

Winter Market Outlook Commercial property markets: repositioning for recovery

IPD Australia and New Zealand
Thursday 3 June 2010

On the pulse of
the property world



Outline



- ① Overview and index results
- ② Market analysis
- ③ Summary

Outline



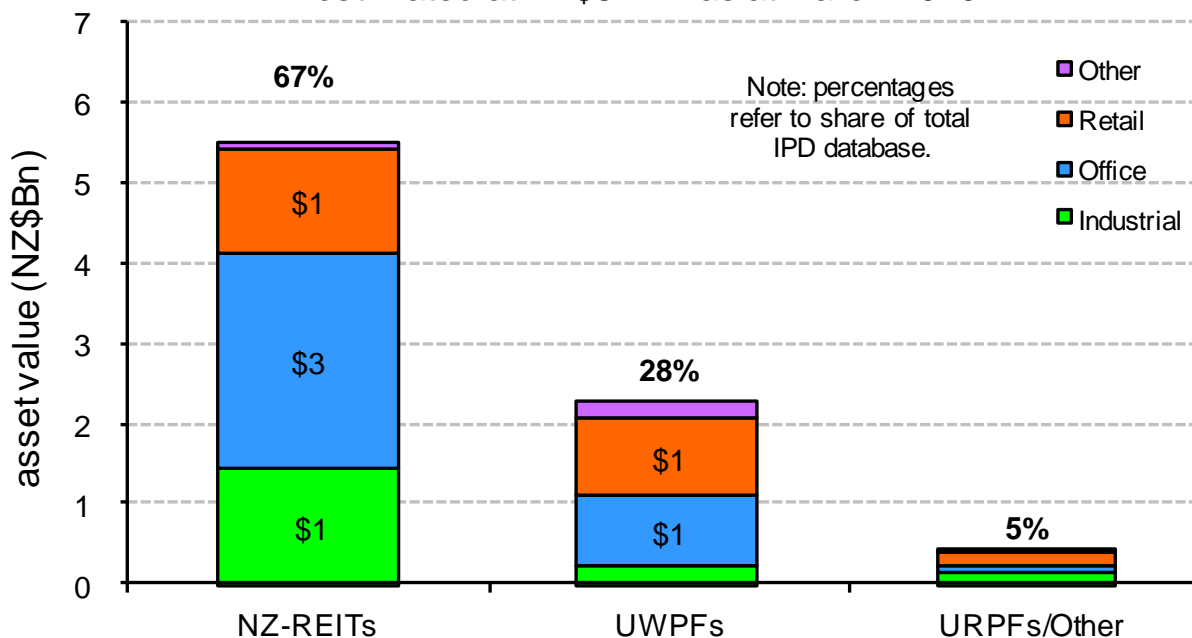
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IPD property database

- database represents c\$8Bn of property assets with large exposure to REITs



Size of IPD database by property segment
estimated at NZ\$8.2Bn as at March 2010



Note: percentages refer to share of total IPD database.

- Other
- Retail
- Office
- Industrial



Note: "Other" denotes other corporations and government.

Source: IPD Research.

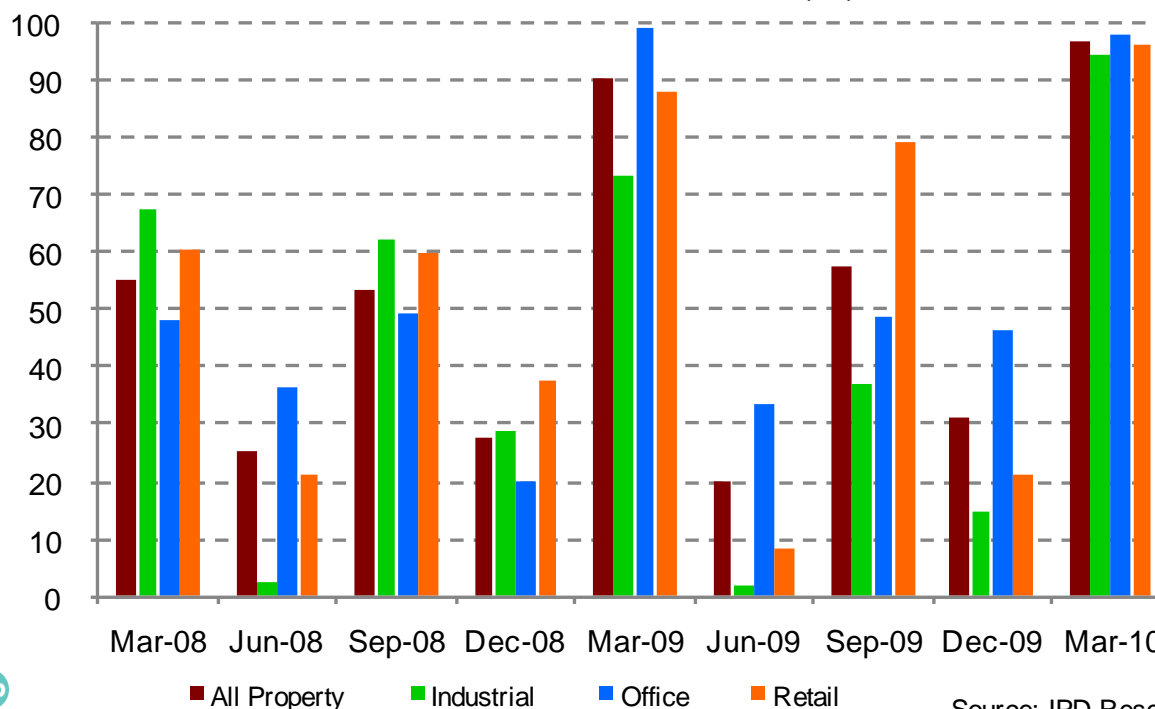
- IPD data bank: 9 data providers, 366 assets valued at NZ\$8.2bn. Additional 100 assets to be captured from next quarter.
- Sector exposure: retail (29%), office (45%), industrial (22%) and other (4%).

