

May 2023

APAC Real
Estate
Winds of
Change

Keppel Capital
watch

Photo credit: International Bund Gateway in Shanghai rated LEED Platinum

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Executive Summary

As the world emerges from the COVID-19 pandemic, we find ourselves on the cusp of a number of important transitions which will bring about economic and capital market adjustments in the process. Nonetheless, with these transitions, there will also be new opportunities for investors.

Perhaps the most important change is the end of the era of “cheap money”. After two years of near-zero interest rates, major central banks have had to raise policy rates sharply as they look to tame elevated inflation despite slowing economic growth. As long as labour markets remain resilient enough, monetary policies are likely to stay restrictive until inflation rates fall back to target levels.

Another high-impact transition will be the journey to net zero. The real estate sector has a big part to play, with many brown buildings requiring retrofitting to green certified ones. Landlords in Asia will be incentivised by green rental premiums in the near term and motivated to avoid brown discounts or end up with stranded assets in the longer run.

There is a generational shift in the global workforce, with Baby Boomers making way for “Generation MZ”. The new-generation workforce tends to place importance on issues such as ESG, work-life balance and hybrid work. Employers and landlords must actively reposition their workspace offerings to meet the employees’ aspirations, such as improving indoor air quality, providing amenities and digital connectivity to support hybrid work.

On the back of geopolitical considerations and lessons learned from the pandemic and the Russia-Ukraine conflict, the age of globalisation is making way for more regionalisation. As economic integration deepens, there will be demand for quality logistics and office space in key trading and services hubs in Asia. Alternative real estate sectors, such as R&D laboratories, medical offices, senior living and student accommodation, will also become more mainstream, offering investors a means of diversification.

In the process of these major transitions, there may be market dislocations as capital allocations adjust to the new realities. While these could present challenges to the status quo, they also present opportunities in Asia for forward-thinking asset managers and investors willing to put themselves in the best positions to catch the winds of change.

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Introduction

Change is the only constant

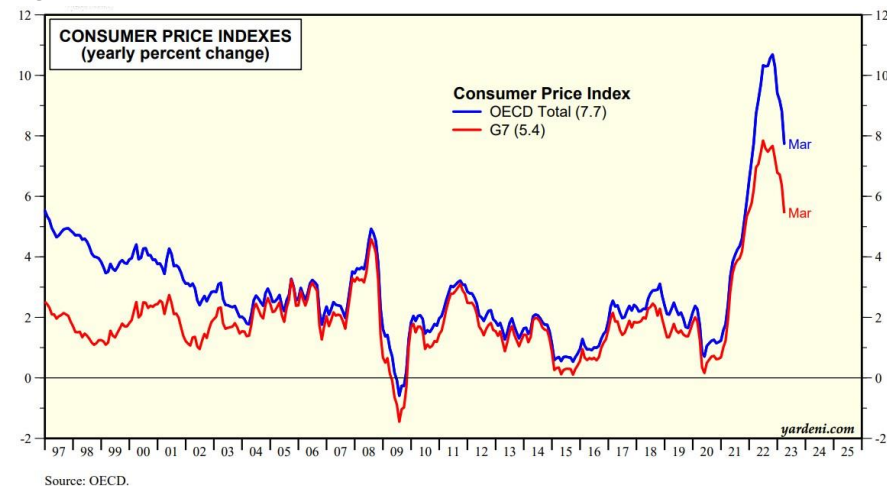
After nearly three years of lifestyle and economic disruptions due to the COVID-19 pandemic, much of the world has now transitioned into “living with COVID” in 2023. This is not the only change. We believe that the world is on the cusp of multiple important transitions, chief of which would be the end of “cheap money” and immense urgency to accelerate decarbonisation and sustainability efforts. Many of these transitions may bring about economic and capital market adjustments in the process, but at the same time offer investors new prospects if they seize on the right opportunities.

2023-24 Macro Outlook

End of cheap money

As the global economy emerges from the depths of the COVID-19 pandemic, many governments and central banks face a new challenge, i.e. taming stickily elevated inflation rates which have driven up costs of basic commodities, leading to what is being termed as a “cost of living crisis” since 2022 (Figure 1). There are various drivers of higher prices. These include supply chain disruptions caused by the protracted Russia-Ukraine conflict since February 2022 and the recovery in private consumption of both goods and services after pandemic measures were eased and borders reopened, underpinned by healthy corporate and household balance sheets and generally tight labour markets.

Figure 1: Global inflation rates



After resorting to easy monetary policies to tide through the pandemic, many central banks have reversed their accommodative stance as inflation rates exceed target levels. By 2Q22, major central banks such as the US Federal Reserve (Fed), European Central Bank (ECB) and the Reserve Bank of Australia (RBA) and Bank of Korea (BoK) in Asia, embarked on a synchronous rate-hiking cycle, with the exception of the Bank of Japan (BoJ) and the People’s Bank of China (PBoC). By the end of 2022, policy rates in the US, Euro area, the United Kingdom, Australia and South Korea have already exceeded pre-COVID levels and are hovering at levels last seen in 2008, potentially marking the end of the era of “cheap money”.

