TURNER DRAKE & PARTNERS

Newsletter

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UPDATE
Carpe Diem

There is an inordinate amount of doom and gloom abroad in the land and an astonishing lack of confidence. Real estate in particular is regarded with all the enthusiasm of a wet Monday. Get a grip Canada; keep a sense of perspective! We have the highest annual GDP growth of any G7 country: we also top the league of the fifteen most highly industrialized nations in the world. Real estate is a bargain, gold waiting to be scooped from the table.

In this issue we take a look at property cycles, and at the opportunities presented by the present situation. We have advice on reducing property taxes and some great news for businesses and property owners in Nova Scotia . . . some not so good news too! The Provincial and Municipal governments in the province, increasingly desperate for cash, are looking (literally) under every stone to find ways of taxing property owners . . . whilst claiming to hold the line on taxes. We have the story.

Despite all the brave talk about free trade, New Brunswick has raised another barrier to inter-provincial business by acceding to industry demands for the licensing of real estate appraisers. We have some observations on its impact on property owners in the province. Continentwide though, it is a different picture. The new open skies policy is already having an impact on our business, and probably yours too.

We also focus on the leasing and sale of real estate in the region's capital. Halifax is host to the G7 summit in June and our little jewel of a city is a hive of activity as landscapers, pavers, painters and construction crews rush to complete their work during the next few weeks. Whilst as taxpayers, we question whether any of the work is necessary (the city already looks pretty good to us) government can find less useful ways of wasting our money. Anyway, we're sure that our visitors will find that Halifax is indeed a treasure to discover.

IN THIS ISSUE

Finally we poke around polluted property and offer our observations on the impact of recent changes in provincial law concerning the environment. And of course it's Spring again: fresh fiddleheads, sweet lobster and cold white wine. Terrific!

SPREADING OUR WINGS

Although we are based in Nova Scotia, much of our work is concentrated on properties in the other Canadian provinces (currently New Brunswick, Prince Edward Island, Newfoundland, Ontario, Alberta) . . . a reflection on our reputation countrywide . . . or locally?

We operate from a single base, Halifax, because it is more cost effective than running satellite offices. It has enabled us to assemble a team of real estate professionals with great depth and breadth of expertise; who because they are located in the same office cross pollinate ideas. For example, a client wishing to dispose of a "problem" property can also call on the assistance of our Property Tax Division to reduce the assessment and thus facilitate the sale.

So, if you want appraisal, valuation, property tax, sales, leasing or counselling advice on a property in New Brunswick, Prince Edward Island, Newfoundland or elsewhere, do what the locals do, pick up the phone and call us. We'll even pay for the call (1-800-567-3033). If your property portfolio is spread across Atlantic Canada, we offer one stop shopping with an emphasis on "value adding" advice. We can reach most cities within 60 minutes, and thanks to the recent liberalization of air travel there are at least 7 flights a day to most centres! In fact by June there will be 13 airlines serving

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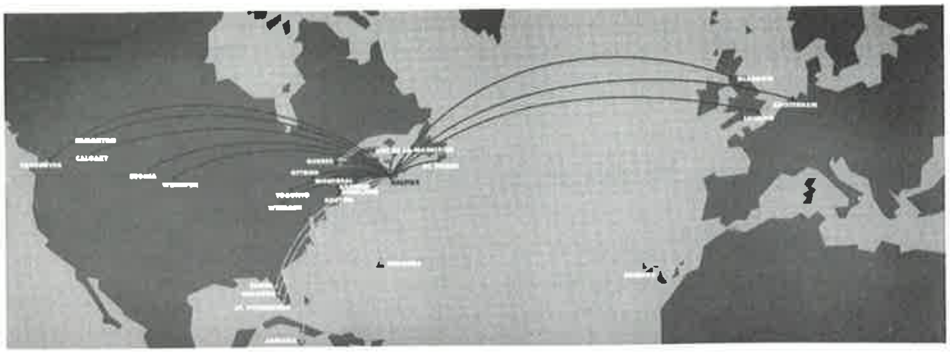


