REIT VALUATIONS TURN COMPELLING

APREA

Covid-19 Is Proving To Be A Game Changer

The impact of the pandemic has been pervasive with economic dislocations now reverberating across the world, hitting consumption, tourism, and supply chains. Financial market volatility has also increased with equity prices dragged lower through 2020.

While REITs have not been spared in the current selloff, the recent price drops have upped the distribution yields of the region's REITs, which rose to 4.4% in February, from 4.0% in January, according to the GPR/APREA Composite REIT Index. Yields for Singapore REITs rose 0.3 percentage points to 5.3% in the same period.

Undoubtedly, investors have lumped REITs with other equities and sold them down as a whole. However, the recent retreat in prices means valuations are now looking attractive. REITs in the region offer among the highest returns globally. S-REITs boast the highest yields among the region's established markets and remain backed by some of the island's prime commercial real estate assets (Chart 1).

Chinese listed real estate rebounded and recorded the best performance in February. The unprecedented effort from the government to contain the coronavirus outbreak has buoyed investor confidence. Additional fiscal and monetary stimulus measures are still expected to strengthen consumer and business sentiment. Meanwhile, Malaysian REITs were the top performers among the mid and smaller markets. This performance comes on the heels of the recent appointment of Prime Minister Muhyiddin Yassin.

The outlook for the global economy continues to be downgraded

But it is hard to see this global downturn arising from a public health crisis to be the end of a business cycle. Global central banks and governments have been generally aggressive in responding to the health and economic crisis to facilitate a recovery once the disruptions abate.

It is easy to get caught in this ball of frenzy and worry amid this 24-hour coronavirus coverage. And we all have to take a deep breath and remind ourselves that this too shall pass. While it has been a wild ride over the past several weeks, and buying equities, especially REITs, may be far from everyone's minds, we need to hit pause and constantly review our strategies as events evolve.

A market rout is an opportunity to take stock and position

Historically, returns for REITs have demonstrated lower volatility over the longer term (Chart 2), supported by their stable dividend pay-outs. The main reason is that the overall performance, especially for office and industrial, is tied to relatively long-term leases. Nonetheless, the world is now reeling from the sharp downturn in tourists especially those from Mainland China.[1] Hospitality properties have thus been impacted by lower tourist expenditures and occupancies. Many retailers have temporarily shut their doors. Still, what has also clearly emerged is the importance of the logistics sector, especially as suppliers ramp up production with a surge in online orders. Furthermore, in an unexpected employment boost, some grocers and essential stores that remain open have been looking to poach from those dislocated.[2]

While it is hard to imagine economic growth amid lockdowns and shutdowns, this is not '08-09. Recovery, whether U or V-shaped, will have to happen and companies will need to be open for business. Some hard-hit real estate sectors are already being given some relief funds to help blunt the economic fall-out from this natural catastrophe. Nonetheless, we find many REITs in Asia Pacific to be well-capitalized with leverage well within guidelines, high levels of corporate governance and have generally been prudent in their acquisitions. Their strong cash flows and lines of credit should help weather the downturn and in turn, offer value, and potentially gaining from the region's economic ascent as income streams gradually stabilize in the medium term. Valuations are also expected to benefit from widening spreads as governments undertake monetary stimulus to offset the impact from the COVID-19 outbreak. The Bank of Japan's pledge to double the pace of purchases for J-REITs will, for example, support prices. Further, we can take comfort that the commercial real estate sector in Asia Pacific had a lot of momentum going into the crisis which should allow for a quicker return to normalcy.

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[1] The coronavirus has grounded Chinese tourists. The global travel industry may not recover for years, CNN, February 28, 2020.
[2] Coronavirus Sparks Hiring Spree for Nearly 500,000 Jobs at Biggest Retailers, Wall Street Journal, March 23, 2020.