With their credibility on the line, central banks walk the tight rope of bringing down inflation without resulting in an economic “hard landing”. At the point of writing, inflation rates remain stickily above target despite some indications that they may potentially have peaked. Given still-resilient labour market conditions and cost pressures transitioning from goods to services as a result of post-pandemic reopening, central banks continue to guide on the possibility of more rate hikes and/or the potential of holding policy rates higher for longer. We believe this also signals a new paradigm for monetary policy, where central banks will be reluctant to return to Quantitative Easing in the absence of another major economic shock or financial crisis.

Growth outlook of advanced economies

In the US, the Fed exited from its two-year long zero interest rate policy in February 2022. The Fed also began Quantitative Tightening (QT) in June 2022, as it looks to reduce its bloated balance sheet which had doubled from USD 4.2 trillion in end-2019 to just under USD 9.0 trillion in April 2022. As of May 2023, the Fed rate stood at 5.00 - 5.25%, translating to a cumulative increase of 500 bps within the span of 15 months. Personal Consumption Expenditures (PCE) inflation, the Fed’s preferred inflation gauge, may have eased from a 40-year high of 7.0% in June 2022, but remains substantially above the Fed’s target of 2%.

As the real economy still appears resilient, economists became less pessimistic on the US economy’s GDP growth in 2023, with the International Monetary Fund (IMF) lifting its growth forecast from 1.4% to 1.6% in its April 2023 outlook report¹. Nonetheless, the IMF still expects further growth deceleration in the latter part of 2023 and 1H2024 as Fed policy gets more restrictive and hence is forecasting US GDP growth to slow to 1.1% in 2024. The recent collapse of Silicon Valley Bank (SVB) and Signature Bank in March 2023 rocked financial markets but banking regulators appear to have stepped in early enough to prevent contagion and avoid a 2008 Global Financial Crisis-type of financial crisis for now.

With US unemployment rate hovering near 50-year lows despite such a steep rise in interest rates, the Fed may persist with restrictive monetary policy. Expectations for the terminal Fed rate have been lowered following the collapse of SVB but if the impact is contained, the Fed is still expected to stick to its dual mandate of price stability and maximum sustainable employment. Nonetheless, even if a financial crisis can or has been averted, uncertainty over the US’ growth outlook has risen sharply in the wake of recent events and the risk of a sharper slowdown later this year remains on the cards.

A similar monetary policy outlook applies to most of the G7 central banks, with the exception of Japan for now. Despite sluggish growth prospects in the UK and the EU, bringing still-elevated inflation rates under control remains the key priority for these central banks. The ECB went ahead with a 50-bps rate hike on 16 March, even as Swiss banking giant Credit Suisse faced a crisis of confidence requiring a hasty bailout from its rival UBS.

¹ IMF, World Economic Outlook, April 2023

Overall, based on the IMF's latest forecasts made in April 2023, average growth rates of global advanced economies are expected to slow from 2.7% in 2022 to 1.3% and 1.4% in 2023 and 2024 respectively, weighed down by Europe and the UK in 2023 and the US in 2024. The recent bank bailouts are timely reminders that substantial macro headwinds remain on the horizon with a number of European economies on the verge of recession in 2023. Other risks include the prospect of an escalation in the Russia-Ukraine conflict and worsening geopolitical tensions involving the US, China and North Korea, amongst others.

APAC growth outlook

The growth outlook for the APAC region has seen significant improvement at the turn of the year, mainly on the back of China's COVID-19 reopening. In December 2022, the Chinese government abandoned its "zero-COVID" strategy which had weighed on both consumer and business sentiment due to the uncertainty of its implementation. By 8 January 2023, China reopened its borders, effectively signaling its intention to "live with COVID".

