

Market Overview

The occupier and developer sectors of Auckland’s industrial market have remained under pressure over the last year as a result of a still weak economy. Market conditions are unlikely to significantly improve until the economy experiences a number of consecutive quarters of strong economic growth. Yields stabilised over the latter part of 2009, in particular for better quality properties, tenant demand and enquiry, however, remains well below that of recent years. Investors have become more discerning in terms of not only building quality and location, but also price and tenant quality.

Table 1 presents a summary of indicative prime net effective rents and land values for Auckland’s main industrial sub-markets as at March 2010.

Table 1: Market Summary by Sub-Market – March 2010

Location	Prime Rents (net)		Land Values (\$ psm)
	Office (\$ psm)	Warehouse (\$ psm)	
North Shore / Albany	\$200 - \$230	\$95 - \$110	\$300 - \$450
Mt Wellington / Penrose	\$165 - \$200	\$90 - \$100	\$300 - \$450
Airport Oaks	\$170 - \$225	\$90 - \$100	\$225 - \$275
East Tamaki	\$165 - \$215	\$85 - \$100	\$275 - \$350
Wiri	\$170 - \$190	\$85 - \$95	\$175 - \$250

Source: Darroch Research

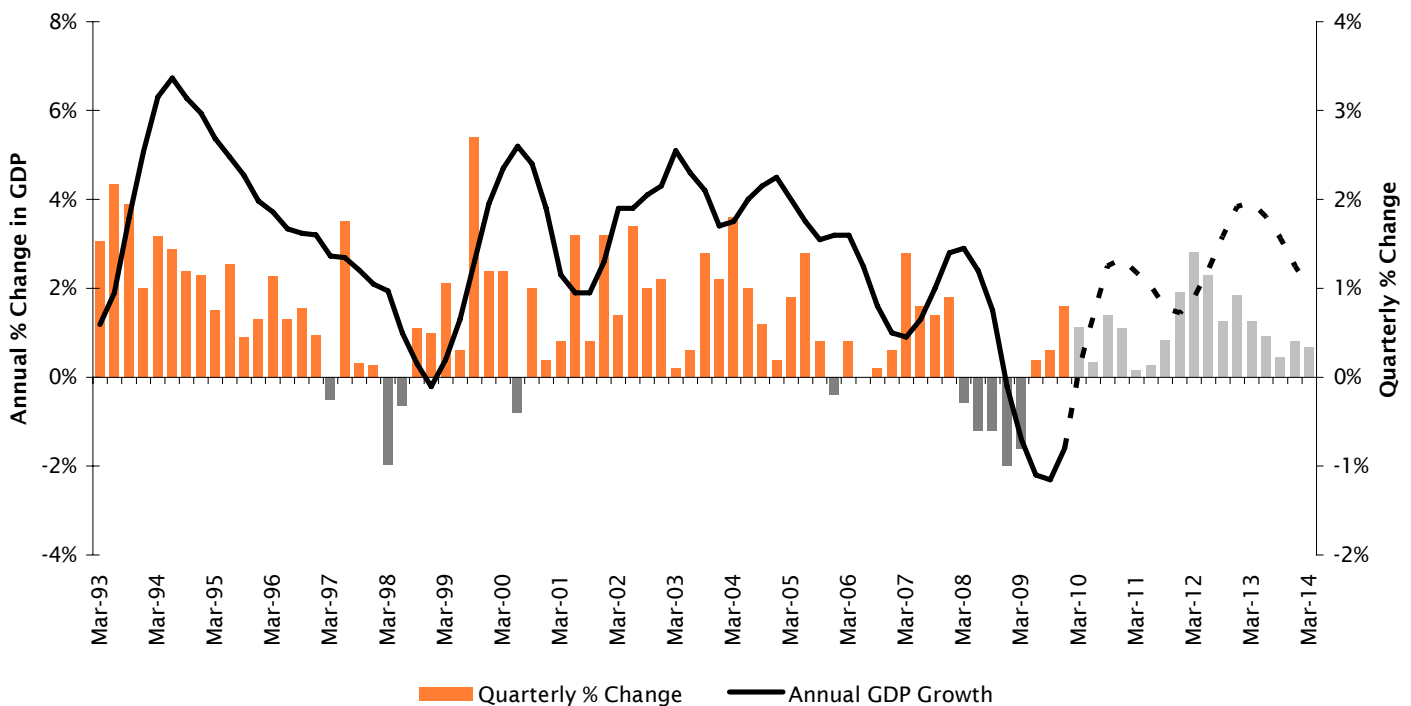
Following many years of very strong value growth, industrial land values across the region have experienced decline, vacancy rates are up and rents have softened across the board. As a result the level of industrial development activity, which over the five years up until early 2008 was uniformly strong throughout Auckland’s key industrial precincts, has fallen away, with the number of industrial building consents issued falling by approximately 46.6 % over the year to February 2010.