Chart 1

Asia Pacific REITs
Weighted Average Dividend Yield Through February

Country/Region

≥ USD50 Million Free Float Market Capitalization		< USD50 Million Free Float Market Capitalization	
Japan 3.8%	**Australia** 4.5%	**Thailand** 4.8%	**Taiwan** 2.3%
Singapore 5.3%	**Hong Kong** 4.3%	**Malaysia** 5.3%	

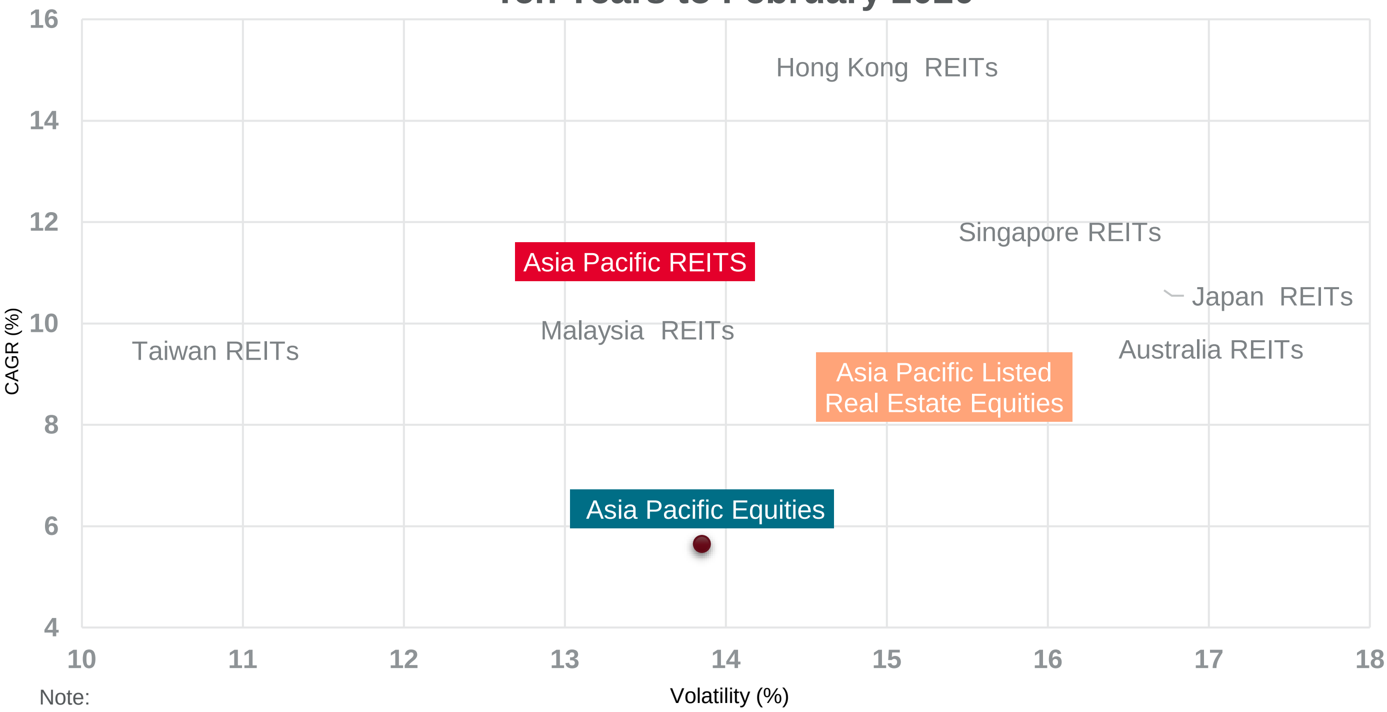
Sector

Diversified 4.7%	**Hotel** 6.3%	**Office** 3.9%	**Retail** 5.2%
Healthcare 4.9%	**Residential** 4.2%	**Industrial** 3.4%	

Note:
As of February 28th 2020. All data are calculated on local currency denominated basis.
Source: APREA, Global Property Research.

Chart 2

Compound Annual Growth Rate and Volatility
Ten Years to February 2020



Note:
As of February 28th 2020. All data are calculated on USD denominated basis.
The following asset classes are covered:

- REITs – GPR/APREA composite REIT Index
- Asia Pacific Listed Real Estate Equities – GPR/APREA composite Index
- Asia Pacific Equities – MSCI Asia Pacific Equities Index

Source: APREA, Global Property Research.