Revaluation profile of database

- profile varies markedly across quarters



Trend in asset valuation profiles by sector
share of revalued NZ assets (%)

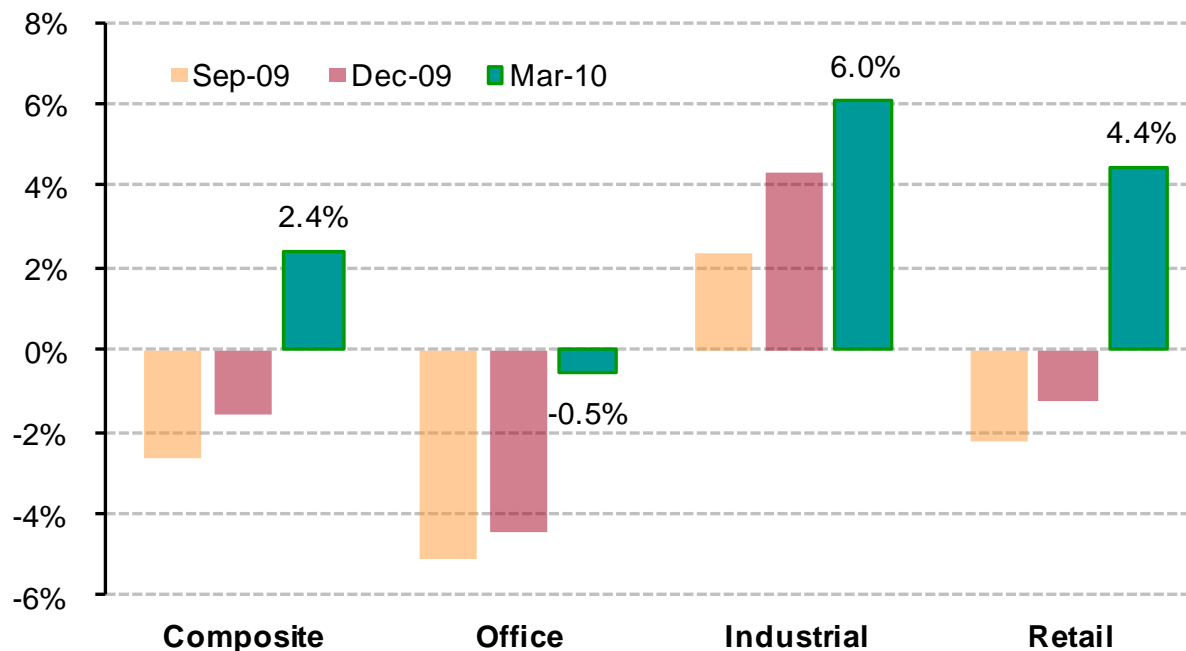


- Figures reflect the share of quarterly asset valuations in the IPD database.
- A high level of revaluations take place in March quarter followed by September quarter.

Property investment returns - direct property return performance moves into positive territory!



Performance across core property sectors nominal annual total return for New Zealand



Note: direct property returns based on PCNZ/IPD Index.

Source: IPD Research.