The Economy

New Zealand's economy experienced a consumer led slowdown over the early and middle part of 2008 which was then compounded by the global credit crisis and subsequent global economic recession. The economy contracted for five consecutive quarters, up to, and including, the first quarter of 2009, however, since then this negative trend has reversed and the last three quarters have seen positive growth of 0.2%, 0.3% and 0.8% recorded respectively. The outlook is for growth to continue to recover, albeit at a slow rate, with GDP, on an annual basis, forecast to be positive by the first quarter in 2010.

Figure 1 demonstrates the trend in annual and quarterly economic growth (GDP) since 1993 and in addition presents the growth forecast up to, and including, March 2014.

Figure 1: National Economic Growth



Source: NZIER

The economic recovery, however, remains vulnerable to a range of global and domestic influences.

In terms of positives a number of factors can be cited:

- Stronger global economic growth;
- Continued strength in the Australian economy, New Zealand's key trading partner, combined with a relatively low NZD / AUD cross rate;
- A strong rebound in commodity prices during 2009;
- A significant increase in late 2009, in Fonterra's payout for the 2009 / 2010 season;
- A recovering manufacturing sector;
- A recovery in residential building, albeit off a low base;
- Above trend overseas migration gains;
- Increased government infrastructure expenditure; and
- Lower interest rates, albeit the bottom in the current cycle has now passed, may take some pressure off household's budgets.

However, some of these factors will be offset by:

- Ongoing labour market weakness and potentially still rising unemployment;
- Short term regulatory uncertainty prior to the 2010 budget;
- A forecast easing in net overseas migration gains;
- Interest rates for the non residential sector are likely to remain high with tighter lending criteria and restrictions on the availability of credit; and
- Continued, albeit declining, volatility in overseas and domestic capital markets.

There are still some downside risks associated with current economic forecasts, both global and New Zealand growth remains fragile, and current growth expectations may overstate what is likely to occur. The upside for Auckland will be driven to a large extent by the degree to which the recovery in net migration is sustained numbers and also by the relative flow of tourists into the country. The 2011 Rugby World Cup may be the catalyst that assists to boost growth to levels at, or above, the long term average.

Land Supply

Over the five year period up until early 2008, strong economic growth resulted in a rapid uptake of industrial land and a significant increase in the amount of development activity in Auckland’s industrial market and, over this time, most industrial areas have saw land values at least double, if not triple. However, over the last year or so land values, particularly in fringe locations, have softened.

There have been few industrial land sales over the past year compared with the number seen over recent years. Examples of recent land sales are presented in Table 2.

