

Valuations play catch-up with reality

Property observed

Robert Harley

Yesterday's worse than expected national accounts point to the next step down in the value collapse for Australia's office towers, shopping centres, hotels and industrial facilities.

The economy is weakening. Rents are slowing or turning down, vacancies are growing and business failures are on the rise. Property values will have to reflect the lower income and increased risk.

The \$14 billion in valuation falls recorded by the listed property groups at December 31 was a big number. But it is only a first instalment. In their half-year presentations, Stockland managing director Matthew Quinn and Dexis chief executive Victor Hoog Antink foreshadowed further falls.

The hard question is how far. John Garimort, a director of global property data group IPD, says the total fall will be about 20 per cent. Southern Cross Equities analyst Charlie Aitken says the collapse will be closer to 40 per cent.

So far the valuations support Garimort. But the sales evidence is with Aitken.

On IPD's latest analysis, of more than 400 valuations undertaken in the December quarter, the fall since the valuation peak in December 2007 has been about 8 per cent — a figure close to the downturn

recorded by the latest revaluations in listed property.

But the sales tell a different story. In December, Stockland sold its 300 Ann Street tower in Brisbane for \$38 million — down 15 per cent on the 2007 valuation. At the same time the group sold an industrial facility in Smeaton Grange in Sydney's south-west for \$10 million — down 29 per cent.

Even more recently, the ING Industrial Trust sold an industrial investment in the Sydney suburb of Lidcombe for \$14.3 million — 31 per cent less than the December 2007 valuation.

Valuations always lag. They lag

Further falls will not only breach covenants, they will tip some REITs into negative equity.

on the way up and on the way down. Some rose higher than others and will fall further. But eventually they catch up.

In the early 1990s Australian commercial property values — based on valuations — dropped 32 per cent over three years, according to IPD. Significantly, this market, as recorded in the valuations, is falling faster than in the last crash.

No wonder real estate investment trusts have crumpled so far. Further valuation falls will not only breach

covenants, they will tip some REITs into negative equity.

The collapse in values will also eat into unlisted property trusts and syndicates that were able to turn in a remarkably good performance last year — based on those lagging valuations.

And the banks and other financiers, which have \$160 billion of exposure to commercial property, are already discovering how much their collateral is eroding.

Garimort says the market, and the valuers who interpret it, are trying to price three key changes — the lower level of investor demand, the significant increase in assets for sale and concern about the covenant strength of the tenants.

All three are deteriorating.

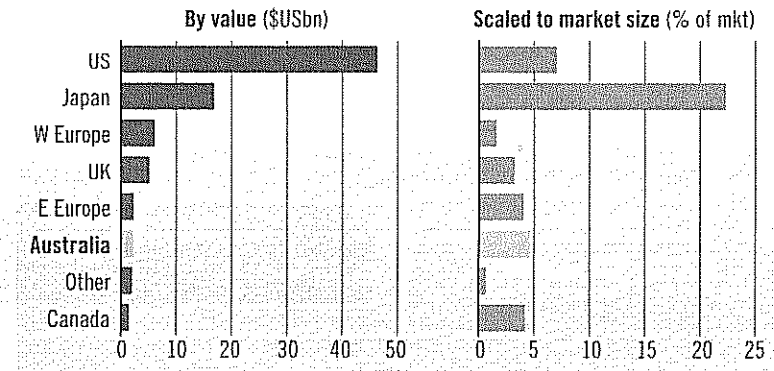
United States-based Real Capital Analytics is now tracking distressed real estate assets around the globe. On its calculations, more than \$US82 billion (\$124 billion) of "significant" commercial properties or mortgages are now in foreclosure, administration or are already repossessed.

So where is the bottom? "One of the things that makes a bottom is stupid, stupid, stupid low asset values," said Steven Roth, chief executive of the US-based Vornado Realty Trust at this week's Citigroup Global Property CEO Conference. "We're getting to at least the first or second stupid," he said.

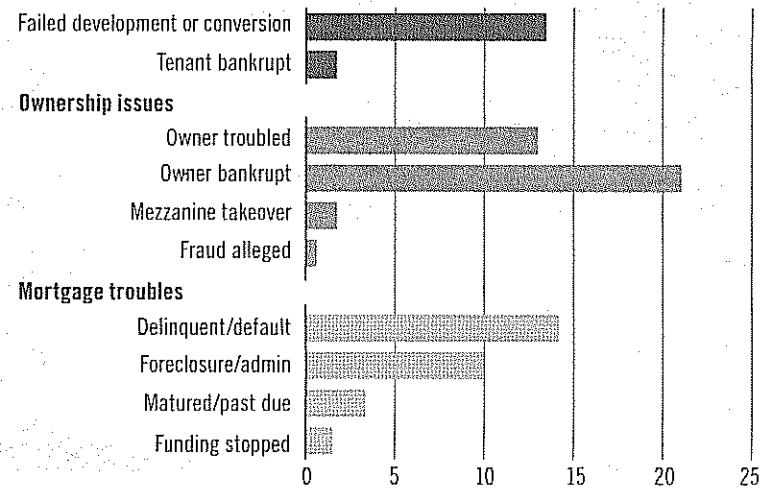
Australia has a way to go.

In distress

Value of distressed commercial property by region



Types of trouble (\$USbn)



SOURCE: REAL CAPITAL ANALYTICS