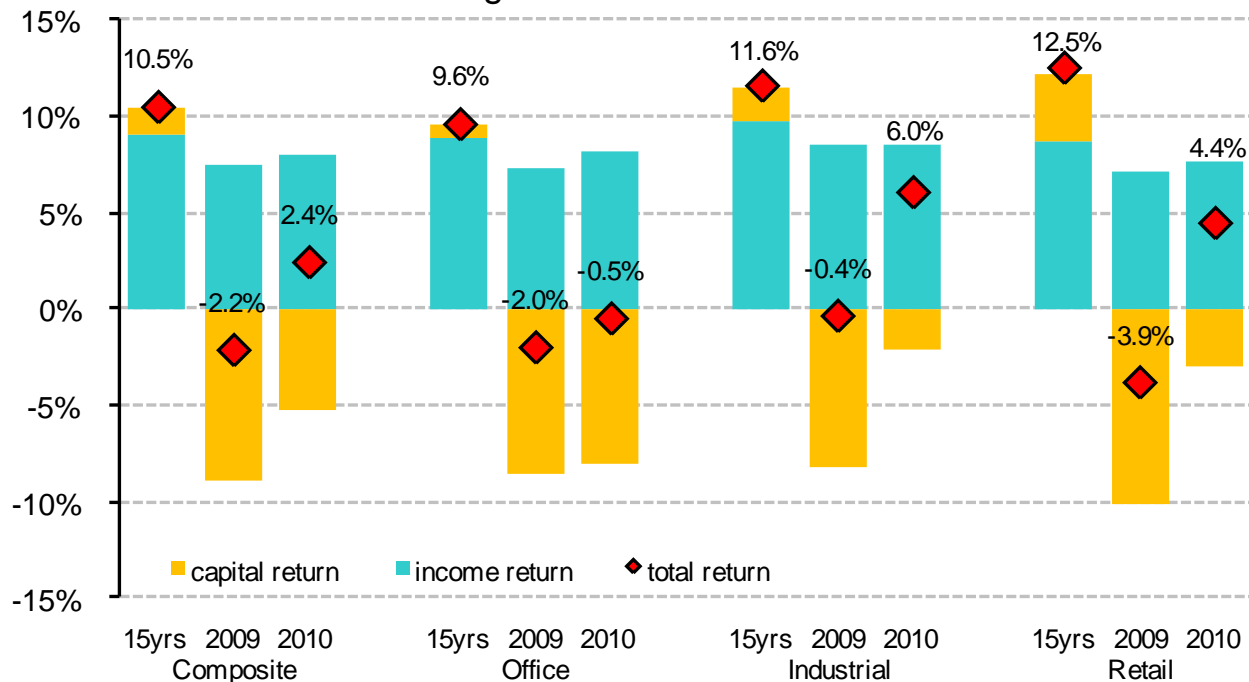
- Total annual return for Q1:10 stood at +2.4%. This compares favourably with -1.6% in Q4:09 and -2.7% in Q3:09.

Property investment returns

- overall improved performance but varies across sectors



Performance across NZ core property sectors
historical average nominal annual return to March



Note: direct property returns based on PCNZ/IPD Index.

Source: IPD Research.

- Property income remains stable averaging 9% for the total direct property market.
- Poor performance driven by capital returns; posting a negative annual return of 5%.

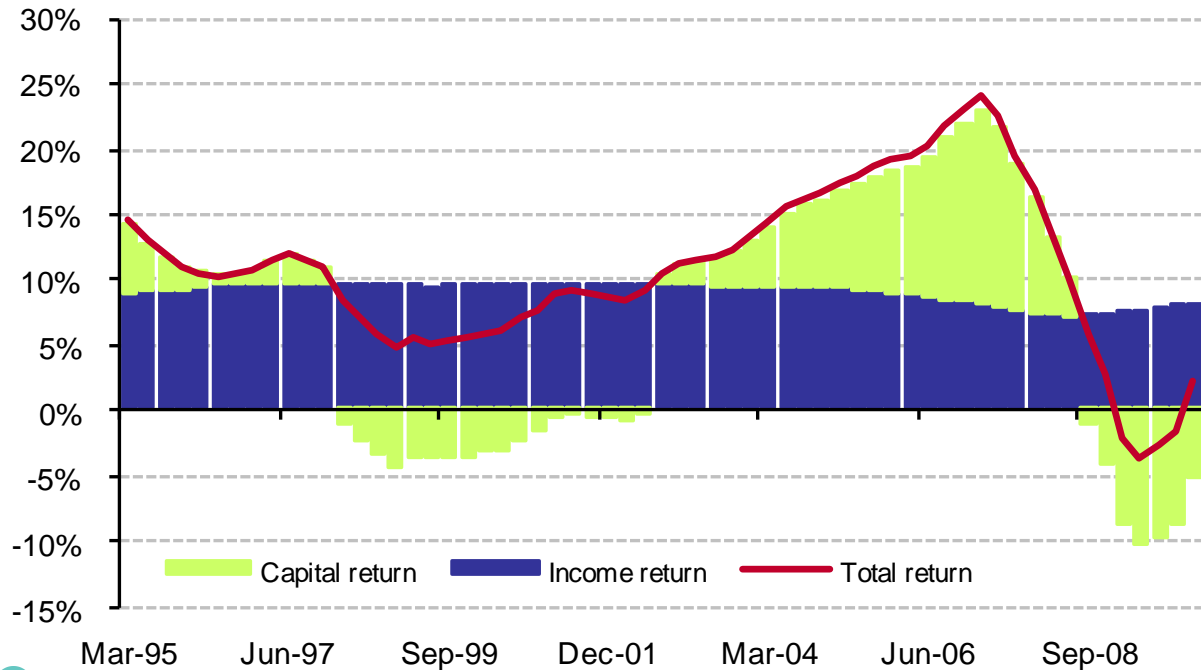
Property investment cycle

- market in recovery phase with decline in capital growth decelerating



Total return for NZ direct commercial property

rolling annual return on quarterly rests to March 2010



Source: IPD Research.



