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# Are Reits with overseas assets unloved in Singapore?

By Sing Tien Foo

A REAL estate investment trust (Reit) is an investment vehicle that pools capital together to invest in income-generating real estate assets, which are illiquid, immobile, and lumpy. A Reit is structured to facilitate efficient flow-through of income generated from physical real estate directly to investors. The distributable earnings are tax-free at source in Singapore and other Reit markets like the US, Australia, and Japan.

Singapore Reits (S-Reits) invest in real estate, which must make up at least 75 per cent of the portfolio. At the outset, S-Reits focus on real estate investments by type, leveraging experience and expertise in a particular sector and local market.

The "pure-play" S-Reits appeal to institutional investors who add new real estate market types not yet included in their portfolios. S-Reits also give retail investors opportunities to invest in commercial real estate, such as Vivo City, Suntec City, Raffles City, etc, which will otherwise not be possible with their limited capital.

As local sponsors gained confidence from the early S-Reit listings, they set up new Reit vehicles that hold overseas real estate. These Reits listed before the global financial crisis in 2007 are broadly divided into 2 groups.

The first group holding geographically diversified real estate in the logistics, warehouse, and hospitality sectors includes Frasers Logistics & Commercial Trust (previously known as Frasers Logistics & Industrial Trust) and Ascott Residence Trust.

The second group holding sector-focused real estate outside Singapore includes CapitaLand China Trust (previously known as CapitaLand Retail China Trust), Lippo Malls Indonesia Retail Trust, Ascendas India Trust, and First Reit.

As the S-Reit market grows and gains reputation, more foreign Reits package overseas real estate portfolios and list them on Singapore's bourse. IReit Global was the first pan-European real estate portfolio Reit listed on Singapore's bourse in August 2014. City Developments acquired half of the stake in IReit's asset manager from Tikehau Capital, a French alternative asset management group, in 2019.

China sponsors followed the bandwagon with the listings of 4 China-focused Reits on Singapore's bourse, including BHG Retail Reit in 2015, followed by EC World Reit in 2016, Dasin Retail Trust in 2017, and Sasseur Reit in 2018. In recent years, Reits with real estate assets located farther away in the European and US markets emerged to tap capital via listings on Singapore's bourse. The small size of the local real estate market pushed more local Reits to pursue growth through acquisitions of properties outside Singapore. More S-Reits looked abroad for promising investments. Foreign real estate acquisitions hit a record high of S$11.8 billion, accounting for about 91 per cent of the total assets acquired in 2021.

Today, only 3 of 43 Singapore-listed Reits (that is, Far East Hospitality Trust, Frasers Centrepoint Trust, and Sabana Industrial Trust) hold 100 per cent of Singapore real estate in their portfolios.

The market seems to have significantly under-valued overseas real estate relative to those in Singapore. The charts show that Reits holding overseas real estate were priced at significant discounts to book values, despite offering high dividend yields. The market price to book value ratio and the dividend yield of the overseas-centric Reits average at 0.766 times and 7.08 per cent as of May 20, 2022, compared to 1.054 times and 4.59 per cent, respectively, for Reits with some exposure to local real estate markets.

The undervaluation of overseas-centric Reits could be explained from the perspectives of diversification strategies, local bias in stock valuation, and control spans of Reit managers.

### Geographical diversification

Geographically diversified real estate is not always effective in reducing systematic risks, especially in markets where real estate prices are highly correlated. Some Reits choose strategies to avoid value dilution by adding real estate of the same type from other countries. Commercial and retail Reits with a high concentration of real estate in Singapore include Mapletree Commercial Trust, Frasers Centrepoint Trust, OUE Commercial Trust, and CapitaLand Integrated Commercial Trust. These Singapore-focused Reits appeal to institutional investors who already hold diversified real estate portfolios outside Singapore. But Reits with geographically diversified real estate may not fit into the diversification strategies of these investors. Diversification outside Singapore may not add value to some Reits.

However, other Reits in the hospitality sector, such as Ascott Residence Trust and Frasers Hospitality Trust, and those in the logistics and warehouse business, such as Frasers Logistics & Commercial Trust, and Mapletree Logistics Trust, hold real estate in different markets for strategic reasons, not for diversification motives. Firms need to take up warehouse and logistics space across countries to support the supply chain operations of businesses. Diversifying real estate outside Singapore creates a competitive edge and adds value to these Reits' portfolios.

