The Whillans Report

AUCKLAND MARKET UPDATE / 3RD QUARTER 2015

Whillans Realty Group Completes $170 million in Q3

Another strong performing quarter for my team who completed nine sales totalling $170 million. Interestingly, these sales were evenly split between local investors and Chinese developers, with the majority of sales transacted off market, reflecting both the strength of our client base and our strong links into the rapidly growing Chinese market.

Sales included the Hobsonville Town Centre site for $16.15 million (Brokers Henry Thompson and Kathy Ying), a 137 lot subdivision in Parkview Drive in Gulf Harbour for $16.3 million (Kathy Ying). And Henry Thompson sold 86 Parnell Road for $8.6 million and 272 Parnell Road for $11.25 million.

Recognising the growth of our Asian business we welcome Analyst Ellen Feng to the team. With a double degree in Psychology and Statistics, and fluent in Mandarin and Cantonese, Ellen joins us having previously been an analyst with the New Zealand Government.

Moving into the last quarter of 2015, my team has never been busier as we launch our final round of marketing campaigns, wrapping up what already has proven to be a stellar year.

Bruce Whillans
Managing Director — WHILLANS REALTY GROUP
bruce.whillans@whillans.co.nz

Parkview Drive, Gulf Harbour

86 Parnell Road, Parnell

272 Parnell Road, Parnell

Countdown Lincoln Road

Aeroparks, Airport Oaks

Hobsonville Town Centre

Market 2015 Third Quarter Update

CBD Office (Q3)

The CBD office market continued to experience strong net effective rental gains over the first half of 2015, led by falling vacancy rates and reduced incentives being offered by landlords. The total CBD vacancy rate now sits at 7.3%; the lowest level in nearly two decades. Measured against Australia's capital cities, Auckland now has the second lowest CBD office vacancy rate in Australasia. Prime effective rentals increased by 4.7% in the year to September, with secondary office rentals improving by 10.7% over the same period. Cap-rates are now on par with their pre-GFC lows, with the indicative prime office yield firming 31 basis points in the last six months to 6.91%. Prime office vacancy rates at 1.6% continue to hover near structural lows, but there are downside risks to vacancy levels over the medium term if all proposed office developments eventuate. With the ten year average CBD office net absorption rate around 17,000m^2 (25,000m^2 for prime), demand will be unable to keep pace with the mooted supply coming on stream in 2018 and 2019. We anticipate that this new supply will push the total CBD vacancy rate above its 10 year average of 9.9%. Relief may, however, come in the form of significant secondary office conversions and the likely withdrawal of several of these slated office projects as indicated by some developers.

Auckland CBD Office Market Summary* (CBRE)

	PRIME	SECONDARY	PREV 6MTH TREND
Vacancy	1.6%	11.4%	Decreasing
Effective Rent	$391.00	$225.00	Increasing
Yield	6.91%	7.75%	Firming
Incentives*	5.6 mths	6.4 mths	Decreasing

***Based on an indicative new 9 year prime and 6 year secondary lease**

Auckland Industrial (Q3)

The secondary industrial market recorded robust growth in the 12 months to September with indicative net effective rental rates improving by 4.6%. Prime industrial rentals are showing signs of activity improving by 3.6% over the last year. Yields continue their downward projectory with prime industrial firming by 28 basis points in the last 12 months and secondary yields firming by 27 basis points over the same period. Growth in industrial land values appear to have stalled, improving by 0.6% in the last six months and only 2.1% year-to-date. Despite this lull in land values, it is still difficult for new build 'spec' projects to stack up. However, it is encouraging to see prime industrial rentals appreciating at a faster rate than land values, a critical step towards making new build development feasible.

Auckland CBD Industrial Market Summary* (CBRE)

	PRIME	SECONDARY	PREV 6MTH TREND
Vacancy	0.6%	2.6%	Decreasing
Effective Rent	$121.60	$90.50	Increasing
Yield	6.69%	7.92%	Firming
Land Value	$525	$225	Flat

The Whillans Report

AUCKLAND MARKET UPDATE / 3RD QUARTER 2015

Market 2015 Third Quarter Update Continued

CBD Prime Retail (Q3)

Indicative Queen Street rentals surged over the six months to September, supported by a flurry of new leasing activity on lower Queen Street. In the last six months, indicative retail rentals improved by 31.5% and now sit at $3,400/psm. Top end retail premises are leasing for well over $3,500/psm, with smaller retail premises achieving rates in excess of $4,000/psm. The indicative prime CBD retail yield improved by 10 basis points to 5.29% over the first half of the year. Nespresso, Chanel, Tiffany, Peter Alexander, Elizabeth Arden, Hugo Boss, Farmers, and Country Road have all commited to new premises with Swedish retail giant, H&M, commiting to its first door at Sylvia Park.

Auckland CBD Prime Retail Market Summary* (CBRE)

	AVERAGE	HIGH	LOW	PREV 6MTH TREND
Rent	$3,400	$4,000	$2,600	Increasing
Yield	5.29%	5.00%	5.50%	Firming

Has Mixed Use Land Peaked? Brendan Keenan *Senior Analyst*

Is the market for Mixed Use land about to peak? What effect do net migration, Chinese capital controls and the wider residential housing sector have on this market?

