INSIGHTS

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In Conversation With Our Asian Property Securities Fund Manager

Pearly Yap
Fund Manager

The SICAV Asian Property Securities Fund ("the Fund") recently won the Edge Lipper Fund Awards Best Fund over 3 years, delivering strong risk-adjusted performance. What is behind your winning strategy?

Eastspring Investments use a bottom-up, valuation driven investment process to pick stocks across Asia Pacific ex Japan that we expect will outperform over the long term. Drawing on the strength of our experienced 18-person investment team, we make company visits to meet with company management and engage with policy makers to better understand economic conditions in both developed and developing markets.

Specifically, for property investing, behavioral biases seem to dominate investment decisions. We believe most property specialists tend to be backward looking and over-emphasize historical transaction asset values in their valuations of property companies. For example, a recent trend of capital and rental appreciation can reinforce perception that the company's fundamentals and future earnings will be improving. This very often causes share prices to move to extreme levels that may not necessarily be justified by company fundamentals.

In our view, we believe that asset prices should ultimately be supported by robust income generation. As such we will also look at the company's management quality and balance sheet and assess if the country's macroeconomic fundamentals are favorable.

Sources : Eastspring Investments (Singapore) Limited, Mar 2013

What are the attractions of investing in Asian REITs?

We believe that investing in REITs offers something for everyone.

Compared to physical property investing, REITs trade on a stock exchange and provide ample liquidity unlike a physical property where transaction can be highly illiquid and cashflow might be tied up for years. A REIT or property fund investor does not have to worry about the logistics of owning a physical asset, e.g. negotiating tenancy agreement. Also, a REIT is unitized (i.e. highly affordable an investor can buy a unit of REIT which typically does not cost much) and usually holds a portfolio of properties diversified across different sub-sectors, such as malls, offices, or apartments. On the other hand, an investor buying a house or apartment requires significantly larger upfront capital investment and, for most investors with ordinary income levels, is likely to be concentrated in a single property which means higher risk and volatility in potential return. Investors can also expect to receive regular dividends from REITs investment, akin to bonds. In recent years, monetary easing (i.e. increase in global money supply) has led to lower sovereign bond yields. Thus, the dividend yield offered by REITs should appeal more to income-focused investors as compared to bonds with lower yields, especially since interest rates are expected to remain low for the foreseeable future.

Finally, over the last 10 years, property outperformed the other major asset classes – equities and bonds – on a global basis. Given that property securities and other equity securities do not have the exact same up and down cycles, adding a property securities fund into an investor's portfolio can enhance diversification and risk-adjusted returns.

Asian REITs have delivered impressive returns over the past 5 years. What underpinned the strong performance?

High occupancy rates, strong rental reversion, and leasing renewals from growing business activities in the region have generally contributed to Asian REITs' performance in recent years. Many Asia Pacific markets have seen rising real estate values as abundant liquidity in the global financial system lifts property asset prices. These factors plus investors' preference for higher yielding stable securities have contributed to REITs' strong performance, generating returns for investors from both yield and asset value appreciation.

To what extent do property cycles affect REITs and how will the current property cooling measures imposed in some regional markets affect performance?

In general, property cycles result from a mismatch of demand and supply. Due to the influx of liquidity from developed markets, property prices, especially residential properties, have been escalating in recent years. Various governments in the region, notably China, Hong Kong and Singapore, introduced property tightening measures to curb property speculation and manage expectations of property prices in their markets. Property developers have

Sources : Eastspring Investments (Singapore) Limited, Mar 2013

been negatively affected from such measures and in response investors have been embracing REITs which offer exposure to appreciating asset values while delivering regular dividends and deemed as safe. Nevertheless, especially in Hong Kong, we believe that the underlying residential prices should remain robust despite the measures and that the developers' balance sheets are healthy enough to take advantage of the landbanking and asset turns.

Based on your outlook, how would you be positioning the portfolio in 2013?

Regionally, the Fund will continue to recycle out of expensive names, especially in Singapore and Hong Kong. The Fund may also build up positions in ASEAN property names where economic growth is more supportive, consumer debt is lower and there is more opportunity for sustained long-term growth.

In Australia, we view REITs favorably in terms of relative valuations and the favourable interest rate environment (i.e. interest rate expected to remain low). But REITs in Hong Kong and Singapore have gone up substantially. Therefore in Hong Kong we continue to like developers for the reasons mentioned in the previous question. In Singapore we will continue to be invested in resilient high-dividend names, but we are underweight residential property due to the downside risks in residential prices.

Over the long term, there are many structural factors that will underpin a wave of long-term structural growth in real estate markets in ASEAN, such as increasing urbanization, young working-age populations, and robust economic growth. ASEAN countries, such as Thailand, Indonesia, and the Philippines, currently represent a small fraction of the Asian property benchmark, but will be the main beneficiaries of these trends. We intend to invest in high quality names in ASEAN markets to participate in the coming wave of growth.

What are the unique features of your Fund?

- The Fund aims to achieve total return by having a good blend of REITs and non-REITs in the portfolio (most Asia ex Japan focused funds tend to be very weighted in non-REITs).
- The Fund aims to pay out regular and above market dividends (i.e. relative to the benchmark yield).
- Lastly, the Fund is a concentrated, best-ideas portfolio and benchmark-agnostic (we only invest in a company because we like it and not because it is in the benchmark).

Sources : Eastspring Investments (Singapore) Limited, Mar 2013

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