New Zealand Research Report | November 2016

Global industrial rental rankings

In the latest Colliers International global industrial survey (tracking industrial rents in 145 cities) New Zealand ranks comparatively highly, but still provides cheap rents when compared to other major cities across the globe.

Colliers International's global industrial survey of 145 cities from June 2016 showed Auckland, Christchurch and Wellington's average prime net rents are rising, but globally cheap, ranked 35th, 50th and 66th respectively. This compares to the ranking in June 2015 of 38th, 51st and 71st respectively.

The top industrial rents are more than three times the rate of New Zealand's most expensive city – Auckland. Top spot globally was Hong Kong with an impressive NZD$348 per sqm p.a. Hong Kong knocked London (Heathrow) off the top spot in the June 2015 survey. Hong Kong also had the highest prime office rent in Colliers International's latest global office survey with NZD 2,901 per sqm p.a.

Warehouse rents in New Zealand have been increasing steadily, especially in areas with the strongest tenant demand, often increasing up to 4% p.a. Rents will rise further over the medium-term with market reviews in locations like Auckland likely to reset expectations. However, the lower inflation environment will hold back some of the rent rises where these are inflation linked.

Global industrial rents and yields

Rank	City	Country	Average Prime Warehouse Rent (sqm, pa)	Average CBD Cap Rate/Initial Yield (%)
1	Hong Kong	China	NZD$348	4.00%
2	London - Heathrow	United Kingdom	NZD$327	4.75%
3	Tokyo	Japan	NZD$282	5.40%
4	Singapore	Singapore	NZD$226	3.50%
5	Oslo	Norway	NZD$218	5.50%
6	Honolulu, HI	US	NZD$204	n/a
7	San Francisco Peninsula, CA	US	NZD$190	5.00%
8	Bristol	United Kingdom	NZD$185	5.25%
9	Stockholm	Sweden	NZD$181	6.00%
10	Sydney	Australia	NZD$158	6.66%
35	Auckland	New Zealand	NZD$118	6.07%
50	Christchurch	New Zealand	NZD$101	7.20%
66	Wellington	New Zealand	NZD$93	7.86%

Source: Colliers International Research. Ranking based on USD/NZD Rate of 1.4.

Global industrial rental rankings (cont…)

Industrial property in New Zealand received the highest level of investor confidence for property fundamentals like vacancy, rents and yields in the latest Colliers International Investor Confidence survey.

In the September 2016 quarter, the average investor confidence for industrial property in the three main centres of Auckland, Wellington and Christchurch, was a net positive (optimists minus pessimists) 39%. This result was higher than investor confidence nationally as well as for the office and retail sectors.

Investor confidence exhibited in the sector has pushed yields for New Zealand's industrial investors to some of the strongest rates globally.

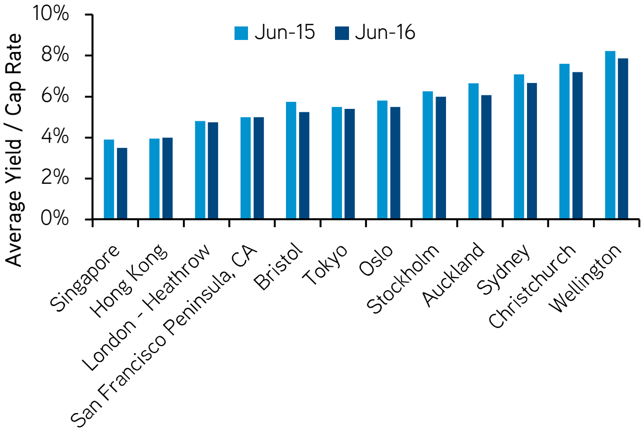
The average industrial prime yield for cities with the top 10 rents is 5.1%. This was 5.3% in June 2015. This compares with Auckland at 6.1%, Wellington at 7.9% and Christchurch at 7.2%.

