REAL ESTATE

Eye on future trends

Niche markets and deregulation are creating new property investment opportunities

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A NEW post-Global Financial Crisis (GFC) real estate investment market landscape continues to emerge. The environment is characterised by growing cross-border money flows, a push to diversify portfolios, and a willingness to think laterally by looking beyond the traditional sectors. As more investors search the globe for new opportunities, here are four trends which we believe will influence global activity in 2016.

Specialist property

Specialist property continues to evolve as a segment, led by fixed income sectors such as healthcare and retirement accommodation. It also encompasses automotive hotels, student accommodation and even private rented-sector residential accommodation. The key reasons for the growth in demand for specialist property relate to changing market requirements. For example, 20 years ago the demand for purpose-built facilities for the elderly or students was relatively limited. However, strong growth in the ageing population and expansion in student numbers – combined with generally poor-quality existing provision – have stimulated occupier demand.

Another major reason for increased investor interest in specialist property has been the drive for diversification, particularly following the GFC. While sentiment in global real estate markets has improved markedly, some parts of the traditional market have been challenging until recently. The less cyclical nature of specialist property is also appealing to investors.

In recent years, we have seen institutional buyers in Asia acquiring student accommodation. In May this year, Far East Orchard expanded into Europe to develop student housing. A couple of years ago, China's Gingko Tree Investment Ltd bought a 40 per cent stake in UPP Group Holdings Ltd, a major provider of university accommodation in the UK, from Barclays Capital Inc.

Knight Frank's Student Property Department, on behalf of The International Mutual Fund, was also recently marketing the Ardent Portfolio – a collection of 25 student accommodation properties located across 12 University cities in the UK.

As demand and competition for investment product have risen, yields across the traditional sectors have been squeezed. As a result, investors have sought alternative ways of protecting and enhancing their wealth. Assets such as petrol stations, service areas, data centres and waste management facilities are now playing an increasing role in property investment portfolios.

Deregulation

Government regulation exerts a major influence on global capital flows and can help to make or break real estate investment markets. Changes to regulation – such as the removal of ownership restrictions or legislation to allow new investment vehicles – can also help to attract significant amounts of inbound capital, an example being India's new Real Estate Investment Trust (Reit) legislation in 2014. The Indian Reit sector could be worth as much as US$100 billion within a few years. India has also recently relaxed its rules on foreign investment in real estate.

Significant recent changes include the decisions to allow Chinese and Taiwanese insurance companies to invest in international real estate in 2012 and 2013 respectively. Chinese insurers have since made inroads into major international real estate markets and, on paper, have a potential US$220 billion to invest in overseas property and other assets. Taiwanese insurers meanwhile have initially focused on major cities in the US and Asia-Pacific (Shanghai and Tokyo), while London has been the core European destination to date.

In the US, one potential major change relates to the much discussed relaxation of the Foreign Investment in Real Property Tax Act of 1980 (FIRPTA). Currently, foreign investors account for just 17 per cent of the US commercial market – considerably lower than the UK and Europe (around 50 per cent and 60 per cent respectively). An easing of the FIRPTA regulations could lead to a doubling of investment in larger US cities such as New York and San Francisco.

In Asia-Pacific, perhaps the most significant recent news is the Trans-Pacific Partnership free trade agreement between the US and a number of Asia-Pacific countries including Singapore, which, if ratified, is expected to help boost cross-border property investment.

