The currency impact

Cross-border real estate investment returns
June 2015
Currency moves help lift canny global real estate investors

Outlook for 2015

Foreign exchange has been volatile over 2014 due in part to major central banks adopting different economic policy changes. While the US Federal Reserve had halted its quantitative easing (QE) program, the Bank of Japan is still pursuing its QE policy and the European Central Bank has begun buying German and Italian government bonds. These policies have been instrumental in driving the US dollar up against both the Yen and the Euro. The first quarter of 2015 has seen a sharply falling Euro and a strong US Dollar, which traded higher against all the major currencies except the Swiss Franc.

What does this mean for real estate investors? Are there certain cities that particular investor groups should be putting on their investment radar to ride on the expected currency gains, or are they better off investing domestically?

What matters to investors diversifying into real estate outside their home markets, is the combination of currencies and total returns from property. For example, what return does a Japanese Yen investor get on a one year total return basis when placing his or her money in the Sydney office market? For a UK Pound investor who buys into the Singapore market, what is his return once the round trip is made from Pounds into Singapore dollar real estate and then back into Pounds?

We have crunched the numbers for total returns for Prime/Grade A office markets in ten cities in Asia Pacific in eight currencies - US dollars, Euro, Pound Sterling, Australian dollar, Singapore dollar, Japanese Yen, Renminbi and South Korean Won - and compared them against the returns a local currency investor would have got.

In 2015, we expect real estate transaction volumes to continue rising, when measured in local currencies, however the rate of global growth may decelerate due to volumes in the Euro area looking lower when recorded in USD. The rate of increase in USD could moderate to between 5-10%, and reach between US$740-760 billion.

The Fed’s impending decision on whether there will be interest rate hikes from the current low of 0.25% will have global consequences. The prospect that interest rates could rise anytime between this summer and the end of the year has already led to the US Dollar surging against the Pound and the Euro. This will also have a significant impact on foreign capital flows, leading to consequences for real estate markets.

JLL’s real estate forecasts for 2015 show that foreign investors denominated in Euros will have enormous advantage in most markets, with overall returns of between 23% and 43% for investment in Prime/Grade A office assets in major global cities. The outlook is also favourable for investors using British Pounds, Japanese Yen and Australian Dollars, which are forecast to yield in the 7-25% range across major markets.

- by Dr Megan Walters and Ankita Prasad

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2015 forecast 1 year holding period returns

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<thead>
<tr>
<th></th>
<th>Local</th>
<th>USD</th>
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- Below -5%
- -4% to 0%
- 1% to 5%
- 6% to 10%
- 11% to 15%
- 16% to 20%
- 21% to 25%
- Above 26%
Looking back at 2014

The final quarter of 2014 saw a new record for global real estate investment markets, with transaction volumes of US$230 billion recorded. This brought the total volumes for 2014 to US$710 billion, a 20% increase on 2013.

In keeping with the strong currency depreciation, Euro and Yen investors had high returns in all Asian markets, particularly in Australia, China, India and Korea. USD investors would have been best off investing locally due to their strong currency; they had lower returns than the local property returns in all key Asian markets, as well as in London.

While real estate investment in local markets with local currency produced positive returns overall, some markets were more lucrative than others. Investment in Prime/Grade A office assets in Tokyo using Japanese Yen returned 23% on a total return basis in 2014, reversing the trend of previous years. However, investment in Hong Kong offices with the Hong Kong Dollar would have returned 3% on a total return basis in 2014, the weakest performance recorded. (See Table 1).

Some Asian investors could secure larger returns by taking their capital offshore, taking advantage of relative currency movements. The biggest overall return was from Japanese Yen investors in Shanghai and Seoul Prime/Grade A offices, which produced returns of 26%. Australian Dollar investors had the highest returns in Beijing, Shanghai and Seoul (19-20%), while Korean Won investors performed best in Shanghai, with one-year returns of 15%.