Table 2: Land Sales Activity

Address	Location	Site Area (m ²)	Zone	Sale Date	Sale Price	Sale \$psm
25 Bishop Dunn Place	East Tamaki	3,374	Bus 6	Apr 10	\$1,113,000	\$330
2 Chonny Crescent	Wiri	30,000	Bus 5	Jan 10	Confidential	< \$200
138 Wiri Station Road	Wiri	8,000	Bus 6	Dec 09	\$1,640,000	\$205
41 Carbine Road	Mt Wellington	22,086	Bus 5	Dec 09	\$9,000,000	\$407
70 Hastie Drive	Mangere Bridge	8,000	Bus 5	Nov 09	\$1,600,000	\$200
14 Pavilion Drive	Airport Oaks	2,737	Bus 5	Nov 09	\$600,000	\$219
48 Crooks Road	East Tamaki	8,695	Bus 6	Nov 09	\$3,750,000	\$431
8 Alfred Street	Onehunga	7,578	Bus 6	Sep 09	\$2,400,000	\$317

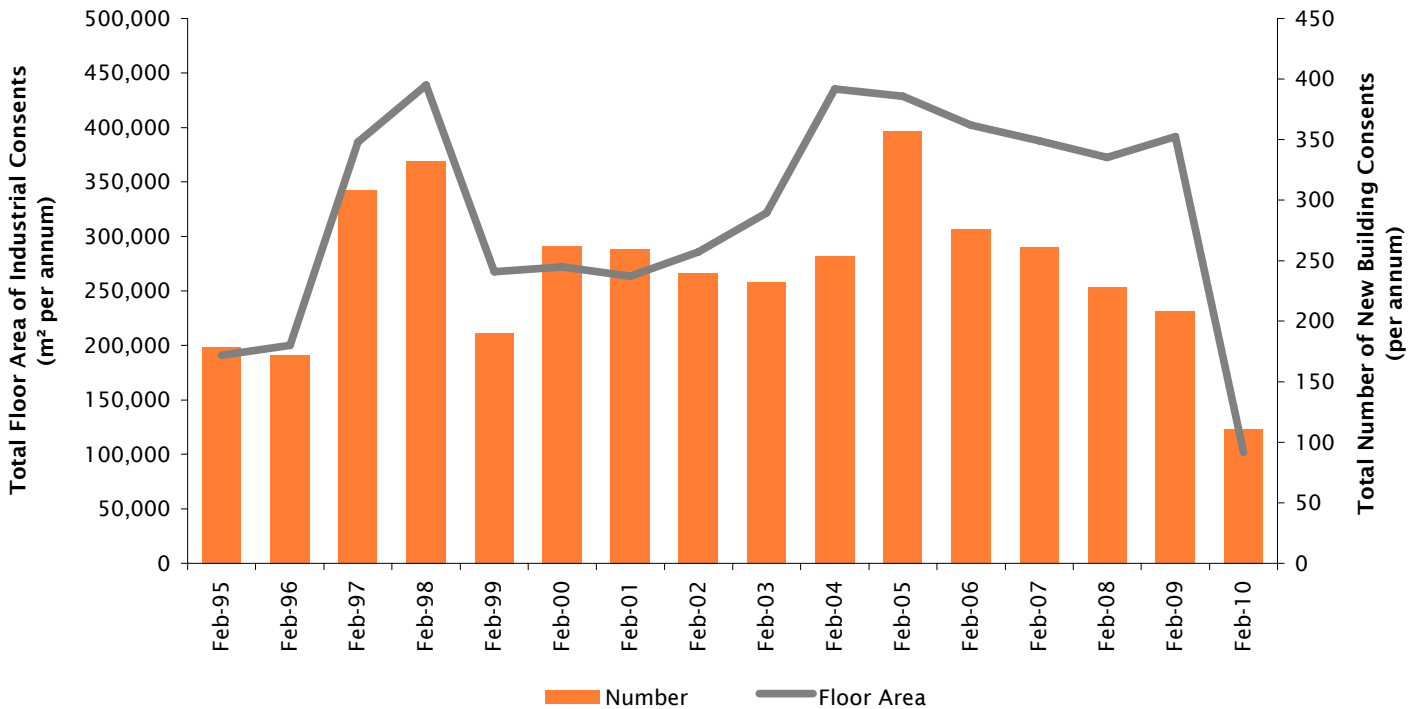
Source: Darroch Research

Development Activity

A large proportion of recent development activity has been concentrated in and around Manukau City and has been driven by freight forwarding / logistics operations seeking greater integration of their distribution / storage and transport functions. These developments have focused on the construction of modern, high stud distribution facilities close to major transport nodes. This trend is expected to continue, however, the limited availability of industrial zoned land in and around South Auckland is resulting in a north and south development drift.

