

# 2012 PROPERTY MARKET REVIEW



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

## Summary:

Another year has passed and despite mixed reports locally about improvements to the local business environment, we cannot claim all is rosy yet. Our evidence is mixed. We have seen some good up-take of lease renewals and new leaseings. However, natural vacancies caused by expiring leases and the odd business failure still see the lead times for filling any premise that becomes vacant as very long.

Again we find ourselves saying whilst the last year saw the continuing effects of the global financial crisis, Canterbury earthquake catastrophes impact on the business sector, it is our view that this year we will experience a modest improvement. That is what happened last year.

## Introduction:

We are pleased to bring you our 2011 Property Market Review.

Once again it has been an interesting, if not difficult year. The global financial crisis (GFS) as it is called has now dragged on and into an unprecedented 4th year. As always we look forward to the time these conditions abate and we can get back to business in an improved environment. Although this time cannot be yet predicted a recent Colliers June survey holds some hope;

*"This month we provide update annual forecast for Christchurch, Wellington & Auckland's commercial markets. Generally they reinforce the picture of stabilisation as the pre-cursor to recovery, that we have noted in recent data."*

It's our view though that there are lingering problems in the business sector. We have experienced a reasonable start to the year with some new leaseings of smaller properties, however, we are still hearing reports of business retrenchment. The country's terms of trade as recently reported have been excellent, but the rising dollar value has not helped. Property valuations that have been falling for most of the last 4 years seem to have stabilised, though revaluations are all well below earlier levels.

In spite of this protracted recessionary period we can only repeat that 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 with our bank rate pre-tax distributions\* for our portfolio standing at just over **11%** for the 2010/11 financial year.

The coming year requires us to deal with not just the regular demands of the business cycle on property, but also further inflationary pressure, the introduction of the depreciation on property changes and on the positive side, tax reductions. All of which will impact your investment returns. Historically, property has proved to be the most reliable storer and protector of wealth, benefiting significantly in inflationary periods.

## Property:

New Zealand property is poised to again become the target of overseas investors, especially from Australia where capital gains taxes and stamp duty provide comparative disadvantages and their relatively high dollar enables them to buy a \$1.30 worth of property for each \$1 they invest. Whilst the positive of this lies in pricing pressure, the negative is that it becomes harder for us to compete to get quality opportunities.

## The Budget and tax:

Once again this has been and gone and is now largely forgotten.

Some of the main points were;

Forecasts a return to surplus on 2014-15 – a year earlier than predicted in December, we suggest this is a bit optimistic, but are hopeful.

Proposals to the sell-off of shares in four state-owned energy companies and to reduce its majority shareholding in Air New Zealand. It will retain a majority stake in all five firms. GAIN: \$7 billion. Whilst not a big contributor to relieving our difficulties, of some help in our view.

Then there's a parcel of taking and giving which as we see it can only be fiscally neutral, over the 4 or more years.

Overall, not a lot really, but this years budget should be if anything slightly positive in the business environment. Let's hope.

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

Again, we see encouragement for property investment in its proven long term performance relative to other investment options.

Looking at the **Eriksens Master Trust Survey Results to 31 March 2011** we find the average for All Growth Funds is;

1 yr	2 yrs	3 yrs	4 yrs	5 yrs	%
5.1 (20.3)	12.3(-3.1)	.07 (-4.6)	-2.8(-2.2)	1.2(2.2)	

*Last years the numbers in ( )*

Two things seem to emerge from looking at these returns;

1. Even after the stellar 2010 year, one year on, the returns of the "All Growth funds" sector remains abysmal for a full five years.
2. The high volatility of equity markets.

So it really does get back to what is important, **what happens on average and over time.**

Compare the returns on your Guideline portfolio to other portfolio investments and you'll appreciate the power that lies in your property portfolio with an 11% average income distribution\* for the year, after nearly four really difficult years.

Whilst each Guideline investor's returns will vary due to the actual portfolio held, time of acquisition and the holding time, our estimates show that with all that was going on last years distributions on a *triple net return*<sup>®</sup> basis across the portfolio was over 11% on a since inception basis. And remember the time frame since Guideline commenced its first group that is still in the portfolio is over 27 years.

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

According to the information provided in a recent seminar by an advisor the capital needed to support you in retirement has increased significantly.

"In 2008 you needed \$730,000 to generate \$60,000 of income a year... in 2011 that level of capital needed has almost doubled to over 1.5 million!"

In fairness, this relates to the returns currently available on term deposit, however, if you held the whole Guideline portfolio you'd still only have needed around \$550,000 invested.

## Current gross yield estimations for other investment assets are;

- 6.2% NZ Shares
- 5.6% Bonds, company
- 5.1% Balanced portfolio
- 4.5% Bonds, NZ Govt
- 4.2% Short term deposits
- 2.4% Global shares.

## The benefits of direct investment in professionally managed property:

- \* High distributable income (compare with current bank rates in the 3-5% range, and the average for NZ sharemarket top 10 companies at 6.2%)

- \* Low correlation to other investments, should be seen as a key benefit.

- \* 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.

We are sure, you like all of us are certainly hoping for a stronger turnaround. As this is being written a National Bank Business survey has reported a modest decline in the nation's business confidence. It is now over 27 years that Guideline has been growing the property portfolio you have invested in. We are proud to be able to say that most of those investors from our first year of operation are still with us. We trust that is testimony to their satisfaction with what we have been able to provide for them, and thank you for their support and loyalty.

## Some of Our Property Statistics:

**Over the last twelve months our activity has included:**



- Rent reviews for 20 tenancies (with 9 increases)
- 2 rental reductions
- 0 reviews incomplete at this time
- 13 new leases
- 8 re-negotiated expiry's
- 9 vacancies 31/3/11
- 70 total tenancies

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*\* Bank rate equivalent and "Triple Net" are terms used by Guideline to describe distribution level. They refer to the full income distributed on initial investment amounts including acquisition costs, and after all operating costs, allowances and management have been deducted.*