

CBRE Global Investors

Recently, **Alex Eidlin**, managing director – Asia Pacific with Institutional Real Estate, Inc., spoke with **Richard van den Berg** of CBRE Global Investors. The following is an excerpt of their conversation.

Tell me about CBRE Global Investors and its history in Asia.

CBRE Global Investors is one of the largest global real estate investment managers with more than US\$90 billion in assets under management for approximately 600 institutional investor clients worldwide. We offer a full range of investment programs across the risk/return spectrum. These programs include commingled equity funds and separate accounts, debt investment, global multi manager programs and listed global real estate securities vehicles. We operate via regionally focused investment teams and employ more than 1,100 staff across 32 offices in 21 countries. CBRE Global Investors is part of the CBRE Group, which is the world's largest commercial real estate services and investment firm, in terms of 2012 revenue, with more than 100 years of experience. Our Asia business is a combination of three investment companies starting with Rodamco Asia in 1995, ING Real Estate in 1996 and CBRE Investors in 2006 coming under the umbrella of CBRE Global Investors in 2011. This experience and track record of almost 20 years is still evident in our current team, of which I am probably a good example, having started with Rodamco Asia in 1995. Over these 20 years, we have invested across Asia in most investable countries in both development and existing assets through commingled fund structures as well as separate account mandates. Since opening our first office in Asia, the combined organisation launched nine different funds and managed several different separate account mandates. In addition, we were selected as a replacement GP for two separate funds in 2009 and 2010, both of which faced financial difficulties as a result of the GFC.

What is the most important aspect when considering investment in Chinese real estate, and where do you see the opportunities now?

The Chinese economy and real estate market are supported by growth. That is fundamentally different from more mature markets and, therefore, offers a completely different set of opportunities and risks. During the past 20 years, China has had an annual economic growth rate of more than 10 percent, which has filtered down into all aspects of the real estate market. This has taken place from an extremely low base, both in economic as well as in real estate terms. Imagine that from 1950 to 1990 a real estate market did not exist in China; instead, virtually all real estate was developed by state-owned enterprises and allocated to their employees. The design and quality was often inadequate and maintenance was poor. Hence, almost 40 years of pent-up demand was accumulated in virtually every sector of China. Economic transformation since 1990 has led to the privatisation of businesses and the gradual establishment of a sizeable middle class. This is fuelling the demand for real estate — from office to housing to retail to hospitality. However, a construction boom has also taken place since the early 1990s. Fundamentally, there are areas where demand has greatly outpaced supply — or vice versa — and it is crucial to differentiate and invest in areas with favourable fundamentals.



Richard van den Berg is country manager – Greater China with CBRE Global Investors. He is a member of the Asia Executive Committee, the Regional Management Team and the Asia Investment Committee and is responsible for the performance of the portfolios in Greater China and activities in China, with oversight of the Shanghai and Taipei offices. He has more than 20 years' experience in international property management, development and investment, and serves as the fund manager of the China Opportunity Fund.

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Opportunities usually come with challenges. What are some of the challenges you see today when investing in China?

One of the challenges is to understand and interpret the government's policies, especially its overall effect on the real estate market. China is not unique in this situation as land, housing and infrastructure are being controlled or heavily influenced by the government. At times, central and local governments share different interests and objectives, so it is important to have an investment strategy which sits in the sweet spot for both. For us, that is investments that target end-users from the rising middle class, whether it be housing, commercial or logistics properties.

Even with these tight purchase restrictions and tight mortgage requirements, price corrections are minimal in China. Do you see a housing bubble there given this situation?

From an outsider's perspective, China's double-digit annual growth in residential property prices may appear to be the hallmark of a bubble. But this assessment would fail to put the data point into the context of similarly rapid income growth — a rise in wealth that may be difficult for residents of developed countries to relate with. With average annual disposable income growth of 13 percent over the past 15 years, the 10 percent annual appreciation in house prices is far less worrying. Further, China is not one market; there are many different submarkets with different supply and demand characteristics. There are more than 100 cities of more than 5 million people in China, and they each have many submarkets. Even though you might conclude that, in general, prices in first-tier cities have risen too fast, there could still be favourable investment opportunities within these cities. But it will be important to have in-depth local knowledge and a team on the ground to spot them. We do not think the Chinese market has bubble characteristics as national affordability is still quite good, consumer debt levels are low, interest rates are moderate by historic standards, and demand, especially on the back of a growing economy and urbanisation, is strong. In fact, Chinese buyers typically have a strong holding

power because of very low debt usages historically — between 1998 and 2012, the ratio of leverage used in home purchases was about 35 percent nationwide. Moreover, more than 86 million of new urban dwellers are forecast for China by EIU in the next five years [see chart to the right], which no doubt will generate additional housing demand. However, in a country with the world's largest population, there are inevitably areas where the opposite is true and investors should stay away, maybe for many years to come.