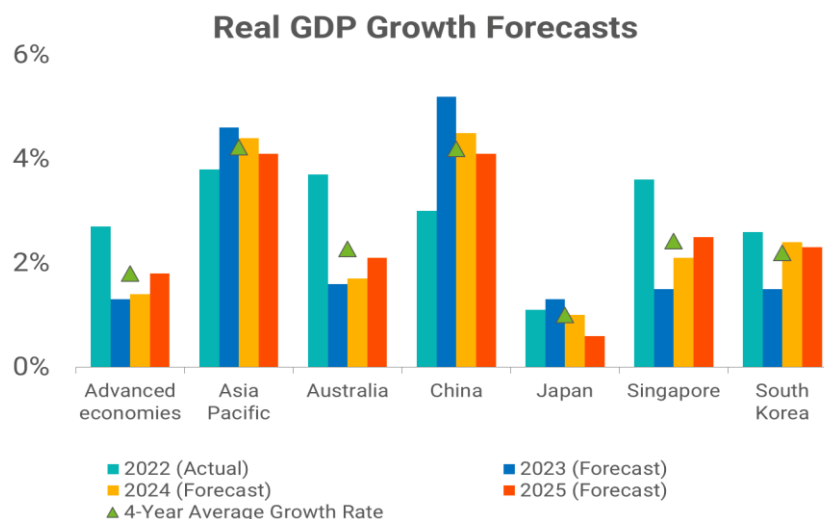
With the reopening, China's consumer and business activities will gradually normalise, potentially to pre-COVID levels. At the recent "Two Sessions" held in March 2023, outgoing Premier Li Keqiang announced a GDP growth target of "around 5%" for 2023, which has been seen by most economists as conservative. Much of the growth will likely be more evident in 2H2023, as continued pro-growth policies take effect under a new leadership team, albeit still helmed by President Xi who will begin his newly-elected third term.

The government will focus on further developing its "dual circulation" strategy. Favourable policies will likely target supporting household consumption, stabilising the housing market, providing targeted lending to private enterprises and state-led investments into key industries such as renewable energy and advanced technology. The PBoC lowered the Reserve Requirement Ratio (RRR) for banks by another 25 bps with effect from 27 March to release c. CNY500 billion of liquidity into the banking system, signaling its readiness to provide calibrated support to the Chinese economy.

China's economic recovery will provide regional economies with some favourable ripple effects, partially mitigating weakening demand from the advanced Western economies. As business confidence and consumer activities in China pick up momentum, countries such as Japan, South Korea and Singapore can expect to see year-on-year improvements in their exports to China. Moreover, with the relaxation of cross-border pandemic measures, most Asian economies can look forward to the return of outbound Chinese tourists to boost their local retail and hospitality sectors.

Taking China's reopening into consideration, the IMF has lifted its overall GDP growth forecasts for Asia to 4.6% and 4.4% in 2023 and 2024 respectively. This will be a significant improvement from 3.8% growth in 2022 when China was held back by its "zero-COVID" strategy. With relatively brisk growth rates expected for Asia, the region will remain the leader in economic dynamism in the immediate future while the Western advanced economies continue to face recessionary headwinds (Figure 2).

Figure 2: GDP growth forecasts



Source: IMF World Economic Outlook (April 2023), IMF APAC Regionak Economic Outlook (May 2023)

On the monetary front, the BoK, the RBA and the Monetary Authority of Singapore (MAS) all opted to stand pat during their recent monetary policy decisions in April. While noting that inflationary pressures remain higher than desired and for longer, these central banks are taking time to assess the effects of previous monetary tightening amid heightened global macro uncertainty. Depending on domestic economic conditions, these central banks have not ruled out further tightening if inflation remains elevated, as evidenced by the RBA’s resumption with a 25-bps rate hike on 3 May.

Separately, the BoJ’s new Governor Kazuo Ueda remains of the belief that Japan’s cost-push inflationary pressures will gradually wane, thereby maintaining its ultra-loose monetary policy remains appropriate in the near term with short-term rates remaining at -0.1%. However, markets are expecting Ueda to tweak the BoJ’s Yield Curve Control in the coming months which could see longer duration rates rising incrementally. As for China, pressures on consumer prices remain benign even as the economy adjusts to a post-COVID environment. This allows the PBoC to maintain an accommodative stance to encourage domestic consumption, stabilise the housing market and encourage investments.

Table 1: Inflation and policy rates of selected economies

	Last headline CPI (% yoy)	Policy Rate in January 2022	Policy Rate as at 3 May 2023
US	5.0%	0.25 - 0.50%	5.00 - 5.25% (↑)
Australia	7.0%	0.10%	3.85% (↑)
China	0.7%	2.85% *	2.75% (↓)
Japan	3.2%	-0.10% **	-0.10% (-)
Singapore	5.5%	1.76% ***	2.71 (↑)
South Korea	3.7%	1.25%	3.50% (↑)

Source: Various

* PBoC’s 1YR MLF rate

** BoJ’s short-term rate

*** Singapore’s 10YR Govt Bond Yield

Real estate implications:

After benefitting from many years of ultra-low interest rates, real estate markets are now in the midst of adjusting to the higher interest rate environment. In the immediate future, the investment markets will be constrained by wide bid-ask spreads as prospective buyers adjust their underwriting on higher cost of capital assumptions while most asset owners are not in distressed situations to sell at large discounts.

If we are right in that interest rates could stay higher for longer, or at least unlikely to return to near-zero levels, investors will have to be even more selective in their asset allocations in the coming years. With Asia still a relatively bright spark economically, markets with strong demand and supply fundamentals will continue to outperform in the medium to long term.