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<thead>
<tr>
<th>Market &amp; currency</th>
<th>Local Investment Return</th>
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<td>Tokyo</td>
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A good example of currency working for investors can be found in the sale of the Arco Tower Office and Meguro Gageen wedding complex. Mori Trust acquired the complex in September 2014 for JPY130 billion (close to US$1.25 billion), and sold it to LaSalle Investment management / CIC for JPY140 billion (US$1.18 billion) just five months later. Because of currency movements, LaSalle Investment Management / CIC saved 6% in US Dollar terms, while Mori Trust realized 8% in Japanese Yen.

### 2014 1 year holding period returns

<table>
<thead>
<tr>
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Market commenters in foreign exchange are predicting a 3% depreciation in Asian currencies over 2015, with expectations of depreciation even higher if the tightening of US monetary policy leads to larger outflows from the Asia Pacific region. The Federal Reserve is expected to hike interest rates in the second half of 2015 after unwinding its quantitative easing program. By contrast, most Asian central banks are acting in the opposite manner by implementing easing measures. The Bank of Japan has undertaken massive stimulus efforts, the People’s Bank of China has cut interest rates for the third time in six months, South Korea’s central bank lowered its interest rate to an all-time low and rate cuts are possible in Thailand and Australia.

Outlook for currencies

Currency movements against the USD

- The Chinese Yuan is expected to marginally appreciate in the second half of 2015 as the USD starts weakening
- The Japanese yen’s losses are likely to have reached the end and are expected to rebound by year-end
- The Korean won is expected to continue to slide further and fall to 1,140 won against the USD
- The longer term outlook for the Australian dollar remains challenging with the RBA stating that the currency remains overvalued and must decline substantially
- The MAS is likely to allow the Singapore dollar to continue appreciating at a modest pace as GDP is on track to grow by 2-4% in 2015
- Market commenters predict that the Euro will fall by 10% during the next 12 months with respect to the USD
- The Pound is likely to come under pressure in 2015 with the UK’s largest trading partner, the Eurozone, posing a risk
“Investors are finding there’s more property available for their money in certain markets thanks to the continuing strength of the US dollar. The strong dollar is influencing activity in the Euro Zone, Japan and Australia, where local market activity has increased.”

Arthur de Haast,
Head of the International Capital Group
USD investors had the highest five year annualized returns in Beijing – 24%

USD investors had foreign exchange losses in all major Asia Pacific markets in 2014

Strong currency led to USD investors being best off investing locally
Euro investors had the highest total returns in Shanghai in 2014 – 22%

Euro investors had the highest five year annualized returns in Beijing – 28%
GBP investors had fairly consistent returns in most Asia Pacific markets.

GBP investors had the highest total returns in Shanghai in 2014 – 15%

GBP investors had the highest five year annualized returns in Beijing – 25%
Who reaped the highest returns in London?

“As we have seen US investors are already the biggest cross-border investors globally, and the double digit rises we have seen in the currency against their favourite destinations such as the Euro, Pound, Yen and Australian Dollar indicate further outbound movement of capital into these locations during 2015.”

Stuart Crow,
Head of Asia Pacific Capital Markets

2014 one year holding period return - London

Japanese Yen investors performed best in the London Grade A office market in 2014 with total returns of 24%
Local markets proved to be attractive for RMB investors

RMB investors had the highest total returns in Shanghai and Seoul in 2014 - 12%

RMB investors five year annualized returns (2010-2014)

RMB investors had the highest five year annualized returns in Beijing – 22%
Capital outflows from China into foreign real estate has increased 160% in 1Q 15 compared to the same period last year and any further appreciation of the RMB will further drive capital flows into real estate abroad. Naturally a stronger yuan makes overseas assets more affordable for Chinese buyers.

Alan Li,
Head of Investment, Shanghai

Who reaped the highest returns in Beijing and Shanghai?

