

Strategic
Consultancy

Retail *Intelligence*

Rome wasn't built in a day:
Christchurch *Retail*, Red Zones
and the Rebuild



Executive Summary:

The prohibition of redevelopment in large parts of Christchurch is significantly impacting the shape of the urban environment of the city. This is being executed through the identification of Red Zones.

The majority of the residential Red Zones are located in;

- the east of Christchurch (along the Avon and in related areas usually associated with waterways or former waterways);
- in the north-east of Christchurch (e.g. Brooklands); and
- in the beach area of Waimakariri District (i.e. Kairaki Beach).

There are currently about 5,000 properties in the Christchurch City Council area and around 100 properties in the Waimakariri District Council area in the residential red zone.

Future trends suggest:

- A hollowing out of the area of Christchurch around the Avon River.
- A population drift to the North of Christchurch
- A population drift to the Southwest of Christchurch
- A significant uplift in populations of the small towns around Christchurch

Growth in retail spending in these areas will create additional demand for close to 80,000 sqm of retail space.

Just over 40,000 sqm of retail development is currently in the pipeline suggesting there remain opportunities to tap into this growing demand profile heading forward.

We see the greatest opportunities in the Supermarket / Grocery space, DIY, Home Furnishings and Food and Beverage sectors.

This development is however not without its challenges as stakeholders in Christchurch remain prickly to proposed intensification at the periphery at what they often see is at the expense of the CBD.



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Introduction

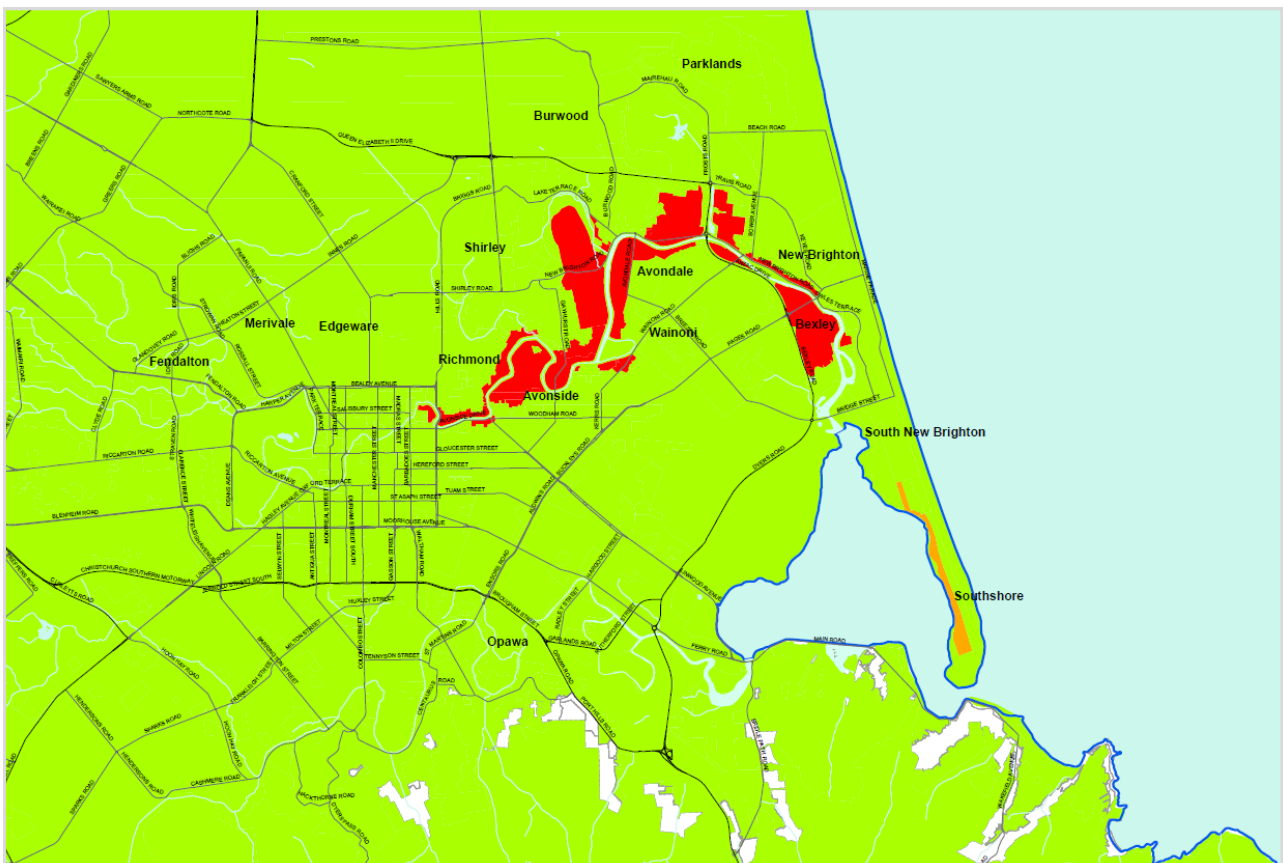
The Canterbury earthquake on 22 February 2011 changed the Christchurch landscape forever. However dust from the financial and economic aftershocks is only now just settling. As the rebuild kicks into gear and the residents of the area begin to accept that the recovery of Christchurch may take as long as a generation, the shifting demographic trends in the region are becoming clear.

