

## PGIM Real Estate

# Investing in Asia Pacific



**Benett Theseira** is a managing director at PGIM Real Estate and head of Asia Pacific. Based in Singapore, Theseira is responsible for the development and implementation of the strategy and oversight of PGIM Real Estate's businesses in Asia Pacific.

Recently, **Jonathan A. Schein**, senior vice president, managing director of global business development at Institutional Real Estate, Inc spoke with **Benett Theseira** of PGIM Real Estate. The following is an excerpt of that conversation.

*Can you give us a quick overview of PGIM Real Estate's Asian platform?*

PGIM Real Estate has around \$67 billion of assets under management globally. Of that total, around \$5.8 billion is in the Asia Pacific region. We have been investing in the commercial real estate markets in Asia Pacific since 1994, and today we have more than 70 professionals in five locations across Asia Pacific. Over the years, we have invested in markets across the region, including Singapore, Japan, Australia, China, Southeast Asia, India and South Korea.

*What has PGIM achieved in those more-than-20 years?*

Because we've been in Asia for more than two decades, we've experienced a lot of the cyclical ups and downs, and we've learned a lot over that time. We were a pioneer in terms of fiduciary standards and global investment management practices in Asia, and with the depth of our investment experience in the region, that gives us a very strong platform. We were also one of the first global investment managers to focus on investing in core real estate in Asia, from over a decade ago at a time when others were focused on opportunistic investments.

With core investing being a part of our DNA globally, we believe we are well-positioned to manage these types of

strategies in Asia. Our experience in Asia has shown that the stable cash flows and more reliable returns we have been able to generate historically for our partners and investors through market cycles are a testament to our strategy to minimize the risk we take with our investments. This approach certainly paid dividends for us during the financial crisis.

*How do you work with Asian clients that want to invest in the US or Europe?*

Because we are an integrated, global firm, we can provide investment opportunities around the world for our Asian clients. We have a consistent process and strategy across our regional platforms, which make it efficient for investors in one region to access investments in another. In recent years, we have seen capital flowing across borders, and particularly from Asia into our US and European real estate equity and debt strategies. We have also been able to support some separate account mandates. We believe this trend will continue as institutional investment capital sources grow in Asia and investors seek attractive and diversified investment opportunities outside their domestic markets.

*What are your views on the current market environment in the region?*

Certainly, there is an element of slowing growth in Asia, but it is important to keep in mind that these are very large economies. The Chinese GDP, for example, is over \$10 trillion now. So, a 4 percent to 5 percent growth on that base is still double-digit growth when compared in absolute terms to the growth of six or seven years ago. Therefore, we still maintain a fairly positive long-term view on China. There have been some growing pains as it transitions to a service economy, more reliant on local consumption and less on exports, but overall we see the consumption trends growing quite strongly. We also see the development of local companies and businesses, both as domestic leaders and international players. Wage growth has been very strong; urbanisation patterns continue to be

pretty robust. Certainly, there is a delicate balance of managing this transition, which is not easy for such a large economy, but we feel comfortable that the Chinese leaders are aware of the issues, and the actions being taken will help build a resilient Chinese economy in the future.

*Where are the some of the opportunities outside of China?*

Different cities and different sectors within cities across Asia Pacific are at different points of the cycle from a rental growth or valuation movements perspective, which offers a pretty diverse basket of opportunities. The markets where we currently see the best rental growth are in Australia and Japan. Japan has started to experience many more capital inflows into real estate, both domestically and internationally, as well as rental demand and growth, following the significant stimulus measures introduced by the Abe government. After many years of deflation and stagnant growth, this recovery is creating a sense of optimism that things are finally turning in Japan. We've seen significant growth in tourism, with the number of visitors growing from 8 million four years ago to 20 million last year, with expectations that this number will exceed 30 million in the next few years.

*What about opportunities in Australia?*

After the shift in focus from the commodities cycle, the financial services sectors are recovering in Sydney and Melbourne, which has resulted in improving tenant sentiment and lease-up rates, as well as effective rental growth. In addition, population growth — primarily from immigration — is driving demand for residential and retail. That said, we find the residential sector a little overheated currently and with the banks tightening up on lending to foreign buyers and developers, as well as new regulations introduced to cool the market, there could be some correction in prices.