Halifax when American Eagle joins Delta, Northwest, Air Canada, Canadian, KLM, et al to give us easy access to all of North America, the Caribbean, United Kingdom and Continental Europe. (OK, OK, so the map doesn't show service to Detroit, New York and the remainder of the U.S. . . . do you think **they** show Halifax on **their** map!). Our staff have a formidable array of Canadian, American and British professional and academic real estate qualifications and the experience to match . . . but they're still a pretty down to earth bunch. You'll currently find them clad in hard hats and coveralls peering into pulp mills in New Brunswick, staring at shipyards in Nova Scotia, feeling their way around the Fixed Link in Prince Edward Island, offering advice on offices in Newfoundland and regaling clients on retail facilities in Ontario and Alberta. They're also anxious to work their magic elsewhere . . . so if you have a property in Bermuda . . . Vancouver? Detroit? Hamilton? . . . er, Sudbury?

REAL ESTATE CYCLES

Property values in many sub-markets in Atlantic Canada have now plunged to the levels of fifteen years ago. Nowhere is the impact more marked than in the region's capital, Halifax. It's a little like

being let loose in the candy store after the owner has departed for the night: everything is a bargain! We, who witnessed the inexorable march of property prices ever upwards, over the past three decades experience a sense of unreality at their dramatic collapse during the last five years.

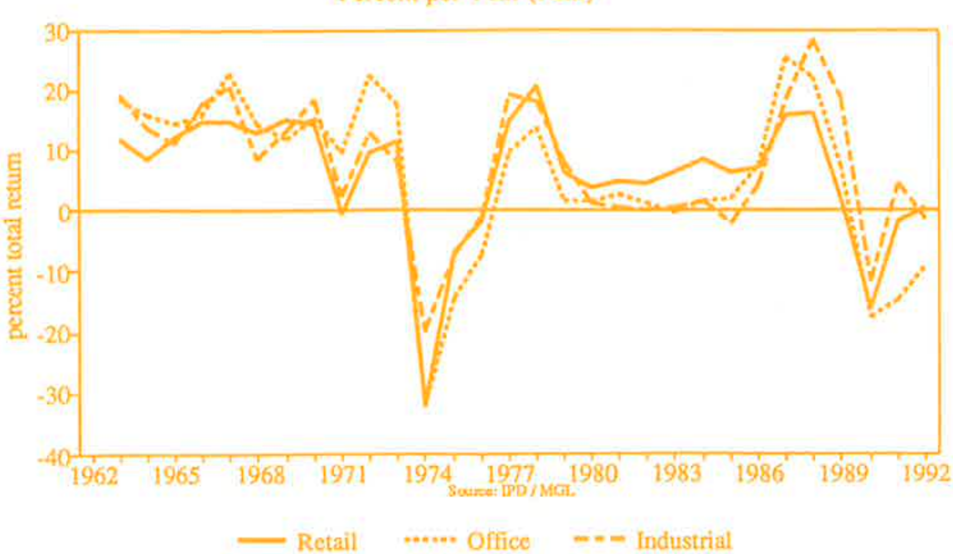
In the city centre, nestling among the sleek office towers are small architectural gems built a century or more ago of ironstone, granite or sandstone. Erected as offices, warehouses, whorehouses or residences for the town's more prosperous citizens they defy the passage of time, comfortably indifferent to the changes wrought upon the metropolis. To those of us who love real estate, they are objects of delight, treasures to be gazed upon during sleepy Sunday mornings, as the mist steals up the quiet streets from the harbour. And always, until now, just out of financial reach. A 6,000 ft.^{2} office building like this, with its metre thick ironstone walls, used to set you back a cool $600,000 (in today's dollars). Not anymore . . . they are now available for less than half that price . . . We believe that many people will look back on the present period as the greatest missed opportunity of their lifetime. Property prices move in cycles and we are now at the bottom of the cycle.

There is a tide in the affairs of man, which if taken at the flood, leads on to fortune. **(William Shakespeare; Man of Property).**

Remember Canary Wharf, the visionary office project on the bank of the Thames? When work started on the project in July 1987, office rents in London's West End had reached £40/ft.^{2}. When the first phase of the project came on stream just three years later the office market had collapsed. This signalled the demise of Olympia and York, the global property company carefully crafted by Canada's Reichmanns over three decades. Guess what? Our New America Network associate in London, James Andrew Badger now reports that the office market is rebounding: good quality office space in the West End is again achieving mid to high £30/ft.^{2} with two cases at £40/ft.^{2} plus. What goes around . . . comes around.