For instance, Seoul's office market remains compelling as it benefits from very limited pipeline supply of new Grade A office space over the next five years. International investors with ample dry powder can potentially capitalise on the tightened liquidity conditions in South Korea to pick up assets at more attractive valuations. Investors can also look forward to more outperformance by positioning themselves to benefit from emerging trends, such as those we highlight in the following sections.

Decarbonisation to move into overdrive

The concept of sustainable real estate development has quickly gained traction among a growing number of stakeholders in recent years. From a macro perspective, the race to reduce global warming has become more urgent than ever. According to the original report from the Intergovernmental Panel on Climate Change (IPCC)², human activities have caused approximately 1.1°C of global warming above pre-industrial levels and that has already led to an increase in the frequency of extreme weather events. The IPCC further warned that the world is set to reach 1.5°C above pre-industrial levels within the next two decades and only the most drastic cuts in carbon emissions from now would help avoid an environmental disaster.

Subsequently at the 2021 United Nations (UN) Climate Change Conference in Glasgow (COP26), participating countries reaffirmed the Paris Agreement (COP21) goal of limiting global warming to well below 2.0°C and pursue efforts to limit it to 1.5°C. However, at the COP27 Summit held at Sharm el-Sheikh, Egypt, in November 2022, countries neither progressed commitments nor showed significant action to further decrease global emissions. It became evident that the world is not doing enough to be able to limit global warming to below 1.5°C.

Clearly, the onus is on all of us to accelerate efforts towards the 1.5°C target. The IPCC believes that all sectors have to at least halve emissions by 2030 and with the right policies, infrastructure and technology in place to change

² IPCC, Climate Change 2021, The Physical Science Basis, August 2021

our lifestyles and behaviours, a 40-70% reduction in greenhouse gas (GHG) emissions by 2050 could be possible.

The real estate sector has a big role to play in the decarbonisation journey. This is because building and construction account for 39% of global carbon emissions, with operational emissions (such as from heating and lighting) making up 28% and the other 11% coming from embodied carbon emissions³, or “upfront” carbon associated with materials and construction processes throughout the whole building life cycle. In some cities like Tokyo and Seoul, buildings can account for more than 65% of carbon emissions⁴ and hence they are critical to the energy transition process.

However, the current pace of retrofitting buildings towards net zero carbon (NZC) is highly inadequate to achieve COP21’s target. JLL estimated that the cost of retrofitting the office stock alone in 17 major countries, including US, UK, Japan and South Korea, will exceed USD 3 trillion, with retrofitting rates in developed cities having to triple to 3.0-3.5% of existing stock per annum from around 1.0% currently.

To address the various perspectives and actions taken by key stakeholders, we summarise some key considerations below.

a) Governments

Cognisant of the role real estate has in this transition, governments typically adopt a “carrot and stick” approach to steer the industry towards more sustainable development. However, policies and regulations continue to play catch-up with science.

While it is important to ensure that new builds are predominantly green buildings, governments also continue to encourage building owners to upgrade and retrofit existing buildings to meet increasingly stringent green and sustainable standards. This is because more than 80% of the building stock that will be standing in 2050 have already been built and the greenest building is “the one that already exists”, when one considers the embodied carbon involved in the demolition and rebuilding processes.

For example, the Singapore government launched the Singapore Green Building Masterplan (SGBMP) in March 2021 setting out three goals by 2030, namely to green 80% of buildings by Gross Floor Area (GFA), to achieve 80% improvement from 2005 levels in energy efficiency for best-in-class buildings and for 80% of new developments to be Super Low Energy (SLE) buildings from 2030⁵. Financial incentives will be provided to support existing building owners who strive for higher energy performance standards, e.g. SLE, by lowering upfront costs of energy efficiency retrofits. Separately, developers/building owners on private sites of at least 5,000 sqm in GFA can enjoy up to 3% bonus GFA beyond the Master Plan Gross Plot Ratio if they achieve Green Mark Platinum - SLE certification alongside other productivity, digitalisation and quality outcomes.

³ World Green Building Council, Bringing Embodied Carbon Upfront, September 2019

⁴ JLL, Decarbonising Cities and Real Estate, May 2022

⁵ Building and Construction Authority of Singapore

b) Landlords/Asset owners

To meet their own and tenants' sustainability goals, an increasing number of landlords in APAC are exploring green leases, but the region lags the more mature markets in Europe and North America. JLL defines a green lease as an agreement between landlord and tenant which sets out environmental objectives on how the building is to be improved, managed and/or occupied in a sustainable manner⁶.

As an example, a tenant might agree to implement energy reduction measures while the landlord might provide recycling services as part of property management. With tenants using approximately 50-65% of a building's energy, such an agreement allows for better alignment of interests. This is particularly relevant today, when energy prices remain elevated in the wake of the Russia-Ukraine conflict. In some instances, green leases supplement the targets and key performance indicators of green or sustainability-linked loans or bonds, which could potentially lower financing costs by a few basis points.