As the profile of where people will likely live, shop and do business in Christchurch over the next few years become more certain, Jones Lang LaSalle has measured some of the long term impacts this will have on the retail property sector.

The Changing Shape of Christchurch

During the first half of 2011 authorities released their final assessment of the 'Residential Red Zones' in Christchurch. These were the suburban Red Zones, the poorer cousins to their more well-known CBD Red Zone. The Suburban Red Zones were the areas located across much of the eastern suburbs of Christchurch that were deemed by the Canterbury

Earthquake Recovery Authority (CERA) to be beyond the pale. Whereas the CBD has now been deemed the rebuild zone where significant new development will take place this will not be the case for the vast majority of predominantly residential properties to the east of the central area.



Source: CERA

The majority of the residential Red Zones are located in;

- the east of Christchurch (along the Avon and in related areas usually associated with waterways or former waterways);
- in the north-east of Christchurch (e.g. Brooklands); and
- in the beach area of Waimakariri District (i.e. Kairaki Beach).

There are currently about 5,000 properties in the Christchurch City Council area and around 100 properties in the Waimakariri District Council area in the residential red zone.

According to engineers Tonkin and Taylor the criteria for defining areas as residential red zone are as follows:

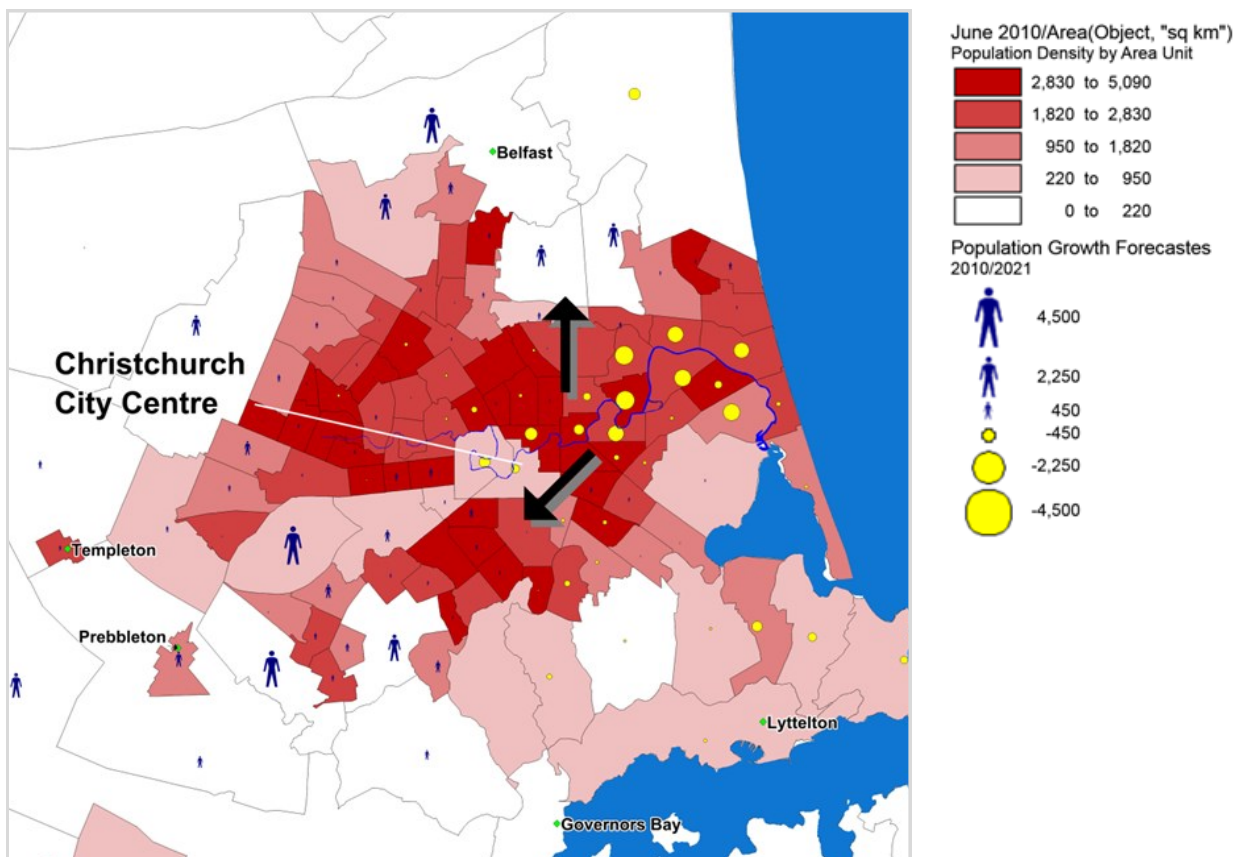
- There is significant and extensive area wide land damage.