The most recent market meltdown in Canada, the U.S.A., United Kingdom and Japan occured during a period which fell within three years either side of 1990,

Total Return by Sector
Percent per Year (Real)



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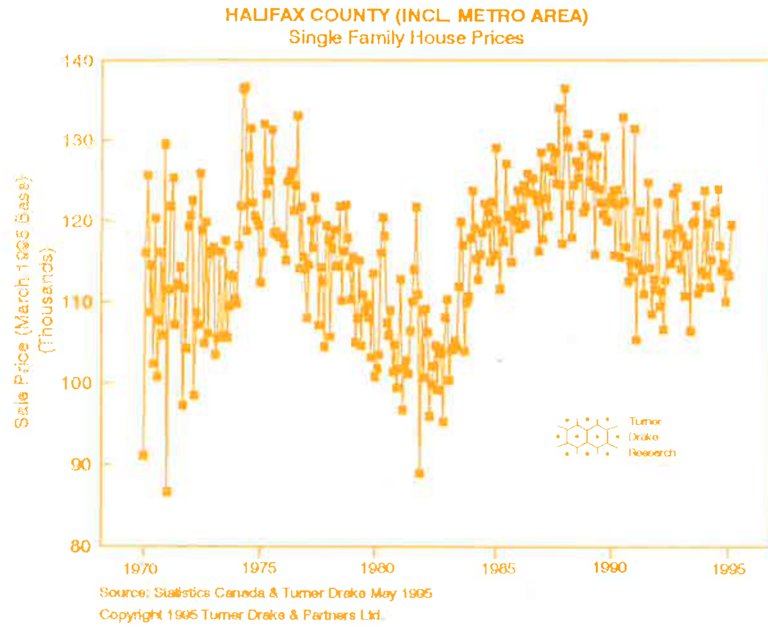
depending on the country. It is very timely therefore, that the Royal Institution of Chartered Surveyors (RICS), the international body of the property profession, chose in May 1994, to publish its study of property cycles. The research was undertaken for the RICS by the Investment Property Databank and the University of Aberdeen. Some of the results are shown in the graph (previous page). The study concluded that:

(1) Property cycles do exist and have a normal duration of four to five years: concomitant with the length of the classic business cycle in the economy. However, although the normal business cycle does influence the property cycle, they are not synchronized. Why? Because of the lead/lag factor. It takes a minimum of two years to bring a major office building on stream; more time is required if a land assembly is necessary. As a result decisions made to expand supply often reach fruition when the economy is entering a recession and demand is contracting. The problem is compounded by many individual developers making the decision to build, all in competition with one another. Too much space is started . . . which then comes on stream just as the previous demand on which it was predicated, evaporates. Vacancy rates soar, and property values dive.

(2) There is a strong correlation between the retail, office and industrial sectors (see graph previous page). Bad news if you are attempting to diversify away non-systematic risk!

(3) It is possible to build fairly simple models to explain the relationship between property markets and the wider economy. The independent variables explaining rental values are GDP (Newsletter Vol. 2, No. 49); consumer spending; financial and business services; and manufacturing activity. Inflation and interest rates also influence certain markets. (This has been the case in Atlantic Canada. Nominal office rents in the Halifax C.B.D. rose more or less steadily during the period 1970 to 1988, despite the fact that the vacancy rate fluctuated between 3% and 17%. The only recognition rents paid to high vacancy rates, was to pause momentarily or dip marginally, for a year or so, but these were minor blips in their inexorable march upwards. For the period 1975 to 1988, rental growth exceeded inflation by 0.6% per annum. Three key events changed the water on the beans and led to a rental collapse from \$22.50/ft.^{2} in 1988, to negligible effective rents per ft.^{2} in 1994. First, the start of the recession in May 1990 coincided with an expansion of office supply: vacancy rates in the C.B.D. soared to 15% from 11% the previous year. Second, in late 1991 the Provincial government was visited by the ghost of Christmas past, got religion and started to tender for its space requirements: this event destabilized the market. Third, inflation fell to an annual rate of less than 1% in 1992, down from a yearly average of 6% for the previous decade: this removed the pressure on tenants to renew their leases at higher rents).

