Thought Leadership Series: Commentary

Asia Pacific REITs Prepare to Take Centre Stage

The Asian Pacific REIT market is entering a phase of rapid growth and development, creating opportunities for investors who seek stable, income-producing securities with a strong performance record.

Real Estate Investment Trusts (REITs) are one of the fastest growing asset classes in Asia Pacific, offering investors a stable and proven investment diversification tool that benefits from Asia's urbanisation story. The regional market is still in its early stages of growth, but government initiatives and increasing demand from institutional and retail investors indicate that development will accelerate in the near future.

The global real estate market has enjoyed a multi-year boom, and REITs are the easiest and safest way for investors to gain exposure. REITs are listed securities that invest in a diversified pool of professionally managed real estate assets with the goal of generating income for unit holders of the fund.

These portfolios of properties provide investors with a diversified and steady income stream through regular dividend distribution. In recent years they have produced strong long-term value appreciation. Asia has more rapidly growing metropolises and newly emerging cities than any other region of the world, creating a natural opportunity for REITs.

Asia Pacific offers market potential

Australia is the largest, most developed REIT market in the region with 47 listings, but Singapore, with 43 REITs and property business trusts, is viewed as the key hub in Asia ex-Japan. Japan, which has recently seen a spike in interest from retail investors, has 35 REITs, while Hong Kong still has plenty of room to grow from its base of 10 REITs.


India and China, the two biggest economies in the Asia Pacific region

The region's two biggest economies, China and India, are laying the groundwork for REIT markets that could potentially become world leaders. Shanghai and Beijing are establishing themselves among the world's top 10 urban economies in terms of scale, status and commercial attraction, and Indian cities such as Bangalore, New Delhi and Mumbai are also garnering attention from investors. India's top seven cities together have more than 400 million square feet of operational office space, and this is expected to grow by approximately 25 million to 30 million square feet annually.

The Securities and Exchange Board of India (SEBI) allowed for the creation of REITs and infrastructure investment trusts (InvITs) in 2014 but the market has yet to gain momentum due to impediments such as state government stamp duties and capital gains tax. In 2016, the government approved the tax pass-through status for dividend income for REIT investors and also allowed mutual funds to invest in REITs and investment trusts, which has advanced the market's development.

China has encouraged the development of various market prototypes — often referred to as quasi-REITs — to test different securitisation formats. These prototypes have generally taken the form of structured financings or asset-backed securities, rather than equity instruments. Further development and a more robust framework is needed to attract institutional and foreign investment funds.

A number of other Asian countries, including Malaysia, Vietnam, Sri Lanka and the Philippines, are also in the process of introducing REIT regimes or upgrading existing schemes to boost market activity. We should expect to see more well-developed and sophisticated REIT markets in the region in the next five to 10 years.

Diversity is just one of many benefits

In the current low-yield global environment, REITs offer a sensible alternative for investors seeking competitive long-term performance. The dividend yields of REITs have historically proven steady despite a variety of market conditions. Investors also benefit from growth in asset valuations, with global REITs matching returns on US stocks over the last 11 years as a result.

With interest rates likely to rise soon, REITs offer a hedge against this risk: Higher interest rates usually coincide with better economic performance, which results in greater business confidence and higher property rental rates.

One of real estate's strongest features as an investment class is its diversification, as it typically has a low correlation with other stocks and bonds. Many investors have diversified into real estate by buying individual properties, but investing in an international portfolio helps limit the impact of property downturns in a specific country or region, while still exploiting opportunities in better-performing markets.

The Asian REIT market has the potential to create access to a diverse array of assets such as retail malls, office buildings, industrial properties, hospitals, serviced apartments and resorts. There is also talk of packaging student housing as REITs. In Singapore, where the REIT market is heavily reliant on foreign assets and REITs are increasingly priced in foreign currencies, there are moves towards making distributions exempt from tax provided that at least 90 percent of the taxable income is distributed.

The growth of Asia's REIT industry also benefits society by evolving and developing the real estate industry and improving assets which serve the needs of Asia's growing middle class. Asia's cities, particularly those in China and India, are undergoing remarkable growth and capital injections from international investors will help them build higher quality, more efficient infrastructure for their citizens. Other benefits include a professionally managed portfolio of assets, and a more liquid and accessible form of real estate investment compared to physical assets.

Fertile ground for REITs

We expect the variety of Asian REITs to grow, offering even greater diversification opportunities. As regional REIT structures are strengthened and developed, market participants will bring an ever widening range of properties to market.

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The Singapore market is particularly poised for growth due to its attractive tax regime and market-oriented regulations that promote the growth of REITs. Singapore is sure to attract a greater diversity of foreign assets and REITs priced in a greater variety of currencies. An early example of this is the recent Cromwell European REIT listing in Singapore. Hong Kong also stands to attract more foreign assets in the future.

Asian REITs will remain an attractive asset class over the near term due to the diversification they offer and their high level of liquidity. They can deliver returns in both low and rising interest rate environments. As professionally managed investments with conservative gearing limits and other governance requirements, they are also relatively safe investments, making them an ideal vehicle for investors who want to access the Asian urbanisation and growth story.