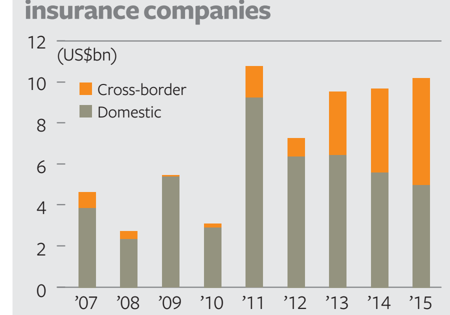
Elsewhere, the recently announced Qualified Domestic Individual Investor programme 2 (QDII2) in six Chinese cities (Shanghai, Tianjin, Chongqing, Wuhan, Shenzhen and Wenzhou), which will lift restrictions on the amount investors can spend overseas, could provide an additional boost to the continued flow of Chinese outbound capital. (see *Figure 1*)

ECO DRIVE
(Above) Marina One is an award-winning mixed-use development in the heart of Singapore's New Downtown, Marina Bay. It is set around a 'Green Heart' at its core and is flanked by two urban parks

PHOTOS: KNIGHT FRANK

ALL ABUZZ
(Left and above) London's King's Cross is being transformed into a new part of the city with homes, shops, offices, galleries, bars, restaurants, schools and even a university

Fig 1: **Acquisition volumes by Asian insurance companies**



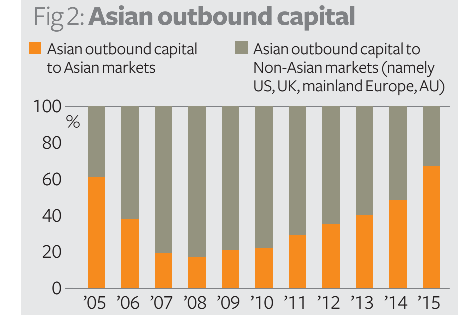
Source: Real Capital Analytics, Knight Frank Research

Mixed-use

The strong recent (and forecast) growth in city living has brought the focus back on how to best integrate the ways in which people live, work, shop and play. Mixed-use projects offer portfolio characteristics that allow investors to spread risk, as well as gain exposure to a fast growing trend that is set to continue for some time. However, investing in mixed-use requires an understanding of a variety of different uses and business sectors, how they interact with each other and, in particular, how to approach valuation for the different components.

Examples of mixed-use buildings and locations around the world range from Marina City in Chicago to the planned Super Tower in Bangkok, and Marina One in Singapore. Europe is also seeing its share of new mixed-use developments, notably Battersea Power Station and White City in London, Bercy Charenton in Paris, and Milanosesto in Milan.

Fig 2: **Asian outbound capital**



This is computed for cross-border transactions. Domestic investments are not included.

Source: Real Capital Analytics, Knight Frank Research

Outbound capital

Traditionally, US investors have dominated global cross-border investment. In fact, in the two years to June 2015, US investors invested more than US$100 billion in international retail, offices, logistics and hotel property.

Major drivers for the acceleration in overseas investment have been a combination of the strong dollar, competition in the domestic market and opportunities to find value – notably in Europe where the property market recovery has lagged.

In the last two years, over 80 per cent of US overseas investment has focused on Europe, with a very heavy bias towards London and Paris, as well as Tokyo. Interest from the US into China peaked in 2013, with the recent economic slowdown impacting buyer confidence.

A slowing domestic economy, measures to cool the housing market and the relaxation of regulations on overseas investments has also prompted many Chinese investors to seek opportunities abroad. As a result, Chinese outbound investment continues to grow, with a total of US$24 billion invested in overseas commercial property in the two and a half years to June. In July, sovereign wealth fund CIC notably bought a US$1.8 billion portfolio of office buildings in Australia, from Investa Property.

But it is not just China that is exporting capital from Asia. The last few years has seen a wave of outbound capital from Singapore, Malaysia, South Korea, China and India targeting real estate opportunities around the world. It is not only the growth in the flows of capital that has been significant, but also the destination. While in 2008, over 80 per cent of outbound capital from the region stayed in Asia, in 2015 this figure has dropped to just over 30 per cent, with the majority of the rest heading to the western markets of Australia, US, UK and Continental Europe. (see *Figure 2*)

With an increasing amount of institutional capital being allocated to real estate and limited amounts of investment grade stock in many domestic markets, we expect total global volumes of outbound capital to continue to grow in 2016. W