AEW RESEARCH

Asia Pacific Market Perspective

Q1 2022

AEW – Asia Pacific Market Perspective – Q1 2022

AEW

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Optimism for the Region Holds

Most of Asia Pacific Has Returned to Normal

- Positivity is building in most of the Asia Pacific region. There is more normal daily activity as borders reopen, pandemic-related restrictions are eased, and people return to the office and retail centers.
- Economic growth is underway, with most of our monitored markets adapting to a lifestyle of living with COVID-19. This renewed activity is benefiting service consumption and international travel after several years of limited activity.
- Risks have skewed towards China due to a prolonged period of movement restrictions to help contain the spread of the virus in some of the country's major cities.

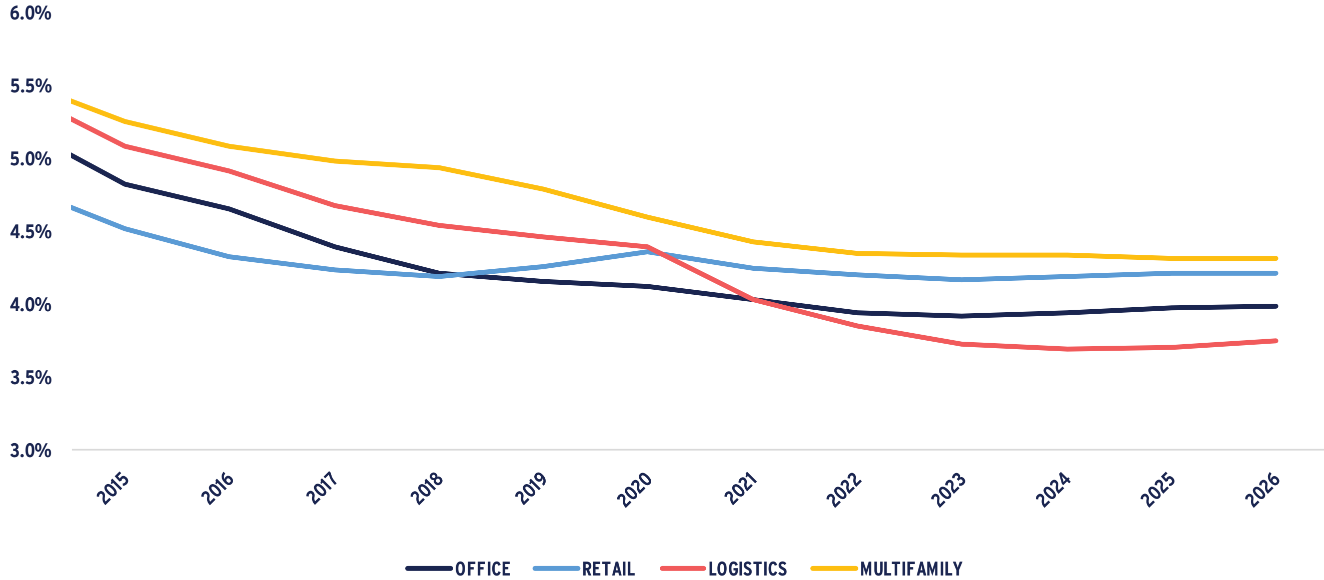
Property Investment Activity Stays Healthy, Uneven Allocations

- 2022 has started out well with the pace of transaction activity closely matching 2021. In Q1, there was about USD27 billion of income producing real estate transactions across major markets in the region.
- Sydney and Singapore saw a sharp increase in deals from last year, while Seoul has maintained its status as the region's most actively traded market. In contrast, Beijing, Hong Kong and Tokyo have seen a pull-back in activity in Q1.
- The uneven performance is likely to continue, especially as investors eschew markets in Greater China due to geopolitical tensions and less favorable local market fundamentals.
- Overall, we expect to see a 10 to 15% increase in transaction volumes for Asia Pacific's major markets, with stronger year-on-year allocations to Australia, Japan and Singapore.

Front Loaded Returns, Followed By a Lower Return Environment

- Recent surveys on investors' intentions indicate more confidence on a recovery in the office sector, and potentially a stronger allocation to retail and hotel investments in 2022, riding on the recovery in travel and spending. Compared to 2021, we can also expect more assets to be put onto the market, as a higher proportion of investors have indicated a willingness to sell assets this year.
- Average debt costs have increased by 0.5 to 0.8%-points in the last quarter, but for most cases, debt costs are still below property cap rates. Investors continue to look through higher debt costs because of expected NOI growth. Outside of China, property yields are either holding firm or continue to see mild compression.
- Most of the region's property markets continue to look attractive on a risk adjusted basis. Expected total return for our markets average 6 to 7% p.a. for the next five years, with returns front-loaded in the next three years followed by a lower return environment.