(4) The external drivers for capital values of investment properties (shopping centres, offices, apartments, multiple tenancy industrial) are bond yields and inflation. Property has traditionally been an excellent hedge against inflation: no inflation . . . ipso facto little reason to buy investment type property.



All of the foregoing is of interest only if the results can be generalized to North America, in particular our region. The conclusions have intuitive appeal and fit the pattern of our experience but we recognize that Newsletter readers are a questioning bunch, a reflection of their superior intellect. (OK, so we're a bit short of work . . . we're not too proud to beg). Realizing that you are now perched on the edge of your chair, quivering with anticipation, we cranked up our computer and asked it to demonstrate that property cycles are a phenomenon of the Atlantic Canadian property market too. Since there is a dearth of commercial data of adequate quality and quantity to withstand the rigorous statistical testing that would be your nom de guerre we had to fall back on our residential sales database. In order to eliminate "noise"

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we converted all of the nominal prices into real i.e. deflated, prices using the StatsCan Consumer Price Index and a March 1995 base. The graph (previous page) therefore shows the property cycles **after** inflation has been removed. Twenty five years is not a great length of time but it does indicate two complete property cycles, each of ten years duration. If history repeats itself, residential property prices will increase in real terms over the next five years, since we should be on the upward swing of the cycle. We anticipate an upswing in the industrial, retail and office markets too. There is already evidence of a recovery in the industrial and retail markets. Carpe diem (seize the day!).

PROPERTY TAXES

Car Dealerships - Don't Sell Your Soul to the Taxman

We hold the view that your real estate assessment should not reflect the value of the dealer franchise . . . and that since most do, many dealerships are over-assessed. There has recently been a plethora of cases in Quebec which, whilst not addressing this particular issue nevertheless provide ammunition for an appeal. Many Ford, Chrysler and General Motors dealerships were built in an earlier age and the facilities are super-adequate for present sales throughput, often to the tune of 50%. The trend to smaller cars and the growth of specialist automotive facilities has reduced service bay requirements. Improved parts delivery and computerized systems now place less demand on parts storage and office space. There is a tendency for space requirements to expand to fill the space available, so all of it may be used even though it is not required. Test whether your facilities are superadequate by comparing the ratio of sales throughput to floor area when the structure was built, with the ratio today. (A rule of thumb is 28 ft.^{2} per car sale per annum). Better still, compare current dealer franchise specifications with your present facilities to test for super-adequacy and deficiencies.

Autoport, Dartmouth, N.S.
($81,700/annum - 28% in tax savings)

Nova Scotia - The 1996 Re-Assessment is on! Nova Scotia is the only Maritime province which still sticks to a tri-annual re-assessment: New Brunswick and Prince Edward Island re-assess annually so real estate assessments there reflect the recessionary fall in property values. The Nova Scotia re-assessment will bring much needed tax relief. The Metropolitan Halifax Chamber of Commerce voiced its concern in April that the re-assessment proceed and it is our understanding that the Assessment Department has finally put the wheels in motion and is mailing out the "request for information forms" to property owners. It is important that you complete and mail them back as requested, since failure to comply prejudices your right of appeal in the future. The assessment roll has to be completed by December 1st so the Assessment Department has insufficient time to undertake their task properly. We strongly advise all property owners to adopt a pro-active stance: ask us to review your assessment **before** the assessment roll closes at the end of November.

Don't shoot the messenger! Pity the poor provincial assessors. They do not set the tax rate nor are they accountable for the spending practices responsible for it. Our Property Tax Division deals with the assessors daily and a couple of years ago we mounted a joint two day training session with the Nova Scotia Assessment Department. By and large they are a decent group of individuals, anxious to do as reasonable a job as possible within their time and budget constraints. So, if they arrive at your property during the next few months, in connection with the re-assessment don't be difficult, they cannot do their job without inspecting your premises. However, there is no need to volunteer information: it is sometimes misinterpreted. The Assessment Department's information request forms which will be mailed to you, should capture all the information that is relevant to the assessment of your property, over and above what should be apparent to the assessor during his/her inspection. (Loose lips, sink ships!).