The amount of development activity in Auckland’s industrial market has eased substantially over the last eighteen months. Figure 2 presents the trend in the number of new industrial building consents issued annually in the Auckland region area since 1995.

Figure 2: Industrial Building Consents



Source: Statistics New Zealand

There had been a steady decline in the number of industrial consents issued over the four years up to and including 2009. Over the last 12 months the number of new industrial building consents in Auckland fell much more dramatically, from 208 in the year to February 2009 to 111 in the year to February 2010, a decline of 46.6%. The floor area associated with industrial consents has also declined significantly over the past twelve months, down from 391,506 square metres in the year to February 2009 to 101,907 square metres in the year to February 2010, a fall of 74.0%.

The reduction in the number of consents is largely in response to a much weaker economy and a reduction in credit availability and its increased cost. Whilst tenant demand for high quality, purpose built industrial premises is still evident, albeit much weaker than eighteen months ago, many are increasingly unwilling to pay the development driven rents associated with such premises. Going forward, in the short term the occupier market will likely see weaker growth and a more cautious approach to relocation.

Leasing Activity

Prime and secondary rents for both the warehouse and office components of industrial property have fallen over the last twelve months. Whilst face rents have shown little change, incentives are now being offered to secure tenants equating to approximately two months rent free for each year of the lease term, reflecting the significant easing in tenant demand and increased competition for tenants.

Examples of recent leasing activity are presented in Table 3.

Table 3: Leasing Activity

Tenant	Location	Area Leased (sqm)	Term (Yrs)	Start Date	Office (Net \$psm)	Warehouse (Net \$psm)
Pacific Ronetesance	Mt Wellington	4,770	1	Mar 10	\$155 - \$165	\$90 - \$100
DHL	Mt Wellington	23,565	6	Nov 09	\$180 - \$190	\$90 - \$100
Auto Parts Centre Ltd	Onehunga	1,297	3	Nov 09	\$70 - \$80	\$60 - \$70
Auckland Private Laundry Ltd	Onehunga	1,403	6	Nov 09	\$130 - \$140	\$80 - \$90
Ricoh NZ Ltd	Penrose	1,881	6	Oct 09	\$140 - \$150	\$80 - \$90
Goodyear & Dunlop Tyres	East Tamaki	2,825	6	Sep 09	\$145 - \$155	\$65 - \$75

Source: Darroch Research

Comments include:

- Pacific Ronetesance has leased a high quality office and distribution warehouse facility constructed in 1996, located on Westfield Place, Mt Wellington. The warehouse provides a stud height of approximately 10 metres to the portal knee. The lease is for a term of one year at a rental of \$575,000 per annum;
- DHL has leased a modern industrial warehouse and office property located on Niall Burgess Road, Mt Wellington. The property was constructed in the late 1990's to high specifications with a stud height of 10 metres to the portal knee. The lease is for a term of six years at a rental of \$1,874,000 per annum;
- Auto Parts Centre Limited has leased an industrial property located on Captain Springs Road, Onehunga. The property comprises a low to medium stud factory with associated offices. The lease is for a term of three years at a rental of \$82,000 per annum;
- Auckland Private Laundry Limited has leased a 1970's era constructed industrial warehouse and associated office accommodation located on Galway Street, Onehunga. The lease is for a term of six years at a rental of \$132,000 per annum;
- Ricoh NZ Limited has leased an industrial building comprising 2 levels of office accommodation and a 5.95 to 7 metre stud warehouse located on Hugo Johnston Drive, Penrose. The lease is for a term of six years at a rental of \$165,000per annum; and
- Goodyear & Dunlop Tyres has leased a re-treading tyre plant providing a low to medium stud warehouse and associated office accommodation located on a large site on Turin Place, East Tamaki. The lease is for a term of six years at a rental of \$246,000 per annum.