- Most buildings are uneconomic to repair.
- There is a high risk of further damage to land and buildings from low levels of shaking.
- The success of engineering solutions would be uncertain and uneconomic; and
- Any repair would be disruptive and take a considerable period of time.

The population of the red zone areas in 2010 was 13,420. Given that the vast majority of these people are relocating we expect the demographic landscape within Christchurch to alter significantly over the next 10 years.

Statistics New Zealand has released their forecasts detailing where they expect the population to both increase and fall as Christchurch residents resettle and as the city itself continues to increase its population base through natural growth and migration.

Population Density as at June 2010 (shaded) & Forecasted Population Growth 2010/2021 (symbol) – Christchurch City Urban Area



Source: Jones Lang LaSalle Research and Consulting; Statistics New Zealand

Macro Population Trends



Source: Jones Lang LaSalle Research and Consulting; Statistics New Zealand

these residents have less available capital to re-enter the market in other centrally located Christchurch suburbs.

As indicated therefore in the Statistics New Zealand data a large proportion of the former residents of the Redzone will not be able to move the short distance they would no doubt like to, in order to remain living in the Christchurch urban area.

Rather a large portion of these residents will need to look to the periphery of Christchurch where bid rents for residential property are lower, in order to be able to afford to rebuild. The pricing characteristics of the satellite towns in Christchurch are also likely to attract Redzone residents which helps explain the strong population outlook for the towns

immediately surrounding Christchurch over the next ten years.

Draining of the Avon: Clearly there is a hollowing out of the area of Christchurch around the Avon River. Avondale, Avonside, Burwood and Dallington will all see significant population decreases as houses are demolished and land reclaimed by authorities.

There has been considerable debate in the media regarding the vacation of these areas with resident protest and a portion of people claiming they will mount a legal fight to stay. The vast majority of those living in the affected area however are more than likely to relocate.

We note that the average price of housing in this precinct was considerably lower than the surrounding areas just prior to the earthquakes. RPNZ data indicates, the median sale price of houses in the residential Redzone was 11% lower than the median sale price in surrounding submarkets. As indicated in the Ministry of Business Innovation and Employment report, issued on housing pressures in Christchurch,

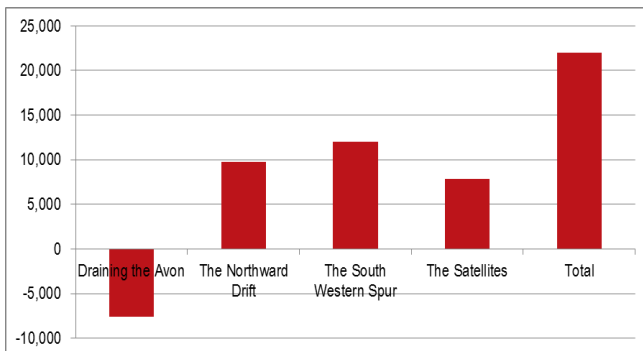
The Northward Drift: Although there is expected to be moderate levels of population growth in most of the areas in Christchurch outside of the residential red zones the majority of future population growth will occur in the areas of Christchurch where there is already subdivided and or large tracts of sub-divisible land. The areas around Northwood, Redwood, Marshlands and Belfast have 2,145 current land sites available. Jones Lang LaSalle estimates that these sites can absorb 5,800 of the 9,720 people expected to settle there over the next 10 years.

