2010 PROPERTY MARKET REVIEW

"Success in property investment is largely about hanging on when others have let go"

Introduction;

We are pleased to welcome you to our 2010 Property Market Review.

It has been an interesting year. One in which, by about half way through, all reports and commentators were suggesting the worst was over and a recovery was underway, but by the end of which these same commentators were saying there's more to come.

The dramatic 2009 rises in global sharemarkets have not continued in 2010. Some investment funds produced stellar returns for the 09/10 year. However, a quick review of their 2-5 year returns shows a completely different, and we would suggest, alarming picture.

When looked at over the longer term, commercial property as an investment class shows favourable income out-performance over other investment classes. Investors holding a portfolio of reasonable property interests over the last 5 years have done very well comparatively. This is certainly the case for those holding a portfolio of Guideline property interests.

Whilst global problems persist (Greece, Spain, Portugal etc) and we surely have to be alert to some further bad news not all the signs are bad. For NZers, recent improvements in our commodity prices should slowly be reflected in better times here. Until then though, our analysis points to on-going strains in the broader business community. Short term, vacancy rates may yet rise, but remember long term evidence demonstrates *"Success in property is largely about hanging on when others have let go"*

Tony Alexander of BNZ states in a recent Business Confidence Survey

"There has been a decrease in the net percent of respondents expecting the economy to improve over the coming year to 33% from 42% a month ago. But this result is still well above the five year average…".

Further afield, and to rescue us from an international financial and economic meltdown of Depressionary-scale, governments in the major countries most impacted by the crisis – the US, the UK and the Eurozone - have borrowed truckloads of trillions to pave over the crisis. According to economist Rodney Dickens "..more super tankers of government debt! The normal consequence of which is inflation." He goes on to say "The inflation threat is not imminent, but it needs to be taken seriously."

Our point is that if, or when, it does occur one of the major impacts will be to push up property values, and again we feel we'll be the beneficiaries.

Property;

During the year under review, property values have been in decline. There has been a continuing stream of value reduction announcements by listed entities. You will have noticed reports like; "The carrying value of Goodman Property Trust's property portfolio fell 1.9 percent or $28.4 million to $1.5 billion in the six months to the end of March." Listed property vehicles like the Goodmans, PFI, Kiwi, ING, etc are constantly revalued.

Sales and new building consents remain extremely low. There does seem to be a recent small tick-up in both stats. When recovery does occur this should lead to upward demand pressure for existing stock, as any recovery will likely precede an increase in new development.

According to Jones, Lang La Salle's latest industrial property research report, "Auckland's industrial market is poised to enter the next phase of the property cycle, with expansion across the Auckland region expected over 2010. However, before the market can exhibit strong signs of growth, expect a period of consolidation."

The Budget and tax;

We now know the budget content and will have read many of the plethora of subsequent comments and analysis. Reductions in personal and company tax rates are welcomed, albeit a bit on the late side. On the other hand and of relevance to property investors, the tax benefits of depreciation have been reduced. The full affect of this is yet to be worked through. We have looked at the affect on Guideline distributions for the 2010 financial year. It seems that the tax advantaged portions of our portfolio accounted for about .5% on the original investments. We have more work to do yet but we believe it will prove to be of marginal effect. Somehow the boffins and the politicians have concluded that if a building has a longer than 50 year lifespan, it doesn't depreciate. We have news for them, as would any other property organisation. Just consider the costs of constant R & M requirements, and the need to modernise to remain viable. These costs are to counter the effects of depreciation and just maintain a buildings value. Hence, to counter the effects of depreciation you will be aware we accumulate a "Long Term Sinking Fund" (LTSF) for each property. These are provisions for just this purpose. It is the land that generally appreciates over time.

What happens on average, and over time, that's what counts.

In the face of the extended global recession, many businesses have found it more difficult to survive, and some have fallen.

Naturally, when events like this occur, property cannot be expected to defy the trend. The question is, to what extent is a portfolio (as opposed to any individual asset) impacted by such issues.

Looking at the **Eriksens Master Trust Survey Results to 31 March 2010** we find the average for All Growth Funds is;

1 yr	*2 yrs*	*3 yrs*	*4 yrs*	*5 yrs*	
20.3 (- 15.10)	*-3.1*(-6.80)	*-4.6* (-1.40)	*-2.2*(1.30)	*2.2*(2.50)	%

Last years the numbers in ()

The 2010 year (1 yr) did produce a whopping return. Effectively a recovery for the previous 2 years from hell. However, what is really important is what happens on average and over time. It is not until you get to the 5 yr average that a positive return emerges, and then only at 2.2% pa.

Compare the returns on your Guideline Portfolio to other portfolio investments and you'll appreciate the power that lies in your property portfolio.

Whilst each Guideline investor's returns will vary due to the actual portfolio held and the holding time, our preliminary estimates show that with all that was going on last years distributions on our ***triple net return***© basis across the portfolio was over 11%. Our since inception estimate for the average annual distribution across the entire current portfolio is 10.0% pa. And remember the time frame since Guideline commenced its first group that is still in the portfolio is 25 years.

Hence our view: **"Success in property investment is largely about hanging on when others have let go"**

Better Times…..When??

Again referring to the Jones Lang La Salle research "Both tenants and owners are proceeding cautiously, but are in higher spirits than in 2008 and 2009."

A Bayley's report starts "Watch out for rising rents in the coming 12 months. That's the warning from finance Minister Bill English following the Government's Budget announcement released today." We are not so sure increases will happen too easily, eventually though any increased costs in ownership will get passed on. Treasury, according to Finance Minister Bill English, is predicting already that levels of rent - both in the commercial and residential arenas - will probably rise as a result over the next few years. Remember though, the depreciation changes do not affect land (which has never been depreciated) or chattels.

And from the ANZ, **Standing Out**

Not many governments around the world at present are able to improve their fiscal position, return to surplus within five or so years, and deliver across the board tax cuts – including company tax. The fiscal forecasts revealed in today's Budget will be the envy of most Finance Ministers.

The benefits of investment property:

Low correlation to other investments, producing stable income streams, should be seen as a key benefit. Constant higher levels of income, Hedge against inflation, ensuring both your capital value and income grows over time, these are some of the rewards obtained only through sound property investment.

Some of Our Property Statistics:

Over the last twelve months our activity has included:

Rent reviews for 16 tenancies (with 4 increases)
1 rental reductions
0 reviews incomplete at this time
7 new leases
8 re-negotiated expiry's
68 total tenancies
11 vacancies 31/3/10 (5 as the result of building subdivisions)

Best Wishes from
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the advantage of experience

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