

The NZ Property Development Market

Good Times

Tough Times

Learnings from the last cycle

Future Opportunities

by Patrick Fontein, 14th June 2012

- 1. Good times of the last property cycle**
- 2. Tough times: when the world turns bad**
- 3. Learnings from the last property cycle**
- 4. NZ Property Market Opportunities**
- 5. Future NZ Property Industry Participants**
- 6. Industry Issues to be Resolved in Coming Cycle**
- 7. Future Requirements for NZ Property Professionals**

Good Times of the last Property Cycle

Patrick Fontein Background

Founder and sole Director of the Kensington Group of companies in 1995 and between then until 2008 completed 20 commercial and multi-unit residential development projects, ranging in size from \$5-40M each, mainly in Greater Auckland.

Kensington's Harbourside Business Park was awarded NZ's top property development Award, the Rider Hunt Property Council Supreme Award in 2005.

Good Times of the last Property Cycle Harbourside Business Park



Good Times of the last Property Cycle Commercial Project examples



Good Times of the last Property Cycle

Residential Development Project examples



Good Times of the last Property Cycle

Patrick Fontein Background

- Auckland President of the Property Council of New Zealand from 2002 to 2004. On PCNZ Auckland Executive since 1995.
- Auckland Council Urban Design Panel Chairman: served on Auckland City's (and now Auckland's) UDP since 2004.
- Property Industry Representative on MfE Urban Design Protocol Advisory Board in 2003-2004.
- Property Council of NZ's Urban Design Champion since 2005.
- Served as the Inaugural Board Chairman of the NZ Green Building Council from 2006-2008.
- Awarded a Fellowship from the NZ Property Institute in 2005
- In 2006 was awarded the NZ Property Institute "Industry Award"

Good Times: NZ Property Development Market Conditions prevailing from 1994 to 2006

**Slow start
to 1990's
from 1980's
Recession**

- Huge vacancy in office and industrial markets in early 1990's
- Multi-unit residential started from converting vacant office buildings and encouragement from Auckland City Council with rates relief.
- Start of new multi-unit residential from mid 1990's
- Steady growth of multi-unit residential from new wave of developers

**Finance
Brokers
created
finance
availability
which drove
land prices**

- Finance structuring on larger projects mainly through specialist brokers
- Brokers created finance structures which enabled substantial leverage on land. Ready finance availability drove land prices higher and higher.
- Very aggressive lending policies from all Banks and 2nd Mortgage finance companies.
- To participate in the development market from 1998 to 2006, developers forced to pay the higher land prices (unless land banked from earlier).

Tough Times: (Macro) Global Finance Crisis (relative to NZ Property Development in 2008)

International
Finance
Markets in a
major mess

- 2006-2007 US Collateralised Debt & Sub-prime crisis
- Aug-Sept 2008 Lehman Bros collapse,
- Global Banking system on verge of collapse
- Governments bailing out Banks in most countries



NZ 2nd
Mortgage
Finance
Market also
in major
distress

- Structural problems in 2nd Mortgage market. Borrowing short from Ma and Pa, lending long to developers on long term projects
- Dodgy finance companies collapse. Loss of confidence from investors.
- Run on finance company deposits, finance companies can't repay quick enough
- Most of NZ larger property development projects funded by 2nd mortgage funds

NZ's primary
banks
couldn't get
access to
cash

- NZ Banks reliant on overseas debt markets for funds
- GFC totally dried up international funds. NZ Banks short of cash
- Bank's response is to stop lending wherever possible
- NZ Govt has to guarantee deposits, propping up Banking system
- Direct instructions to Bank managers to call in development land loans

Tough Times: Huka Falls Resort in Taupo

2008 Debt: \$20m 1st ANZ; \$10m 2nd Mortg; \$8m Cash Equity



Tough Times: Huka Falls Resort in Taupo

2008 Debt: \$20m 1st ANZ; \$10m 2nd Mortg; \$8m Cash Equity

ANZ Bank
call early
meeting to
prepare for
Finance mkt
issues

- Late 2007, ANZ sends 2 senior managers from Aus to ready NZ development clients for finance market tightening
- Feb 2008: ANZ call formal meeting to review all NZ projects, incl HFR.
- March 2008: next formal meeting: ANZ request “downsizing action plan”
- April-August 2008: complete existing HFR stages, no new stages to commence; downscale project outgoings.