To further their own net zero journey, many landlords are increasingly relying on new technology and tapping on renewable energy to reduce their carbon footprints. For instance, many asset owners in Singapore are leveraging photovoltaic (PV) systems to tap on solar energy on their building rooftops. The actual contributions by onsite PV systems to total energy usage remain small given the variability of power generation due to the inability to generate solar power at night and on days with heavy cloud cover. Landlords can further procure Renewable Energy Certificates (RECs) or where possible, use direct energy contracting and power purchase agreements (PPA) with renewable energy suppliers to ensure long-term supply of green energy.

Besides lowering operating expenses, landlords of green buildings can potentially gain from higher rental incomes compared with owners of brown buildings. There is evidence that a green rental premium exists in Asia, albeit to varying degrees depending on the market. Based on a study by JLL⁷, a rental premium exists for green certified Grade A office assets across 11 Asian cities, when building location, age and amenity factors are held constant. JLL also noted that rental premiums are lower in cities with more availability of green certified Grade A office space due to supply and demand dynamics. For instance, the highest green premiums were identified in Hong Kong, where less than one-third of the Grade A office stock is green certified, whereas in Singapore where 90% of the Grade A office stock is green, the rental premiums were observed to be between 4% and 9%.

On the other hand, the cost of inaction on the part of asset owners is expected to soar over the medium term. Government regulations regarding green certifications will only get more onerous, occupiers with their own ESG commitments will shun poorly or non-rated buildings and banks will be increasingly unwilling to fund acquisitions or refinance existing loans related to brown buildings. To avoid brown discounts, landlords and asset owners

⁶ JLL, "Green leases: Setting the tone for responsible leases", September 2022

⁷ JLL, "The value of sustainability", November 2022

should act quickly to keep up with technological advances and ensure their buildings remain among the best in class to stay competitive.

Real estate implications:

We believe the preference for green office space amid this sustainability transition presents an opportunity for value-add investors to participate in the world's decarbonisation efforts. The next 5-7 years will likely present immediate opportunities as stakeholders, including regulators, occupiers, landlords and investors, race towards meeting their first decarbonisation milestone, typically slated for 2030.

In the immediate term, many older assets will require capex to upgrade to green certified buildings. The green rental premiums and lower operating expenses will serve as financial incentives, while remaining relevant to the ever-demanding ESG requirements of tenants. In the longer run, landlords who fail to act will be effectively penalised as their brown buildings become stranded assets, unable to attract tenants or even secure refinancing.

Other transitions with real estate implications

1) Baby Boomers to Generation MZ workforce

The global workforce is undergoing a seismic generational shift. The last of the Baby Boomers (those born between 1946 and 1964) will likely be retiring from the workforce within the next ten years. In their place will be workers from "Generation MZ", collectively made up of the Millennial generation (born between 1981 and 1996) and those from Generation Z, also known as Zoomers (born between 1997 and 2012). By most estimates, Generation MZ will make up more than 70% of the global workforce by the year 2025.

While it is important not to generalise and stereotype, studies suggest that there are broad nuances among the various generational cohorts due to differences in their shared historical contexts and life experiences. For instance, a survey conducted by Deloitte⁸ revealed that environmental protection was a top priority for Generation MZ. The majority of respondents would also like their employers to do more to fight climate change and if they are unsatisfied with their employers' societal and environmental impact, they are more likely to leave their jobs within two years.

In addition, following their COVID-19 experience, three-quarters of the Generation MZ surveyed by Deloitte would rather not return to the office full-time, preferring hybrid or remote work instead, with the added flexibility of how and when to work for better work-life balance. With the three-year pandemic proving that hybrid work is feasible, it will likely remain the default, just as how Asian societies progressively pivoted to a five-day work week at the turn of the century.

Real estate implications:

It is thus important for employers and building landlords to take the different workspace preferences and employee motivations into account when

⁸ Deloitte, The Deloitte Global 2022 Gen Z and Millennial Survey, May 2022

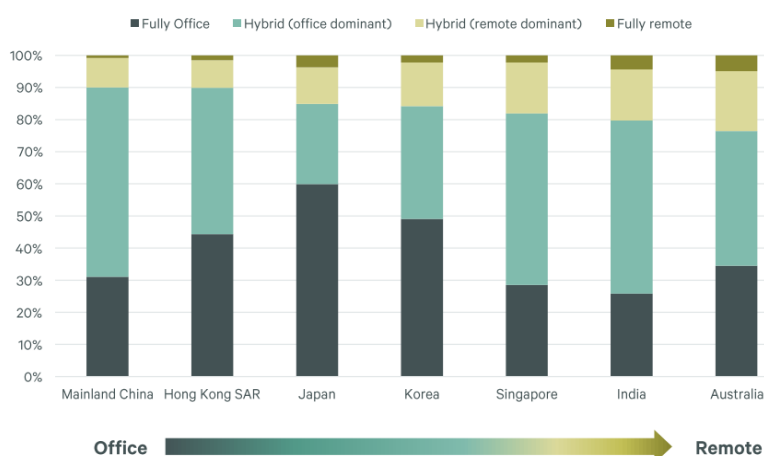
considering workspace options in order to attract and retain talent (including the non-Generation MZ cohorts). Importantly, the workplace of the future should be able to meet employees’ increasing focus on ESG, work-life balance and facilitate hybrid work.

