THE FUTURE OF PROPERTY DEVELOPMENT

By Sir Paul Strasser

(This address was delivered by Sir Paul Strasser, who is not only Managing Director of Parkes Developments Pty. Ltd. but has many other property interests, to a luncheon meeting of the Institute in Sydney on 12 April)

Recently I delivered a lecture in Canberra about finance and development in the future money market, and naturally knowing that finance is dependent upon economic and political decisions I did my "crystal ball gazing" which is what I call making assumptions. After I delivered the lecture, which luckily for me was successful, I was attacked by my friends who said that I recommended to the Government some measures which I thought they should deliver over the next few years. Therefore I want to clarify this time that when you ask me about the future of property prospects in Australia, I have again had to make some assumptions and these assumptions are based by me on logical conclusions, as knowing the past 40 year history of the labour movement in the world, and the past 25 years of the Australian political scene the measures which I expect the new Government to deliver over the next few years and the consequences of all those on the property market. Please do not misunderstand me on those Government regulations which I think will be delivered, as they are not my recommendations they are only my logical conclusions of what the present Government will do over the next few years.

As all of you are security analysts or dealing with securities you surely know that every part of the economy is dependent on the other part of the economy, so before deciding or even trying to guess what will be the future of the prospects of property development in Australia, we have to guess what kind of economy we expect.

1. In my opinion the overseas balances will decline through lower export earnings and higher imports, and through no capital inflow or much reduced capital inflow.

2. Higher welfare payments and welfare laws will result in higher taxation and new taxation forms which will be similar to some capital gain tax, or perhaps value added tax.

3. Bigger bureaucracy and higher welfare payments will result in an inflation which will not be less that 5% per annum.

4. Migration will be cut partly because of the Government decision and partly because English migrants will be now more attracted to emigrate to Western European countries rather than to Australia.

Let's deal with the property developments first item by item and after finishing I will deal with the listed property companies and property trusts.

1. City urban development has taken a tremendous upsurge in the last 10 years, and I have no doubt that the capital cities, especially Sydney, Melbourne, Perth and Brisbane are overbuilt. There is a surplus of office space but I always believe that the supply and demand law automatically regulates the building market. Therefore what is the reason for the fact that still new plans are being put forward and new buildings are being commenced. The cause and reasons are twofold:-

a) The English developers came to develop the Australian cities in a big way owing to the much more attractive yield on the Australian Investment Market than the English yield. The English developers were able to borrow practically unlimited
amounts of money on the Euro Dollar Market, and even for currency purposes it was clever for them to invest in Australia as they could afford to leave part of the building vacant for a few years, knowing that the capital repayment was 10, 15 or 20 years away, and in the meantime the American Dollar devaluation and the Australian Dollar revaluation immediately provided them with a bigger capital profit. All these things which they hoped would happen and which they legally built up did occur as we all know, and therefore the English developers do not regret having invested in the Australian capital cities even if some part of their office buildings stand vacant for a few years.

b) The second reason is that a new demand has arisen and that is the demand to safeguard the value of capital in these inflationary times where the capitalist automatically accepts that a yearly inflation of 3% to 4% is natural and a yearly inflation of 5% to 6% is possible, so there arises a new demand to build on today's prices. Even if for some years it does not bring in a full return it preserves the value of the money, or especially take into consideration that on buildings there is a 2:1 gearing then it preserves 3 times the value of the invested equity.

The first reason has been stopped by the Government through the rule that no foreigner can invest in Real Estate. The second rule still exists so Urban development, even on a reduced scale, will still go on in capital cities.

2. Commercial developments and shopping centres will continue to be built, and even the Government is keen that good shopping facilities should be established in areas where workers live in big numbers. Further commercial developments will come to decentralised cities to be built, and to new areas where the Government wants to release land on a lease basis instead of freehold basis. So the commercial development and shopping centre development will go on.

3. As the Government is committed to full employment, naturally light industry, irrespective of much higher imports, will go on, therefore factory development will be the same or bigger than in the last 10 years.

