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Asian Investors Make the Move Into Europe

Vistra's Caroline Baker and Michael Sheahan examine why Asian investors are increasingly targeting European real estate markets, the countries and property types they are focusing on, and the drivers behind this significant shift towards the west.

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What is the current state of play for Asian investors looking at Europe? Are they targeting particular types of assets?

Michael Sheahan. Right now, there is a real focus on logistics for Asian investors – although that's also true of real estate investors generally. Logistics is the hot area that has been growing significantly and being chased quite aggressively, and this is probably reflective of the shift in the way people shop. Second to logistics would be office space, which remains attractive.

In alternative real estate, there's definite interest in student housing and co-working space – these are getting more attention from investors generally and Asian investors in particular.

Caroline Baker: I'd second everything that Mike has highlighted. From our position in Singapore, we're definitely seeing logistics as a preferred type of asset. What's more, the global logistics market is set to expand, so properties in this sector are something that Asian investors are likely to remain very interested in.

Alongside that, commercial property remains a core element of their investment programmes, and we have also seen movement in student accommodation. Indeed, we currently have one fund that is completely focused on student accommodation. While it's certainly nowhere near the majority, it's an increasing percentage of what we are looking at.

On the flipside, have any asset types fallen out of favour recently?

MS. Retail is an area that is getting less focus than it has historically, and it's interesting to note this is happening at the same time there is increased interest in logistics. One particular trend we're seeing in that space is more diversification of asset use – for example adding or increasing residential components to complement large retail developments. We think that's a trend that will gain more momentum.

Are any European countries of particular interest to Asian investors?

CB. It does depend on the type of fund – be they core or opportunistic. The opportunistic funds are tending to look more at developing Europe. In places like Central and Eastern Europe [CEE], Warsaw is a very big investment destination. Meanwhile, some of the more established funds are looking at 'second-tier' cities, such as Amsterdam, Madrid, Helsinki, Lisbon and so on.

A lot of this boils down to what investment appetites are like and where there are deals to be had. We have seen a number of deals go into the UK property market, but they tend to be smaller deals than they were previously. I would say that core investments have shifted out of the UK, predominantly to Germany and Paris.

MS. Like Caroline, we still see capital going into the UK, but there is some wariness as a result of Brexit and currency fluctuations between sterling and the euro. I'd agree that there is plenty of activity in Continental Europe, while there is also a lot of confidence and activity specifically in CEE.

What are the drivers behind Asian investors looking at Europe?

MS. There are a variety of factors, such as currency trends and availability of stock. Take Korea, for instance – the Won trend has been encouraging Korean investors to look abroad right now. This is combined with market maturation in the region, so they are looking further abroad than they have done historically – away from Asian stock into European stock.

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CB. Valuations in Asia are higher than they have been in the past 10 years. There is a lot of investment focused on Asia coming from investors coming outside of the region, so that is driving up valuations in some of the core markets. And competition is getting higher, so even to get into some of these deals is more difficult – you need to have readily available cash because there can be a bidding war for some of these assets.

MS. When it comes to stock, availability in Asia varies across the region. Take markets like Australia where Asian managers might have looked to in the past – they are very mature markets – pricing is comparatively high as yields are low. So perhaps it's not surprising that we are seeing more activity in locations like the CEE, where yields are potentially more attractive.

CB. Another consideration is that Asian asset managers are becoming more sophisticated and are looking globally. So, because they aren't able to get deals locally, they're looking to diversify their holdings and are willing to take a step into Europe where they may not have been previously. It's also worth noting the increasing pool of capital that is coming from funds in Asia, which needs to go somewhere.

So exactly who are these investors and are they coming from particular countries?

CB. From my experience, the number one investor into Europe is Singapore, while South Korea and Hong Kong also have a significant presence. I understand that Singapore outweighs China in terms of capital, which is outstanding when you compare the size of the two. But those are the main ones that we see – and then, from a broader Asia-Pacific perspective, Australia has a lot of pension money invested in Europe.

On the subject of China, that is definitely one to watch. It has historically been difficult to get money out of China, but that is changing, so I do expect to see Chinese capital growing in Europe, albeit slowly to begin with.

MS. We're certainly seeing a lot of activity in Europe from Korean investors. We actually hosted a delegation from the Korean Financial Investment Association in our Amsterdam office in September. And as Caroline pointed out, although they have historically been quite active, we have seen increased activity coming through from Australian managers in the last couple of years.

As for the way investors access real estate, we're seeing

more direct investment activity – institutional investors are increasingly acquiring assets directly with European managers sourcing specific types of assets on their behalf. That's certainly one trend we're seeing.