Orderly and
structured
process by
ANZ results
everyone
being repaid

- Taupo residential sales market very difficult, but HFR project is surviving
- Sept 2008: Orewa Receivership; HFR continues sell-down
- Oct-Dec 2008: Continue sell down; all construction finishes, everyone paid
- Feb 2009: New Ownership and Director structure in place, keep selling down completed properties in an orderly fashion.
- Feb 2010: ANZ fully repaid; 2nd Mortgagee now 1st and controls land
- Today: New stages of development re-commenced

Tough Times: Kensington Park in Orewa

2008 Debt: \$65m 1st BNZ; \$20m 2nd Mortg; \$32m Cash Equity



Tough Times: Kensington Park (KP) - Orewa

2008 Debt: \$65m 1st BNZ; \$20m 2nd Mortg; \$32m Cash Equity

Great sales start. Need BNZ to provide funding suited to large staged project: IFM

BNZ insist on passive shareholder PG's even though BNZ had earlier agreed no PG

Receivership. BNZ reject \$35m cash bid turned down. BNZ net \$13m BNZ pursue Patrick to bankruptcy

- Late 2005: BNZ provided KP Shareholders Agreement: no Shareholder PG's
- June '06: Settle land \$38m; start Infrastructure & Stage 1 houses at KP
- Sep-Dec'06: Soft Sales launch: sell \$30m: 50/61 Stage 1A,1B properties in 4 mths!
- Feb '07: KP provides 33 page report to BNZ: Integrated Funding Model (IFM)
- Mar'07: Sales go crazy: 1,300 people at official launch weekend: sell \$15m in 1 wk
- Jun '07: Formal written IFM Offer from ANZ: BNZ says will match, need time
- KP decide to stay loyal to the BNZ, despite ANZ offer for IFM; presales \$70m
- Sept'07-May'08: BNZ impose new credit rules: 10 in 8 mths: want investor PG's
- Sept'07-May-'08: Shareholders Equity increased from \$14m to \$32m cash
- April-Aug '08: Stg 1B units settling: BNZ loan from \$65m to \$42m; 39.5%LVR
- May '08: KP wins 3 International Prop Awards: Top 10 in world; 3,500 entries
- Apr-Aug '08: BNZ insist on PG's from KP's 3 passive investors; who refuse.
- 13 Aug '08: KP call formal BNZ meeting, no PG's. BNZ: "we'll get back to you"
- 25 Aug '08: BNZ 1st response: issue "Formal Default Notice": "expired land loan".
- Patrick in impossible position: BNZ insist on new conditions; investors refuse PG's.
- 11 Sep'08: BNZ Call in Loan = Receivership: BNZ: "Best manner to recoup BNZ \$"
- Oct-Nov '08: Carrus Gp approach PF. Carrus offer \$35m cash u/c, settle Dec '08.
- Jun '09: BNZ sell KP to John Sax for \$20m; BNZ net \$13.1m after \$6.9m of costs
- Oct '09-Now: Southpark re-start KP; same MPC concepts; PF consults for KP;
- Oct'09: BNZ start PF bankruptcy action, "allege gross financial misconduct"
- Oct'10: BNZ have 4 lawyers in High Court. PF at Court to defend personal integrity.
- Judge: "You made an error of judgement, you should have matched your land loan term repayment with your ability to pay". No misconduct found in 20 pg Judgement
- Oct'08: NZ Govt bail out the BNZ for 2nd time, guaranteeing bank deposits

Learnings from the last Property Cycle: Behaviour of others in Adversity

Until adversity hits, you will not understand the true depth of your relationships

How did
People
respond to
those in
Tough Times

- Do you offer real proactive support when someone in Tough Times needs it?
- I received tremendous support from many people: I will always be grateful
- Some people responded in an odd manner. In the end it reflects badly on them
- One senior manager just didn't show up to work for 7 days, when we needed him most. Didn't answer his phone: He went to Australia for a week!
- Most staff, suppliers, purchasers, industry colleagues were very supportive

How did
**Partners /
Suppliers**
respond to
adversity

- What do you say to you 10 year old son when he asks: "Dad, what are these 2 men in black jackets with baseball bats doing at our front gate?"
- Creditors/suppliers use a wide range of tactics to get to the front of the queue!
- You learn a lot from your partners in adversity: make sure you are aligned!!
- When a customer is in strife, do you use this to your advantage or help them? True loyal partners or suppliers help out those in trouble, rather than exploit!

How would
your
Financier
respond to
adversity ?