The Satellites

This suggests that much of the urban fabric in the area is yet to be defined by actual available sites and in place infrastructure. The market does however have a firm idea of where future land developments will take place and clearly there remains long run population demand to absorb these sites.

The South Western Spur: As is the case with the areas to the north of Christchurch's urban area a significant amount of residential subdivision had already occurred to the southwest of Christchurch in the areas around Prebbleton, Wigram and Halswell. There are both available sites as well as substantial tracts of sub-divisible land the area that we have termed the South Western Spur. As such Jones Lang LaSalle's forecasts suggest a 71.8% increase in population to 2021 or 12,010 more people moving to the area.

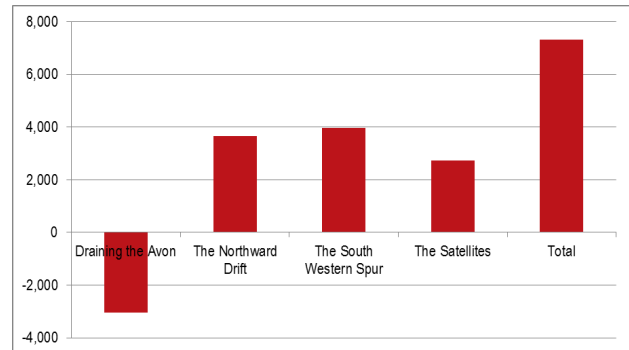
Total Population Gain or Loss by Precinct 2011-2021



Source: Statistics New Zealand & Jones Lang LaSalle

The South Western Spur currently has a total of 2,329 residential sites in development which Jones Lang LaSalle estimates can accommodate some 6,300 people. Of these sites however only 65% currently have consents in place and only 45% are currently on the market for sale.