In this report, we will examine the historical performance of Mixed Use land values, and the relationship between Mixed Use land and Auckland apartment values. We will also determine and evaluate developing trends in the housing market, which provide an interesting insight into the future performance of this sought-after land category.

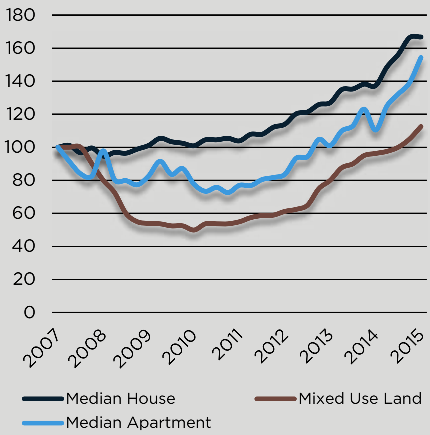
The majority of Mixed Use land under the current operative district plan is centred around the CBD fringe; in the suburbs of Eden Terrace, Newton, Ponsonby, Newmarket and Parnell. The Mixed Use zone delivers a high degree of flexibility as it allows for residential, office and retail development. The zone has a 15 metre height limit and a maximum floor area ratio of 4:1.

Under the Proposed Auckland Unitary Plan, the zone will retain many of its existing features, however, additional density will be introduced with an increase in height limits.

While the Mixed Use zone is influenced by both the office and retail markets, residential development makes up the lion's share of land use. By way of example, a 1,000m² development site can potentially cater for upwards of 250 office workers, however, the same site would only be able to house 40 apartments, or approximately 70 occupants. Residential development inherently requires more land and it therefore has the biggest influence on Mixed Use land values.

By overlaying the performance of median Auckland apartment prices with Mixed Use land values, and by using the previous market peak as a base, a clear relationship emerges between the two markets.

Mirror Markets
Mixed Use Land, Housing and Apartment Index

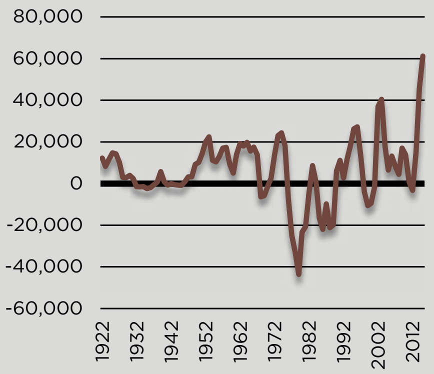


When the global financial crisis reached New Zealand in the first quarter of 2008, apartment and land prices began a precipitous three year decline. It was not until the second half of 2010 that both markets hit their rock bottom, losing investors, developers, and their creditors billions of dollars. Measured against their pre-GFC highs, apartment prices lost approximately one third of their value and Mixed Use land prices lost 50% of their value.

Following the collapse of mezzanine finance companies and a freeze on development lending by major trading banks, the extent of the decline was more severely felt across land values. Underpinned by physical improvements and capable of generating income, apartment values fared better. However, median Auckland house prices barely dipped below their pre-GFC peak over the same period and have recorded strong year-on-year growth since 2009.

Since Statistics New Zealand began record keeping in the early 1920's, the data showed that from mid-2013 until now, net-migration went from having consistent growth to the strongest net-migration gains ever recorded. We are currently experiencing the largest migration wave in New Zealand's history and it was no coincidence that

Migration Skyrockets
Annual Net Migration Sept 1922-2015 (Statistics NZ)



by the second half of 2013 the housing market shifted from respectable to turbo-charged growth.

The performance gap between the Auckland apartment market and the wider Auckland housing market has gradually closed since 2011, with the apartment market on track to realign itself with the median house price index. The migration gains over the last 24 months have propelled apartment values to new highs, and in the process, they have sent Mixed Use land values back above their pre-GFC peak.

While this is good news for owners of apartments and Mixed Use land, it also serves as a cautionary warning sign that we could be reaching the peak of this cycle. In boom times, the premium paid between safe and riskier assets narrows, as it has between apartment values and the median Auckland house price. A similar situation is developing between Prime and Secondary office and Prime and Secondary Industrial assets across Auckland.

While it is still early days, there is anecdotal evidence of residential fatigue. Choppy median sales results, lower auction clearance rates and affordability limits being tested, suggest the market is beginning to tap the brakes.

Continued... Has Mixed Use Land Peaked? Brendan Keenan *Senior Analyst*

Macroeconomic data is also weighing in with lower GDP growth, weak wage inflation and unemployment drifting upwards. At the same time, record migration, lower borrowing costs and rising rental rates across Auckland are providing a counterbalance to these negative forces. However, the new IRD reporting rules and tax measures aimed at investors will create further headwinds, offsetting future growth.