Therefore, employers will increasingly look to establish their offices in green certified buildings and potentially on green leases, where they can be seen doing their part to reduce their carbon footprints and cut wastes.

In addition, more corporate occupiers in Asia will design their workspaces around employee well-being. A certification like WELL will grow in popularity in order to attract and retain talent. Managed by the International WELL Building Institute (IWBI), WELL judges the built environment on seven major categories comprising air, water, nourishment, light, fitness, comfort and mind. Occupiers, and landlords, will also increase engagement with office workers and even the surrounding community through events and activities.

In Asia, most workers have returned to office (Figure 3), but the post-pandemic “office re-entry” has been more pronounced in cities such as Singapore, Shanghai, Seoul, Tokyo and Ho Chi Minh City, whereas physical occupancies in Melbourne and Sydney were still at 47% and 61% of their pre-COVID levels as of February 2023⁹. With some form of hybrid work arrangement here to stay, companies will increasingly provide opportunities for their employees to work out of flexible office space and provide “third places” to encourage collaboration and socialising when they are back in their offices. Digital connectivity is also critical, especially if the technology available to the worker in the office is superior to what he/she can access at home. Certifications like WiredScore and SmartScore could see increased take-up by landlords in Asia as a means of staying the best in class. When used appropriately, smart building technologies such as Internet of Things (IoT) sensors could also further building owners’ sustainability and future-proofing efforts through more efficient management of power usage and indoor environmental quality.

Figure 3: Working patterns across Asia as of December 2022



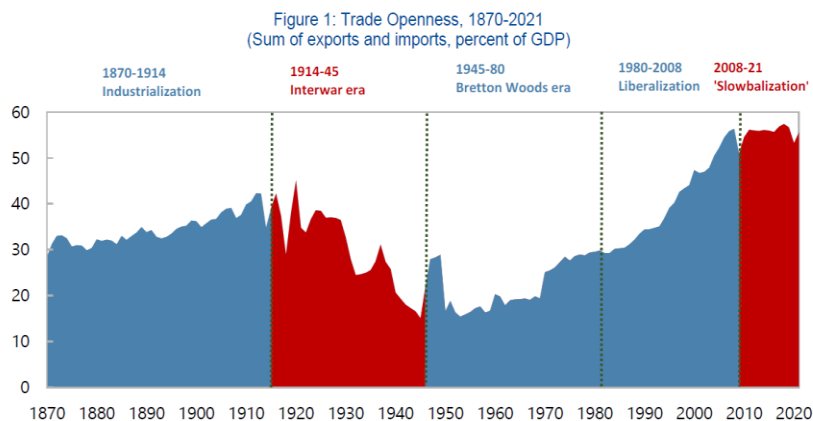
Source: CBRE, December 2022

⁹ Property Council of Australia

2) Globalisation to regionalisation

Globalisation can be described as a process of increasingly free flow of ideas, people, goods, services and capital across national borders leading to greater economic integration. The global economy has seen great benefits from globalisation in the post-war era (Figure 4), on the back of increased trade liberalisation which included China’s accession into the World Trade Organisation (WTO) in December 2001.

Figure 4: Trade openness over the years



Sources: Jordá -Schularick-Taylor Macroeconomic Database; Penn World Data (10.0); Peterson Institute for International Economics; World Bank; and IMF staff calculations.
Note: Sample composition changes over time

Based on the IMF’s estimates¹⁰, in the years that followed the Global Financial Crisis in 2008, the world entered a new phase of “slowbalisation”, characterised by slower expansion of cross-border lending and trade. However, there are now signs that the global economy may be fragmenting.

Early indications of this came from the Trump administration’s trade war with China since 2018. As a continuation of bipartisan stance in the US, the Biden administration has not only kept the tariffs in place, but further placed trade restrictions on China’s access to advanced semiconductors and chip-making equipment. More specifically, the CHIPS and Science Act signed by President Biden in August 2022 is a conscious attempt to “home-shore” or “friend-shore” the production of cutting edge semiconductor chips, with the US President proudly declaring that “the future of the chip industry is going to be made in America”¹¹. Furthermore, the supply chain disruptions brought about by the COVID-19 pandemic and the Russia-Ukraine conflict raised additional national security concerns particularly around basic commodities like energy, food and water.

We believe there will be more examples of supply chain diversification, as the global manufacturing system moves away from the “just-in-time” model which served well for over 40 years, to the “just-in-case” model to improve the redundancy, hence resilience, of the system. However, within Asia, early worries of widespread factory relocations out of China have been overblown.