Total Gain or Loss of Households by Precinct 2011-2021

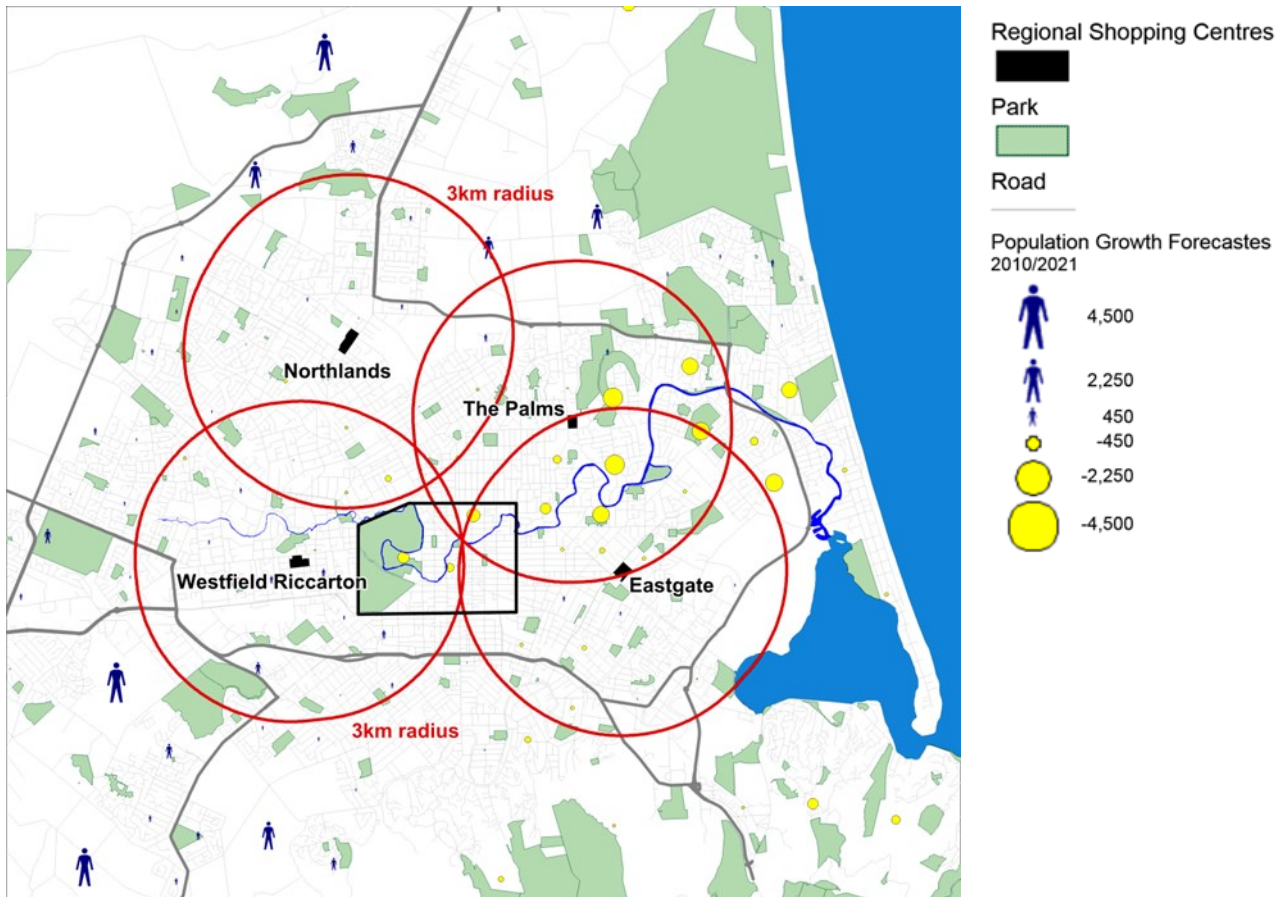


Source: Statistics New Zealand & Jones Lang LaSalle

The Satellites: Although we expect to see a redistribution of 21,980 people within the existing Christchurch urban area over the next decade we also expect to see the growth of Christchurch's satellite towns. Population growth of 7,830 is expected across Lincoln, Rolleston, Kaipoi, Rangiora and Woodend. Once again the availability of land plays a part in this forecast growth however another key driver is the affordability of housing. With many residents whose insurance pay out may fall short of a total residential replacement value the only affordable housing options are likely to be in towns outside of the main Christchurch urban area.

How Demographic Change Will Impact the Retail Landscape

Regional Shopping Centres – Population Growth/Redistribution Impacts 2010/2021



Source: Jones Lang LaSalle Research and Consulting; Statistics New Zealand

In the map above we have placed the four major regional malls in Christchurch alongside the CBD. We have drawn a 3km radius around these malls to demonstrate where the growth areas and loss areas are likely to impact retail catchments.

Northlands: Northlands' primary catchment is likely to benefit from the Northward drift of population. Northlands was already well positioned to experience growth in its catchment from new residential development before the Canterbury Earthquakes, however now we are likely to see the pace of urban development pick up.

The Palms: The Palms has seen a significant loss of population from its primary catchment which consists of several suburbs sitting directly in the Redzone. The challenge for this property is to extend the reach of its secondary catchment into the areas north of Christchurch that are likely to see strong population growth heading forward.

Eastgate: As is the case with The Palms, Eastgate has seen a reduction in the number of people in its primary catchment. The challenge for this centre will be extending its secondary catchment into the Port hills and growing populations to the south of Christchurch.

Wesfield Riccarton: Westfield Riccarton is well located to take advantage of growth in the South Western Spur. The risk for this property is emerging competition in its secondary catchment and preventing over trading in its primary catchment.

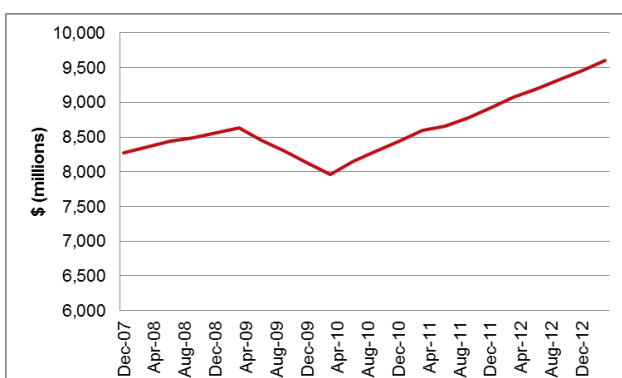
CBD: Prior to the Earthquake the CBD in Christchurch was home to between 30-35,000 sqm of retail space. Anecdotal evidence suggest that retailers were ‘not thriving’ in the CBD although it is difficult to tell whether this sentiment was driven by the recent recession rather than the underperformance of the sector as a whole.