Outline



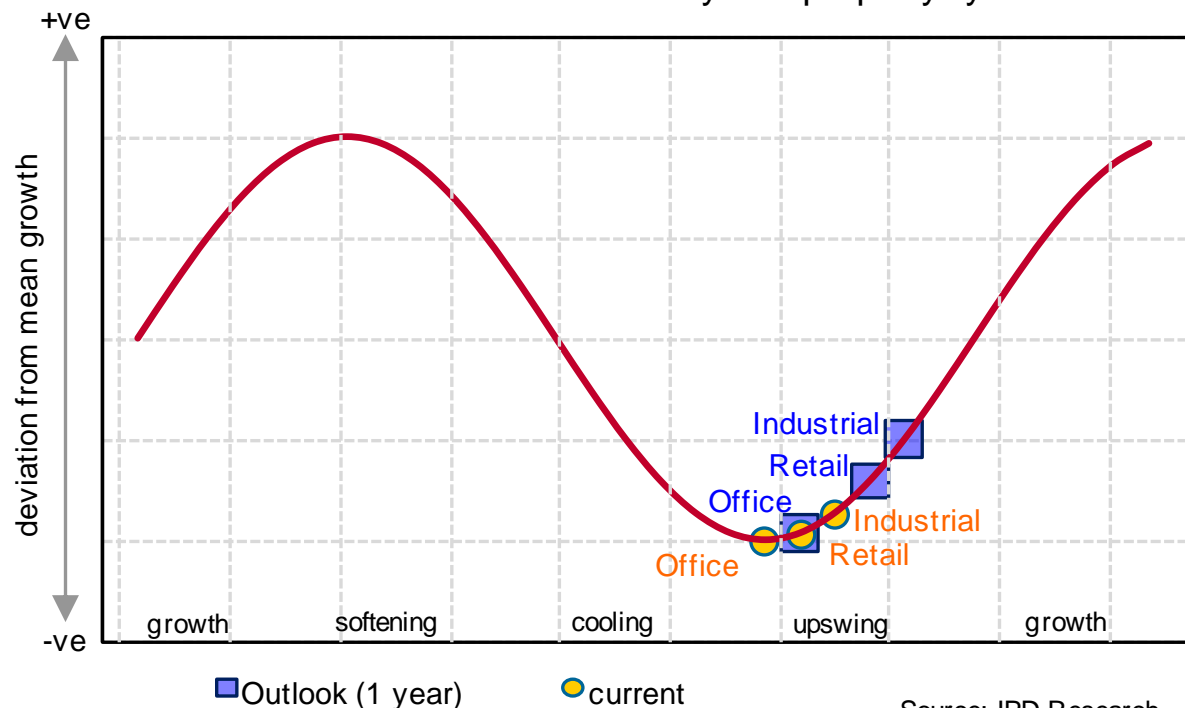
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Core property sector markets - generally positioned at early stage of recovery



NZ property space market cycle

Position of markets on the stylized property cycle

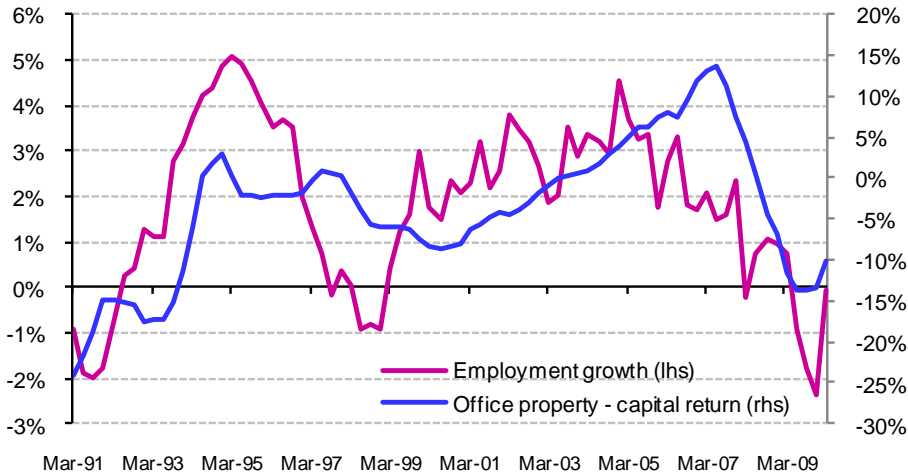


- Core sector markets currently positioned at the trough of the property cycle.
- Core sector markets to be positioned at early upswing phase of the cycle within 12 months.

Office and retail property sectors - signs that underlying economic drivers are improving

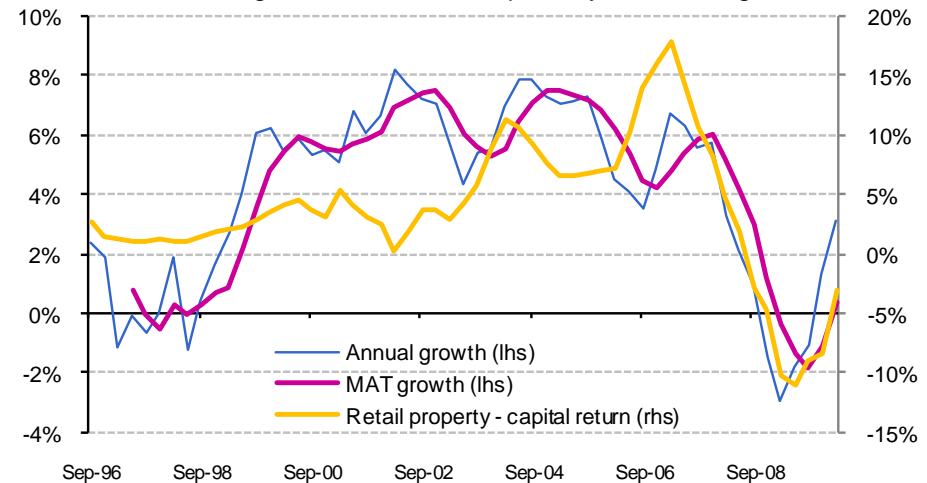


National employment versus office property
annualised growth and return on quarterly rests ending Mar-10



Note: employment series is seasonally adjusted and capital return series is expressed in real terms. Source: Statistics NZ and IPD Research.