CB. I would say that around 95% of Asian investors are from a typical investment base – pensions funds and so on – but there have been a few interesting areas of note. For instance, we have seen an increase in family money looking at doing smaller opportunistic deals – we have one fund that is family money with a mandate to invest in the UK.

MS. It's also worth noting how Asian-based managers are maturing as well – take a Singapore-based business such as Mapletree, for instance. Whereas multi-jurisdictional fund managers have tended to predominantly be based in the US or Europe, we now see larger managers emerging from Asia.

Can you put a figure on the increase of Asian investors getting into Europe recently?

CB. Anecdotally we know that more work is being done. We are doing more business with Asian investors in Europe and have a number of European-focused RE funds. In the past, most of the activity was intra-Asian investment, with only a small percentage of our funds portfolio going to Europe, but that is changing.

If you look at the statistics from Colliers International, Asian investment in the CEE accounted for around 9% of the total for the region in 2018, compared with a practically negligible amount only as recently as 2015.

What about headwinds? Is there anything that is likely to put a brake on Asian investment into Europe?

MS. It's very easy to focus on Brexit right now [at the time of writing, the 31 October deadline was approaching]. But the reality is that we are looking at it from a commercial point of view as we would with any jurisdiction that has regulatory change taking place.

Admittedly, in terms of capital flows, I think there is less investment going into the UK as a consequence of Brexit – not just from Asian investors – but there is still activity going on. It all comes down to how appealing the UK is as an investment jurisdiction, and where you have a currency that has been deteriorating, it becomes less attractive.

of investment in the CEE in 2018 came from Asia

Where there may be a shift is in where managers choose to structure their holdings or the jurisdictions they invest into. So, we see Luxembourg as benefiting significantly from Brexit, for instance. But that really has more of an impact on how investors access UK assets and structure their holdings. In terms of holding structures or the way Asian investors access those UK assets, I don't think that will necessarily differ from investors from other regions.

CB. The reality is that things are constantly shifting – regulation changes and currencies fluctuate, it's part of everyday life in global real estate. It's just that Brexit is something of an extreme, uncertain and complex example.

Right now, the Korean Won is in a strong position and the euro has been quite stable, so Continental Europe and CEE at the very least remain attractive for Asian investors. The key, as always, is understanding the local market, not going in blind, and making sure you work with local partners.

You mentioned earlier how investment into Asia had affected valuations in the region – is there a danger that all this Asian money coming into Europe might do the same?

MS. It certainly can't be ruled out. People talk about yield compression, and that has been going on since the global financial crisis and the implementation of quantitative easing. This, combined with constantly increasing pools of cash that need to be placed by institutional investors, means that real estate has become much more a mainstream asset class.

So, with Asian money coming into Europe, we're seeing large amounts of capital being raised, and that just increases the pressure on yield – hence them moving into what were secondary markets like CEE, hunting for yield. But exactly the same issues come up – with a finite amount of stock, more and more investors are chasing assets, which drives down yield.

You also touched on Asian investors shifting away from the US – is that a trend you expect to continue?

CB. To be honest, I think the shift is something of a blip. The US is one of the world's biggest economies and that is likely to remain the case for quite some time, so I do think there is a lot of potential there.

It comes down to the nature of the funds again. In terms of finding opportunistic investment, it's understandable there has been a shift to Europe, especially some of the more developing countries. But when you consider core funds, I think that people will shift back to the US eventually. It's just that there is a measure of political uncertainty right now, not least with China.

Finally, how do you anticipate Asian investment in Europe to play out in the next 24 months?

MS. I don't think there are likely to be any significant changes, and anticipate continued interest from Korea, Australia and Singapore managers in particular. In terms of markets, I think the UK clearly carries risk and may be a less interesting market for a time depending on the outcome of Brexit.

As for Continental Europe, most notably the CEE, I certainly think there will be continued interest there.

CB. I agree with Mike in that Europe is going to remain an attractive proposition, particularly some of the smaller European countries. I think core commercial is still a very important component, particularly for pensions funds who are generally risk averse. However, we also have a number of real estate funds that are seven-year closed-ended that are looking at opportunities as they have to get in and get out. So, it really depends on the type of investor you are and the investment strategy you want to implement.

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Despite having noted that there has been a move away from Asia, I think that Asian investors are going to start looking inwards again. I think there will be a shift to look at some of the more developing Asian countries – we are seeing Vietnam, Cambodia, Myanmar and the Philippines becoming interesting for some real estate investors.

With a growing middle class here in Asia, and a constantly changing global real estate market, how and where Asian investors place their money is going to remain an interesting sector to watch.