- Many people say they have a great relationship with their bank. However it's not until adversity hits that you will understand the depth of your relationship.
- Who said all Banks were the same? Their response to adversity varies a lot.
- A number of Banks took a proactive approach, recognising the entire finance industry was in meltdown. How can we work together to optimise outcomes?
- In Adversity would your Bank be: "your Partner" or a "good times" friend?

Learnings from the last Property Cycle:

Behaviour of Yourself in Adversity: “Integrity?”

“Tough Times” define a person’s true character and inner moral fibre

How do you
Yourself
act when
faced with
adversity?

- All developers have assets in separate companies and trusts. Should you use assets gained from earlier achievement to assist new ventures or ring-fence?
- As troubles start to arise, do you quickly shuffle the cards and hide assets?
- When faced with huge financial stress, will your morals and ethics stay strong?
- When others start to use unsavory behaviour, how do you respond? Maintain your level of integrity or stoop down to their level of behaviour?

My response,
right or wrong:
Commit 100%
of previous
gains Integrity
is more
important than
our personal \$

- All our assets were protected in family trusts, since starting the company.
- KP’s 3 passive shareholders were to be the main cash equity providers.
- When KP needed more cash, my wife and I sold all our commercial properties, increased the mortgage on the house, sold the beach property, boat, everything
- A further \$18m cash was injected into KP by shareholders from Sep’07-May’08
- Many other developers have all their assets still protected even whilst bankrupt
- Maintaining integrity has provided many rewards: Huge support from many in the industry and much assistance in initiating new consulting engagements.

**Personal
Learnings**
for the next
Property Cycle

- **PG’s:** Why should one provide Personal Guarantees? Especially when a Bank knows your full personal financial affairs, and if these don’t change, should they not take some of the risk in a Project for the Margin they collect?
- **Contingencies:** I used to think we managed risks pretty well. Not well enough! Have far more back-up contingency for every conceivable eventuality.

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- An aerial photograph of a large commercial building complex, likely a corporate headquarters or regional office. The building is a long, multi-story structure with a white facade and a prominent red sign that reads "OLIVER YOUNG". The building is surrounded by parking lots filled with cars, and there are green spaces and trees interspersed throughout the site. The overall scene depicts a modern, well-developed commercial area.
- 1. Master Planned Communities**
 - 2. Mixed Use Intensification Projects**
 - 3. Converting dead Malls to Mixed Use Centres**
 - 4. Residential 4-20 Unit Projects on 1,000 - 2,000 m2 sites**

NZ Opportunities in the next 5-15 years

Master-Planned Communities

Master-Planned Communities will be the dominant major community format

Auckland University Campus

- \$1.2B Campus Expansion
- 10 Year Programme
- Will include substantial Residential for Mixed Use



NZ Opportunities in the next 5-15 years

Master-Planned Communities

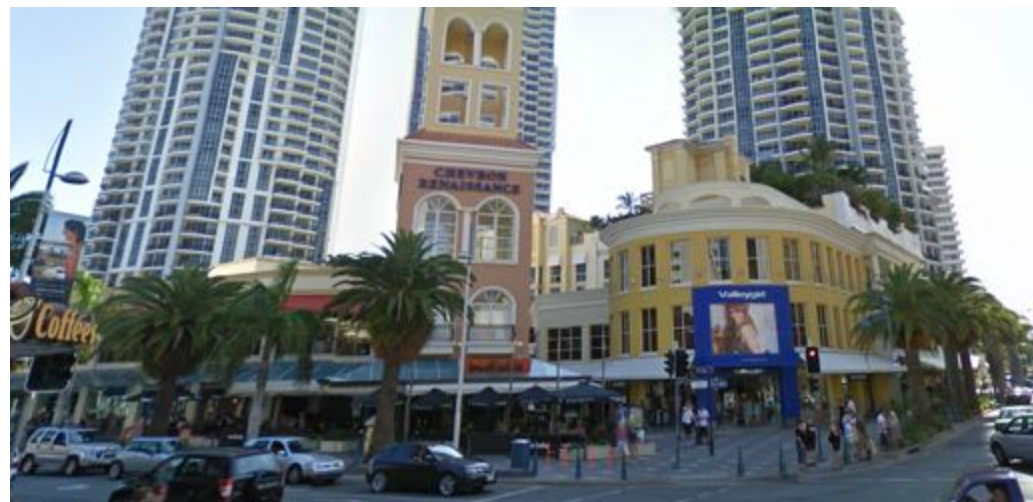
Master-Planned Communities will be the dominant major community format

Tamaki TOD (Transit Oriented Development)

- 16 Hect site, by Tamaki Train Station
- Auckland Council and Charta Group (through Kauri Fund) are partners
- Mixed Used Developm commence 2014
- Office, Resident, Retail



NZ Opportunities in the next 5-15 years Mixed Use Intensification Projects



All NZ's larger Councils are promoting intensification.
Mixed Use projects in NZ will grow in number and progressively scale.

