IN THE REAR-VIEW MIRROR

BAYLEYS' CORE COMMERCIAL AND INDUSTRIAL BUSINESS LINE LEADERS REFLECT ON THE YEAR THAT WAS.

ROBUST LEASING ACTIVITY ACROSS all commercial property sectors has been a highlight of 2022, but as the year draws to a close, some market fundamentals are changing.

In the high-inflation, high-interest-rate environment, where banks are tightening up on loan-to-value ratios and closely monitoring debt levels, we'd expect to see more stock come up for sale as leases expire and, some likely softening of values.

With escalating rental rates, this gives owner-occupiers a look in, with ownership seen as an offset to inflation.

With open borders and a loosening of pandemic mandates, international tourism is back on the table, and offshore capital is tentatively circulating in the property market.

In acknowledging that there are still significant headwinds in the market, there have also been some wins, so let's take a look at how 2022 unfolded in each of the key sectors of Bayleys' commercial business.

Ryan Johnson
National Director Commercial & Industrial

From a macro perspective, what an anomalous year it has been – particularly the last six months or so.

Without being melodramatic, when else in history have we ever seen such levels of volatility and risk all colliding at once in such a spectacular way?

There's geopolitical tension and war, a global pandemic that has a long tail and game-changing health mechanisms, an economic maelstrom with debt crises and recessionary traits, and climate change threats.

The speed of change seen in the wider real estate market has been astonishing.

Last year was Bayleys commercial and industrial's strongest yearly result ever – and despite the challenges, this year has been our second best.

However, sales volumes have gone from peak to trough in lightening quick time, the cost of debt is rising by the day, and although income is a hedge to inflation, it's not a level playing field out there in property land.

While industrial and large-format retail are clipping the income ticket quite confidently – I don't think any building owner will truly be resting on their laurels given the hot-blooded economic environment.

However, while institutional capital is now hovering in the wings reluctant to make decisions in the short term because of the volatile market, and other property owners are opting to wait the market out, there's always a deal to be done.

The balance sheets of all commercial property owners will be sorely tested in the coming year, but you can bet your bottom dollar – counter-cyclical opportunist buyers will emerge.

Bayleys has shown that being a full-service agency with breadth and depth nationwide has had tangible benefits for our clients, and we're up for whatever 2023 throws our way.

Chris Beasleigh
National Director Retail

City centres were hit the hardest during peak pandemic, but CBD retail is recalibrating as office workers return, and tourism rebounds.

Retail has been complex, with a 50-50 split of the best of times and worst of times experienced by different operators.

Leasing activity is strong in suburban and neighbourhood shopping centres and retail strips, especially for grab-and-go stores and service providers, on the back of hybrid working dynamics and people spending closer to home.

The most in-demand segment of the market remains large format for both sale and lease, and a lack of available storefront and support warehousing space is thwarting some domestic and international business growth plans.

Several large retailers are commissioning purpose-built distribution centres to support the online side of their business, while on the retail property sales front, institutional investors and owner-occupiers are purchasing well-located properties in identified growth areas.

We're seeing strong interest from overseas retailers wanting to break into or expand across the New Zealand market, with baby products, sporting goods and athleisure segments growing.

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>
> CHRIS BEASLEIGH, BAYLEYS NATIONAL DIRECTOR RETAIL

The entertainment segment is also gaining traction with sophisticated new-look gaming and bowling arcades and experiential virtual reality centres – all linked in with food and beverage – finding favour as face-to-face interaction returns.

Staffing remains a significant challenge across the retail sector and despite loosened visa entry requirements, this is likely to endure.

Despite staffing shortages, wage hikes, a tighter financing environment, and ongoing supply chain fallout, the biggest positive to come out of 2022 is the sheer resilience of the retail sector and we salute that.

Wayne Keene
National Director Hotels, Tourism & Leisure (HTL)

As tourism was New Zealand's number one export earner pre-pandemic, the commercial accommodation sector was

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WAYNE KEENE, BAYLEYS NATIONAL DIRECTOR HOTELS, TOURISM & LEISURE

kneecapped when borders were closed and only now is it starting to bounce back – albeit with squeezed staffing.

On the sales side, our HTL team has seen strong demand for mid-sized accommodation properties, predominantly freehold going concerns and freehold investments.

Businesses-only deals require more equity, so they’ve proven harder to fund as banks adjust expectations on loan-to-value ratios.

Other notable challenges in the commercial accommodation arena are aging assets showing high deferred maintenance, a clear gap in the market for new development of mid-size assets, rising interest rates and cost of materials, and the continued secondment of motels for emergency and transitional housing.

