The 1980s have been a period of increasing sophistication in the Australian property market as investment and asset managers develop new techniques for dealing with volatile influences.

The growth of tourism (on the back of a lower dollar as well as John Brown) has led to significant opportunities for new property investment. The revival of rural commodity prices is also seeing a resurgence of interest in rural property, not only as a lifestyle but as an integral part of wide-ranging property portfolios.

One would hope that the push to develop our exports through manufacturing will also give a stimulus to industrial park development, particularly for the high-tech-oriented area of the market.

A word of warning must be given in regard to industrial relations. In the past, concern by institutional developers about risk exposure during the development and construction phase of building projects has seen significant major contracts deferred or cancelled in parts of the country. Despite recent positive moves, industrial disputes remain a concern to major property investors and developers where long lead times and construction programs, with associated high holding costs and interest charges, can put in complete jeopardy the achievement of a satisfactory development.

Today, as in the past, the effects that union disputes and associated delays have on the total capital outlay can be extremely grave and remain the greatest single factor in the causes of cost over-runs.

As a result it has become of greater importance to select building contractors and construction managers with a proven track record in their ability to minimise union action and reduce delays and additional costs to the absolute minimum.

At the risk of preaching to the converted it would not seem inappropriate to point out that property, either in the form of direct property ownership or exposure to the market by property trust units, must be an important element of any balanced investment portfolio.

The traditional benefits of property investment — moderate income return, sound capital growth and low risk — have always been linked with the offsets of low to moderate liquidity and relatively high management demands. These factors have always been well appreciated by investment managers concentrating on balanced long-term investments portfolios.

The intense competition of recent years for funds management has been coupled with increasing emphasis on shorter-term results, and worldwide five-year bull markets. It became imperative for managers to have the potential for greater exposures at short notice to the most volatile area with the highest short-term rewards, i.e. the equity markets. Consequently, direct property exposures had to be reduced to free up portfolios despite property's excellent longer-term
As the bull markets slowed, many managers have naturally adopted the alternative strategy of holding units in property trusts to give increased property exposure but without long lead times. This has been, and will continue to be, one of the factors which have caused the dramatic increase in the size and number of such entities.

Despite a body of evidence to support the view that property has matched or even outperformed the share market over the longer term, a comparison of returns from the property and share portfolios of major funds over the past five years clearly evidences the opposite over the shorter period. The property sector has performed in the range 15-17 per cent while domestic shares have achieved more than 30 per cent in the same time frame. It is interesting, though, that one of our major funds yielded well over 20 per cent for the 12 months to July, thereby giving returns above or matching all other sectors of investment, bar one, over the same period.

In looking to the future, I believe there are several very strong influences facing us which give a very positive outlook for both the shorter and longer-term position of the industry.

Significant changes in the property investment area will ensure continued growth in property by participants other than the traditional institutional investors.

Changes in FIRB restrictions, the growth of the property trust industry, single-property unitisation schemes, the advent of listed property companies, and taxation changes related to depreciation allowances are already affecting the property investment area in a beneficial way and will continue to do so.

With the relaxation of FIRB restrictions we are already seeing a significant inflow of funds from overseas into the Australian property market. Property publications and newspapers are full of reports of major investments by both Japanese and New Zealand investors.

In looking forward, it is appropriate also to examine the recent changes in the scale of individual property developments in Australia. This escalation in cost affects considerably the nature of future ownership and development.

Major remodelling of Australian capital cities took place during the 1960s and early 1970s in a period of growth fuelled by both foreign investors and institutional investors.

However, as a consequence of previous growth and redevelopment, prime sites have become scarce and costs have escalated dramatically. We see this in record prices being paid for major, well-positioned sites in Sydney, Melbourne and Brisbane in particular. The high cost of sites, coupled with the demolition of quite significant buildings, such as the CRA building in Melbourne, combined with larger and taller structures, have led to a demand for very substantial capital investment in extremely large development projects.

As a result there are many projects, under construction and planned, with total values in the range of $100 million to $500 million, and even higher — figures which only a few years ago would have been considered totally unrealistic.

Such projects include the Melbourne CRA site redevelopment at a figure probably in excess of $500 million, the 101 Collins Street project of about $250 million, the Brisbane Myer/Remm retail development at $470 million, and the Central Plaza office project in Brisbane at $300 million or thereabouts. There are many others, including the Sydney Gateway office development by my own company of some $400 million. Individual properties of even $100 million value are of a size difficult for most investment managers to handle comfortably in a balanced property portfolio. They create an undesirable “lumpiness” unless the portfolio is extremely large. As well, many managers need to reduce their development risk through exposure to “landmark” buildings in prime CBD locations, although they may be keen to have a significant interest in a successful finished project.

It is not so long ago that our largest property portfolio had more than 120 properties, averaging about $5 million each. The same portfolio now has 12 interests averaging $50 million, giving far superior performance to the portfolio left behind. However, we have to recognise the greater volatility inherent in the “lumpier” portfolio, and the significant problems major changes in cash flow will cause, whether they be positive or negative. These new “difficulties” and the magnitude of new developments have led to a requirement for new methods by which investors can participate without upsetting the balance of their portfolios, or figure in the market even when the sums involved preclude total ownership by a single investor due to the constraints of available funds.

Some of our major fund managers now gain their entire exposure to property through their investment in property trusts. Of a group of 10 managers with a total of $3.6 billion invested in property, $1.15 billion, or 32 per cent, is via trust vehicles. The growth of the trusts has enabled much greater specialisation to take place. This is evident in the range of trusts now available, some being a balance of office, retail and industrial, some retail only, and some CBD office only. More recently, interest is also being shown in rural property trusts.

I have no doubt that my organisation will greatly increase the number and type of listed property vehicles we manage. These vehicles will allow investors direct access to the portfolios, at the same time giving investors in our retail and corporate products their indirect exposure to the property markets through the same vehicle. Other forms of unification and sectorisation of property development and ownership are being seriously considered.

I would not be surprised if managers of property funds came to the view that property asset companies, rather than trusts, may be the direction to follow to ensure easier control and management, to allow gearing on a simpler basis, and to avoid some of the pitfalls of the current taxation position of trusts.

Clearly unification is a new and emerging area of property investment in Australia and much will be discussed and written about it before all of the advantages and disadvantages are fully appreciated. Another trend in recent times has been the marketing of what might be described as “entrepreneurial” financing packages. These have the potential to cause significant changes to the way in which major projects are funded during the development and investment phase. This will result in a shift away from the traditional debt/equity funding and mortgage loans.