Investment Market

Investor demand for industrial property was strong up until 2008; however, demand has eased over the last eighteen months, particularly for higher value properties, as access to credit has become much more of a constraint. Good quality investment stock continues to remain tightly held nonetheless, although a number of owners have selectively divested.

Recent investment sales include:

- 21 Lady Ruby Drive, East Tamaki, was sold in February 2010 for \$4.84 million on a yield of 9.0%. The property has an 8.5 metre stud height and provides additional land for future development. At the time of the sale the property was leased to Ashton Scholastic with almost 3 years remaining on the lease;
- 10-12 Autumn Place, Penrose, was sold in January 2010 for \$5.2 million on a yield of 9.9%. The property was sold vacant with 12 months deferred settlement, however, with a right to occupy from November 2010;
- 182-190 Wairau Road, Wairau Valley, was sold in January 2010 for \$5.2 million on a yield of 8.9%. The property comprises a 3,377 square metre 1970's industrial building on a 9,472 square metre site, plus 77 carparks. At the time of the sale the property was leased to Smartpay Cadmus Limited;
- 645 Great South Road, Penrose, was sold in December 2009 for \$15.2 million on a yield of 7.7%. The property currently comprises a sealed yard area plus a small workshop; however, we understand the sale was subject to the construction of a new 1,360 square metre office building. The property was sold as part of a portfolio subject to a sale and leaseback agreement to Downer EDI Works Depot with a lease term of 20 years;
- 7-9 Niall Burgess Road, Mt Wellington, was sold in November 2009 for \$22.0 million on a yield of 8.5%. The property comprises a modern warehouse and office property featuring high stud, constructed to high specifications in the 1990's. Commencing at the date of the sale a new lease was granted to tenant DHL through to 2016 with 2 and a half months rent free; and
- 78 Springs Road, East Tamaki was sold in September 2009 for \$53.0 million on a yield of 8.8%. Situated on the corner of Springs Road and Kerwyn Avenue, this is the main property on the Fisher and Paykel Appliances Global Headquarters campus, comprising 2 large high stud warehouse manufacturing areas and a high quality head office complex. The property was sold subject to a sale and leaseback agreement to Fisher and Paykel Appliances for a term of 15 years from settlement.

Yields have continued to ease over the past 12 months, although Prime yields appear to have stabilised over the latter half of 2009. Secondary industrial yields, in the face of increasing vacancy and weaker rents, may face further yield softening over the short term.

Table 4 presents a summary of investment trends in the Auckland region.

Table 4: Auckland Industrial Investment Trends

Location	Market Rate		Investment Market	
	Yield	Market Outlook	Demand	Availability
Mt Wellington	8.00% - 9.50%	Stable	Selective*	Variable
East Tamaki	8.25% - 9.75%	Stable	Selective*	Variable
Airport Oaks	8.50% - 9.75%	Stable	Selective*	Variable
Albany	7.75% - 9.75%	Stable	Selective*	Variable

Source: Darroch Research

* Demand still exists for high quality, well leased properties; however, investors are being a lot more selective than over the recent years.

Table 5 presents the total return delivered by retail, industrial and CBD office property over the last year, two years, five years and ten years.

Table 5: Retail, Office and Industrial Annual Compound Returns

To December 2009	NZ CBD Office	NZ Industrial	NZ Retail
1 Year	-9.8%	2.4%	-1.3%
2 Years	-1.9%	3.6%	-1.2%
5 Years	11.8%	11.8%	10.7%
10 Years	10.0%	11.5%	11.5%

Source: Darroch Research and the New Zealand Property Council

N.B. Return series are based on the New Zealand Property Council's Index up to March 2006, and since then Darroch's return series

Returns across all New Zealand property sectors have been relatively strong over the last 5 to 10 years, however, the past 24 months has seen a significant fall in returns across all property sectors. Both the CBD office market and retail market have under performed the industrial sector in terms of annual returns, whilst the industrial market is the only property category to maintain positive returns over the last 2 years. Typical yields for industrial property have increased, albeit only slightly, over the past year, ranging between 8.00% and 9.75%.