Japanese Yen investors performed best in the Beijing Grade A office market in 2014 with total returns of 25%

Shanghai outperformed Beijing with Japanese Yen investors getting total returns of 26% in the Shanghai Grade A office market in 2014
JPY investors had the highest five year annualized returns in Beijing – 31%

JPY investors had the highest total returns in Shanghai and Seoul in 2014 – 26%

JPY investors bagged the highest total returns in Shanghai and Seoul in 2012-2014

JPY investors one year holding period returns 2012-2014

JPY investors five year annualized returns (2010-2014)
“The government’s resolve to keep the yen weak has also made real estate more affordable. Japan is cheap considering how much property prices have gained in Singapore and Hong Kong.”

Akihiko Mizuno, Head of Japan Capital Markets

Who reaped the highest returns in Tokyo?

Japanese Yen investors performed best in the Tokyo Grade A office market in 2014 with total returns of 23%
AUD investors five year annualized returns (2010-2014)

AUD investors had the highest five year annualized returns in Beijing – 26%

AUD investors one year holding period returns 2012-2014

AUD investors had the highest total returns in Shanghai in 2014 – 20%
Australia’s record low interest rates and the depreciation of the Australian dollar since late-2014 will continue to spur overseas demand for real estate even as bond yields have risen.”

Andrew Ballantyne, Head of Capital Markets Research, Australia

Who reaped the highest returns in Sydney and Melbourne?

Japanese Yen investors performed best in the Sydney Grade A office market in 2014 with total returns of 23%

Japanese Yen investors performed best in the Melbourne Grade A office market in 2014 with total returns of 23%
SGD investors had the lowest returns in their home market.

**SGD investors one year holding period returns 2012-2014**

![Graph showing SGD investors one year holding period returns 2012-2014]

**SGD investors five year annualized returns (2010-2014)**

![Graph showing SGD investors five year annualized returns (2010-2014)]

**SGD investors had the highest five year annualized returns in Beijing – 23%**

**SGD investors had the highest total returns in Shanghai in 2014 – 15%**
Who reaped the highest returns in Singapore?

“The relative stability of the Singapore dollar which has depreciated by about 5% compared to the US dollar over the last 18 months, reinforces Singapore’s status as a safe haven for investors, particularly in light of other regional currencies that are down 15% to 25% over the same period.”

Greg Hyland,
Head of Singapore Capital Markets

2014 one year holding period return - Singapore

Japanese Yen investors performed best in the Singapore Grade A office market in 2014 with total returns of 15%
KRW investors had the highest five year annualized returns in Beijing – 23%

KRW investors had the highest total returns in Shanghai in 2014 – 15%

Korean investors performed well in China.
“With the appreciation of the won likely to continue into 2015, foreign investors into Korea are set to reap high property returns. There is likely to be stable growth in the market due to strong economic fundamentals and the country’s improving international standing.”

Yongmin Lee, Head of Research, Korea

Who reaped the highest returns in Korea?

Japanese Yen investors performed best in the Seoul Grade A office market in 2014 with total returns of 26%
Who reaped the highest returns in India?

Japanese Yen investors performed best in the Delhi Grade A office market in 2014 with total returns of 24%

Who reaped the highest returns in Hong Kong?

Japanese Yen investors performed best in the Hong Kong Grade A office market in 2014 with total returns of 19%
Methodology

In order to calculate the total one-year holding period return, the change in capital value over the year has been added to the starting yield, with the assumption that the yield is consistent throughout the period. It has not been adjusted on a q-o-q basis.

The five year annualized returns are calculated using the compound annual growth rate method.

Submarkets

- Melbourne: CBD Prime
- Sydney: CBD Prime
- Beijing: CBD
- Shanghai: Pudong
- Hong Kong: Central
- Singapore: Raffles Place
- Seoul: CBD Prime
- Tokyo: 5-kus
- Delhi: CBD
- Mumbai: CBD
- London: West End

Sources

- JLL REIS data - rents, capital values, yields
- Oxford Economics - foreign exchange

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