Interest rates remain low, encouraging private investors, syndicators, unlisted and listed property vehicles to remain active in the most traded commercial property sector in New Zealand.

A shortage of stock and high levels of competition in the hotspots of recent years have boosted activity for the likes of Palmerston North, Tauranga, Hamilton and Dunedin which have not historically experienced the same levels of yield compression as the main centres.

The level of enquiry for sub-$5 million industrial property has kept competition high, with increasing purchase prices seeing yields often reaching 5% with firmer yields for sub $2 million properties.

Average Industrial Cap Rate/Initial Yield



Source: Colliers International Research

Commercial Interest Rate Guide	
Date	3 Year Term (Indicative Borrowing Rate)
Dec-15	5.36%
Jan-16	5.49%
Feb-16	5.22%
Mar-16	5.10%
Apr-16	4.83%
May-16	4.85%
Jun-16	4.88%
Jul-16	4.77%
Aug-16	4.59%
Sept-16	4.52%
Oct-16	4.57%
Nov-16	4.81%

Source: ANZ Bank & Colliers International. Note: the lending rate quoted in the table is not necessarily what you will be offered, and should be regarded as indicating medium term trends.

New Zealand Key Economic Indicators – November 2016

	Jun-16 (yr rate)	June-16 (qtr rate)	Mar-16 (qtr rate)	Q-o-Q Change	June-15 (yr rate)	Y-o-Y Change	2017F*	2018F*	2019F*
GDP Growth	3.6%	0.9%	0.9%	0.1%	2.4%	1.2%	3.4%	2.9%	3.6%
Current Account (% of GDP)	-2.9%	NA	NA	NA	-3.6%	0.7%	-3.5%	-4.5%	-5.0%
Retail Sales (ex-auto)	6.6%	2.5%	1.4%	1.1%	5.5%	1.1%	6.8%	5.6%	5.3%
	Sep-16 (yr rate)	Sep-16 (qtr rate)	Jun-16 (qtr rate)	Q-o-Q Change	Sep-15 (yr rate)	Y-o-Y Change	2017F*	2018F*	2019F*
CPI Inflation	0.2%	0.1%	0.4%	-0.3%	0.4%	-0.2%	0.7%	1.7%	1.8%
Net Migration Gain (000's)	70	18	17	1	61	8	69	64	54
Unemployment Rate	5.1%	4.9%	5.1%	-0.2%	5.5%	-0.4%	4.8%	4.2%	4.2%
	Sep-16 (yr rate)	Aug-16 (yr rate)	M-o-M Change	Sep-15 (yr rate)	Y-o-Y Change	10 Year Average	2017F*	2018F*	2019F*
Tourist Numbers Growth	11.6%	10.8%	3.6%	12.7%	-1.0%	3.9%	8.5%	6.5%	4.9%
Official Cash Rate	2.00%	2.00%	0 bps	2.8%	-75 bps	3.84%	1.75%	1.50%	2.25%
90 Day Bank Bill Rate	2.2%	2.2%	-1 bps	2.9%	-62 bps	4.1%	2.0%	1.7%	2.2%
10 Year Government Bond	2.4%	2.2%	21 bps	3.3%	-89 bps	4.7%	3.0%	3.5%	3.7%
Floating Mortgage Rate	5.6%	5.6%	0 bps	6.0%	-40 bps	7.0%	5.1%	4.7%	5.2%
3 Year Fixed Housing Rate	5.0%	5.0%	0 bps	5.2%	-20 bps	7.1%	NA	NA	NA
Consumer Confidence	121	118	3%	111	9%	119	NA	NA	NA
NZD vs US	0.73	0.72	1%	0.63	15%	0.74	0.72	0.68	0.67
NZD vs UK	0.56	0.55	1%	0.41	35%	0.46	0.55	0.50	0.48
NZD vs Australia	0.96	0.95	2%	0.90	7%	0.85	0.94	0.90	0.87
NZD vs Japan	74	73	2%	76	-2%	74	76	80	81
NZD vs Euro	0.65	0.65	1%	0.56	16%	0.57	0.62	0.57	0.58