National retail trade versus retail property
annualised growth and return on quarterly rests ending Mar-10



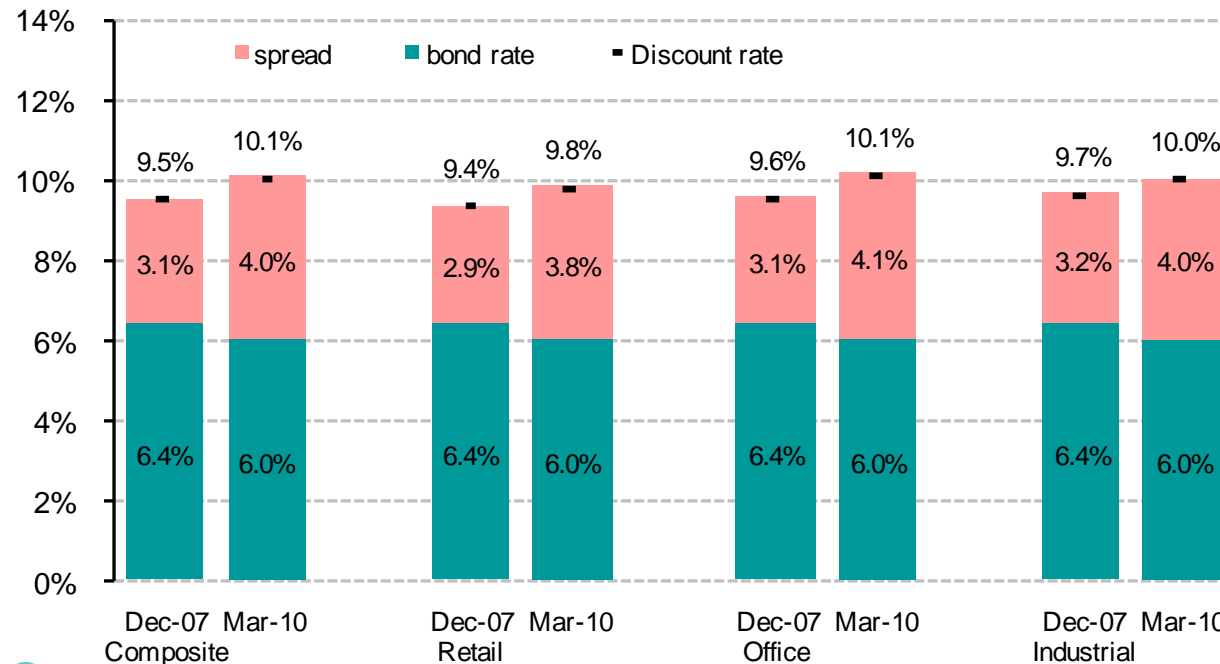
Note: seasonally adjusted series. Source: Statistics NZ and IPD Research.

- Early signs emerging that the labour market is improving with unemployment retreating and employment growth strengthening.
- Retail sales also showing signs of strengthening.

Trends in discount rates - a blow-out in the risk premium: to persist over the short-term



