy put warrants if you want the market to fall and call warrants if you think prices will rise — but the price movements have to happen within a specified period.

For example, if you think the average London house price will fall by the second quarter of 2004 you could buy a put warrant.

According to Halifax, the average house price in London was £220,525 in the last quarter — January to March 2003.

Last week, Goldman Sachs offered a £220,000 put warrant costing 28.3p, which gives you the right to sell the house-price index at the strike price up to, and including, August 4, 2004. If you bought 100,000 warrants it would cost £28,300. For each £1,000 that house prices fall below £220,000 you would make 1p per warrant.

If you decide to sell the warrants when the average house price has dropped £40,000 to £180,000, you would make 40p per warrant.

That means you would get £40,000 back — a profit of £11,700 after your original costs of £28,300. House prices will need to fall to at least £191,700 for you to get your investment back.

If the price quoted when you sell is £220,000 or higher, you will lose the money you invested. If you haven't sold by close of business on August 4, 2004 Goldman Sachs will automatically do it for you.

Certificates are similar to warrants, but simpler. They are not geared, but allow an investor to track the performance of an asset without buying it.

Once issued, warrants and certificates can be traded in the same way as shares, so if house prices do not move in the way you expect you could sell them before the expiry date.

You don't pay stamp duty on covered warrants and certificates, but profits may be liable to capital-gains tax.

You will have to pay stockbroker's commission. Comdirect is charging £1 a trade in covered warrants from Goldman Sachs and SG Securities until the end of July. It normally charges £12.50 a trade.

Goldman Sachs: 0845 609 1555 (www.gs-warrants.co.uk)