Source: NZIER, Colliers International Research *March year forecast

Office property market

New Zealand Prime CBD Office Indicators		
Prime Rentals (% Change)	12 months to Sept-16	12 months forecast
Auckland CBD	4.7%	2.5%
Wellington CBD*	0.0%	0.0%
Auckland Metropolitan	1.2%	1.1%
Prime Capital Values (% Change)	12 months to Sept-16	12 months forecast
Auckland CBD	10.6%	4.6%
Wellington CBD*	10.6%	2.0%
Auckland Metropolitan	2.3%	4.7%

Source: Colliers International Research *Gross rents

We have recently updated our Auckland Metropolitan Office vacancy survey covering more than 1.7 million sqm of space. This is the highest amount of stock since the survey began in the mid-1990s.The latest vacancy rate of 5.6% reduced from 6.3% a year ago, and is the lowest we have seen in eight years. It is also the third lowest result in the past two decades.

Both prime and secondary vacancy have decreased with prime at 4.6% down from 5.7% in September 2015, and secondary at 5.5% down from 6.0%.

New developments continue to provide the leasing market with new stock to consider, including the recent completion of the Cider Building and office space at NorthWest Shopping Centre. We are also seeing refurbishments and redevelopments returning to the market increasing supply further.

Vacant space has reduced by almost 10,000 sqm in the past six months. A large portion of this is due to the lease at Manukau Tertiary Centre by MBIE (Ministry of Business and Employment).

With a strong development pipeline and high employment growth predicted in this sector, we expect favorable conditions for landlords to continue.

Prime Office Vacancy*			
	Jun-15	Jun-16	Jun-17 Forecast
Auckland CBD	0.7%	1.9%	4.6%
Wellington CBD	2.0%	2.8%	2.9%
	Sept-15	Sept-16	Sept-17 Forecast
Auckland Metropolitan	6.3%	5.6%	5.8%

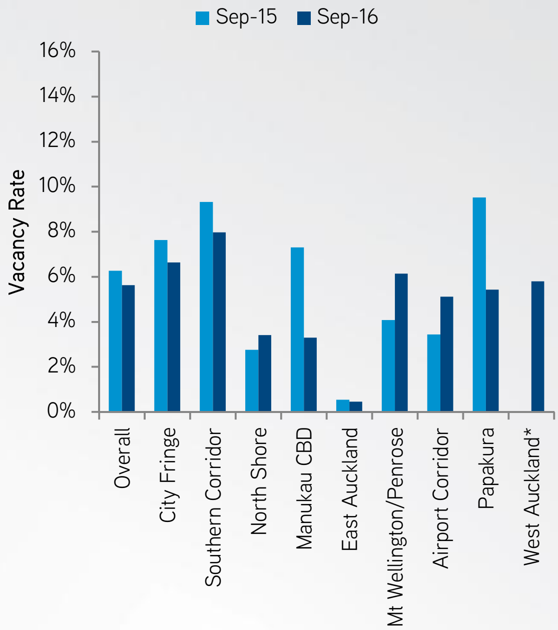
Source: Colliers International Research *Refers to Premium and A Grade office vacancy only

155-167 Fanshawe Street

Wynyard Quarter, Auckland Central

The 3,789 sqm freehold site at 155-167 Fanshawe Street in Auckland Central's Wynyard Quarter sold for $23.2 million. The site is one of the only available freehold development opportunities in this location. The ex-Caltex site sold with vacant possession.

