

ASIA PACIFIC LISTED REAL ESTATE:

A CONTEXTUAL PERFORMANCE ANALYSIS



SUMMARY
VERSION

ABOUT APREA

APREA is a non-profit industry association that represents and promotes the real estate asset class in the Asia Pacific region. It is the industry body for the suppliers and users of capital in the real estate sector. It embraces the four quadrants of real estate. APREA's mission is to:

- Represent and promote the Asia Pacific real estate asset class
- Encourage greater investment in the Asia Pacific real estate sector through the provision of better information to investors, improving the general operating environment, encouraging best practices and generally unifying and strengthening the industry
 - Enhance regional and global networks for capital suppliers and users
- Represent the sector to governments and regulators to improve the commercial operating environment for members

Its membership comprises real estate companies, listed real estate trusts, unlisted property funds, investment managers, investment banks, property securities fund managers, institutional investors, real estate consultants, corporate advisors, stockbrokers, investment advisors and universities.

APREA membership is the gateway to a network of the industry's most influential decision makers and provides the opportunity to influence and participate in the development of the real estate markets in Asia.

APREA's achievements in education and information dissemination, and focus on improving the general real estate operating environment, have firmly entrenched it as the leading representative body for the industry in the region.

In particular, its achievements in driving regulatory improvements within the listed real estate trust sector extend beyond existing markets and pave the way for the emergence of new markets in other Asian countries.

For additional information on APREA, please visit www.aprea.asia.



INTRODUCTION

The full paper is divided into ten sections:

Section 1 presents the background and rationale for this paper **Section 2** examines the differences between this and previous studies **Section 3** is a review of the academic and practitioner literature on this topic **Section 4** describes the growth of the market

Section 5 provides a detailed performance analysis

Section 6 presents an analysis of the impact of including Asian listed real estate in a global portfolio

Section 7 looks at the different corporate governance structures of Asian REITs to see if there is a performance impact

Section 8 provides an overview of forthcoming regulatory changes

Section 9 provides an insight into fund manager perceptions of the sector

Section 10 presents the conclusions of this study

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BACKGROUND

It is well understood that Asia Pacific listed real estate markets are diverse and present differing levels of maturity. However, it also known that the overall expanding capital markets across the region are now providing the depth and liquidity necessary to support increased investor interest in the region as a whole. This has been particularly noticeable since 2007 when the Asian share of global real estate indices has increased. The peak to trough decline of around 45% suffered in the commercial real estate markets of the US and the UK was not seen in Asian markets, which had a more conservative legacy of debt accumulation at both the corporate and individual levels.

REIT legislation, long established in Australia, has been introduced into other markets in the region, with an increasing level of adoption, thus providing another capital option for both investors and asset owners/managers. At the end of 2013, the free float market capitalisation of Asia Pacific REITs in the TR/GPR/APREA Composite REIT Index was US\$184 billion, comprising 129 REITs, of which Australia accounted for US\$68 billion (27 REITs).

Despite this progress it should be remembered that REITs still represent a minor proportion of the real estate universe. Studies and surveys such as APREA's *The Significance of Real Estate in Asian Pension Funds* have highlighted impediments to investing in real estate in Asia, including unfamiliarity with the asset class and lack of information. Global institutional investors tend to view Asian real estate as higher risk and therefore require an appropriate "risk/reward" solution. The APREA commissioned report on *The Benefits of an Allocation to Real Estate for Institutional Investors* generated some new analysis of the performance of REITs in Asia (ex-Australia) since their inception in 2001 and triggered discussion around the need for more research of this nature on a broader and more regular scale. The performance of Asian listed real estate was again in the spotlight at the annual APREA Property Leaders Forum in April 2014, where this report, together with another APREA report on *Exploring the Linkages Between Listed and Direct Real Estate in Asia*, were presented.

In 2011 APREA established an Investor Outreach Committee, the objective of which is to promote Asian real estate as an asset class and in doing so address the issues and concerns of the kind referred to above. In this regard APREA is becoming more closely aligned with the investor outreach endeavors of NAREIT and EPRA.

APREA therefore sought to commission an analysis of the performance characteristics of listed real estate in the Asia Pacific region, building on the two recent APREA reports, to provide a platform for greater information about this asset class and in so doing help to deal with the challenges referred to above.

Asia Pacific real estate would benefit from greater investment by global institutional investors in many respects, including the following:

- The encouragement of a continental market for real estate in Asia
- The promotion of efficiency and transparency of local real estate markets through the involvement of strong powerful players (e.g. corporate governance)
- The generation of new sources of funding for Asian listed real estate vehicles

This report seeks to provide a contextual framework from which an analysis of the Asian listed real estate sector can seek to provide greater understanding of the sector as a clearly identifiable asset class, and promote further development and acceptance by asset owners and investors globally.

EXECUTIVE SUMMARY

This paper seeks to provide a better understanding of the performance of listed Asia Pacific real estate, the factors which determine this performance and current and potential roles and applications within portfolio management. Throughout this paper we focus primarily on the Asia Pacific region, that is Asia plus Australia and New Zealand. On occasions, however, for specific reasons we have narrowed the definition to Asia, which will not include Australia and New Zealand.