Turning to your company's investment philosophy, what is unique about CBRE Global Investors in Asia?

In short, it is our true long-term commitment to Asia that has enabled us to assemble a team of loyal real estate professionals over the years. We have built a solid, proven performance track record across up and down market cycles. The Asia region is possibly unique in that the maturity and development level of the real estate markets vary considerably across countries. Furthermore, government involvement in some of these countries has created significant hurdles with regard to licenses and capital flow restrictions for foreign investors. As a manager, this requires having reliable and experienced professionals on the ground while maintaining the highest compliance and risk management standards. We have diligently built up our teams of professionals across the region, which has earned us the trust of investors and partners. Another key element is that most of our decision making is done by our regional management team and investment committee. This enables us to act quickly should an opportunity presents itself while still complying with the international standards for which the CBRE Group is known for. Finally, as a firm we put a lot of emphasis on the importance of our independent in-house strategy and research team in setting out investment strategies as well as vigorous involvement in the entire investment process, especially in the underwriting of new investments. This ensures strict investment discipline and objectivity, which we believe are the most important factors to ensure long-term successful investment performance.

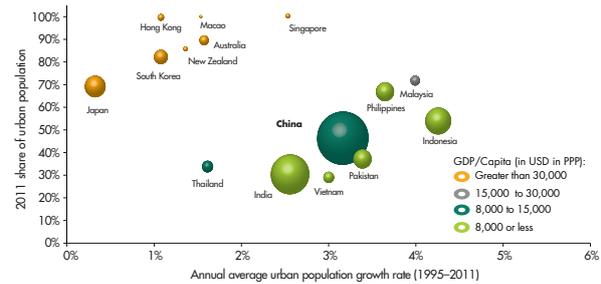
What is your investment process?

Our overall investment process combines both a top-down and a bottom-up approach. For a top-down approach, a strategic framework is constructed as a general guideline to kick off the process. In addition, our strategy and research team provides fundamental analysis that will integrate macroeconomic factors such as GDP, government policies, affordability, supply and demand figures, etc, and formulate them into a sectoral and regional strategy with specific risk and reward objectives in mind. Then the other disciplinary teams drive the bottom-up approach. The acquisition team provides deal availability, the asset management team offers value enhancing and execution capability, the finance team considers financial structures and regulatory constraints, and our internal investors services team makes sure investors' demands are met accordingly. We have a regional investment committee chaired by our Asia CEO, which ensures specialists are adequately involved during the entire process and also that decision making takes place in a timely manner — which is key for doing business in Asia.

What is your track record, particularly in China?

We started our Asian business in Hong Kong and China in 1995 and 1996, respectively. We initially

China's share of urban population and growth rate within the context of Asia Pacific



Note: Size of the circles represents the urban population in each country. Sources: Economic Intelligence Unit, United Nations Development Program, CBRE Global Investors

invested with our own balance sheet and subsequently for various regional and China-focused commingled funds. We have invested in every real estate sector, developed projects on our own and in partnership with Chinese developers, and also acquired standing income-generating assets. We have encountered various bull and bear markets, such as the Asian financial crisis, the SARS period, the latest global financial crisis and numerous government interventions across different market. Obviously, the realised returns of investments vary in relationship to the type of investments and timing, but we are proud to say that on a weighted average our net return of all of our China investments stands at over 15 percent, in renminbi. Just prior to the global financial crisis, between 2006 and 2008, we invested in nine mixed-use and residential development projects, of which we have realised eight, providing net returns ranging between 5 percent and 25 percent, in renminbi. We believe the returns from our investments in this period of severe market stress help demonstrate our ability to ride the up and down cycle.

What comes next?

Although we believe China's rising middle class will continue to provide great investment opportunities in the years to come, changing market conditions and government policies are opening up interesting opportunities in areas which have not existed before. The latest government policies are intended to cool off the speculative segment of the residential markets, especially in the first-tier cities, while encouraging mixed-use developments to ensure more efficient land-use. Further, en-bloc sales of commercial property were quite rare historically, as these largely depended on foreign players, yet local insitutional investors have been encouraged to invest in income-generating real estate, thus opening up exit opportunities that hardly existed before. We continue to favour an opportunistic strategy with a combination of mixed-use development projects in first- and selected second-tier cities, existing mispriced commercial investment in first-tier cities, residential developments in second- and third-tier cities, and logistic developments in infrastructure hubs around first-tier cities. ❖

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