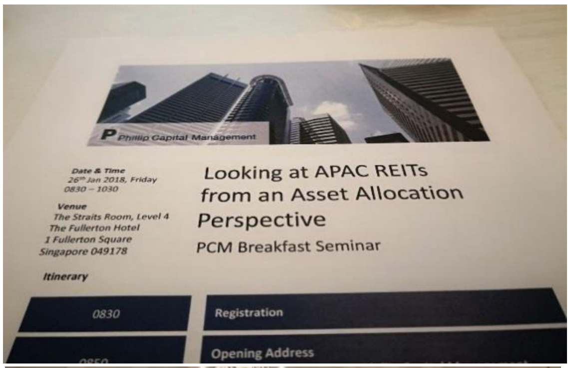
## Phillip Capital Management Seminar

# Looking at APAC REITs from an Asset Allocation Perspective

"Asia Pacific REITs should be considered as part of the strategic allocation, given their long-term diversification and return characteristics. Tactically, they also possess price momentum and still-attractive valuation", was the final words from Teck Leng Tan, Sr. Fund Manager at Phillip Capital Management while speaking in a seminar focusing on Asia Pacific REITs from an Asset Allocation Perspective. In this article, we will summarise the presentation and the discussion that followed.




The Smart money is investing in the Real estate – Big public money (Sovereign Wealth Funds, Pension Funds) and big private money (High Net Worth individuals). Large Sovereign Wealth funds such as GIC allocate 10% of their portfolio to real estate and Norway pension fund allocated 3% of their total portfolio to real estate. The interest in real estate has grown not just on the institutional front but also from that of a wealth management perspective. Wealth managers have been guiding HNWI's towards an asset allocation model that now incorporates REITs alongside stocks and bonds. In the Capgemini Wealth report 2017, global HNWI had close to 15% of their investment portfolio in real estate.

Sovereign wealth funds invest in physical real estate more because their size allows them to buy big-ticket property. They can also add value to the property and control the destiny unlike if they buy listed real estate. However, ultimately, money flowing into physical real estate will support valuations and benefit REITs indirectly. Also, some sovereign wealth funds are also some of the biggest holders of REITs (e.g. Norway Oil Fund is a big shareholder of Ascendas REIT, Mapletree Commercial, Mapletree Logistics).

The trend was mostly prompted by diversification away from traditional asset classes, inflation hedge and tangibility of the asset class, which is important to high net worth investors.

Studies (Ibbotson in the US, PCM's own S-REIT study) show adding RE to a portfolio mix does result in enhanced returns. In PCM study modelled three types of the portfolio over ten years. Portfolio A was a traditional asset allocation model, 60% Singapore equity, 40% Singapore bonds. Portfolio B and C introduces S-REITs into the mix; 10% REITs, 20% REITs respectively. Though REITs had equity-like volatility over this period, adding them enhanced portfolio return significantly.

Asia-Pacific REITs did well last few years, but looking at valuation metrics (yield spread, price-book) versus their respective historical trends for Australia and Singapore, it still looks attractive still (eg. SG: 1.1X P/B vs year 2007's 1.6X; AU: 1.1X P/B and yield spread of >2% vs year 2007's 1.6X and <0% respectively).

Hence, asset-allocation wise Asia-Pacific REITs should be considered as part of a strategic allocation given their long-term diversification and return characteristics. Tactical-allocation wise, they also possess price momentum and still-attractive valuation.

In the panel discussion that followed, David Mok, Head of Research and Investment at IPP, corroborated Teck Leng's points by mentioning his experience of deploying and benefitting from REITs in their portfolios. He emphasises that long-term view is necessary when investing in REITs. As a wealth manager – deploying REITs into a portfolio from a long-term perspective has delivered. But as a wealth manager, there is also a need to switch for client portfolio returns tactically. There is a necessity to have a long-term view if one wishes to allocate to REITs strategically.

Adam Grabow, VP, Institutional Business Development of Morningstar Asia, elaborated how index creators use the concept of moats to define a quality REIT. He also quelled investors' concern regarding the REIT ETF's liquidity being somewhat unfounded since the liquidity is determined by the underlying holdings' liquidity as well as market makers ensure ample liquidity.

The audience participated through questions to the panellists. Snapshots below

1. REITs have had a very good run – outperforming equities almost everywhere except the USA. So the next question is have they run up too much – from a price to book basis; REITs is close to its historical mean so yes the yields have gone down, but from a fundamental value basis is still keeping close to its long-term valuation.
2. REITs have grown in acceptance globally are seen as an alternative to traditional asset classes in some pension funds (pension funds have been allocating to physical Real Estate), but not all funds have the necessary scale for that.
3. Real Estate allocation among the large sovereign wealth funds is about 10-13 %. Norway fund has 3% of portfolio in Real Estate
4. Wealth managers do see the yield component as an important benefit of using REITs especially in a low rates environment but do emphasise a need for a long-term investment horizon as REITs have higher volatility vs Bonds.

*The seminar was organised as part of Phillip Capital Management's ongoing initiatives to educate, inform and collaborate with our clients and partners. The event took place on 26 January 2018 at the Fullerton Hotel, Singapore.*

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