Of particular concern is the recent crackdown by Chinese authorities on the illegal flow of money leaving China. In an attempt to control money exiting China, authorities have clamped down on shadow money agents and other illegitimate practices used for siphoning funds out of the Middle Kingdom. Our previous Whillans Report indicated that the flow of capital leaving China would continue to grow exponentially. However, who could have predicted the reaction by Chinese officials following their stock market meltdown and a weakening economy? While their hardline response has only served to boost demand to get funds out of China, authorities are making it increasingly difficult for Chinese nationals to do so.

Backroom methods; such as pooling $50,000 USD payments through friends and family members, overpaying for imports, buying fake consultancy services and forging deals with foreign subsidiaries are being put under the microscope. The effects of this crackdown was first flagged by the Australian Financial Review last month as Sydney auction rates plummeted and Chinese buyers remained visibly absent. We are now beginning to see a similar drop at the major residential auction houses here in Auckland.

If Chinese authorities maintain this stance there are risks of a fallout, particularly within the apartment market targeting investors. The ability to get funds out of China means settlement risk is a real possibility, and this could have a wider knock-on effect for the apartment and land markets.

With practical completion for many projects one to two years away, there is still plenty of water to go under the bridge. However, there are downside risks as the economic situation in China deteriorates and the government attempts to control capital flight. While the larger institutional and billionaire class Chinese investors have the means to legitimately invest outside of China, the financial success of many development projects still depends on end user takeout by private individuals, many of whom are Chinese nationals.

We predict Mixed Use land values will begin to reach their cyclical peak over the next six months. Although, a serious correction does not seem to be on the cards, the heady days of double digit land growth appear to be fading. Movements in house and apartment values, net migration and Chinese capital controls should all be key metrics to watch when assessing where the Mixed Use land market is heading over the rest of the year and into early 2016.

Auckland CBD Land Sales

CBD Land Sales

Address	Property	Proposal/Development	(m²)	Sale Price	$/psm	Date
28 Shortland Street	Auckland Star Site	Resource Consent for a 26 level tower with 171 carparks.	2,010	$26,000,000	$12,935	Apr-14
85-89 Greys Avenue	Carpark	No known consents.	5,223	$18,000,000	$3,446	May-14
57 Wakefield Street	Golden Pool Massage Centre	No known consents.	767	$3,780,000	$5,019	Jul-14
35 Albert Street	Ex Angus Steak House Site	Resource Consent for 29 level, 225 unit apartment tower.	1,265	$11,500,000	$9,091	Aug-14
302-328 Queen Street	St James Theatre	Resource Consent for 39 level tower with 332 apartments.	3,051	$34,500,000	$11,307	Aug-14
85 Customs Street	Ex Proposed ANZ Bank Site	Resource Consent for 35,305m² office tower and 200 car parks.	1,667	$32,000,000	$19,196	Aug-14
39-47 Union Street	Ex Xanadu Site	Resource Consent for 182 apartments and 291 carparks.	3,774	$12,200,000	$3,232	Sep-14
75 Victoria Street West	Ex Palace Hotel	Resource Consent for 15 level tower.	522	$7,000,000	$13,409	Sep-14
46 Albert Street	APN Site	No known consents (lease to APN returning $2.6million p.a.)	4,258	$42,000,000	$9,863	Oct-14
184-200 Pakenham Street West	Wynyard Quarter	Future development pipeline for Goodman Group.	9,793	$40,100,000	$4,094	Oct-14
26 Poynton Terrace	Carpark	Currently being promoted for Oasis Apartment development.	334	$2,200,000	$6,586	Oct-14
44 Sale Street	Accent Building	Plans underway for a new 10,000m² spec office building.	2,175	$10,765,000	$4,949	Nov-14
52-54 Sale Street	Schischka Engineering	No known consents.	749	$3,750,000	$5,006	Dec-14
520-536 Karangahape Road	Carpark	No known consents.	1,272	$5,010,000	$3,938	Mar-15
27 Rutland Street	Vacant	Plans for 12 level student accommodation development with 146 units.	309	$4,150,000	$13,430	Mar-15
36 Fort Street	Ex Brothel House	Plans to develop high-rise mised use tower.	282	$3,000,000	$10,638	May-15
70-74 Anzac Avenue	Abandoned Building	Plans and marketing underway for high-rise apartment development.	742	$6,000,000	$8,086	May-15
38 Airedale Street	Two Level Building	Two level building. No known consents.	230	$1,475,000	$6,413	Jun-15
79-83 Beach Road	Car rental	Two level building. No known consents.	814	$5,600,000	$6,879	Jun-15
35 Whitaker Place	Vacant Land	Resource Consent for 1,082 student beds in twin tower scheme.	3,071	$14,100,000	$4,591	Jun-15
38 Airdale Street	Two Level Building	Marketed as a development site.	230	$1,465,000	$6,414	Jun-15
151 Beach Road	Ideal Electrical	Sold to a developer. No known consents.	1,032	$6,800,000	$6,589	Sep-15
2 Anzac Avenue	Carpark	Corner of Anzac Avenue and Beach Road.	938	$9,500,000	$10,127	Sep-15
7-9 Halsey Street	Millar Paterson Metals	Reported in NBR that buyer is considering a mixed use development.	561	$3,085,000	$5,500	Oct-15