# Global Real Estate Conference: Insights

## Asia's Influence on the Global Real Estate Market

**Presenters:**
Andrew Lim, CFO, CapitaLand Group
Peter Kim, Managing Director, International Real Estate, Asia QuadReal
Junya Kato, Partner, KPMG in Japan

**Junya Kato (JK):**

**For this session, we will talk about Asia's influence on global real estate market. My name is Junya Kato, from KPMG and I'm moderator of this session. And we have two speakers here. The first speaker is Mr. Peter Kim from Quadreal. Mr. Kim, could you kindly briefly introduce yourself and Quadreal, please?**

**Peter Kim (PK):**

Thank you, Kato-san. My name is Peter Kim and I am the managing director for Asia for Quadreal's property group based here in Hong Kong. We are a global real estate investment manager and operator, headquartered in Vancouver, British Columbia. And we have international offices that we maintain in New York, in London and here in Hong Kong. So my responsibility for Quadreal is I mainly look after the Asia Pacific portfolio and investment activity on behalf of the company.

**JK:**

**From your company information, company brochure, I understand Quadreal has total assets under management globally 44 billion U.S. dollars. That's a massive amount of money, and from U.S. investment portfolio, you allocated your investment into Asia about six percent, which is about 2.7 billion U.S. dollars. My first question is do you have any reason of your allocation in Asia Pacific region and do you see any say investment objective by doing so?**

**PK:**

Yes, sure. So maybe to take a step back, when we made the decision years ago to open an office here in Asia, with the obvious intent to really focalize our investment activities for the region from within Asia, I think what we found compelling about Asia Pacific back then still persists in many ways today. We like the fundamental economies of the markets that we target for investment here in this region. We liked a lot of the sector formation that we've been seeing, particularly in logistics in many markets where years ago, it still remained somewhat of an emerging asset class. And even in some markets today, very vanilla tried and true asset classes like multifamily or as we call it in North America, but perhaps better known as built to rent here in many of the markets in Asia, are very, very nascent in their formation and evolution and we've been enjoying seeing how a lot of these assets, these asset classes and even submarkets have played out around themes or strategies that we've seen elsewhere, or at least in other parts of the world, you know, student housing is certainly something that we've been seeing a lot more and more of. In fact, we've invested heavily into it in Australia and that's an offshoot of a similar formation of student housing as an institutionalized asset class in North America.

A lot of those reasons that we liked back then we believe still persist today and then in terms of I guess going back to your earlier question around how we see this continuing in Asia, you're right, we are less than ten percent of our global portfolio in Asia today, while we don't have any strong or hard allocation requirements directionally at least, we do foresee, or we do hope to see Asia comprising well over ten percent, you know, somewhere between ten to 20 percent of our global portfolio going forward.

**JK:**

**Okay. Thank you, so you are thinking about increasing your portfolio allocation into Asian region and in order to do so, how do you think you could achieve it? Do you like to prefer to establish your own platform in the region to increase your investment or do you prefer to work with local partners?**

**PK:**

That is a great question. So for the moment, internationally, and by international I mean really outside of Canada, our strategy to date has been to partner with those who we believe to be best in class operators in each of the markets that we have highlighted for investment or that we're interested in investing, and really teaming up with those, as we call them, local sharpshooters to find those investments or series of investments that we believe to be interesting for us and most important for our clients. Now this differs a bit from how we operate in Canada, where we are a fully integrated operator. We source, we develop, we lease and continue to manage many, many of our residential and commercial assets all throughout Canada. And thus, most of our, call it 1,300 employees globally, sit in Canada to support those.

We're a lot leaner here, and not just here in Asia, but similarly in Europe and in the United States. As I said, in terms of increasing the percentage of Asia Pacific investments vis-à-vis our global portfolio, these are just really directional aspirations, than any hard allocation requirements, but how we intend to do so, or to execute on that plan is to continue to team up with the best operators for the best strategies in each of these markets that we target. Capital is typically not an issue for us, so it's really less about the check sizes and more about making sure that we have the right partner and the right alignment to ensure that we can execute on our plan.

The other thing that I might mention, and we don't do it as much in Asia, is that we do, we have been focusing a lot in terms of making investments in the operating partners or companies themselves. And that's another way that we've found, particularly elsewhere in the world to really scale up, particularly around those themes or strategies that we find particularly compelling. So Asia, of course, as you know better than most, it's a wider and more diverse geography and region than say North America. And so it does make OPCO investing a bit more challenging for us out here. But we certainly have not ruled that out.