*You mentioned that core is part of your DNA, but what is your approach in the value-add space?*

We also have a lot of experience investing in value-add strategies, having executed numerous office and retail repositioning initiatives, as well as participated in retail, office and residential developments. But even in such instances, we look to minimise risk with these investments by not overleveraging or taking too much locational risk. In some cases, we've also used mezzanine financing to fund developments to offer a better risk-adjusted return, for example, with recent residential projects in Sydney. Local banks are increasingly reluctant to fund development, and that has caused a funding gap for some developers. We have avoided taking on the construction risk or the full risk of the sales outcome, but are still able to achieve good returns, benefiting from the strong demand for housing in the area. We've also recently invested in residential development with a local partner in Malaysia. We have been investing there for many years, so we know the market well. Malaysia has very interesting demographics, with more than half of the population below the age of 40 and, as a result, we are seeing very strong household formation and long-term support for the mid-tier residential sector. The market certainly has its challenges, but that has simply resulted in less capital chasing deals, so we are able to execute our strategies on a very attractive basis.

#### *What other strategies are you pursuing?*

Our strong network of on-the-ground professionals and partners enables us to opportunistically acquire properties at below market rate. For example, we have seen certain periods of volatility in China, which have resulted in mispriced opportunities. During recent times, we have acquired office assets at very attractive pricing by taking a calculated risk that the volatility will ease after a short period of instability — and so far, this strategy has worked in our favour. Our view is that China will be a very good market long-term, so it is to our benefit to pursue attractive opportunities today, if we find the right asset at the right price.

#### *Are there sectors or countries you are avoiding?*

Because sectors and countries are in different parts of the cycle, this makes some sectors more attractive than others. In Singapore, for example, we are seeing a weakening in rents in the

office sector because of excess supply and slower growth. We are also seeing a weakening in the retail sector because restrictions on foreign workers have made it difficult for retailers to hire and have driven up the cost of labour. It has made it hard for them to expand and, in some cases, caused consolidation because they can't get enough manpower. We are able to navigate through that, however, because of the experience and expertise that we have in the sector, coupled with our critical mass of being one of the largest retail property owner-operators in Singapore. We have also seen weakening in the broader industrial sector due to both foreign-worker restrictions and the ongoing economic restructuring. But long term, we continue to see a positive outlook for the logistics sector, mainly because Singapore has placed a lot of focus on establishing itself as a leading regional logistics centre and has been ranked as the number one logistics hub in Asia. As always, real estate is all about location, and Singapore is well located.

#### *What makes PGIM Real Estate different from its competitors?*

PGIM Real Estate's value proposition stems from the longevity of the experience that we have in the region. Our strength comes from our knowledge of the local markets, an understanding of their nuances, and our ability to access and execute different types of transactions. Asia is not an easy market to execute in, and understanding those nuances means that we can avoid some of the mistakes that may be made by others without that local knowledge. Our ability to develop relationships locally is key in getting better access to transactions, particularly off-market, as well as access to good partners that

help us execute even better. As a firm, we have very effective governance and risk overlay to ensure best practices and global standards. Our regional businesses, whether in the Americas, Europe or Asia Pacific, have their own regional investment committees, largely staffed by senior executives within the region, which I feel makes for better-quality decision making by senior team members with a more granular understanding of the region. At the same time, our global chief investment risk officer sits on each committee and, together with his team of regional underwriters, helps to ensure that the regional teams follow prescribed investment processes and procedures, and that there's adequate consultation with all key constituents. The combination of local knowledge and international best practices that we have as a firm comes together to really enhance our ability to select, decide on deals and, ultimately, execute on them.

#### *Finally, what would you say to investors who are looking at Asia?*

Asia's GDP is already a very significant part of global GDP, and in the next 15 to 20 years, its share is expected to grow to at least half of the global GDP. In terms of the real estate universe, it's going to grow to 40 percent of the investable stock globally. So, investors should seize the opportunity to look at Asia for both diversification and growth. On the capital front, we think Asia has great potential for raising capital because we are seeing growth in wealth funds, insurance companies and superannuation funds. The various cities are also improving significantly in liquidity and transparency. In the decade to come, Asia will be a significant source of capital for global investment, as well as a large source of opportunity for global investors.

## CORPORATE OVERVIEW

PGIM Real Estate is the real estate investment business of PGIM, Inc, the global investment management businesses of Prudential Financial, Inc (NYSE: PRU). Redefining the real estate investing landscape since 1970, PGIM Real Estate has professionals in 18 cities in the Americas, Europe and Asia Pacific with deep local knowledge and expertise, and gross assets under management of \$66.9 billion (\$48.4 billion net) as at September 30, 2016. PGIM Real Estate's tenured team offers to

its global client base a broad range of real estate investment vehicles that span the risk-return spectrum across core, core-plus, value-add, debt, securities and specialised investment strategies.

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