**ASIA PACIFIC YIELDS BY SECTOR
2022 TO 2025F**



Source: AEW Research, JLL, PMA

Growth Maintained but Pressure Points Rise

On The Growth Pathway, Risks In China Mount

- GDP growth for AEW's monitored markets in the Asia Pacific region is expected to average 3.0% in 2022. Rising fuel costs, supply chain disruptions and higher inflation are key risks in the near-term.
- Despite downgrades from the start of the year, China's year-on-year growth will still be the strongest in our region. For Australia, rising commodity costs have been positive for GDP and it is the only market in our region with an upgrade in growth outlook over the past month.
- Outside of China, most countries have successfully pivoted to a living with COVID strategy. As such, we expect minimal future disruptions to everyday life and hence, an opportunity to recapture growth. Meanwhile lockdowns in China have impacted already fragile supply chains and if prolonged, may threaten to lower domestic and foreign demand, with the risk of spilling over into regional economies.

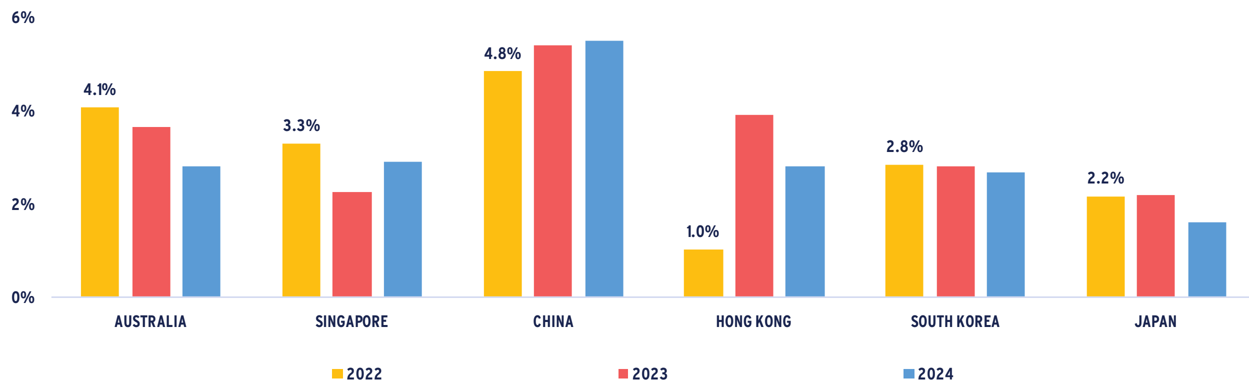
Recovering Labor Markets and Consumption Outside Greater China

- Consumption activity has picked up, most notably in Singapore and Australia, as retail sales for Q1 exceed expectations.
- Labor markets are rebalancing, supported by a return to normal and easing of border restrictions. In Singapore and Australia 41,000 and 149,000 jobs were created respectively in Q1. In South Korea, year-on-year employment increased for the 13th consecutive month.
- While labor market weakness was present in Hong Kong and China for Q1, the following quarters do show promise of improvement. In China, government departments have been instructed to provide aid to manage unemployment – these stimulus activities include cash handouts to individuals and businesses.
- Hiring is expected to maintain momentum in Q2. According to the Manpower Group Survey, the Asia Pacific region showed +28% increase in hiring intentions over the quarter with a positive employment outlook across all our monitored markets.

Fiscal Support and Monetary Policy Stance Diverges

- Although inflation is rising globally, it has been less prominent in Asia Pacific when compared with the U.S. and Europe. To a certain extent, this is due to government interventions, as well as supply chains in the region being less affected by Russia's invasion of Ukraine.
- Similar to commentary last quarter, monetary policy is divergent in our region.
- Central banks in South Korea and Singapore started tightening monetary policy last year, ahead of the Fed. The Reserve Bank of Australia (RBA)'s previously dovish tone took a turn in Q1, and rates were raised for the first time in 11 years in May 2022. Meanwhile, Japan and China's central banks have reinforced the need to support business activity to shore up growth and will maintain loose monetary policy. Alongside this, currency depreciation for the JPYUSD and CNYUSD is likely to extend further.

