

2015 PROPERTY MARKET REVIEW



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

Summary:

The now overused term “rock-star economy” attributable to New Zealand, whilst subject to much debate, has now moved in some economists minds to the “Goldilocks” economy. A consensus of economists now forecast steady growth. It is our view that our embrace of such confidence could lead to an over-optimism and potential disappointment. However, whilst we make this cautionary comment, pessimists we are not.

As always, all indicators do not align. Take the falls in commodities prices, the high Kiwi and its impact on exporters and our balance of payments just to name some of the influences that should keep the lid on the all-out optimists.

The CPI fell to a 0.1% rise quarter towards zero for the year's first quarter thanks in large measure to low oil prices.

Seems, from their tone, the Reserve Bank was unlikely to cut rates this year. This, despite current market pricing and despite New Zealand's interest rates being much higher than the rest of the world's. On the other hand, and assuming things remain as they are, we see it is possible and reasonable to expect a rate cut a later in the year. At the time of writing another lower dairy price and a reduction in the Australian interest rate to 2% are being announced. Negative market shocks can and do occur. Property incomes and values tend to always lag the market so we see a continuing improvement during the 2015/2016 year.

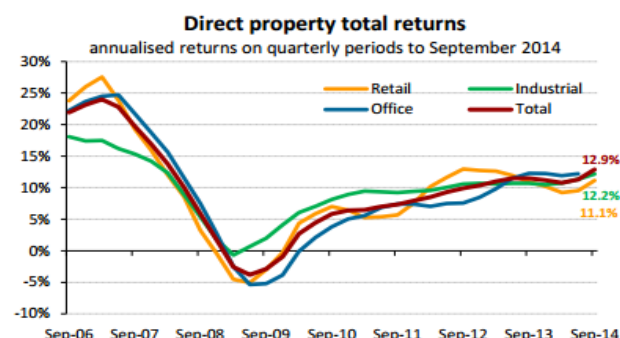
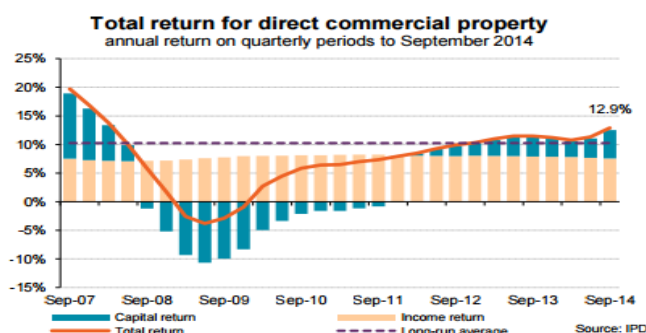
The commercial investment property market has had a more than reasonable year, as has the NZ and most overseas share-markets. According to the Eriksen's Master Trust Survey to 31/3/15 Growth funds returned 13.5% over the year, balanced funds gained 11.3% and conservative funds rose 7.7%. (See 1yr – 5 yrs averages).



Property:

A comparison over medium terms direct property seems to always demonstrate returns above the average that can be expected from other investment classes.

Direct property returns are typically considerably less volatile, but with a good balance of income and capital display a very strong average. A look at the IPD graph below published by the Property Council of NZ displays an average over the last 7 years (to sept 2014) of 10%. Income, the real long term reason for investing in direct property (or should be) fluctuates between about 6% and 8% pa. Also look at the Guideline Factor (our average returns) and compare that to bank rates over the last 10 years.



The 2nd IPD graph shows the value and importance of holding a diversified portfolio of property interests. This graph breaks the total returns graph above into its constituent property types since 2006.

As a Guideline Investor you will probably hold a reasonably well diversified portfolio and therefore attract the benefits of not relying on the outcome of any one sector at any given point in time. Obviously though, no portfolio can escape the over-all market risk, as the graphs indicate impacted in the 2007-2011 period.

The Guideline Factor;

Estimated results for the year ending 31/3/15 for the current Guideline portfolio;

Average triple net© income distributions; 10.4%

Income plus average capital appreciation for the year; 15+%

Note; Each Guideline investor's returns will vary due to the actual portfolio held, time of acquisition and the holding time, our estimates show that distributions on a triple net return© basis across the portfolio on a since inception basis. And remember the time frame since Guideline commenced its first group that is still in the portfolio is over 30 years.

The market results for any given period will also not reflect the cyclical effect of any individual property. That is to say, in the best of times a specific property might encounter refurbishment demands or tenancy issues, the opposite might have occurred in a poor market time. Each property has its own market cycle, influenced by age, upgrade requirements, lease terms and the coincidence or otherwise of these.

Looking at the **Eriksen's Master Trust Survey Results to 31 March 2015** we find the average for All Growth Funds is;

1 yr	2 yrs	3 yrs	4 yrs	5 yrs	%
13.5(13.2)	10.9(12.5)	10.9(6.4)	7.7(6.28)	7.3(7.7)	
(Previous years in ())					

The NZSE Gross index has returned 12%, 28% and 13.8% respectively over the last 3 years.

The average annual over the last 10 years has been 5.37%

The strength in the industrial sector forges on in New Zealand. It is supported by high occupational demand, rising rents and aggressive investors competing for the limited stock available.

“The health of the industrial sector is a reflection of the health of the New Zealand economy. There are around 640,000 full time equivalents (FTEs) working in the industrial sector, accounting for a third of New Zealand's employment and a third of its GDP.

“Occupational demand for industrial premises in Auckland is high, with the vacancy rate achieving another record low, now at 2.6%. Prime rents are growing and yields are firming. Forecasts are for further rent rises between two per cent and three per cent p.a. with yields firming by 25 to 50 basis points pa.

“Average prime yields, which are already at a record low 6.7% in the prime sector, are forecast to reach low 6.0% by 2015 and 2016.

“Greater levels of demand and the reduction in options for tenants searching for new or alternative space, provides the perfect positive storm for landlords to review their stance on rental growth.” Colliers.

In Tauranga the trends are similar. Recent sales are demonstrating low yields pretty much across the range.

Tauranga CBD is a different beast. Whilst any sales reflect the low yield trend, earthquake proofing demands and modest demand has resulted in relatively high levels of retail vacancy. There has also been movement, again largely due to the above issues, to lower rent locations. The move from Devonport Road to Grey Street and thus the vacancy swap between the two streets is a reflection of this. Now, as earthquake proofing works are completed, the does seem to be some vacancy absorption.

Large office developments on the CBD periphery over the last few years have also impacted life downtown. The return to the CBD of TrustPower expected later this year will start to restore the office worker numbers in the city. Whilst it may be a few years yet, the prospect of a university in Durham Street is also being looked forward to with some anticipation.

Some of our recent statistics;

Over the last twelve months our activity has included:

Rent reviews for 18 tenancies (with 13 increases)

1 rental reduction

8 new leases

3 re-negotiated expiries

8 vacancies 31/3/15

61 total tenancies

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Property; Investment

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