There is a stated intent to limit the amount of retail to be rebuilt in the CBD and if this ‘limited amount’ of retail is achieved, we are confident that this will perform well against the backdrop of demand likely to be generated from a completed CBD. We can already see however a supply pipeline for retail in the CBD that, if completed, is likely once again to oversupply the CBD. Timing is the big question that overhangs the CBD market as the CBD will most likely take at least a decade to retain its former glory.

Quantifying the Market Opportunities

Disposable Household Income:

Below we have included a chart that details total annual retail sales in the Canterbury Region over time.



Source: Statistics New Zealand

Despite considerable comment from the retail sector that business remains a struggle the macro profile in Christchurch paints quite a rosy picture. In the chart above the impact of the global financial crisis can be seen through 2008 and 2009. Certainly from March 2009 to March 2010 total annual retail sales in Canterbury fell close to 8%. However growth in retail sales in the region has since been significant and entirely positive.

Retail sales reached pre GFC levels in Canterbury in Q1 2011 – the same quarter in which the second and more damaging Canterbury Earthquake struck. Total retail sales in Canterbury are now 16% higher than they were prior to the GFC and we note that this much larger total retail spend is being spent across significantly fewer shops.

We anticipate retail sales to continue to grow both on the basis that the regional as well as the New Zealand economy is showing strong signs of recovery, but also on the basis that Christchurch will continue to see strong underlying population growth over the next 10 years.

This continued strong performance of the retail sector in Christchurch adds impetus to the fact that the shape of the underlying demographics is changing. If the size of the retail pie is increasing in size and population is concentrating in new areas this represents a double whammy hit for those locations in the north and southwest of Christchurch that are likely to see the bulk of new development heading forward.

Total Retail Sales Attributable to Population Growth

We have analysed the likely real disposable income gains and losses arising from the internal shift in population in the Christchurch CBD. Overall the increasing Christchurch population figures infer an increase in gross household disposable income of NZD 550 million over the next 10 years.

In terms of how this translates to retail spending and demand for retail floor space the overall impact will be significant.

We expect overall demand for retail floor space to increase by close to 80,000 sqm over the next 10 years as the population within Christchurch grows. This belies the fact however that the area around the residential Redzone has seen approximately 26,800 square metres of demand shift elsewhere. The most significant gains will be seen in the South Western Spur which demonstrates the largest increase in demand by a delta of 8,000 sqm of retail space.

	Total Shift in Population 2011-2021	Estimated Change in Demand for Retail Floor Space (Sqm) 2011-2021
Draining the Avon	-7,580	-26,800
The Northward Drift	9,720	34,400
The South Western Spur	12,010	42,500
The Satellites	7,830	27,700
Total	21,980	77,800

Source: Statistics New Zealand & Jones Lang LaSalle

Likely Future Supply

Jones Lang LaSalle has analysed the known supply pipeline for private retail development in Christchurch. We have sought to exclude government and or Christchurch City Council developments to get a true understanding of the amount of retail that is likely to come on line over the next five years given the consents and known projects that are currently in play. In addition we have netted out projects that are currently being built to replace existing space that cannot be repaired but still remains operational.

The total retail pipeline currently consists of \$268 million worth of work. We note that the current potential supply pipeline is just over 40,000 square metres or just over half the total anticipated increase in demand for floor space. These figures suggest that the amount of retail space coming on line is unlikely

Likely year of completion	Total Value of Work (est NZD Millions)	Total Likely Floor Area (Sqm)
2014	29.9	5,945
2015	101.8	18,244
2016	68.3	11,304
2017	35.0	5,000
Total	235.0	40,492

Source: Pacifecon & Jones Lang LaSalle Research

to oversupply the market given that we expect close to 80,000 square metres of additional demand over the next ten years. We note however that the total projects currently in the pipeline for the Christchurch CBD exceeds 14,000 sqm which is substantial given the lower densities that have been proposed for the future CBD precinct.

Opportunities

Clearly the whole Christchurch urban area will continue to see growth however the greatest benefit is likely to befall those areas on the periphery that have vacant land to convert into a new built community as demonstrated above. As this new housing rolls out the biggest winners will be those retail providers that can associate with a growing urban area.