Nova Scotia - Mining Tax Revenue. It is not surprising that spendthrift provincial and municipal governments are strapped for cash. Despite a clamour of protest from labour groups, and private sector organizations such as the Canadian Federation for Independent Business, governments continue their time worn policy of dishing out grants and loans to "persuade" firms to establish facilities here. (The provincial government recently paid a multi-million dollar corporation $17,000/job!). The provincial Assessment Department appears to be turning over every stone (sorry!) in an attempt to locate more tax revenue. Mineral producers, such as gypsum quarries are the latest target. Under the Assessment Act

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"minerals, gas, oil, gems, salt, gypsum, commercially extractable stone or rock, precious or rare earth, moss or fossils in or under land" are taxable. However, this section of the Act has been honoured more in breach than observance . . . no longer however, the Department is now proceeding to assess them. The question to be answered is whether the value of the sub-surface rights is already reflected in the value of surface land. We are now compiling a dossier on the problem. If you are contacted by the Assessment Department, or suspect that they may be about to levy an additional assessment, please give Tom a call (1-800-567-3033).

Howard Johnsons, Saint John, N.B.
($52,000/annum - 41% in tax savings)

New Brunswick - your appeal period has now expired. Our Property Tax Division is working in all areas of the province. If you have filed an appeal and have not contacted us yet, please do so as soon as possible so that we can integrate your appeal with our inspection program.

Situated on both banks of the Miramichi in northern New Brunswick is Repap Enterprises' Miramichi Pulp and Paper, a complex of five mills. In addition to the experimental Alcell plant, ground wood pulp and Kraft mills; there are two giant coated paper mills, among the most modern and fastest plants in the world. Thundering away 24 hours per day, 7 days a week, they produce high quality glossy paper for the North American market. Like many other plants in Atlantic Canada, they are over-assessed. Heavy industry, treated as tax milch cows in a less competitive era, now has to compete on a world stage. A major point of issue for heavy industry in the province, is the assessability of electrical distribution systems within the site boundaries. The Geographic Information Corporation, the government department charged with assessing real estate has usually assessed them. Now the New Brunswick Court of Queen's Bench has ruled that an electrical distribution system is **not assessable** if its primary purpose is to supply power to equipment and machinery. Although the ruling is under appeal it will, if upheld, have major implications and further enhance the province's attractiveness as a location for industry.

Newfoundland - we are currently undertaking assessment appeals in St. John's and Mount Pearl. If you have filed an appeal in these, or other jurisdictions please give Rick a call (1-800-567-3033), he will be returning shortly to undertake other inspections.

Polyclinic, Charlottetown, P.E.I.
($22,000/annum - 12% in tax savings)

Prince Edward Island - your appeal period ends on the 19th June. We have mailed a set of decision rules to help you determine whether your property is over-assessed. If you would like additional advice, please give Mike or Tom a call (1-800-567-3033).

LICENSING LAW IN NEW BRUNSWICK

In 1993 a private member's bill was introduced in New Brunswick to make it illegal to offer appraisal or any other type of valuation advice without a license. The bill was promoted by the local chapter of the Appraisal Institute of Canada, a trade association of appraisers. Quebec is the only other province in Canada with licensing and the concept has been rejected everywhere else. The bill also provided for the regulation of advertising and a minimum tariff of fees. We opposed the bill and our president Mike Turner appeared before the Standing Committee on Private Members Bills. We questioned the morality of granting a monopoly to what is essentially a private club interested in their own gain; and the inefficiency and cost of erecting yet another inter-provincial barrier to trade. We also expressed concern that a body with monopoly powers would have no incentive to improve standards and suggested that the consumer was the most discriminating arbiter: more competition rather than less, was the only proven way to improve standards. Our arguments, and those of the only other out of province intervenor, the Hardman Group, did not carry the day and licensing came into effect on January 1st 1995. Although we firmly believe in the free enterprise principle that businesses in New Brunswick are best served if they are

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able to chose the most cost effective service, unfettered by government regulation, licensing is now law in the province. **Accordingly all of our senior staff are now licensed to practice in New Brunswick** and we will continue to service our expanding client base there as we have for the past nineteen years.