Discount rates across property sectors
New Zealand



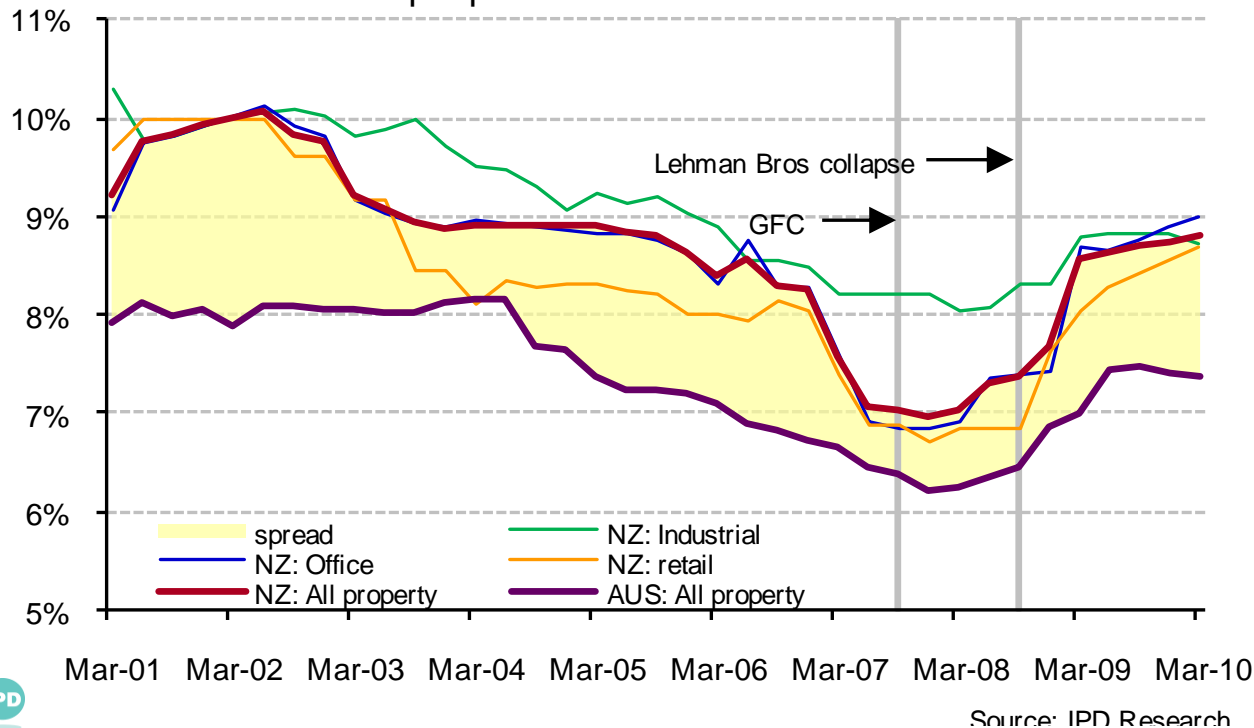
Source: IPD Research.

- The long-run spread between property discount rate and 10YR Treasury bond rate is c400bps.

Property investment yields - cap rates stabilising



NZ average property portfolio cap rates
sample period: Mar 2001 - Mar 2010



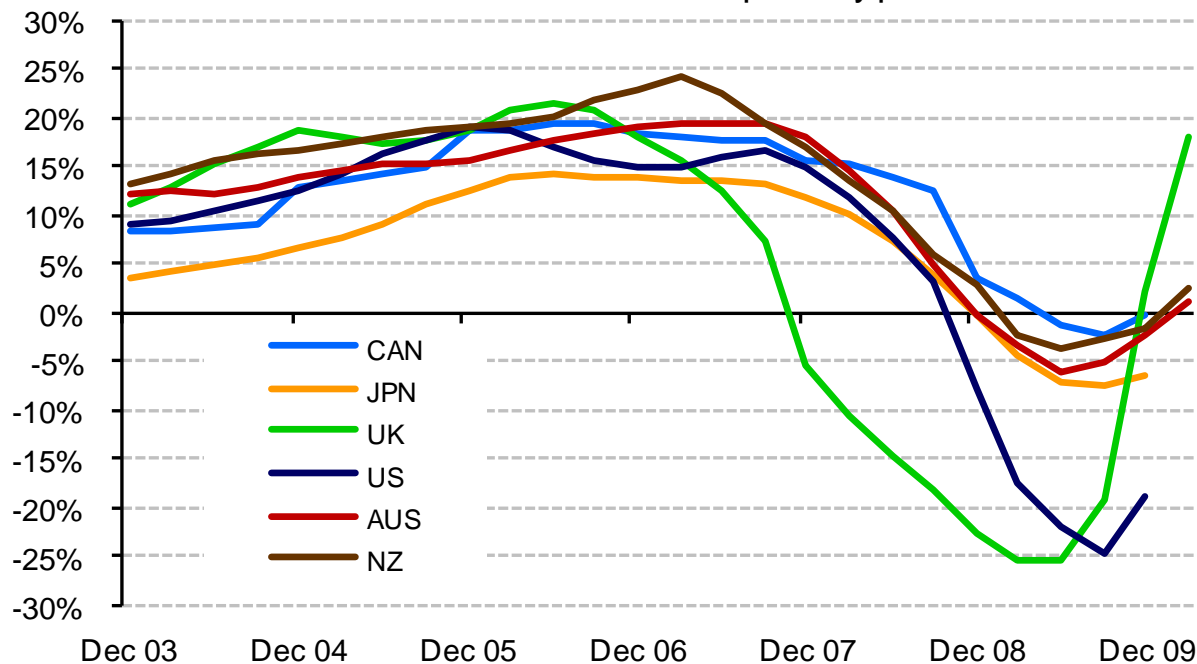
- Softening in property cap rates in 2008/09 reflected deteriorating capital market conditions (CMC) with an upward re-rating of investment risk and weakening space market fundamentals (SMF).
- Spread between AUS and NZ cap rates: average c120bps. Got to 60bps just prior to GFC.

Global property cycles

- NZ and AUS experience shallow downturn with signs of recovery



Return profiles for selected property markets
annual nominal return on quarterly periods



Note: direct property returns based on global IPD indices.