Market Outlook

A significant realignment of financial markets coupled with questions around the strength of the economic recovery, has resulted in an extremely uncertain operating environment for many businesses. Market conditions are unlikely to significantly improve until the regional economy experiences a number of quarters of strong economic growth. As a consequence, we anticipate that development activity, despite recent increases in business confidence and manufacturing activity, will continue to be constrained for some time to come. We would therefore expect industrial development activity, over the next year, in the Auckland region to be well below its five year average.

Over the last two years industrial land values have fallen significantly over the whole Auckland region. This is a response to a range of factors including much weaker end user demand, credit constraints and a general repricing of all asset types, including land. Whilst the 2008 / 2009 recession will continue to have a negative effect over the short term, the demand for vacant development sites is likely to strengthen over the medium to long term. Over the short term, the investor market will also be constrained by the increased cost and reduced availability of credit, however, over the longer term, developers and investors envisage a shortage of suitably zoned sites to develop in preferred locations and consequently, where able, are likely to land bank sites as they become available. Investors are still seeking good quality industrial investments, however, investment activity is stronger at the lower value end and as property values increase the number of potential investors falls away.

The period up until late 2008 saw industrial rents increase as a result of strong demand and increased development costs. The escalation in rents has reduced the affordability of new space for tenants and consequently, going forward, we are likely to see tenants increasingly weigh up the advantages and efficiencies associated with new space compared to their existing premises, against the additional cost.

Over the last year rent levels, in the face of much weaker tenant demand and increased vacancy, have fallen across the market. Yields have continued to ease over the past 12 months, although Prime yields appear to have stabilised over the latter half of 2009, and while some further yield softening is possible, particularly secondary industrial yields, we anticipate a degree of stability emerging over the next twelve months.

For more information,
please contact:

Darroch Limited
Level 16
Auckland Club Tower
34 Shortland Street
Auckland NZ
Tel: +64 (0)9 309 3040

www.darroch.co.nz

Contacts

Key Auckland Contacts

Consulting and Research

Ian Mitchell
+64 (0)4 460 3857
ian.mitchell@darroch.co.nz

Property Services

Andrew Potter
+64 (0)9 374 6659
andrew.potter@darroch.co.nz

Sales and Investments

DTZ New Zealand Limited MREINZ
Licensed Real Estate Agent (REAA 2008)
Kevin Richards
+64 (0)9 374 6621
kevin.richards@dtz.co.nz

Valuation

John Darroch
+64 (0)9 374 6613
john.darroch@darroch.co.nz

Plant and Machinery Valuation

Peter Todd
+64 (0)9 374 6619
peter.todd@darroch.co.nz

New Zealand Office Contacts

Auckland

John Darroch	+64 (0)9 374 6613	john.darroch@darroch.co.nz
--------------	-------------------	----------------------------

Wellington

Milton Bevin	+64 (0)4 460 3853	milton.bevin@darroch.co.nz
--------------	-------------------	----------------------------

Christchurch

Lance Collings	+64 (0)3 363 5044	lance.collings@darroch.co.nz
----------------	-------------------	------------------------------

Disclaimer and confidentiality clause

Every effort has been made to ensure the soundness and accuracy of the opinions, information, and forecasts expressed in this report. Information, opinions and forecasts contained in this report should be regarded solely as a general guide. While we consider statements in the report are correct, no liability is accepted for any incorrect statement, information or forecast. Darroch disclaim any liability that may arise from any person acting on the material within. Readers should take professional advice from a member of Darroch prior to acting on any matter contained in this report.

All Rights Reserved. No part of this work can be reproduced or copied without prior permission in writing from Darroch Limited.

© Darroch Limited *in international alliance with DTZ*