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Rethinking Opportunities in Asia

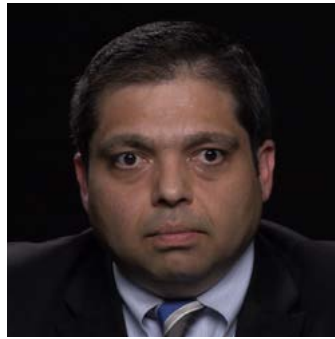


Rethinking Opportunities in Asia

Commercial real estate deal flow in Asia fell 41 percent in the first half of 2015, prompting many investors to rethink their strategies in the region. For Prudential Real Estate Investors and Townsend Group, that translates to plenty of short-term and long-term opportunities.



Benett Theseira,
Prudential Real
Estate Investors



Prashant Tewari,
Townsend Group

Asia's commercial real estate markets had become increasingly volatile long before China's equity markets wobbled in late summer 2015.

Indeed, deal flow in 2014 was down 24 percent compared to a year earlier, while in the first half of 2015, transaction volume fell \$159B, or 41 percent, according to data provider Real Capital Analytics, the latter driven by a two-thirds fall in development site acquisitions as well as 30-percent-plus declines in office, industrial, and hotel deals.

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As value recovery took hold in the U.S. and Europe, it seemed many investors turned their attention away from Asia.

Yet in the wake of rising volatility and falling transaction volume, managers and institutional investors are beginning to refocus their attention on Asia as short-term opportunities re-emerge alongside the longer-term growth stories of the region.

“Asia is going through a transitional process,” says Prudential Real Estate Investors’ head of Asia Pacific, Bennett Theseira. “It’s had many years of strong growth, [but] it’s actually good that there is some element of correction or headwind in the markets, because it creates opportunities. It brings values to a much more rational level.”

And those opportunities are coming across the risk spectrum, he adds, as well as across different countries.

“Asia offers both long-term and short-term opportunities,” says Theseira, who leads PREI’s \$4.7B Asia portfolio, which is invested in six countries, predominantly in the core and value-added space and across all the property food groups.

“In general, based on the long-term fundamentals of the region, we advocate a long-term hold—particularly for core assets. But apart from that, because of the growth of the markets, which creates some volatility, there are great opportunities for short-term [investments].”

Seeing a plethora of opportunities is a view shared, in part, by Townsend Group principal Prashant Tewari, who leads global investment strategy for the Cleveland, Ohio-based investment manager.

“There is growing interest in our client base in Asia real estate,” says Tewari, who believes that in “years to come, Asian real estate is going to gain increasing prominence in our client portfolio.”

Townsend is focused on value-added, repositioning opportunities in the region, not least in India, where the firm—alongside a sovereign

wealth fund—recently invested in a senior-secured lending platform for condo developments. However, Tewari thinks it’s important to understand the unique elements of each country’s economy and how uncorrelated the Asia region is as a whole before investing.

“In the developed markets of Japan and Australia, Japan has a stagnant growth outlook, while Australia has a healthy growth outlook,” says Tewari. “On the contrary, when you look at the emerging economies of China and India, in India you have a high growth rate that is accelerating, and China, up until now, had an even higher growth rate. This lack of correlation among the economies in one given region is a little unprecedented.”

For Theseira, such a lack of correlation among Asian economies and real estate markets means execution is key to the success of any investment strategy.

“Asia is a complex market,” says Theseira, who argues that boots on the ground is part of any successful deal execution. “There are different markets and different cultures, and relationships are important. In order to be successful you need to have a local presence, you need to have people that are either local or have a great understanding of the local culture.”

But just being able to read a market or pick a good asset isn’t enough, Theseira continues. “Execution is key. In many cases, the level of asset management execution in the Asian markets is fairly weak, and so our ability to work with development partners or joint venture partners, bring in quality standards, or a much more developed approach to real estate asset management – I think that adds a lot of value.”

Tewari agrees, saying that it’s not just boots on the ground that ensures success, but also a robust investment strategy and asset selection.

“I wouldn’t want to say one is more important than the other, but if you have a stack of cards and you pull one out, the rest of the tower

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falls down,” Tewari says. “So each one is really important, especially in a region like Asia. It’s very important to have the right asset, it’s very important to have that asset located in the right location, and it’s also very important to have the right partner that you want to work with.”

And when it comes to location and assets, both Theseira and Tewari agree there are plenty to choose from in Asia, depending on the investor’s risk appetite.

On a short-term basis, Theseira says the next six to 12 months will generate good buying opportunities in China, thanks to the recent equity market volatility and government attempts to cool down property markets—particularly when set against the country’s long-term growth story.

“We see a lot of supply issues in various cities, including in the second- and third-tier cities that have caused a lot of headwinds in the market,” Theseira explains.

Theseira also sees retail as one of the most attractive food groups across Asia today, fueled by strong consumption and demographic trends. “With the suburban malls, you find these assets are very resilient, because they are based on necessity shopping, targeted local consumers, and they’re able to ride through different economic cycles, owing to the nature of the consumer and the product [the malls] cater to,” he says.

Australia is on the radar of both

Theseira and Tewari, with the Townsend principal saying people often lose sight of the country’s high population growth. “If you look back, Australian real estate has outperformed most of the other regions, and there’s no reason to believe that a lot of that wouldn’t continue in the future.”

But even countries with slower population growth, such as Japan, offer opportunities for investors.

“Even in these developed parts of Asia, there are real estate sectors that are emerging,” Tewari notes. “We’re doing a lot of work in senior housing in Japan. We’re looking at student housing in Australia. We’ve made a recent investment in self-storage in Singapore. So even within developed Asia, there are emerging [property sectors] that provide outsized returns to investors.”

A build-to-core strategy is another part of the equation in developed countries, with Tewari saying that while Townsend currently doesn’t like core income properties, “we like to build to core in these [developed] markets... Because core is in such short supply in these markets, you have a very healthy demand for core assets, primarily from local investors.”

Theseira echoes Tewari’s comments: “The reason for going to development is all about the long-term opportunity in Asia and the growth of core real estate... And over time, we do see a lot of potential in the region’s markets, thanks to their long term growth.” ■

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