Auckland Metropolitan Office Vacancy



Source: Colliers International Research
*New to the survey

A Selection of Office Sales Activity						
Address	Location	Price	Vendor	Purchaser	Sale Price ($/m²)	Yield
155-167 Fanshawe Street	Wynyard Quarter, Auckland	$23,247,000	Z Energy	Developer	$6,000 (Land Value)	Vacant Possession
The Landings – Timpany Walton Lawyers (office unit)	Timaru, Christchurch	$2,439,000	Timaru Retail Project Ltd	Private Investor	N/A	6.9%
7C Antares Place	Mairangi Bay, Auckland	$1,700,000	Private Trust	Private Trust	$3,602	Vacant Possession

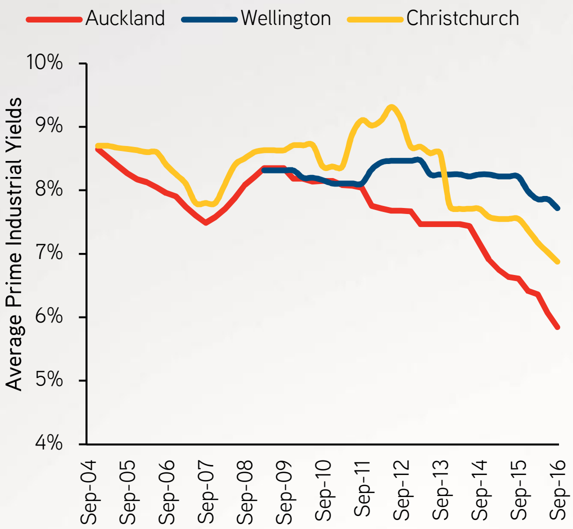
A Selection of Office Leasing Activity				
Address	Location	NFA (m²)	Lessor	Lessee
23 Customs Street East	Auckland Central	655	Argosy Property Limited	Fronde Systems Group
5 High Street	Auckland Central	207	Vulcan Lane Properties	Talent International NZ Ltd

8-14 Newton Street

Mount Maunganui, Tauranga

8-14 Newton Street in Mount Maunganui sold for $5.3 million to Ample Escalation Ltd. Situated on two freehold sites over 6,500 sqm, the properties are leased to two tenants.

Industrial Main Centres Prime Yields



Source: Colliers International Research

Industrial property market

New Zealand Prime Industrial Indicators		
Prime Combined Rentals (% Change)*	12 months to Sept-16	12 months Forecast
Auckland	5.9%	2.0%
Wellington**	4.6%	2.5%
Christchurch	1.0%	0.0%
Prime Capital Values (% Change)	12 months to Sept-16	12 months Forecast
Auckland	20.3%	5.0%
Wellington	12.8%	6.0%
Christchurch	10.9%	2.25%

Source: Colliers International Research
* A combination of industrial office and warehouse space at a ratio of 20:80 ** Gross rents

A global trend spurring purchasers on to push up prices has been the lower interest rates on offer. According to the indicative 3-year commercial borrowing rate from ANZ Bank (see page 2), the rate has decreased from 5.42% to 4.81% between September 2015 and October 2016. Despite this, not all purchasers across New Zealand have acted in the same manner when it comes to purchasing behaviour.

In the past year, Auckland average prime yields have decreased by 133 basis points. In Christchurch and Wellington, average prime yields have decreased by 83 basis points and 44 basis points respectively.

Although each region has its 'pros and cons', Auckland's average prime industrial yield has been pushed lower than the change in debt costs over the past year. This highlights the strength of the investment market, as well as strong tenant demand, increasing land values and limited availability. However, purchasers that have not focused on these metrics when purchasing may need to reconsider as the rate of change in interest rates seems to have changed over the last month.

Industrial Vacancy			
	Feb-15	Feb-16	Feb-17 Forecast
Auckland	2.6%	2.2%	2.2%
	Nov-14	Nov-15	Nov-16 Forecast
Wellington	5.4%	3.6%	3.3%
	Sep-14	Sep-15	Sep-16 Forecast
Christchurch	3.1%	2.1%	3.1%

Source: Colliers International Research

A Selection of Industrial Sales Activity						
Address	Location	Price	Vendor	Purchaser	Sale Price ($/m²)	Yield
8-14 Newton Street	Mount Maunganui, Tauranga	$5,310,000	The Outlook Partnership	Ample Escalation Ltd	$1,373	5.97%
14 Andrew Baxter Drive	Mangere, Auckland	$3,135,000	Private Vendor	Private Trust	$2,652	5.1%

