

## Weighing up CBD property

Most investors know that location is important when it comes to buying a house. However, there are other criteria to be considered when looking at prime CBD (central business district) property as an investment.

As a general rule, CBD property produces a good return on capital and is a valuable part of a well-diversified property portfolio. The main reason for this is the prestige value of prime property in a popular location, i.e. CBD. Companies wanting to establish a dominant presence or image will pay a premium in the form of higher rents, which in turn means higher property values.

While this is all good news for investors, the basic concept of supply and demand will ultimately determine the performance of the sector. For example, during a belt-tightening period back in the early 90s, demand for superior CBD property dropped dramatically in Auckland, reducing investment returns.

Demand can wane for many reasons, but it most typically happens during tougher times when corporates have to restructure and focus on their core activities to improve their bottom lines. In this scenario, they may choose to close or sell some divisions, resulting in a reduced demand for CBD office space. In addition, technological advances in communications mean there may be less need for physical proximity to do business.

Fund managers monitor these trends, using a combination of current information and past experience in property investment to gauge fair value at any one point in the property cycle.

They are also likely to apply the following fundamentals to their investment decisions in respect of all physical property investment:

- Major/financially strong tenants
- Longer-term leases
- Regular rent reviews (every two years)
- A location where historically there has been consistent demand for space, but one where there is also no pending major oversupply
- A building capable of meeting the demands of a modern user.

Investment fundamentals generally don't date, and this checklist makes as much sense now as it did back in 1990.