¹⁰ IMF Staff Discussion Notes, Geoeconomic fragmentation and the future of multilateralism, January 2023

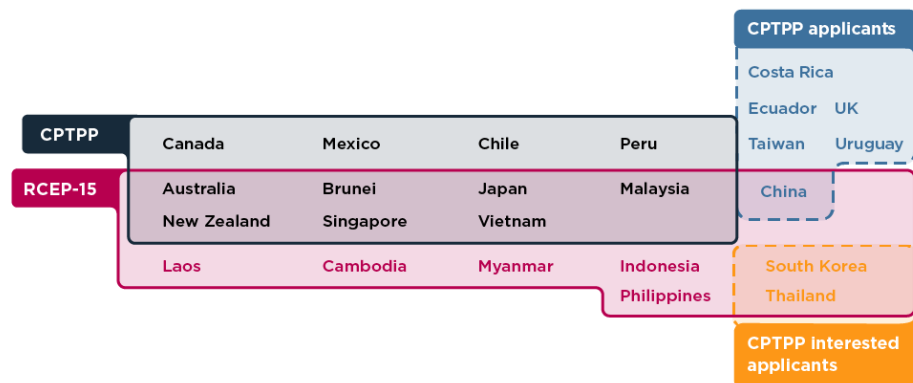
¹¹ <https://www.politico.com/news/2022/08/09/biden-ends-slog-on-semiconductor-bill-with-signature-00050530>

While certain manufacturers have set up new facilities in lower-cost markets such as Vietnam and Bangladesh, this is mainly on the back of corporations adopting a “China plus one” strategy for diversification.

Setting aside geopolitical tensions and considerations, APAC economies are likely to experience more regionalisation and economic integration. The Regional Comprehensive Economic Partnership (RCEP) comprising 15 APAC member nations which make up around one-third of global GDP and one-quarter of world trade came into effect on 1 January 2022. When all 16 members have ratified the agreement, RCEP will become the world’s largest free-trade agreement (FTA) by GDP. This could be further complemented by the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP), especially if China, South Korea and Thailand eventually also become members of the trade pact (Figure 5).

Figure 5: Incumbent and potential member nations for RCEP and CPTPP

Trade agreement members, applicants, and interested applicants



Source: Peterson Institute for International Economics (PIIE)

China’s extensive and increasingly advanced supply chain ecosystem will be hard to replicate or even replace. With deepening economic integration, there is scope for regional emerging economies to be a natural extension of China’s supply chain by taking on the lower-end, labour-intensive parts of production, while China itself will focus on higher value-add industries. Countries like Vietnam and Indonesia will continue to reform and open up in order to attract Foreign Direct Investments (FDI) to fund industrial development, with Asian neighbours like China, Japan and Singapore expected to remain the key sources of capital.

Real estate implications:

On the back of robust capital inflows supporting industrial development, there will be a need for better quality real estate in APAC too. For emerging economies like Vietnam and Indonesia which will take on the mantle of regional manufacturing hubs even as the local middle-class grows, there will be continued healthy leasing demand for high-quality logistics warehouses. Even in an advanced economy like Singapore, which is a global trade and high-value manufacturing hub (e.g. aerospace and pharmaceuticals), end-user demand for the investment-grade logistics warehouses will remain keen amid deeper trade integration.

To support the intra-regional flow of goods and services, Asian financial hubs such as Singapore, Shanghai, Tokyo and Seoul will likely see increased demand for professional services such as trade financing, cross-border payment and settlement, legal and advisory and international arbitration. Multinational corporations are likely to expand their regional presence as well, either establishing or growing their regional headquarters in key cities like Singapore and Shanghai or opening up offices in the emerging cities such as Ho Chi Minh City and Jakarta to support and oversee their local operations. These will underpin leasing demand for high-quality office spaces in the capital cities within Asia.

3) Alternatives becoming mainstream

Following the COVID-19 experience and upheavals caused by the Russia-Ukraine conflict, societal, demographic and lifestyle changes are accentuating demand for alternative real estate here in APAC.

First, with most advanced Asian economies experiencing greying populations and also for health and national security reasons, more capital will be channelled into life sciences, including healthcare, pharmaceuticals, biopharmaceuticals and medical devices. Cities with access to ample talent and capital will also be key life sciences hubs in Asia, including Singapore, Beijing, Shanghai, Tokyo and Melbourne.

Second, with the rise of the middle-class in Asia, the collective wealth accumulated by retiring cohorts will generally be greater than their preceding generations. As their living standards and life expectancies have improved, so too will their expected quality of life in their later years. They will be more discerning when consuming services, such as the quality of healthcare and eldercare. They will also increasingly look to participate in lifestyle and cultural activities to maintain their bodies and minds.