A Selection of Industrial Leasing Activity				
Address	Location	NFA (m²)	Lessor	Lessee
99A Carbine Road	Mount Wellington Auckland	4,103	Derence Properties Ltd	Southern Pines Products Ltd
23/25B Porana Road	Wairau Valley, Auckland	1,850	Family Trust	Local Manufacturer

Retail property market

New Zealand Prime CBD Retail Indicators			
Prime Rentals (% Change)	12 months to Sept-16		12 months Forecast
Auckland	3.4%		4.0%
Wellington**	3.7%		2.0%
Prime Capital Values (% Change)	12 months to Sept-16		12 months Forecast
Auckland	10.3%		4.0%
Wellington	4.2%		4.2%
CBD Retail Vacancy (%)	Jun-15	Jun-16	Jun-17 Forecast
Auckland CBD	2.5%	2.7%	2.2%
Wellington CBD	8.3%	8.9%	7.1%

Source: Colliers International Research **Gross rents

Retailers should expect a boost in retail spending this summer that will take spending to new record highs. However, the accompanying chart shows that not all locations nationally will be able to set new spending records. This will likely flow through to subdued rent reviews over 2017, despite many landlords looking to increase rents after a long period of stability.

Canterbury's retail spend has remained steady over the year. Annual spending growth slowed primarily due to lower spending on household items as the peak in the residential re-build market is starting to take effect. We forecast December quarter 2016 spend will reach just over $3 billion, slightly below last year's result.

Historically lower than its southern counterpart, consumers in Waikato picked up the pace in late 2014 to spend as much as Wellingtonians. However, similar to Canterbury, the growth in retail spend in Waikato and Wellington regions has flattened out in the past 18 months. Landlords trying to convince retailers that better times ahead will enable them to increase rents may find some steady opposition.

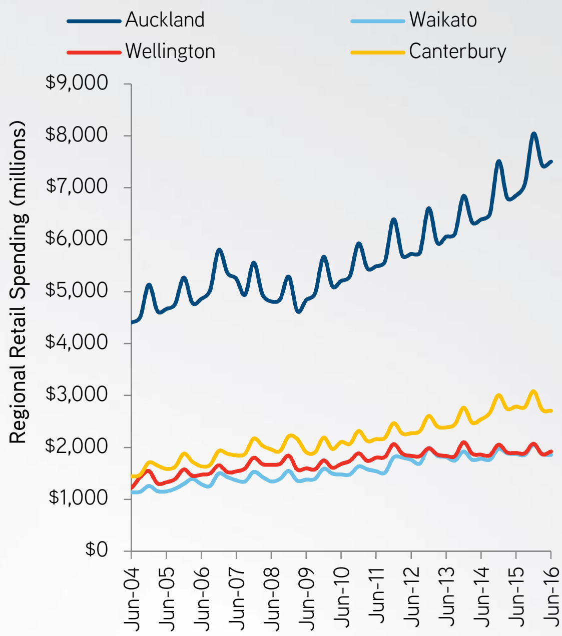
Expectations are for Auckland to continue on its growth trend that started in 2008, bringing the eighth consecutive year of outperformance. Auckland retailers should be budgeting in rent rises for 2017, and purchasers should consider firmer yields.

The Landings

Cnr Theodosia Street and Elizabeth Street, Timaru, Christchurch

Four new retail units in Timaru's The Landing have sold for more than $3 million to various purchasers, reflecting yields between 6-6.6%. Retail units sold are leased to Columbus Coffee, Burger Fuel, Pita Pit and Hells Pizza.