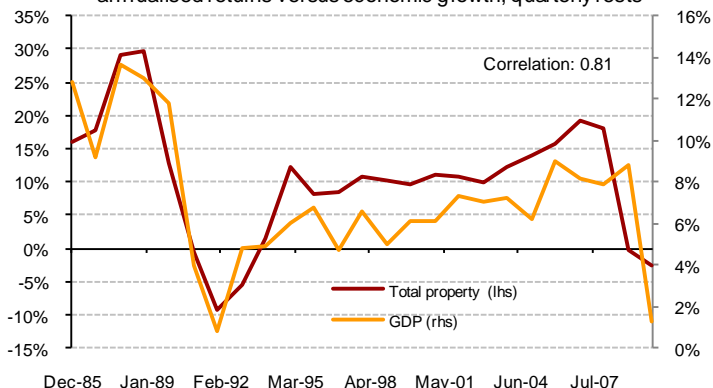
Source: IPD Research.

- Countries with steep declines in capital growth have experienced a rapid deterioration in the real economy and the labour markets.

The influence of macroeconomy - the impact of real economy varies across country property markets



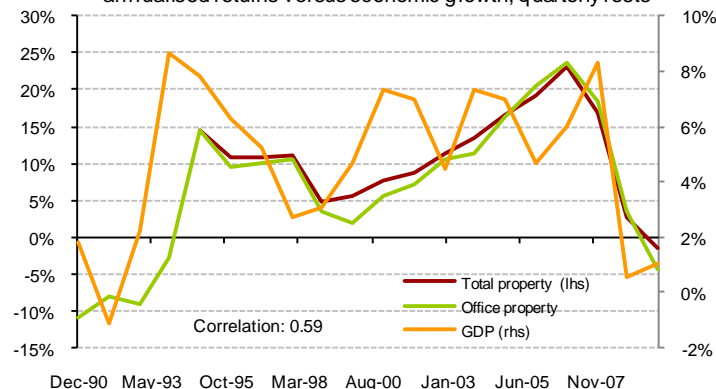
AUS direct property and the macroeconomy
annualised returns versus economic growth, quarterly rests



Note: return and growth rates expressed in nominal terms.

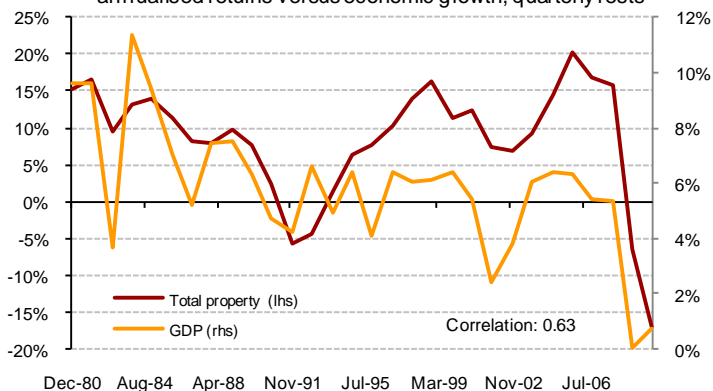
Source: IPD Research.

NZ direct property and the macroeconomy
annualised returns versus economic growth, quarterly rests



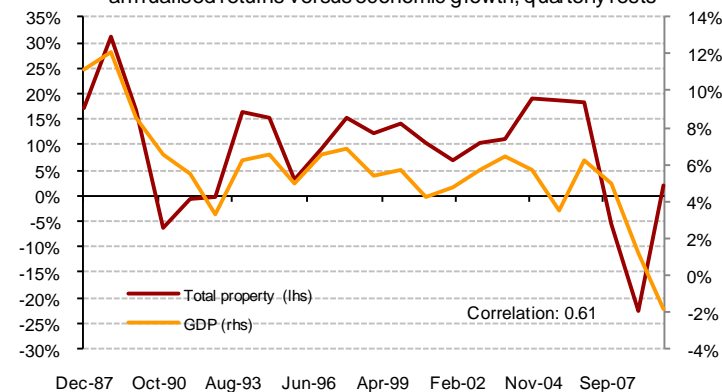
Source: IPD Research.

US direct property and the macroeconomy
annualised returns versus economic growth, quarterly rests



Source: IPD Research.

UK direct property and the macroeconomy
annualised returns versus economic growth, quarterly rests