**JK:**

**Okay. Thank you. Next point I would like to further talk with you is your investment strategy. Comparing to your home countries and home markets, say North America market, Asian markets tend to be diverse and sometimes, it's less transparent. And also, because you are investing in foreign countries, you need to think about foreign exchange rate risks and interest(?) risks, which pertain to each country. In order to make a return, which overcomes its risks, do you usually apply for different strategy of your investment in Asia comparing to your investment in home market, in North America?**

**PK:**

It's a great question. So in terms of I guess underwriting for a lot of the regional specific risks that we can sometimes run into here, as well as the basket of FX considerations that we also have to assume when underwriting our returns, the FX part is, I wouldn't say it's easy, but there's a well trodden path in terms of how we approach that. We do try to borrow locally as and when it makes sense, and, and(?) fortunately, for many of the markets here in Asia in which we investment, they are some of the world's lowest interest rate environments. And so taking on domestic debt does serve as a natural partial hedge to the FX exposure that we undertake.

And then in terms of the residual exposure on the currency, we also do buy currency forwards and puts, again, as and when it makes sense. So we do have an active hedging policy in place where we try to (Audio Dropout) real estate risks. There are other risks that I believe are particular … I wouldn't say particular, but perhaps more pronounced here in Asia. I do think that political risks, political risks exists anywhere, regardless of where you are in the world. But I do think that policy risk is something that we often think about perhaps a bit more often here than (Audio Dropout). There's tax structuring risks and I think how we get around that is to work with very good tax advisors, such as yourselves and others in the market. And there's even, at its most basic level, adjudication risks, whereby we do recognize and acknowledge that in some of the markets in which we invest, it might be very difficult for us to enforce certain governance provisions that we may have agreed to or documented with our partner.

And so, how does that … I guess back to your question, does that change, or does that impact our way of how we view investing here in Asia, or do we apply any different strategies, I think the short answer to a very long (Audio Dropout), we tend to underwrite for shorter durations here in Asia, particularly in markets like China, for example, where there is no freehold ownership of land, it's all based off finite land (Inaudible). And so without boring you further, in very developed markets such as Japan and Australia, we have underwritten our real estate investments to up to ten years. In other markets like China, Korea, we typically start out underwriting opportunities for say five years. We also increase or decrease the risk premia tied to a lot of those risks that I just talked about earlier, the tax structuring, the policy, the legal risks and try to build in enough buffer such that if any of these risks do materialize, we have enough cushion there to at least bring home a decent return.

**JK:**

**So as you mentioned, the early stage of a discussion, you Quadreal would increase your investment allocation into Asia towards around ten percent or more.**

**PK:**

Yes, I mean assuming the opportunities are there of course. Again, these are directional aspirations more than anything else.

**JK:**

**Do you see any challenge in achieving that goal? I mean increasing your portfolio allocation in Asia to more than ten percent? Do you have any challenge?**

**PK:**

Not from a fundamental perspective. I mean as I said, we do like the growth that we see in many of the economies here in Asia. And some of that growth might be tapering off like in China, for example, where the GDP growth rate has certainly come down from ten years prior. But as each of the economies continue to grow year on year, in terms of the absolute amounts of gross domestic product that these countries, many of whom are no longer small or emerging in that sense, even a four or five percent growth can be an enormous needle mover. Not just for real estate, but for many other asset classes as well. And so, the answer is no, I don't see much to really keep me up at night in terms of whether or not should the opportunities exist, we could increase our allocation, or at least increase the percentage that Asia Pacific composes in respect to our (Audio Dropout).

We have a lot of great tailwinds behind us. The underlying growth in the various economies that comprise Asia or compose Asia on a relative basis certainly seems a lot more attractive than perhaps other markets in the West. So I think, as has been the case for some time, the winds are on our side. And so long as we have no more black swan events or unknown unknowns, I think the future looks pretty.

**JK:**

**Okay. Thank you very much for providing us with your great insight of your investment in Asia Pacific region, Mr. Kim, thank you again for taking time for this discussion.**

**PK:**

My pleasure Kato-san. Thank you for having me.

**JK:**

**Thank you. We have another guess speaker, Mr. Andrew Lim. He's the group chief financial officer of CapitaLand. He oversees CapitaLand's global investment from the perspective of CFO. Mr. Lim, could you kindly introduce yourself and CapitaLand, please?**

**Andrew Lim (AL):**

Thank you, Kato-san. It's a delight and a pleasure for me to participate in the KPMG conference. Thank you for having me. So for those who are not familiar with CapitaLand, we are today a leading diversified real estate player centered in Asia. We have a global footprint with about 20 percent of our business outside of Asia in developed markets such as Europe and North America. But most of our business is centered within our core(?) market here in Singapore, and equally so in China. We have two other core markets, Vietnam and India, so all four of our co-markets are in Asia. Most recently, we've just made an announcement, which is quite substantial to the group, where we will be spinning off our fund management business into CapitaLand Investment Management and privatizing the development side of CapitaLand. So that is a very recent development and will quite fundamentally transform what CapitaLand will be in terms of the public market exposure. But as a single ecosystem, we will very much remain one CapitaLand.

