Aberdeen Asset Management

Russell Chaplin is CIO of Aberdeen's property team and is a member of the property team's management board. He is responsible for the investment process and its application throughout the property business and manages the research and strategy team. He was previously at UBS Global Asset Management, Henderson Global Investors and PMA.

CORPORATE OVERVIEW

Aberdeen Asset Management is a global investment management group, managing assets for both institutional and retail clients from offices around the world. Its mission is to deliver strong fund performance across diverse asset classes in which Aberdeen believes it has a sustainable competitive edge. Aberdeen Asset Management is an active property investment manager with a local presence in key international markets. The group offers separate accounts and commingled funds, including funds of funds.

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Recently, ***Geoffrey Dobrmann,*** *editor-in-chief of* The Institutional Real Estate Letter – Americas, *spoke with* ***Russell Chaplin,*** *CIO for the property team of Aberdeen Asset Management. The following is an excerpt of their conversation.*

What are the top reasons for investing with Aberdeen?

Firstly, we are not part of a wider banking group or insurance group, so we live or die by the performance that we deliver for our clients. Secondly, our approach to property investment and our process sets us apart: we are absolute value investors. And, finally, our footprint is broad, though it is focused in Europe. About 90 percent of our assets under management are in Europe, and we're one of the biggest real estate fund management firms in Europe [*Pensions & Investments*, October 2013] — and the largest independent firm.

Many U.S. investors moving overseas believe they need to get a return premium. Why should they consider investing in core assets outside their borders?

I'd flip that around the other way: If you are only comfortable investing in core assets in your domestic market, why would you take on additional risk when investing overseas? Core assets across the globe deliver very similar levels of return in the long run. You're not going to get a risk premium investing in core assets; you're just going to get what the local market produces — somewhere between 6 and 8 percent unleveraged over the long run, depending on the market. The idea that you needed a risk premium really came in when people were making direct investments outside their home market. They aren't able to buy many assets, and they are investing in markets that they did not know as well as the locals. It's a perfectly valid strategy, but it is a return-seeking strategy. If you are going to pursue that strategy, then you typically are going to be taking on higher risk. There's no "free lunch." The U.S. represents between 35 percent and 40 percent of the total value of the global real estate market [IPD, January 2013], and we think it makes sense even for a U.S. investor to have some of that core real estate exposure outside the domestic market. Regarding Europe, the continent's issues of the past few years have been pretty well publicized, but it probably looks worse from the outside than it does from the inside. And we think that the European opportunity set is still fairly broad.

Where do you see opportunities in the market today?

The world's a big place, so we look very broadly. In terms of opportunities, we're typically looking for quality, and we define quality as durable income, which means either long leases or a series of short leases with minimum down time. And we're looking for the potential for some capital return through the ownership lifetime. Wherever we can find those types of assets, that is where we'll concentrate. We are focused on individual assets. We're not a group that would instantly write off a country or a sector. In 2011, if you just looked at the aggregate level, Australia performed very well and, as you probably expect, Spain did not perform very well. But in 2011, one-quarter of the real estate assets in Spain actually outperformed half of the assets in Australia, and the spread of returns between the strongest and the weakest performing assets was about 55 percent [IPD, June 2013]. So where would we look now? In Europe, typically in the core markets, and then across Asia Pacific and the U.S. for our multi-manager products.

Tell us about your research and strategy group. What differentiates it from your competitors?

Our research and strategy group is composed of 10 people, so we don't have a massive research and strategy function; however, we feel that we do have a focused research and strategy function. The way we add value through research and strategy is on thematics — that is, where we believe there are big themes that overlay what is happening to property. And we want to make sure we understand those themes and capture any of the upsides and avoid any of the downsides of the implications from our research. The way we look at it, everyone at Aberdeen is doing research. Whether they are asset managers or transactions managers, they're all doing research on the markets all the time, so we want to make sure we're sharing information across the group. Our process is designed so we are making team-based decisions. And we think we make better decisions as a result.

How does your investment process work?