Supermarket / Grocery Retail: Clearly a significant portion of any future increases in retail spending will support additional grocery retail. Given that grocery represents just over 30% of total retail spending we would expect there to be sufficient retail spending growth to support between 8 and 10 additional large format supermarkets in the Christchurch urban area. In particular we would expect to see at least five of these in locations that service the growing South Western Spur with between two and five located in the northern parts of the Christchurch urban area.

Given the changing catchments that have also resulted from the loss of retail through the earthquake there also remains significant opportunities for smaller format and specialised food retail. As supermarkets get bigger and often further apart, there is an opportunity for premium grocery and convenience based grocery to create a wedge between large competing stores.

Furnishings, DIY and Appliances: Clearly a significant portion of retail spend in any area where there is significant new housing is focused on hardware, furnishings and appliances. Indeed overall retail trends suggest that the South Western Spur can accommodate an additional 7,500 sqm of retail of this nature (this equates to some ten thousand weekend's lost to DIY per month) and just over 6,000 sqm in the North of Christchurch.

Food and Beverage: As at March 2013 some 13% of all retail spend was devoted to food and beverage retailing. As the number of traders in this sector and the proliferation of offerings continues this sector is uniquely positioned to create opportunities in the various new subdivisions likely to spread out across the periphery of Christchurch.



Macro disposable income and spending trends for the Christchurch region suggests we are likely to see demand for over 10,000 sqm of new food and beverage space which if we used 80 sqm per outlet, as an average, implies an additional 130 outlet opportunities in the sector over the next ten years.

Challenges

Although in this paper we have articulated the likely shape of the demand scenario over the next ten years we are also aware that the development of retail space in any modern city does not come without challenges.

The CBD's ability to capture comparative retail spend: We question the ability of the CBD to fully capture comparison retail trade. The scale of development in the CBD Blueprint is clearly lower than it was previously and we expect that this will ultimately mean less employees based in the CBD as well as ultimately less economic density.

As such the CBD will not only need to offer a unique retail offer it will also need to have an extremely deep secondary catchment to draw shoppers to the location. The CBD is however ringed by several large, well-functioning, full service regional shopping centres as well as several small to mid-sized centres.

The CBD will certainly have a requirement for retail given the working, tourist and resident population in the CBD. However there remains a significant risk in the overprovision of retail in the CBD given the fact that the already distant urban periphery of Christchurch is only going to grow further away from the CBD over the medium term.

Local attitudes to intensification of retail and CCC attitudes to additional mall space: The demand numbers in Christchurch imply a strong long term demand for additional retail space which in turn implies demand for additional retail mall space.

There remains however a strong and some would argue reactionary aversion to malls in the city. Both local business leaders and Council members, despite claiming that they are pro development and pro job creation, have publicly decried the development or enlargement of retail malls in Christchurch.

This public opposition in the city will be a significant impediment to any developers seeking to take advantage of these long term demographic shifts handing an advantage to any large scale retail already in place which is already likely to be over trading.

Getting retailers to pay the bid rents required for new development: Christchurch remains a unique property market in that retailers are often unable to expand their foot print in existing property that are suitable but currently in another use.



That has a lot to do with the fact that much of the older or secondary retail space that acts to absorb demand in times of growth has either been knocked down or is now substandard to requirements.



As such much of the likely future retail demand will be met with the challenge that it must be accommodated in new space with rents high enough to justify the cost to develop. Retailers, like many property occupiers in Christchurch, have long been able to pay rents far below those that would justify new development.

Anecdotal evidence at new mall developments indicate that in larger markets like Auckland and Wellington property owners struggle to get retailers that are paying rents above the level required for new development elsewhere in the city to commit to new space at that same level. This has stalled several new developments in recent years. In Christchurch where benchmark rents have long been lower than the level required for new development getting retailers across the line in unproven locations will be an even greater struggle.

Conclusions

Clearly the opportunities offered by the changing demographic shape of the population in Christchurch are numerous if not without their challenges.

In essence however the growing number and increasing density of population on the periphery will drive demand for new space. The ultimate enabler of this demand will be whether the stakeholders involved in the process which includes developers, landowners, tenants and of course the Council can come to terms which will allow the market to deliver the right property solutions, in the right quantities with the right market timing.

This of course is the perennial problem for all property markets however getting it right in Christchurch is made more important by the need to rebuild the city to its former glory.

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