4. Home unit development will be somehow less over the next few years than in the last 10 years or more especially in the last 5 years. The reason is twofold:-

a) Through the lower number of migrants the demand will not be as pressing as it was during the past 5 years, and therefore home unit building, which according to Australian customs is a secondary way of living to the cottage way of living will be the first to suffer.

b) The land releases, about which we will speak, will certainly result in a cheaper way of living, even if situated a little bit further out, and I would guess that for a working family it would be better to have a cheap cottage in the Campbelltown/Appin area or Menai/Holdsworthy area than a dearer home unit in say Lakemba, Hurstville, Liverpool or Surrey Hills etc.

5. Investment buildings with rental flats will be reduced in numbers again through 2 causes:-

a) I believe that the establishment of the prices tribunal will be followed by some kind of rent control which always decreases the demand for investment buildings, even if
through the experience of the past 50 years around the world, the rental restrictions are sooner or later stopped and then the value of the building jumps back, including all the capital appreciation, which accumulated during the time of restrictions.

b) Through the fact which I mentioned earlier and about which I will speak later i.e. the possibility for workers to obtain a cheap way of living in cottages.

6. Land subdivision is an important section of business for publicly held property companies we shall deal with it now. There is not the slightest doubt that land subdivisions have been booming over the last 10 years in all capital cities but Perth, where Government measures achieved a stabilisation of prices. I am fully convinced, that especially in Sydney, the Government's intention in releasing large amounts of land in the Menai/Holdsworthy area and Campbelltown/Appin area is to give it to the public on some kind of ballot to the lower earning part of the population and this will result in reducing the extraordinary demand for land. On the other hand the raising of land prices is not an Australian phenomenon which can be explained by the bad handling of re-zoning laws, but it is an international phenomenon as it has occurred in Japan, as well as the U.S.A., Western European countries, Canada and any South American country. The pure fact is again that against inflation there are only three things which assure the capital appreciation of money:-

a) Freehold ownership of property especially of well-located land which cannot be re-manufactured and where its position assures its capital growth year by year.

b) Gold, which in most countries like ours is forbidden to be purchased.

c) Works of art, which especially in Australia, are unobtainable.

All this will result in the Government being able to release large amounts of land to be put on the market or Government owned or Government resumed freeholds and then give away the land on a 99 year leasehold with reasonable lease fees, but this will supply only a certain part of the population. With an additional supply naturally the demand will ease but still there will be a demand for that part of the population who cannot count on priorities in ballots and there will exist an additional demand for investment in land as a capital appreciable item. In such a way I have no doubt that investment in land such as residential land or home unit sites will be still very popular in Sydney or around Sydney and in the capital cities of Australia.

Resort land is something which from time to time is called a "dirty word". With the higher standard of living connected with the Australian way of life with the open air living and especially sailing, swimming, fishing, boating and water skiing, I believe that all resort lands which will be developed on an environmental basis like the big resort places of Europe and the U.S.A., will be a good investment for developers and a good investment for the buyers as well. This is quite apart from resorts developed for overseas tourists, which will start to grow also.

Since the 1920's people have been talking about the collapse of the Florida land boom, and except for the depression years of the 1930's, the Florida land boom is still increasing.
It is interesting to know that one of the members of Australia's oldest families gave me the advice that over the past 180 years of Australian history, at the end of every decade the land values were higher than at the start of the decade. We know quite well that these were 3 collapses in the land boom - in the 1890's, in the 1930's and in 1960 and still, according to the documents of this family at the end of the 1930's, at the end of the 1930 decade and at the end of the 1960 decade the land prices were higher than at the start of the decade. I do not see any reason why this trend would change in the future, so I believe investment in land, whether it is city, residential, pastoral or even property developed resort land will be good.

Summarising the investment, as investment in city properties, flat developments, commercial developments, factory sites and land, you can see that if not "En Globo" in most of them I see a reasonably good chance for capital appreciation over the next decade.

Then the question emerges - does it apply the same way to shares of publicly owned and publicly quoted property companies? Here I would not give a unequivocal yes before studying the prospects of these companies.

