Asia-Pacific Real Estate Investment Trusts (AP-REITs) have become increasingly popular with investors, and deservedly so. AP-REITs can offer a unique, diversified opportunity set across real-estate segments: from established Grade-A office space located in the region's bustling cities to cutting-edge logistical facilities and the growing number of data centres that power cloud applications. This article is the first in a series of three that will provide a comprehensive introduction to this emerging asset class.

An introduction to Asia-Pacific REITs (AP-REITs)

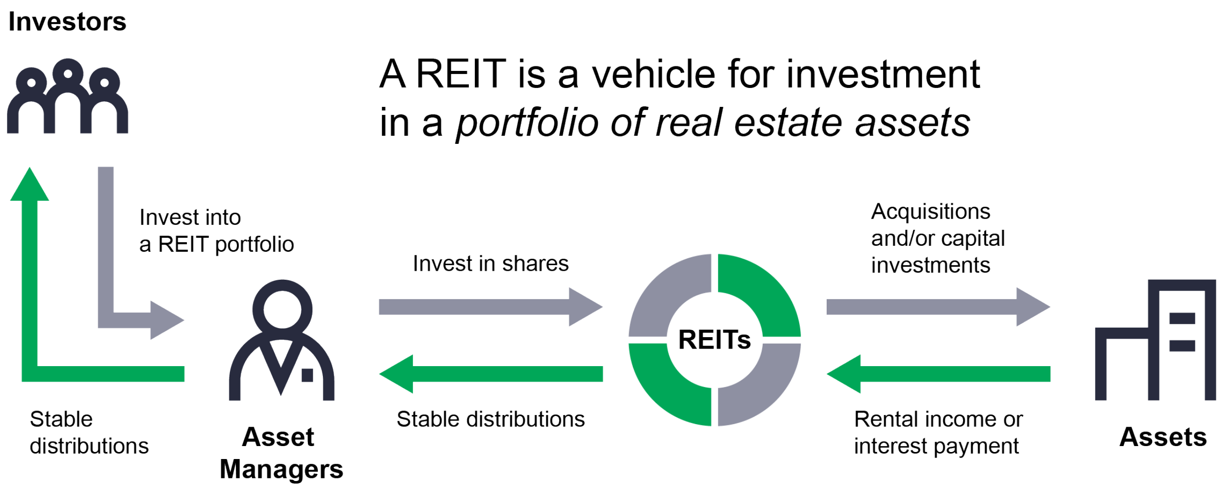
To begin with, we will examine the basic structure and benefits of holding REITs, benefits of portfolio inclusion, the fundamentals of AP-REITs, including the main sub-sectors, and their historical performance. We will then move onto to an in-depth exploration of how AP-REITs perform in different market environments (second article), focusing on movements in interest rates and inflation. Finally, we will look at how the asset class is positioned to perform in 2021 and beyond (third article).

Basic structure and benefits of holding REITs

Investors should be aware of AP-REITs' unique holding structure. Although this section will speak generally of the structure and benefits of REITs, they are also applicable to AP-REITs.

Trusts are mandated to pay out a certain percentage of their operating income to investors in the form of dividends [1]. When investing in a REIT portfolio, investors are purchasing a portfolio of real estate assets through equity shares (see Chart 1). REITs use the capital for acquisitions and management of

Chart 1: How does a REIT portfolio work?



For illustrative purposes only

[1] The percentage of statutory payout varies by jurisdiction, but generally accounts for a significant portion of the trust's earnings.

properties; they aim at paying out the proceeds of received rental income to investors in a stable dividend stream.

With that in mind, there are numerous benefits for investors to hold AP-REITs; many investors hold them for the potential source of income, which include:

- **Potential source of income:** Traditionally, REITs have provided a long-term source of income to investors through regular dividend payouts. Although potential price appreciation opportunities exist, dividends account for much of the asset class's total return and can provide a cushion for investors in a downturn.

- **Opportunity for portfolio diversification:** REITs also offer the potential for portfolio diversification. Over time, REITs have demonstrated a lower correlation with traditional assets, such as global equities and bonds, which may provide protection in an increasingly turbulent global market.

- **Lower minimum investment, liquidity, and preferential tax treatment:** Investors often ask about the potential benefits of investing in REITs versus directly investing in a more traditional investment in private real estate (such as housing or commercial real estate). When compared to private real estate, REITs offer three main advantages:

    - **Lower minimum investment:** AP-REITs require a lower minimum investment when compared to the significant outlay needed for direct real-estate purchases. Thus, investors can gain access to the sector, and often times a more diversified array of holdings.