The growing Asian middle class and the normalisation of border controls will help to underpin demand for education services here in Asia. Besides local private education (such as K-12 schools), the continued urbanisation and industrialisation in Asia will require labour markets with medium to higher levels of technical skillsets. Enrolments into institutes of higher learning, including vocational schools, academies for continual and lifelong learning and universities will remain healthy, both from the local populations as well as international students.

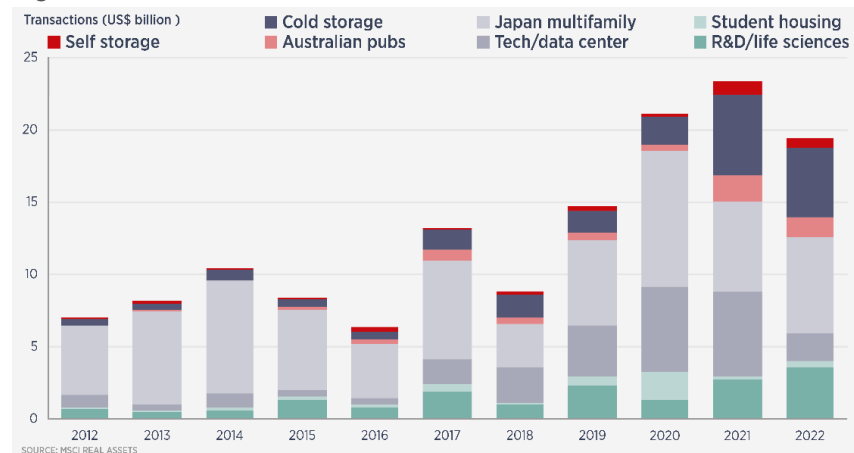
Real estate implications:

Even though many of these alternative asset classes require heavier operational expertise, their end-user demand dynamics tend to be more stable and potentially counter-cyclical to traditional real estate asset classes such as office and retail. By working closely with experienced operators and/or structuring double- or triple-net long leases through master lease agreements, we believe institutional investors will steadily increase portfolio allocation into alternatives in Asia as a means of diversification. Furthermore, these typically longer leases provide better asset-liability management for institutional investors such as pension funds and sovereign wealth funds.

The alternatives markets in Asia may not be as mature as in many of the Western developed markets, but we see ample opportunities for the space to expand (Figure 6). For instance, growth in the life sciences industries in Asia will drive the need for more specialised properties such as R&D laboratories, medical offices and cold-chain logistics warehouses. The ageing populations in advanced Asian economies such as Japan, South Korea and China will be increasingly receptive towards more lifestyle-oriented senior living products. These will likely be independent and active living apartments providing concierge, medical, housekeeping and catering services, amongst others, which were already introduced in the US more than 30 years ago.

Last but not least, the resumption of international student enrolments will underpin healthy demand for student accommodation in popular study destinations such as Australia and Japan. China’s Ministry of Education also announced on 28 January 2023 that it would no longer recognise foreign-obtained educational qualifications earned fully through online study, requiring students instead to physically return to their schools overseas¹². As China is a major source of foreign students in Australia, their return will add upward pressure on Purpose Built Student Accommodation (PBSA) rates in Australia, especially when the Australian market is relatively underserved compared with the UK and US.

Figure 6: Transaction volumes of alternative real estate in APAC



Source: MSCI Real Assets, Savills

¹² <https://monitor.icef.com/2023/02/chinese-students-scramble-to-return-to-campus-abroad-after-ministry-of-education-ends-certification-of-online-degrees/>

Conclusion

The world today is on the cusp of a number of important transitions with significant economic, capital markets and real estate implications. Among the most important will be the end of the era of “cheap money” and the urgency to accelerate sustainability and decarbonisation efforts. Geopolitical and demographic shifts further add to the need to rethink capital and asset allocations.

Amid these transitions, there will be ample opportunities in Asia for forward-thinking asset managers and investors to adjust their sails to the winds of change. These include actively retrofitting offices to meet green standards, positioning workspaces to cater to a new generation of workforce, tapping on the real estate needs from regional economic integration and capturing the early stages of growth for alternative real estate in the region as they become more mainstream.

Keppel Capital is a premier asset manager in Asia. It is the asset management arm of Keppel Corporation Limited, one of Singapore's flagship multinational companies in more than 20 countries. Keppel Corporation provides solutions for sustainable urbanisation, focusing on energy & environment, urban development, connectivity and asset management.

With assets under management of approximately S\$50 billion[^], Keppel Capital has a diversified portfolio that includes real estate, infrastructure, data centres and alternative assets in over 40 cities across key global markets.

Keppel Capital aims to create value and deliver sustainable returns for institutional and retail investors through a range of products including REITs, business trusts, private funds investing in real estate and infrastructure, separate accounts and pooled investment vehicles.

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[^] Gross asset value of investments and uninvested capital commitments on leveraged basis to project fully-invested AUM



Members of Keppel Capital:

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