**JK:**

**My first question is Asia's influence on the global real estate market and why do you investment outside of Asia? Do you have any particular reason of doing it?**

**AL:**

Thank you, Kato. So maybe I'll turn back to my initial introduction of the group and you will have noticed that all four of our core markets are first of all in Asia. The other observation I will make is that three of the four of our core markets are in emerging Asia. And emerging Asian markets investing in development in real estate in these markets presents a very different risk return profile for CapitaLand. So the reason we elect to allocate roughly 20 percent to developed markets outside of Asia is to allow us to balance that risk return profile for the group. Our emerging markets business, we know we tend to target 12 percent plus type of return on equity. And for the developed market side of the business, we are generally around sort of eight to nine percent, ten percent type of return.

So by blending this together, it allows us to achieve risk adjusted return on equity that we feel is commensurate with the types of businesses in real estate that we are involved in whilst maintaining a good exposure from a risk standpoint, from a diversification standpoint, and from a foreign exchange exposure standpoint as well. So as a diversified real estate company, we feel that this balance is an important one to strive towards.

**JK:**

**Okay. Is it fair to say your investment in outside of Asia, I mean in terms of investment strategy, you tend to apply (Inaudible) investment whereas your investment in Asian countries is going to be either opportunistic or value add investment type? Is it fair to say it like this?**

**AL:**

There is an element of accuracy in that, Kato-san, in the sense that as a developer, our development expertise is very much within those four core markets that I talked about. We do not have development expertise outside of these four core markets. So all of our capital that is currently deployed in developed markets in Europe, North America, in sort of completed investment properties, these tend to be core-plus types of investments and we tend to make these investments through our listed vehicles, such as our REITs and our private equity funds, which require or thrive in environments that are liquid, you've got a good investability and a good choice of assets that you can choose from and compete in. And those developed market real estate classes lend themselves to our REITs and our private equity funds. So the short answer is absolutely yes.

**JK:**

**Okay. In terms of investment horizon, do you apply different investment horizon when you invest in say other developed markets comparing to Asian markets, or do you usually apply the same time horizon for your investment in both markets?**

**AL:**

It tends to be a function of availability of product. So I go back to the fact that your developed market, our developed market exposure tends to be in operating liquid investments. And the idea is either to acquire them through our REITs and our funds, in which case, they are core and we acquire to hold. But if they are acquired by us perhaps to incubate or to add a little bit of value, then the investment horizon is quite short because we will look to recycle that capital as quickly as we can by pushing them down into our (Inaudible) vehicles, our REITs and our funds.

Conversely, a lot of the capital that we have deployed in emerging Asia is in development and that by its nature takes a longer period of time. So the investment cycle will have to encompass an additional period of land acquisition, preparation, development, and then hopefully, we stabilize the asset and then we can continue to recycle that into our REITs and our funds. So usually, I would say that our emerging markets time horizon tends to be longer because we are engaged more in development activity in emerging Asia.

**JK:**

**I see. Thank you very much. In speaking about your investment in outside of Asia, I would like to ask you about how do you materialize your investment? I mean you might want to invest through your own platform or do you prefer to work with local partners?**

**AL:**

We have traditionally done almost everything in-house. And we pride ourselves on having investment teams on the ground in our core markets who go out and source for product. We have in our four core markets development expertise and we also have a fully in-house operating platform. So we have the capability as a diversified real estate company to manage the asset, in some cases, all the way through its life cycle, from development to operations to hopefully third-party ownership through our REITs and our funds and recycling that down.

So, I would say that the element of involvement in real estate through its life cycle is much more invested in Asia where we have the full product capability. In the developed markets, there is sort of a lighter touch, more of a pure investment property type of an approach, where we do not have the full speed of development and operational expertise.

**JK:**

**Do you see any challenging issues when you're investing outside of Asia, compared to investing in Asian countries, especially China and Singapore? Do you have any challenges?**

**AL:**

Lots of challenges. Each country has very specific challenges. Our largest market is China. China has tremendous potential that still exists within the real estate space. There are a lot of opportunities, particularly in terms of securitization. We see a C-REIT product that is just emerging that I think can be very interesting to us. We would love to be able to better tap onshore R&D as a source of equity, as a source of capital in growing our FUM pipeline. These are some very interesting opportunities for us as a group.