BROKERAGE DIVISION - A CORNUCOPIA OF OPPORTUNITY

Although the principal focus for our sales and leasing activity is the Greater Halifax Metropolitan Area, our membership in the New America Network affords us access to 210 primary and secondary markets worldwide. New America is the largest investment, commercial, industrial (I.C.I.) brokerage network in North America and most of its 151 members are active on this continent. So whether you wish to buy, sell or lease property in Halifax, Vancouver . . . or any point in between . . . or the United States, Mexico, South America, Europe, the United Kingdom . . . just give us a call (1-800-567-3033) and we'll ask our fellow NAN members to bring their eagle eyes to bear.

Leasing

Many tenants who want to relocate wait until the dying months of their lease before starting to research the market. It is generally too late. The optimum time to start your premises search is nine to twelve months ahead of your lease expiry date. It is advantageous to utilize the services of a single commercial (I.C.I.) real estate broker: virtually all of the space in the Halifax - Dartmouth metropolitan area is available through I.C.I. brokers such as ourselves. Most landlords go to great pains to keep the I.C.I. brokerage community updated on their space availability and hopping from landlord to landlord, or broker to broker is time consuming, expensive and frustrating for all concerned. Using a broker does not cost you anything: it is an efficient way of trawling the market to find the space that best suits your requirements.

The supply of vacant **industrial space** is shrinking and with it generous "free rent" incentives. About a year ago, landlords were offering 12 to 18 months free rent on a five year lease: this is down to 3 to 6 months today. As the economy continues to expand rental incentives will disappear. There is still a lack of confidence on the part of tenants and economic restructuring is still evident, most notably in downsizing and branch closures. Many tenants are opting for short lease terms (2 or 3 years) since there is little inflationary pressure to lock in for a longer term. Despite the economic recovery, demand for **retail space** is weak. However, we are getting more enquiries from prospective tenants looking at the region for the first time. There is a glut of **office space** particularly in the Halifax C.B.D. and rents have weakened over the past quarter. It is difficult to believe that they will go any lower and we believe that they are now at the bottom of the cycle. Suburban areas such as Bedford are attracting greater interest: there is no longer the same imperative to locate "downtown" in Halifax or Dartmouth and tenants are reducing their commuting costs by working closer to home.

If you are looking for space, Russ (tel. 429-1811) will be glad to assist you. Ask him about our tenant representation program.

Sales

It is a buyer's market for virtually every type of real estate. In many sub-markets, properties are available at prices not seen for fifteen years or so. There is a lack of confidence in the economy despite its high growth rate and a property will not find a market unless the purchaser has an immediate use for it. There is a cornucopia of modern **industrial properties**: twenty are listed for sale in the Burnside Industrial Park alone, some at half their original building cost. Most are small: 2,000 ft.^{2} to 10,000 ft.^{2}, but larger properties are also available. **Office buildings** are available in all sizes at prices discounted by 50% or more over their 1988 value. Some of the smaller buildings in particular, present astonishing opportunities for purchasers. **Shopping centres** are available at "all cash" yields of 12% to 13% and offer remarkable opportunities for investors. We have not seen investment opportunities like this at anytime during the past twenty five years. We also have **land** available, suitable for residential development. Verna (tel. 429-1811) can provide you with information on all types of industrial, commercial and investment property.

POLLUTED PROPERTY

A Potent Pot-Pourri

"Eighty percent of all urban sites are polluted", that according to the Royal Institution of Chartered Surveyors is the situation in the United Kingdom. We know of no similar survey in Atlantic Canada, the country's oldest industrialized region, but it certainly accords with our own experience.

Legislation on environmental pollution has rendered numerous sites in Atlantic Canada worthless: indeed the cost of clean-up often far exceeds the value of the property in its "clean" condition. Sometimes the pollution has escaped off site under the adjacent street: the property cannot then be sold without a covenant from the vendor indemnifying the purchaser against future claims. Since such indemnity is rarely forthcoming, and may be insufficient to quell the purchaser's fears even when offered, the fee simple interest is unsalable. If this is the case the only practical way to extract value from the site will be to lease it.

Underground storage tanks are costly to clean-up ($100,000 to $200,000 for a gas station site is not abnormal). Provincial regulations require the replacement of steel underground tanks which do not meet current standards, usually before they are fifteen years old. We will address environmental regulations and their impact on property values in future issues of Newsletter.