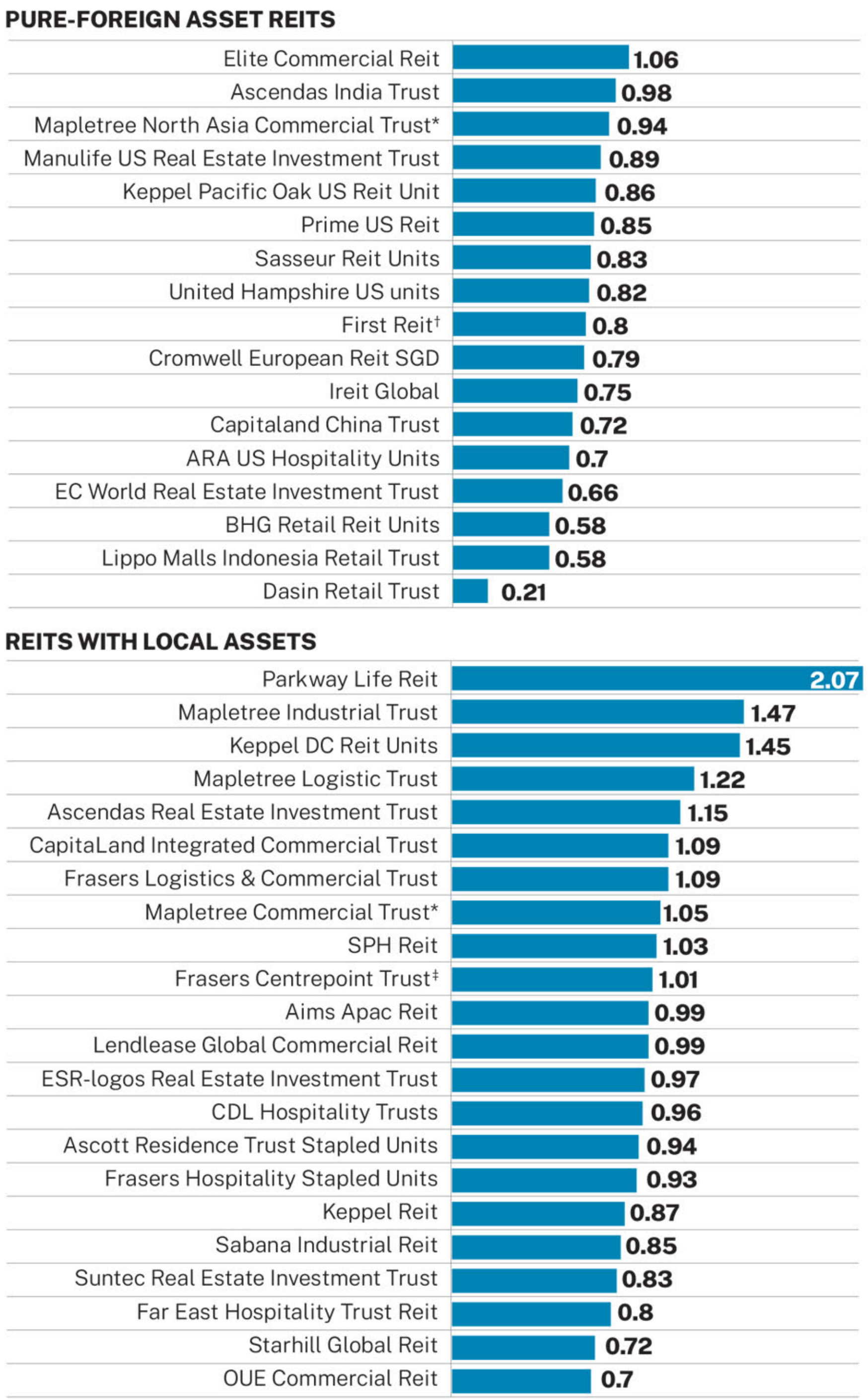
### Local bias

Demand for physical real estate space is mainly derived from local economic activities. Shopping mall managers need to know not just purchasing power, but also the culture and taste of residents in local markets. "Local bias" of investors and analysts adversely distorts the valuation of foreign Reits. Investors, especially retail investors unfamiliar with overseas real estate, are more hesitant to invest in foreign Reits. Stock analysts are also more reluctant to cover foreign Reits, especially those owning real estate in far-away markets.

### Control spans

Reit managers could overstretch their resources and control spans when remotely managing real estate portfolios distributed across different regions. A local management team played an instrumental role in supporting local operations of foreign Reits, especially dur-

**Market price to book value ratio**
(As of May 20, 2022)




*† First Reit holds only 3% of its real estate portfolio in Singapore.*
** The asset holdings of Mapletree North Asia Commercial Trust and Mapletree Commercial Trust were before the merger, which was approved at the extraordinary general meeting on May 23, 2022*
*‡ The asset holding excludes the Hektar Reit shares, a Malaysia retail Reit, owned by Frasers Centrepoint Trust*
Source: Refinitiv, SGX and the Author

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ing the periods when the Covid-19 border controls were in place. For example, Cromwell European Reit establishes property management offices in 17 cities across 11 countries to build long-term relationships with tenants and identify new investment opportunities in foreign markets.

Foreign Reits could trail local rivals in generating value for overseas real estate portfolios, which in turn causes the undervaluation of their foreign assets.

Reits that outsource management and property services of foreign properties to third-party managers may not be able to compete effectively with their local rivals. It is also harder for Reits to scale up their operations and develop a competitive edge without the support of a local team.

The high dividend yield and the underpricing of overseas real estate put a lid on the growth of foreign Reits. While foreign Reits find it a disincentive to inject new assets into their portfolios, local Reits could still leverage the yield gap between local and foreign real estate to expand overseas.

However, they should not pursue overseas growth strategies at the expense of diluting the values of existing Reit unitholders.

They must balance the growth against possible risks in holding foreign real estate in their portfolios.

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