Regional retail spending



Source: Colliers International Research

A Selection of Retail Sales Activity						
Address	Location	Price	Vendor	Purchaser	Sale Price ($/m²)	Yield (%)
The Landings – Timpany Walton Lawyers	Timaru, Christchurch	$2,439,000	Timaru Retail Project Ltd	Private Investor	N/A	6.9%
The Landings - Pita Pitt, Hells Pizza, Columbus, Coffee and Burger Fuel	Timaru, Christchurch	$3,267,000	Timaru Retail Project Ltd	Various Private Investors	Various	6-6.6%
Cotton On, 229 Fraser Street	Tauranga South	$2,260,000	Hadley Holdings Ltd & Mclachlan Enterprises Ltd	Private Investor	$3,358	6.7%

A Selection of Retail Property Leasing Activity				
Address	Location	NFA (m²)	Lessor	Lessee
17 Mayo Road	Wiri, Auckland	13,350	Argosy Property	The Warehouse
43 High Street	Auckland Central	151	Kegg 43 Ltd	EB Games

NZ Listed Property Update

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Despite little change to underlying property fundamentals, the listed property sector has seen a material sell off in recent months, albeit this isn't inconsistent with the broader equity market. As share prices drift back towards asset backing (net tangible assets per share) we see value in the sector which is underpinned by a still buoyant commercial property market and quality portfolios. The upcoming November reporting season will provide colour on how well listed assets have captured market rental growth and benefitted from cap rate compression over 2016. We are expecting strong top line growth for most stocks, albeit this is largely boosted by acquisitions and developments (scale) and not true organic growth, which is reflected in the more modest dividend growth.

Significant re-rating for the listed property vehicles

Listed property vehicle (LPV) share prices have fallen -6.8% on average since the start of September (as at 4 November 2016). We view this selloff as largely macro driven, impacted by rising interest rates. Since its mid-August low, the short end of the NZ interest rates curve is up around +25bp and the long end is up around +45bp. The average gross dividend yield for the listed property stocks is up +50bp over the same period (currently 7.1%), highlighting the currently very strong correlation between property stock prices interest rates. Despite this re-rating, the sector has displayed defensive attributes, outperforming the broader equity market where share prices are down just under -10% since the start of August. Listed property has generated a total return (including dividends) of +4.9% year to date (NZX50G +7.2%), and only given up part of the strong performance seen earlier in the year.

Lower gains implied for asset values

Following the recent pull back in share prices, the sector premium to book value (share price to net tangible assets per share) has pulled back to 8%, significantly lower than the 15%+ premium it has traded for most of 2016 (See chart below). This indicates that share prices are implying a +5% uplift for asset values, equating to around 35bp of cap rate compression excluding any market rental growth. This feels manageable in the current environment, with book values reflecting March and June valuations and continued cap rate compression seen across a number of sectors post this. Argosy is the only LPV to date to report an interim revaluation in FY17, with a +2.6% uplift in asset values across its portfolio for the six months to 30 September.

Strong November reporting season expected

Seven LPV's will report first half FY17 results in November with the recently listed Investore reporting its maiden result. We are expecting significant top-line growth numbers for some LPV's on the back of acquisitions and developments (Goodman and Kiwi Property) as well as lease termination fees (Argosy), however caution reading this as organic growth. Despite the recent increase in wholesale rates, LPV's continue to benefit from historic swaps rolling off and this will benefit interest costs and bottom-lines. Four LPV's have managed to lift dividends in FY17, with a median increase of +2.3%, which is more representative of underlying like-for-like growth. Augusta will be the standout result with significant fees from recent deals driving a +46% lift in earnings. Of interest will be underlying rental growth for portfolios, particularly for Auckland industrial and office assets given the recent market rental strength in these sectors.

Listed property price to net tangible assets

Source: Company reports, Forsyth Barr analysis, Note: Series reflects stock P/NTA's weighted by market capitalisation.

368 offices in 62 countries on 6 continents

United States: 140
Canada: 42
Latin America: 20
Asia Pacific: 81
EMEA: 85

$2
billion in
annual revenue

1.12
billion square feet
under management

13,500
professionals
and staff

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