The starting premise of our analysis is as follows:

- Asia Pacific listed real estate markets are diverse and present differing levels of maturity
- The overall expanding capital markets across the region are providing the depth and liquidity necessary to support increased investor interest in the region
- REITs, long established in Australia, have been introduced into other markets in the region and provide another capital option
- Market capitalisation of Asian REITs (ex-Australia and New Zealand) now exceeds US\$100 billion but REITs represent a minor proportion of the real estate universe
- Studies and surveys such as APREA's *The Significance of Real Estate in Asian Pension Funds* have highlighted impediments to investing in real estate in Asia, including unfamiliarity with the asset class and lack of information
- Global institutional investors tend to view Asian real estate as higher risk and therefore require an appropriate "risk/reward" solution

KEY QUESTIONS

In this paper we set out to answer the following questions:

- **Growth of the market:** How has the Asia Pacific market grown relative to the global real estate universe?
- **Performance analysis:** How has the sector performed relative to other regions globally, as well as other asset classes over the cycles? Are there diversification benefits?
- **Portfolio analysis:** Has having exposure to Asian listed real estate improved performance of a global fund? We use the proprietary fund database of Consilia Capital to assess the impact
- **Corporate governance:** Asian REITs have a different structure to REITs in Australia, the US and Europe. Does this affect performance?
- **Regulatory changes:** Are there potential changes to REIT legislation that could further increase demand?
- **Market perception:** What are some of the issues holding back global investors?

DIFFERENCES FROM OTHER STUDIES

We believe that this study is different from previous studies in a number of important respects:

- Firstly, it examines Asian listed real estate in the context of both global listed real estate, and competing domestic or regional asset classes such as equities and bonds
- Secondly, we have taken actual fund data as well as index data. That is, we are analysing both benchmark returns and the actual, delivered returns to investors
- Thirdly, we have examined the impact of corporate structure and tax status on performance. In particular we draw upon some pioneering work that has been done on the specific topic of whether Asian REIT structures lead to a conflict, or an alignment, of interest with external unitholders
- Fourthly, rather than use a single period, or peak to trough periods, we have broken down the study into an analysis during distinct stages of the cycle, starting with the run up to the Asian crisis in 1997. The purpose is to isolate performance characteristics of Asian listed real estate at different, identifiable stages of the global and regional economic cycle
- Fifthly, we have examined the impact of currency on performance at different stages of the cycle
- Finally, we have isolated the performance differential between investors and developers

CONCLUSIONS

Growth of the market

Asia Pacific has experienced similar levels of growth to the US since the Asian financial crisis and is now valued at US\$542 billion. From a peak of over 50% in the late '90s and a low of about 20% ten years ago, it now represents around 35% of the global listed real estate market.

Performance analysis

Looking at the performance of Asia Pacific listed real estate relative to the global real estate market, we find that with the exception of the period around the Asian financial crisis, the Asia Pacific listed sector has performed consistently well, in both local currency and US\$ terms against a global benchmark.

Below is the summary performance of Asia Pacific listed real estate, the Global benchmark, and the subsequent relative figure. We have shown these in US\$ to enable a consistent comparison, and the calculations are cumulative rather than annualised.

		Global US\$	Asia Pac US\$	Difference
1992-97	Pre Asian crisis	82%	120%	38%
1997-9	Asian crisis	-13%	-26%	-13%
1999-2002	TMT boom and bust	12%	-12%	-24%
2002-2007	Bull market	182%	223%	41%
2007-2009	GFC	-52%	-56%	-4%
2009-2013	Post GFC	125%	159%	34%
2013 -	Tapering	-1%	-1%	0%

In addition, our correlation analysis highlights the importance of Asia Pacific real estate in providing diversification benefits with both stocks and bonds. Emerging Asian markets provide stronger diversification benefits with both asset classes, whereas developed Asian markets provide similar benefits with the Australian, UK and US markets.

Portfolio analysis

Given the dominance of the US in the global listed real estate securities funds market, the decision to go global requires evidence that Asian funds and Japanese funds (the two popular mandates we monitor) can contribute to performance. In only two of the ten years (2005 and 2011) did both Asian and Japanese funds underperform US funds. The correlation of Asian Funds to European and US Funds is lower than for US funds, and below 72% to Japanese funds. By contrast US Funds have a correlation of 90% with European Funds.

Corporate governance

One of the potential areas of concern for investors is the REIT-sponsor relationship which occurs in Asian (ex- Australia and New Zealand) markets. Overall, existing studies appear to suggest that investors do not need to be concerned about potential agency conflicts associated with REIT-sponsor relationships. This is because the interest of REIT managers and sponsors are likely to be significantly aligned with that of other unitholders as most sponsors hold significant unitholdings in the REIT. In addition, given the development-driven nature of the Asian REIT market, the support provided by the sponsors (especially developers) is of particular significance. This has seen strong sponsor backing as one of the important drivers of the growth of Asian REIT markets in the past decade.

Regulatory changes

One of the key elements of a successful REIT market is that the regulators continually revise legislation to maintain growth in the market and reflect trends in international practices. We believe that the current proposed developments (particularly proposed changes to the Hong Kong REIT regulations) would increase the attractiveness of Asian REITs to global investors and facilitate further development of the Asian REIT markets in the future.

Market perception

There are areas where investors believe further improvement could be made, namely:

- REIT managers combining good property skills with good capital management skills
- Buying assets because the acquisition makes sense from the REIT's unitholder perspective, not just to increase AUM (and therefore fees)
- Minimising heavily dilutive equity issues

THE AUTHORS

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Alex gained an MA in the Economics of Finance and Investment from Exeter University and has spent over 30 years specialising in the real estate sector globally. He founded Consilia Capital, which specialises in implementing real estate strategies for corporate and institutional clients, in 2012.

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Annisa recently completed her PhD program in Real Estate Finance at the University of Reading, United Kingdom. Her PhD research is in the area of Asian real estate investment trusts. She obtained her MSc in Money, Banking and Finance from Birmingham University in 2009 and BA in Business and International Finance from Oxford Brookes University in 2008.

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