We don't believe we can manage market returns, but we do believe we can manage risk, so we have positioned ourselves as risk managers. With an individual asset, we are thinking about that asset as a bundle of risks: the tenants, the physical construction of the building, where it is located, and so on. But also when we are managing a portfolio, we're looking at that portfolio as a bundle of risks, and we are managing those risks as well. We are absolute value investors, so we don't move up the risk/return curve when others do. We are buy-and-hold investors for core, and that means we need this single approach so everyone is pulling in the same direction. We're very much team-based as well. Lastly, our focus is on quality first, and then we look at price. After the global financial crisis, we wanted to make sure we didn't just go through the crisis and come out the other end and do the same thing again. We wanted to learn from the experience. Probably the biggest change, in our view, was to adopt this absolute value approach. We focus on quality, and that leads us into points of the cycle where the markets are heavily overpriced or underpriced. And we are doing different things than everyone else; we're taking off risk or putting on risk at exactly the point when other people are doing the opposite.

How do you decide when it is the right time to buy or sell an asset?

We have a framework for deciding when we think something is cheap or expensive. We look at the attributes of individual assets or portfolios, and we look at the risks within those. We try to price those risks according to what we believe is an appropriate return in the long term. This approach leads us to be a bit more countercyclical than others. We began to think that Ireland and Spain were attractive to long-term investors about 18 to 24 months ago, which is probably about 18 to 24 months before other people started to take that view.

How do you evaluate and approach risk management?

We look at some of the more obvious risks, including vacancy in the individual asset, vacancy in the portfolio and lease rollover. One of the metrics that I quite like is to look at the current level of vacancy in the portfolio and add on the lease rollover in the next two years in an effort to "stress-test" the property. If you weren't able to re-lease that space, what vacancy would you be staring at in two years' time in your portfolio? I think that's a pretty revealing statistic. We look at development exposure and other types of income risks, and then we look at concentration risks within the portfolio. We want to have conviction in individual assets so we really believe in them, but we also look at factors such as tenant concentration, individual asset concentrations and exposures to different industries. And then, of course, we look at the leverage. We have concluded that leverage is the dominant source of risk within a leveraged property fund, and so we strive to ensure that our core funds have very low leverage, typically well below 40 percent loan-to-value, and also seek to use leverage in a smart way.

What value does the multi-manager platform bring to investors?

In addition to our direct investment capabilities, Aberdeen also offers custom and commingled fund of funds offerings. We think there are generally two ways of investing in real estate via funds of funds — core income-producing exposure and return-seeking exposure. For those who want to get core exposure, a multi-management platform is an efficient way of screening a very large universe of funds and using experts to screen those on your behalf. It's very efficient for smaller plans and those wanting to invest smaller amounts. At the other end of the risk/return spectrum is a return-seeking private equity approach, and once again the multi-manager platform has an advantage for investors because you have to get completely under the skin of the high risk/return investments you're making. So a multi-manager platform gives investors a dedicated team working to uncover any issues and mitigate the issues in the underlying funds. We think that this is especially helpful for U.S. investors looking for opportunities in Europe and Asia.

One of the biggest issues with multi-manager platforms is the extra layer of fees.

What would it cost to create your own team to do the same level of due diligence that we do for our funds? It is certainly something bigger investors can do, but there aren't many other ways of doing it, and we think we offer good value for the money. We consider our global multi-manager team as an extension of our clients' investment staff. We are their people on the ground around the globe.

Looking out over the next three to five years, where do you see the growth in the Aberdeen Property platform?

We are already a pretty large player across Europe — one of the biggest managers in the Nordic region, fairly big in the U.K. [INREV/ANREV, July 2013]. We believe that our growth within Europe is actually likely to be in the continent, particularly in markets such as Spain, where we are thinking about putting people on the ground at some point. We would certainly like to expand the business on the direct side into Asia Pacific at some point. We have been there on the multi-manager side for six years investing across the region. And then within the Americas, we have had the multi-manager platform for around three years. We don't have direct business in the Americas, and we will look to expand there at some point in the near future. Our client base is typically pension funds, insurance companies and sovereign wealth funds. They are usually focused on core investment, but we would also like to be able to offer higher return strategies in certain markets. We will be putting together more specific strategies for investors in those countries and sectors where we believe that there is a specific short-term opportunity for higher returns. ❖