A real positive of the market this year is the continued support from existing industry participants who have taken the opportunity to secure further accommodation opportunities, with new-entrant investment also back after a two-year pandemic hiatus.

Occupancy figures are on the rise, and accommodation businesses have continued to trend up – a combination of fewer rooms in the market, continued domestic tourism fundamentals, and strong trans-Tasman visitors for the winter season (Queenstown in particular).

The sector continues to regroup and rebuild with displayed confidence from local investors, commitment from smaller brands looking to expand, and international hotel groups showing favour for the New Zealand market.

Jayson Hayde
National Director Business Sales

The business sales sector has been treading shifting sands like all the other market segments, but the real surprise has been how quickly the sands have now started to firm for business operators.

Opportunity has proliferated for those businesses and essential service providers that were largely insulated against COVID-19 restrictions and able to trade throughout with minimal disruption.

The pinch point was always government mandate flux. Sellers and buyers of businesses were prepared to take a punt on uncertainty, however the banks haven’t really known how to navigate the changed landscape when approving funding for business acquisitions through pandemic times.

Hats off to business owners for dismissing the fear, being knocked down and getting up again, accepting that the world continues to turn, and taking the bull by the horns to make decisions that are best for their business and teams.

Throughout this trying time, the local story has amplified, technology has become super-important – and will become even more so – but staffing and looking after those staff remains a challenge.

The cost of everything associated with running a business continues to rise, but revenue doesn’t keep up and in an inflationary environment, something will have to give.

Despite this, business sales transactions are being concluded each week, with some creative solutions to facilitate change and get deals over the line – such as vendor funding, sales of company shares rather than assets and carefully structured acquisitions.

Scott Campbell
National Director Industrial & Logistics

Industrial property remains the best-performing asset class across the commercial sectors, with the ongoing challenge being lack of industrial supply category-wide and both for sale and lease.

Ecommerce, logistics/distribution, “just-in-case” inventory demands and manufacturing continue to drive the market, with historically-low vacancy resulting in 20-30 percent rental growth in the last 12 months.

For the first six months of this year, sales over $20 million were non-existent and in fact, sales overall were down 30-40 percent.

While we’ve noted a softening of values of between 100-130 basis points over the year, that has flattened out somewhat now and we don’t expect values to soften any further due to the cost of replacement.

Likewise, we’d expect vacancy rates to soften, too, as new developments catch up and come on stream.

In sales, vacant stock currently has greater appeal than investment stock, with owner-occupiers now having good support from the banking sector given industrial sector fundamentals.

Although lack of supply has been the biggest determiner of the industrial market, we do anticipate potential friction in the refinancing market on the back of higher interest rates and loan-to-value thresholds.

The biggest surprises to come out of 2022 are the stabilising of land costs – with large developable tracts still in demand – and the resilience of the occupier market throughout the pandemic and now as the industrial market finds a new rhythm.

“THE FLIGHT TO QUALITY CONTINUES, LARGELY TO WATERFRONT OR DOWNTOWN LOCATIONS AND NEW-BUILD STOCK WITH EFFICIENT FLOOR PLATES, FLEXIBILITY, AND INTUITIVE FITOUTS.”

LLOYD BUDD, BAYLEYS EXECUTIVE DIRECTOR AUCKLAND COMMERCIAL & INDUSTRIAL

Lloyd Budd
Executive Director – Auckland Commercial & Industrial

As occupiers move back to the office, with an element of hybrid flexibility built in, office assets have been in strong demand.

The flight to quality continues, largely to waterfront or downtown locations and new-build stock with efficient floor plates, flexibility, and intuitive fitouts that reflect modern ways of working.

Think collaborative space, hybrid meeting and work environments, sustainability-led buildings with measurable benefits, tangible points of difference to attract and retain staff, and proximity to social and civic amenity.

As the office market resets and while occupiers seek to accurately forecast their footprint requirements, sublease opportunities have appeared offering options to a broad range of businesses.

What to do with B and C-grade and fringe-located vacant buildings remains a challenge as discussions around conversion to alternative use, upgrades to higher NBS thresholds, and improved green credentials and amenity are weighed up against market demand.

There’s been a dearth of capital market sale and purchase transactions in the office market and just when we thought this market would recover, interest rates and inflation have thwarted capital flow.

Standout positives in the office sector this year include the resilience of CBD occupancy numbers, the rise of quality assets, and the willingness and tenacity of developers to progress new builds.

We expect ongoing interest from landlords and tenants for co-working or shared space to allow shrink and grow flexibility, more focus on green builds and, perhaps for the first time, real noise regarding timber office building construction over traditional concrete and steel.