These projects will be difficult to fund, requiring developers with scale.

NZ Opportunities in the next 5-15 years

Converting dead Malls to Mixed Use Centres



Transforming Dead Malls into Communities



Shopping Mall redevelopment to Mixed Use will rejuvenate Centres and provide extra housing: much better than now!

NZ Opportunities in the next 5-15 years

Residential 4-20 Unit Projects on 1,000-2,000 m2 sections



Preserve Heritage, but not character! Intensify large urban sites with quality residential



Council needs to control and ensure good quality urban design, which will create attractive and desirable neighbourhoods, all the community can be proud of.

Future NZ Property Industry Participants

Existing NZ Operators, although many are kaput.

There is a huge market gap for reputable residential multi-unit developers: the Aussies are coming!

Australian Corporate “Build Out” Developers don’t want consenting risk and want a “work pipeline”

- Most of the multi-unit residential developers from the last cycle are kaput.
- Many NZ commercial developers have survived, but reticent about residential
- There is a large gap in the market-place for credible multi-unit developers
- Who will be the developers to supply the looming residential shortage?
- There are signs of a new wave of Asian developers starting to operate
- NZ Banks are chasing a new wave of young developers, however these chaps do not have the scale or experience required for big impact.
- As demand for residential property increases and multi-unit becomes more viable, many large Australian Corporate developers will be attracted to NZ
- These companies have all participated or looked at NZ; they’ll target NZ again



Brookfield
Residential Properties

Sunland Group



Grocon
Lend Lease



- The Australian Corporates will be back again: best be prepared!
- Large corporates are not nimble, innovative, and don’t like consenting risk
- The NZ development market will probably assimilate to the Australian and US markets: innovative local “Consenting” developers, who get approvals and on-sell to large corporate “build out” development companies.
- Large corporate Australian developers will look for innovative local developers to partner with. The local developer will “think global, act local”.

Industry Issues to be Resolved in Coming Cycle

1. Community Issues with Intensification

Auckland Plan: Council need to take responsibility to encourage quality intensification

- Councils want intensification, but not in my street! NIMBY's, BANANA's, NIMEY's
- Council Community Communication on benefits of high quality intensification
- Reducing Council barriers inhibiting good quality intensification
- Auckland Plan: Major upzoning required: Political Resilience??
- For Intensification: Need to Upzone 2-3 times the technical take-up.
- *Google: "Studio D4 Auckland Council Property Report"*



Industry Issues to be Resolved in Coming Cycle

2. Providing Multi-Unit Quality Info for Buyers

Multi-Unit Residential Development Quality is a major problem that the industry must address

Purchasers have a lot of difficulty understanding quality issues in multi-unit residential.

As a result this segment has major buyer turn-off.

“Can’t trust multi-unit quality so I will not buy”



When one buys a car, there is huge comparison data and testing to compare models, maintenance issues, etc; What help is available for people wanting to buy multi-unit residential?



Did off the plan buyers expect this type of multi-unit building to be delivered?

Industry Issues to be Resolved in Coming Cycle

2. Providing Multi-Unit Quality Info for Buyers

Multi-Unit Residential Development Quality is a major problem that the industry must address

Studio D4 is assisting the Property Council on providing a Quality Guide for buyers of Multi-Unit Residential

- The Property Industry needs to provide an easy to use quality guide that assists buyers with what to look for in a multi-unit property
- Many in the industry know what to look for. It is time buyers are provided assistance: This should improve buyer attraction to multi-unit
- The Guide could lead to a voluntary Multi-unit Rating tool for projects.

A Guide for buyers and a Rating Tool that will help differentiate quality developments from crap development

The Guide will provide assistance on & the Rating Tool could consider:

- Layout of units viz sun, outlook, adjoining properties
- Sizing of bedrooms, living rooms, bathrooms, hallways, storage
- Quality of materials used, specifications, long term durability
- The urban design and green building merits of the project.
- Design future proofing; future use potential, flexibility, maintenance

A Voluntary Rating Tool provides Customer Pull and Developer Response (as NZGBC Green Star)

A Multi-Unit Rating Tool:

- 1,2,3 ★ for smaller projects; easy to rate.
- 4,5,6 ★ for larger projects; assessment as Green Star.