    - **Liquidity:** AP-REITs are traded daily on stock exchanges throughout the region. Investors have convenient liquidity to buy and sell their investment, as well as clarity on the market price they will receive. In contrast, investments in private real estate traditionally require significant time to complete, with final pricing normally subject to negotiation.

    - **Tax treatment:** Finally, AP-REITs boast preferential tax treatment. Due to the trust structure described earlier, they are not subject to corporate taxation. As such, investors only need to pay tax on the income received.

AP-REITs: A diversity of opportunity for investors

Although the first AP-REIT (ex-Japan) was listed in Australia in 1971, the concept is still relatively new to the region. Singapore has since emerged as the leading REITs hub[2], while lesser-developed markets in Southeast Asia have gained notable momentum over the past five years.

The relative novelty of the asset class, coupled with a diverse range of opportunities, is proving particularly attractive in our view to investors. Indeed, the expanding REIT universe gives investors exposure not only to real estate in more developed economies, such as Australia and Singapore, but also emerging markets, like India and the Philippines, with the latter launching its first REIT in in 2020[3]). Indonesia is also currently working on changes to REIT laws that should allow for listings.

Main AP-REITs sub sectors

The diversity extends to real-estate segments that include established and newer industries. Office and retail REITs represent traditional real-estate plays around the region. Meanwhile, industrial REITs (incorporating data centres and logistics) and healthcare REITs reflect exciting innovations in the asset class. To add value, REIT management teams from these sub sectors would renovate properties and reorganise tenant contracts to generate continuous rental income.

[2] Bloomberg, 22 February 2020.

[3] 1st REIT listing shows PHL market ready to resume business | Philippine News Agency (pna.gov.ph), 13 August 2020.

Chart 2: Diversified sector exposure of Asia-Pacific REITs

Apart from the traditional retail malls, offices, industrial parks and hotels, AP-REITs also encompass new industries like data and logistics warehouses. We believe the emergence of e-commerce and cloud computing would benefit these new industries.

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- **Retail REITs** - Retail REITs own and manage retail stores and shopping malls. Despite the popularity of online shopping, successful retail centres continue to see growth in customer traffic, as contemporary retail centres offer more than just a place for shopping – they create an "experience" for their consumers which online shopping simply cannot match.

- **Office REITs** - Office REITs own and operate office properties in commercial areas, offices in industrial areas, or new office parks outside of commercial centres. Office properties are closely related to economic and business cycles, with rentals influenced by supply and demand.

- **Industrial REITs** - Industrial REITs own and operate industrial buildings, warehouses, or logistics centres for a wide variety of customers. The industrial segment used to encompass light industrial or traditional warehouse properties. However, in the past few years, e-commerce has quickly developed, leading to increased demand for logistics centres and data centres. Some Industrial REITs even focus on high-tech properties that play an important role in driving the e-commerce trend.

- **Hotels and Resort REITs** - Hotel and Resort REITs own and operate hotels and resorts to generate cash flow and profits. With changes to the way people travel and more intense price competition and value offerings, hotels no longer provide just basic accommodation. Operators are adding business services and amusement activities to pursue an enhanced guest experience. They are also bundling hotels with tourist landmarks through unique architectural designs.