I do not want to look into any single companies, I just want to see that my remarks are applied to the top Real Estate Trading and Investment Companies which I would list as Lend Lease, Hooker Corporation, Stocks and Holdings Limited, Westfield Corporation, Development Underwriting Limited, Mainline Corporation, A V Jennings Limited and some others, but these 7 companies would be the top companies. These 7 companies are well managed, have good projects, a good earning rate and their dividend is under 3½% and for some of them such as Lend Lease and Stocks and Holdings and Mainline under 2%. So the question arises as to how good the property ownership will be or even trading over the next 10 years, in view of additional taxation, which in my opinion, might come in, and further reduce the dividend yield. Will it result in a reduction of share value or will the hoped for capital appreciation of the companies re-compensate the public for the additional drop of dividend yield? This is not a question which can be judged by my property knowledge but it must be judged by your Stock Exchange knowledge. All that I can state is that in my opinion these 7 top publicly held property companies will:-

1. Have further capital appreciations
2. Will have good trading results
3. All of them might have a stable dividend instead of an increasing dividend rate through higher company taxation.

Finally I have to speak about property trusts, which are more popular in England but have become quite popular in Australia. The general property trust managed by Lend Lease, Stocks and Holdings Property Trust managed by them and Parkes Property Trusts Nos 1 and 2 managed by Parkes Developments have a dividend yield of between 7½% and 8.2%, so the highest yield on the Stock Exchange of a well run investment with an additional benefit of 50% capital appreciation on all investments. As the taxation set up of property trusts is such that the unit holder pays his taxation according to his income and not according to the rate of income applying to the trust, I think that this is the best way of investing, especially for widows and individual investors who are looking for the highest possible income and where the taxation rate is not too high, and they still have a good capital appreciation for the future. The reason for the
decrease in this very good investment possibility in the last year was because the property prices have gone so high that it was impossible for the property trust to be formed and purchase good properties with a reasonable return.

As the foreign investor will be stopped from the market, in such a way the demand for property might be less and it is reasonable to expect that a 7½% to 8% yield property trust will be formed in the future, and in my opinion, they will be a very good investment and will have a very large future. When you see in England the Abbey Property Trust going to hundreds of millions of pounds or more than our property trusts which only have a maximum of $10 million to $20 million, they are still relatively small and will be increasing in the future. The same applies for property trusts as to public company shares: the property trusts are as good, honest and capable as their manager. They have been misused and abused overseas and will be obviously misused and abused by sharp businessmen in the future here too.

Before I finish, I would like to comment again on the C.B.D. overbuilding which I have mentioned before, and which is such a current topic these days when one speaks of property development.

It should be remembered firstly that a city building is a long term investment. Secondly, I would suggest that the experience of the recent past where office buildings were often fully let before completion, or where they were sold and leased back before completion on rents which turned out very conservative was a boom situation. Now if you build, complete, and spend the next year filling the building then certainly this would be a more normal situation, both historically and on an international experience. The conclusion should not be drawn that this lag time of one year is a disaster, because as I suggest it is a long term project and secondly capital appreciation is taking place, if for no other reason but that to replace the building would cost so much more. Naturally you have to be conscious of the carrying cost effect on profits, but in terms of the companies we have discussed I would remain prudently optimistic.

"Dixi et salvavi animum" which means I have told my opinions and cleared my mind, but naturally please realise that I, like everyone of you here, make daily mistakes, so all I can do is tell my opinion, and if you make any profit out of benefiting from my advice I certainly will not want commission out of it, but on the other hand please do not blame me if any loss emerges from it.

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STANDARDS FOR INTERIM INFORMATION

By M.G. Wright, B.Com., A.C.C.A., F.C.I.A.

(This article was published in Great Britain in "The Accountant" of 28 December, 1972, and permission has been kindly given for its reprinting in this Journal. Although triggered by the U.K. accession to the European Economic Community, it is believed that the article will be of interest to many of our members. The form, content and frequency of interim reports is topical in this country and overseas ideas could be helpful.)

Many European companies, including those in the United Kingdom, publish regular interim reports on the course of their business between annual reports. Such reports may be mandatory...