Future Requirements for Property Professionals “Urban Design ingrained in development culture”

The 10 Basic Principles of Urban Design need to be ingrained in all property professionals

1. Provide Street Front Active Edges



2. Facades that are well articulated



3. Any blank walls are not visible from the street



4. Adequate daylight is provided to occupants



5. CPTED: eg Pedestrian entrances obvious and safe

Future Requirements for Property Professionals “Urban Design ingrained in development culture”

The 10 Basic Principles of Urban Design need to be ingrained in all property professionals

6. Think of thy neighbour



7. Minimise Vehicle entrances at footpaths



10. Building design that responds to site characteristics

8. Undercover car-parking not located on street frontage



9. Sensible use of colour – colour is free



Future Requirements for Property Professionals “Green Building Principles applied cost effectively”

Customer Pull will drive Green Building principles: developers provide cost effectively

- Customer demand for green building initiatives will continue.
- Developers who resist will lose customers.
- Green Building principles are becoming mainstream.
- The most successful developers will be those that apply green building principles cost effectively.



NEXTERRA BIOMASS GASIFICATION SYSTEM

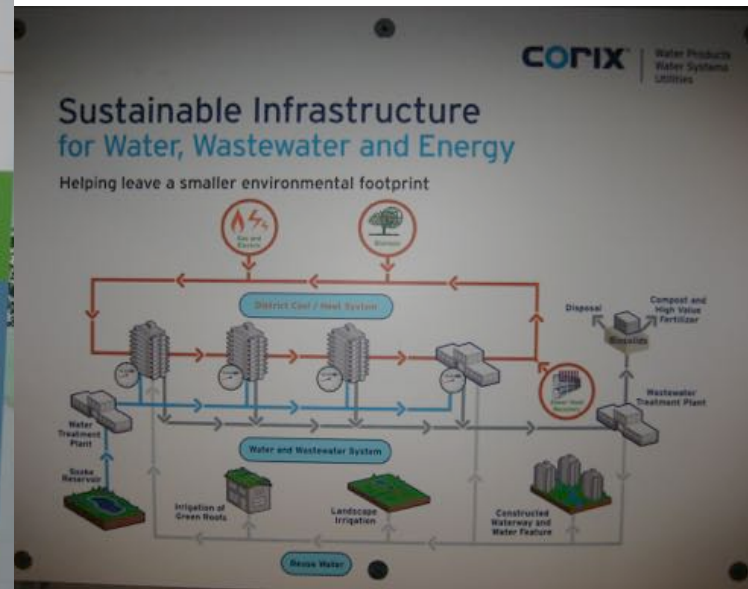
- Converts wood waste into clean burning synthetic gas to displace natural gas.
- Ultra low emissions, no dust, no odour.
- Reduces green house gases.
- Provides heat and hot water for Dockside development.
- System housed in a small, aesthetically pleasing building.
- Proven, simple, clean technology.

ULTRA CLEAN, GREEN ENERGY
BUILT IN/BC BY NEXTERRA ENERGY
PERFECT FOR THE URBAN ENVIRONMENT

How Nexterra's Gasification System Works

1. Feed In: Wood waste is fed into the gasifier.
2. Gasifier: The gasifier converts wood waste into synthetic gas.
3. Purifier: The synthetic gas is purified to remove impurities.
4. Boiler: The purified synthetic gas is burned in a boiler to produce heat and steam.
5. CHP: The heat and steam are used to generate electricity in a combined cycle power plant.

WWW.NEXTERRA.CA



Conclusions and Questions

- 1. Until adversity hits, you will not understand the true depth of your relationships*
- 2. Master-planned communities will be a dominant development concept*
- 3. Mixed use intensification projects will grow in number and scale*
- 4. Converting tired shopping centres to Mixed Use is a big international trend.*
- 5. Small scale (4-20 unit) intensification projects will provide many opportunities*
- 6. There is a big gap for multi-unit developers, likely to be filled by Australian Co's*
- 7. Councils need to take responsibility for communicating intensification benefits*
- 8. Multi-Unit Development Quality is a problem that the industry must address*
- 9. A Voluntary Rating Tool will provide Customer Pull and Developer Response*
- 10. Basic Urban Design Principles need to be ingrained in property professionals*
- 11. Customer Pull will drive Green Building principles: provide cost effectively*