Asia-Pacific Reits offer sweet spot for investors

An office building in Tokyo. Vacancy rates of office space in the Japanese capital are at multi-year lows, according to the writer. As a result of the strong market demand, landlords are able to command higher rents, driving up returns for Reits, which are trading on an attractive yield spread against Japanese interest rates, she says.PHOTO: REUTERS

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UOB highlights stable income generated by this asset class, especially in times of volatility

Wang Hoi Min

The US Federal Reserve recently cut its interest rate for the first time in over a decade. This was to keep the economy expanding against the backdrop of weak global growth and rising trade protectionism.

With central banks in other countries expected to follow suit in cutting rates, the shift in monetary policies may lead to greater market volatility. In view of this, it is timely for investors to review the effectiveness of their investment portfolios in generating returns.

Real estate investment trusts (Reits) can be a sweet spot for retail investors, offering ease of access to those interested in pursuing real estate investments in times of uncertainty and low yields.

Reits are collective investment schemes that pool investors' money to invest in a diversified portfolio of income-generating, professionally managed real estate assets such as shopping malls, offices, hotels and serviced apartments.

The rental revenue or income from these assets is distributed at regular intervals to investors in the form of dividends. With regular dividend payouts, Reits provide a stable, recurring income for investors. Further, as Reits grow their rental income, they can pay higher dividends over time.

BENEFITS OF INVESTING IN REITS

Through Reits, investors without prior knowledge of property management can buy into the asset class. They do not have to face the deterrence posed by high investment amounts required to buy real estate and can also benefit from the liquidity offered by Reits that are publicly traded on stock exchanges.

Other benefits of investing in Reits include:

• Portfolio diversification: Reits have low correlation to stocks and bonds.

• Inflation hedge: Inflation typically leads to higher rents, which is good for Reits.

• Steady income: Reits pass the majority of their income on to investors as dividends.

• Growth potential: Both income and asset value of a Reit can grow on the back of rising rents, asset enhancement and inorganic acquisitions.

In addition, based on current market data, Reits listed in the Asia-Pacific region generally offer higher returns and have been less volatile compared with other asset classes.

OUTPERFORMER AMID GLOBAL TRADE TENSIONS

Investors look for investment vehicles that offer stable income, even more so in times of economic uncertainty. The recent jitters over trade tensions between the United States and China have in part prompted investors to move into Reits for the regular dividends and relatively stable income.

Reits' characteristic of shielding investors from market volatility is also seen in the strong performance of the benchmark indexes at the height of the US-China trade row in May. The MSCI Asia Pacific rose 2 per cent while the S&P Asia Pacific Reits Index gained 3.5 per cent.

INVESTMENT OPPORTUNITIES IN ASIA-PACIFIC REITS

With the world's major central banks, including the US Fed, Bank of Japan and Reserve Bank of Australia, adopting an accommodative monetary stance, global interest rates are expected to stay low.

Historically, Reits have delivered good returns in a low interest rate environment. When interest rates are lower, the yield spread (difference between Reits' and government bond yields) rises and is paid out to investors as dividends.

Also, the fast-growing Asia-Pacific economies are demanding a larger array of services that operate out of properties managed by Reits. This has, in turn, given rise to the set-up of a wider range of Reits that manage commercial, retail, healthcare and telecommunications infrastructure assets.

In Australia, the rental outlook in the office and logistics markets in key cities remains positive due to a tight supply. And the rising demand for e-commerce and supply chain outsourcing is translating into a strong take-up for logistics space, benefiting Reits in this sub-sector.

In Japan, the vacancy rates of Tokyo office space are at multi-year lows. As a result of the strong market demand, landlords are able to command higher rents, driving up returns for Reits, which are trading on an attractive yield spread against Japanese interest rates.

For Singapore, easing supply pressure should support a cyclical upturn across the different property sub-sectors, such as offices, retail and business parks. Positive rental reversion will drive the growth in distribution per unit. Singapore Reits are also trading with attractive absolute yields.

In Hong Kong, despite the continued moderation in overall retail sales, the retail sales of non-discretionary items should remain stable across the business cycle, providing support for returns of retail Reits.

To help investors seek better returns from Reit investments, UOB Asset Management focuses on Asia-Pacific Reits that can achieve above-average growth from rental increases, as well as those active in asset acquisitions, asset enhancement or capital recycling.

Favourable supply-demand dynamics support the rental markets in the region's major cities, while there is strong investment demand in the commercial property market. These factors will help lift the net asset value of Reits in this region.

• **The writer is vice-president, Asia equities, at UOB Asset Management.**