Challenges clearly I think are going to be along the lines of two things. One is the geopolitics and the uncertainty of the international ecosystem, how that plays into asset ownership and capital flows, I think that's going to be something we will increasingly have to pay attention to. The credit situation in China in the short term is an area of concern. We see much tighter restrictions on lending to real estate in the near term, particularly with domestic real estate developers. And here is where I think being conservative in how we manage our balance sheet historically has really helped and will continue to help us going forward. So managing around three red lines, credit exposure is going to be a key to success in China going forward.

Going more globally, I think the tax situation, as it is emerging, coming after an unprecedented amount of government spending, they are going to look for ways to recoup some of that and we see this principally in the form of higher tax rates for all countries, most recently, we saw the U.S. putting forth a global minimum tax proposal that is generally being very well received by many countries. So if that type of mechanism comes to pass, then I think in our investment decisions, we will have to factor higher tax rates into our investment decisions across the board, regardless of where we move(?) it. So I think that's going to be a key driver of our return as we look to deploying capital in the near future.

**JK:**

**Okay, thank you. I have one very curious question for you. It's about development of Asian real estate markets. We have a lot of say (Inaudible) of markets in Asian countries, but we could reasonably assume that within say five to ten years' time, we would see a lot of say Asian real estate market is going to be matured, which mean that more transparent market situation and markets should be good in-depth(?) which is good for your investment I believe. If so, I mean if Asian market further develops and stabilizes and is more transparent, do you think your capital allocation to Asian countries would increase comparing to today's your capital allocation?**

**AL:**

Oh, very interesting question, Kato-san. I think there are multiple facets. One is the diversification aspect. From that aspect, I would say that I would imagine we will continue to retain an interest in very liquid real estate markets. And the U.S. and Europe are incredibly liquid. There are asset classes there that you cannot find in Asia. A good example is rental housing, what we call multifamily in the U.S. I know you have this in Japan. It's a very successful sector. But in many other parts of Asia, it doesn't exist. So, in cases where we may find product sectors that are interesting and investible and liquid, I would say that we may still rely on the developed non-Asian markets for access to those subsectors.

However, your point is that as real estate markets mature and evolve and gradually open up, become more liquid, more investable, is there a potential to increase allocation because we see the ability to manage the risk adjusted return? The answer is absolutely yes. Already we see in our core markets, Vietnam, we are seeing increasing evidence of securitization. Capital market products are being increasingly made available. Vingroup recently listed very successfully, I think we saw the first exchangeable bond into Vietnam being done. India is increasingly becoming much more investable from a U.S. dollar and (Inaudible) dollar perspectives because of the issue with India has always been the FX exposure and the very high tax rate in investing locally and repatriating that capital out.

That gap is starting to narrow and if that continues, then India becomes a market of huge potential in investing in investment properties and potentially even in development that can be measured or managed on a risk adjusted basis as part of a developed, more evolved real estate ecosystem. And then, in China, as I mentioned, we have C-REITs coming up, increasing focus on securitization and transparency of accounting systems and so on and so forth.

So if your question is in the next five years, do we see increasing investability and a more level playing field in terms of developed versus emerging markets, then I would say I certainly would expect that to be the case.

**JK:**

**That's very, very interesting point in your comment, Mr. Lim. And I'm very glad to know that, say honestly speaking I share the same view, so I'm glad to hear that, and I think we say Asian countries are going see more active and more (Inaudible) market in coming five to ten years time. And I also hope that the Japanese investors can also go out more intently to overseas(?) markets, including Asia to seek for stable and good return comparing to our domestic market.**

**AL:**

Indeed.

**JK:**

**And I hope your company, CapitaLand would increase your investment into Japanese market as well.**

**AL:**

Yes, we have partnerships with some leading Japanese developers, some very longstanding partnerships that have endured and are very healthy. We are looking to do much more. We've just recently signed a partnership with Mitsui on logistics, Greenfield development, which we believe is a nice growing sector in Japan. And so we certainly share that view and want to do much more in Japan, as a developed Asian market.

**JK:**

**Okay. Thank you. I hope you enjoyed our conversation today and thank you very much for providing us a very meaningful and insightful information and comments. Thank you very much, Mr. Lim.**

**AL:**

You are very welcome. My pleasure. Thank you and be safe. I look forward to catching up again soon. Take care.