

INVERCARGILL CENTRAL CITY DEVELOPMENT

COMMENT ON RENTAL DEMAND AND RETURNS ON BUILDING STOCK IN THE INVERCARGILL CBD

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Trevor has been involved in a significant number of building projects from 1985 to the present day. These include over 20 structural strengthening jobs in the CBD of Invercargill, the largest job being the Westpac Bank at the corner of Kelvin/Spey Streets.

Geoff has 40 years experience in commercial and residential development projects throughout New Zealand, including the recent redevelopment of a city block in the Exchange area of Dunedin.

Invercargill CBD Retail Environment

In its current format, the Invercargill CBD is not attracting quality tenants and, in my opinion, that is not going to change with a strip shopping format. Today, quality retailers see the advantage in being linked to a powerful anchor tenant, in a building with quality parking attached, or alongside. To adapt existing building stock is not economically viable.

New retailers have not considered the CBD in recent years, because foot traffic/ car parking and tenant mix, is not to the liking of the retailer demanding and willing to pay for, a quality retail site. Our old and heritage buildings are cold and expensive to heat and very expensive to maintain and as the rents have diminished over the years there is not the available surplus money for a property owner to maintain them, resulting the city becoming increasingly rundown.

The earthquake prone building stock available for rent in the Esk/Tay /Dee Streets area of Invercargill has limited demand, even at very competitive rental rates.

Based on recent structural assessments undertaken in the HWCP block - 90% of the building stock is sitting with NBS ratings of 10 - 25%. The existing tenants in the development block cannot remain in occupation, as the buildings are at the end of their economic life.

An example of this is a multi tenanted property on Kelvin Street which is currently on the market for \$1,195,000. This building generates a 10% return with three vacant spaces at date of listing. The potential return is 14.5% if fully occupied. A detailed structural analysis shows an NBS rating of 17% and the quantity surveyor estimate to strengthen the building is approximately \$1,000,000. To do this work is clearly uneconomic as the estimated added value for this building following the upgrade works is say \$400-500,000. So, in this case an investment of \$2,000,000+ dollars results in a building worth approximately \$1,500,000 with an estimated current rental return of 8%. Additionally the building owner is still left with high maintenance costs associated with old buildings.

An example of this is the Stirling Sports store in Esk Street where the roof is constantly leaking. The vacant upper floor results in more rapid building deterioration. Water leaks are not detected for some time, which results in damage to structural timbers.

In my experience, the result of this will be that landlords will not upgrade their old buildings and demolition in approximately 10 to 12 years time is the most likely outcome.

Examples of Typical CBD Buildings

The following are examples of available earthquake prone inner city properties which have not been able to be tenanted for a significant period of time.

45 Esk St.- Sass Cafe - vacant for over 18 months - has been aggressively marketed at a competitive rental of \$18,000 p.a. Previous rental was over \$30,000 pa - I can advise that not one offer has been obtained. When quality tenants call you, they quickly discover that there are few quality buildings they can occupy in the CBD.

59 Esk St - Corner of Cambridge Place Arcade - circa 140m2. Landlord pre September 2017 was asking \$60,000 pa - has been vacant for approx. four years. Over the last year, asking rental was reduced to \$45,000 pa - still no takers. Only tenant - a temporary relocation of Vodafone, while they waited on a new premises to be fitted out in Don Street.

63 Esk St - ex ASB Bank - Tenant relocated due to the earthquake prone status of the building and the fall factor of the neighbouring property The Southland Times. In circa 2015, the building owner placed a family members second hand trading business in the building to pay the fixed costs, as he had no other interest. During the last twelve months, there has not been one quality tenant view the property for a retail use. Community Groups have used the building over the last year to generate some pedestrian activity for neighbours.

67 Esk St. - Southland Times - Obsolete space - front area has been available at \$20,000 p.a. plus GST - again no interest has been generated in this retail area since the Times relocated.

Tenants are typically unwilling to occupy these types of buildings for the following reasons:

- Unsuitable floor area – particularly for larger brands/chains
- Issues with structural soundness of buildings and low NBS%
- Lack of parking – both for employees and customers

Summary

For Invercargill, it is only going to be viable to upgrade buildings when the rental returns can be increased to pay for the capital investment required. This brings me to a complete reduction in value cycle, in the CBD of Invercargill:

- falling pedestrian counts - resulting in reduced retail turnover
- pressure on rental rates to reduce further, to make tenancy viable in a decaying centre city
- lower rentals - resulting in falling property values
- lower property values – leading to loss of rating income

The poor condition of buildings in Invercargill's CBD has resulted in a steady decline in retail tenants locating within this area, leading to the cycle described above. The ability to start from scratch with modern buildings constructed to 100% NBS and requiring significantly reduced ongoing maintenance is in my opinion the best strategy for the city centre to attract new tenants and to retain the existing tenants.

The mixed use development of a city block in the Exchange Area in Dunedin has been credited by Heritage NZ and the Dunedin City Council as being the catalyst for the wider rejuvenation of this part of Dunedin and we believe the redevelopment of the Invercargill CBD block will have the same rejuvenating effect on the wider CBD.