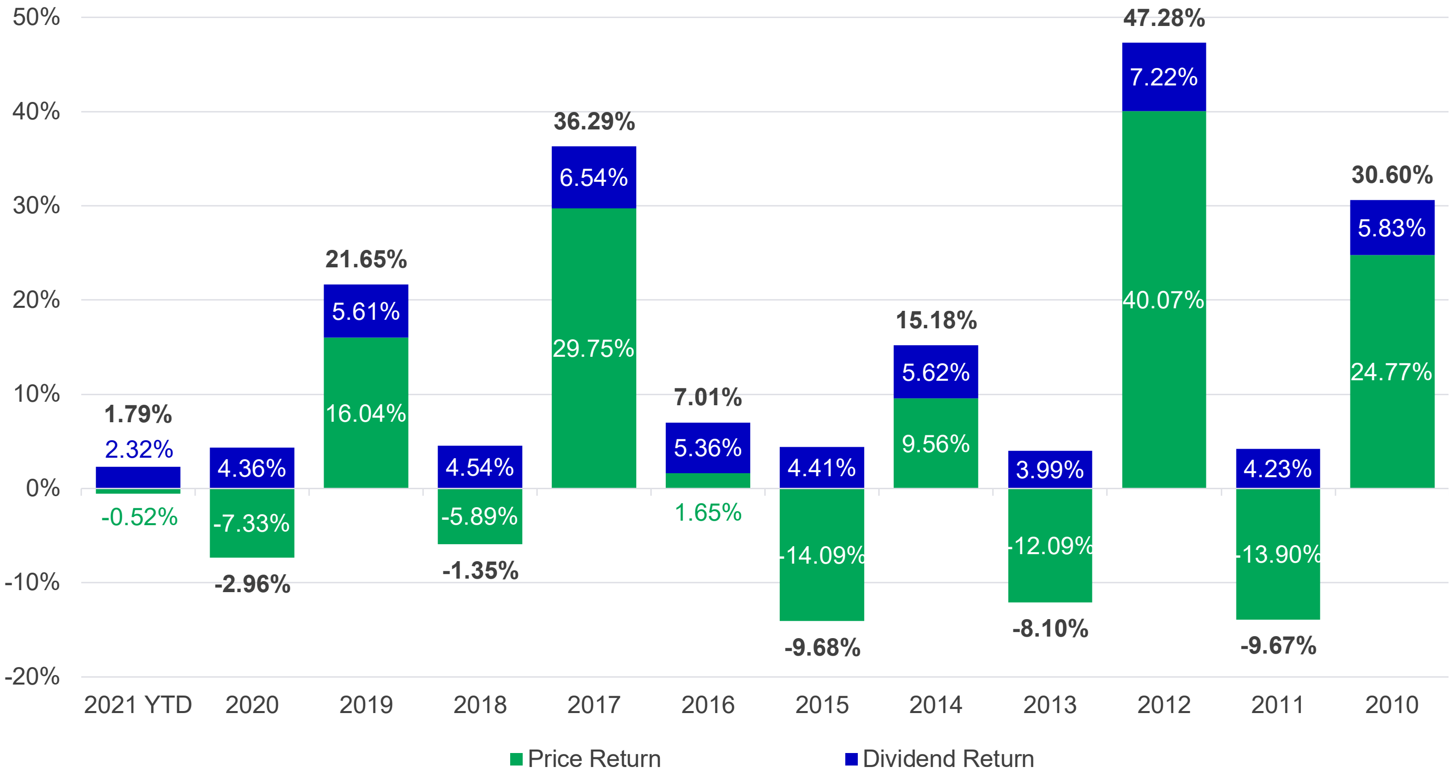
- **Diversified REITs** - Diversified REITs own and operate two or more types of properties, such as offices, retail stores, hotels, and other properties in their portfolios. Due to the diversification of the properties in their portfolios, the operators of diversified REITs have access to multiple income sources. That said, the requirement of management teams is also high given the broader range of underlying properties.

- **Healthcare REITs** - Healthcare REITs own and operate properties related to healthcare, such as hospitals and senior care facilities. Demand for healthcare services is increasing with improvements in the quality of life. The demand for healthcare services is generally price inelastic, i.e., demand remains stable even with increasing prices and changing market environments.

AP-REITs performance over the past decade

Despite the tumultuous performance of global equity markets over the past decade, AP-REITs have posted a positive total return on a cumulative basis from 2009 (as of 31 December) to 2021 (as of 30 June)[4]. Dividend payouts are the main reason: although the prices of AP-REITs have experienced volatility along with the broader market, the income element of the security has provided a cushion for investors. This defensive nature is a key reason why investors are interested in the asset class. In the next article, we will explore in more the elements contained in this chart, looking at how changes in inflation and interest rates impact AP-REITs.

Chart 3: Annual total returns of Asia ex Japan REITs (2010 – YTD 2021)



Source: Bloomberg as of 30 June 2021. Asia ex Japan REITs are represented by FTSE EPRA/NAREIT Asia ex Japan REITs Index (capped). Performance in US dollar.

[4] Bloomberg, as of 30 June 2021. Asia ex-Japan REITs = FTSE/EPRA Nareit Asia ex Japan index (capped); For illustrative purposes only. Past performance is not an indication of future results.

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