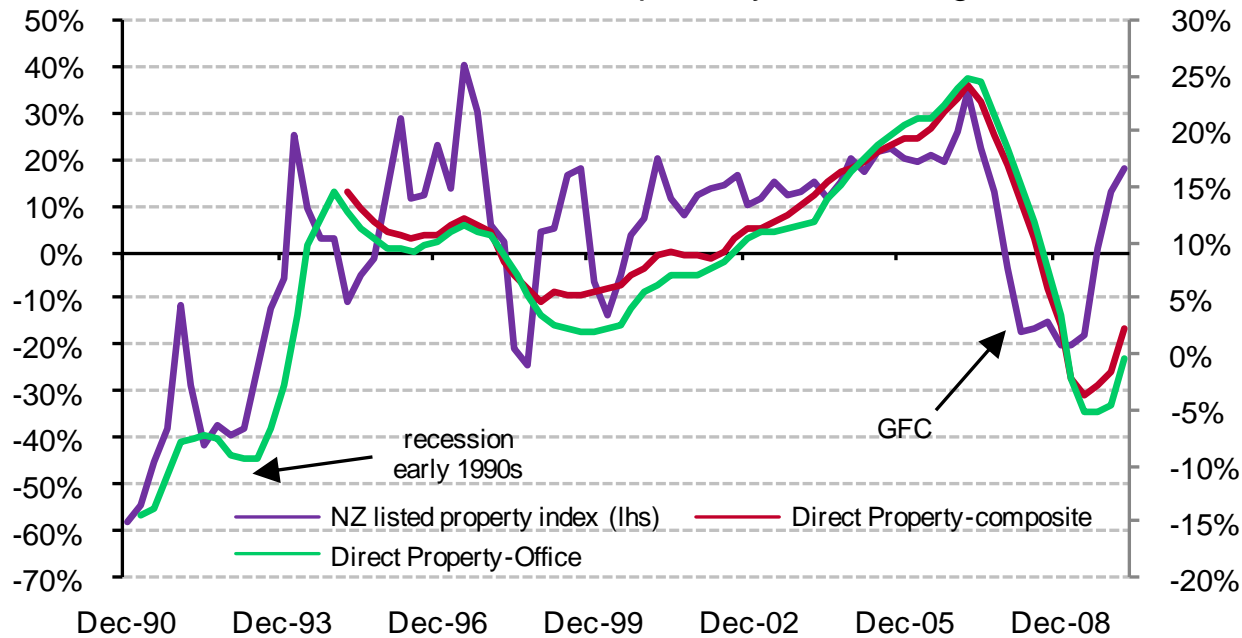


Source: IPD Research.

Unlisted versus listed property - divergence over the short-term, convergence over the long-term



Performance across NZ property asset classes
annualised total return on quarterly rests ending Mar -10



Note: Listed series includes imputation.

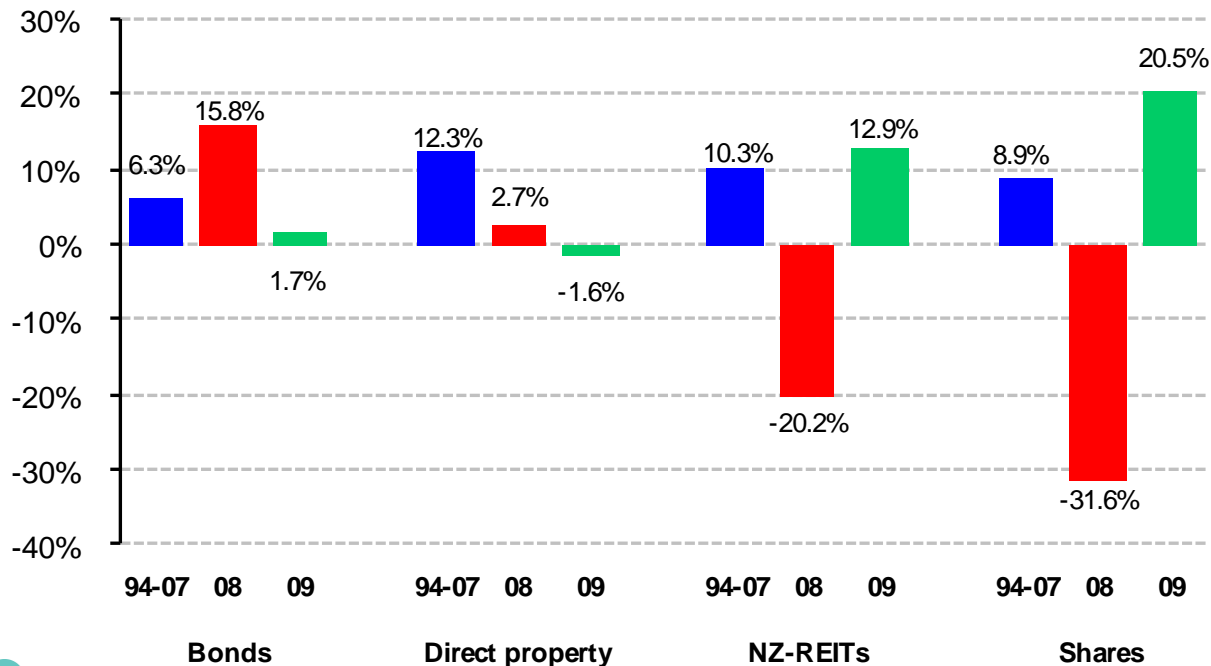
Source: NZX and IPD Research.

Competing asset classes

- direct property compares favourably to other asset classes over the long-run



New Zealand asset class performance
historical annualised total returns to December



Source: NZX, RBNZ and IPD Research.

- Common factor risk saw a downturn in returns in 2008: a significantly departure from long-term averages.
- The current overshooting in returns experienced by specific investment classes suggests that markets are still in adjustment phase towards equilibrium.

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Short-term considerations

- property markets in early recovery phase



- **Macroeconomic conditions**
 - Economy in recovery phase – return to positive growth
 - Economy remains fragile - vulnerable to external shocks
- **Space market fundamentals**
 - Rebalancing of demand and supply: excess supply conditions to persist
 - Conditions vary across core sectors and asset quality
- **Investment climate**
 - Direct property markets in positive territory
 - Asset markets still in transition phase towards long-term return performance
 - Recent emergence of SDC raises uncertainty on recovery profile
- **Property structures**
 - Property segments deviate over short-term; move closely over the long-term

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