ASIA PACIFIC GDP GROWTH
2022F TO 2024F



Source: Oxford Economics, as of May 5, 2022

Property Fundamentals Turn Favorable in More Markets

Office

Bustle of CBD's Return

Apart from China, crowded streets are commonplace again in CBDs as more people return to the workplace in the Asia Pacific region. Reflecting this change, average public transit and workplace mobility across our monitored markets (ex- China) are up 13%-points and 11%-points respectively compared to the start of 2021. In Singapore, all social distancing measures have been removed and the government is encouraging all employees to return to the office by the end of April. Meanwhile in Australia, office occupancy is creeping up again with the latest numbers from the Property Council of Australia (PCA) showing a doubling of occupancy rates from February to March 2022.

Demand From New Economy Sectors Leads

Demand for space in the region is expected to grow by 13 million square feet per annum over the next three years, about 75% higher than the past three-year (2019 to 2021) average. Across all markets, demand from new economy sectors is generating an expansion in occupied space – these include big data, cloud platform, social media, biotechnology, and pharmaceutical. As these occupiers can be in non-CBD locations, we see investment opportunities tilting towards metro or suburban business hubs.

Uneven Performance in 2022

For 2022, we see Singapore, Australia and Seoul office markets outperforming the rest. Singapore is already nine months into its office rent upcycle while Seoul did not have a pandemic-related correction unlike the other markets. Both are seeing healthy leasing activity in 2022 and are expected to see vacancy rates contract as future supply levels drop. Meanwhile in Australia, office rents are expected to bottom in the next couple of months as leasing activity improves and business confidence returns. For Japan and Greater China, markets are expected to remain tenant favorable- underlying vacancy remains high, new demand is limited and there are near-term supply risks.

Logistics

Construction Cost Increases and Delays Aplenty

Worries of supply overshooting demand in 2022 in markets like South Korea and Australia are abating, due to supply chain disruptions and increased construction costs. In South Korea for example, we had initially expected 28 facilities to complete in South Korea's western region between 2021 and 2022, but due to delays, only 17 facilities will be finished within this time frame - the implications for these delays are positive for landlords with the pent-up demand environment expected to continue for the year ahead.

Still More Room For Growth

The sector has seen the strong price growth in the last two years, with average capital values up 10% to 15% p.a., contributing to outsized returns. While there is caution on the performance of the sector going forward, the underlying fundamentals are still positive. Forecast returns for 2022 to 2024 are highest for the logistics sector, but capital value growth is moderating.

Multifamily - Japan

Migration Patterns Return

The multifamily sector is starting the year on a positive note with net migration into Greater Tokyo up by around 10,000 persons in Q1 compared to the same period last year. The most positive net inflow is being seen in the Tokyo's 23 wards, where there were initial concerns that an uptake of work-from-home might result in Tokyo's inner-city neighborhoods losing its pull. This will contribute to positive leasing demand within the city center, On the investor side, we expect another year of strong cross-border investor activity, especially as fundamentals remain solid, the cost of debt is expected to remain low, and currency remains in favor (with the JPYUSD at its weakest levels since 2002).

Retail

Increasingly Sought After By Smaller Investors

Although some fundamentals have improved, the sector remains challenging. Investors that were previously active in the space have reduced exposure and from the select that are still interested, they are targeting fewer markets. In Q1, there have been close to 30 transactions of value greater than USD 50 million, but few have been bought by institutional investors, but rather private capital or high net worth individuals.

Office

AUSTRALIA: Investment activity underscores the confidence in occupier markets

- Positive indicators such as unemployment, jobs growth and better business sentiment are contributing to a healthier leasing environment. Both Melbourne and Sydney saw an increase in enquiries in Q1. This will translate into new leases in the coming months.
- Capital markets are responding to the sector's recovery. In Q1, Sydney saw a major pick up in investment activity. Melbourne by comparison, is a few months behind in its rental recovery and is expected to see several large deals exchange hands in Q2.

SINGAPORE: Strongest rental growth in the region

- Singapore is nine months into its multi-year rent upcycle. Limited supply of quality space in the CBD will support another 8 to 10% rental growth p.a. in the next two years (ending 2023).
- Given the healthy occupier conditions, investment momentum has continued to build in Q1, with close to ten deals of value >$200m transacted. Q2 is expected to be another active quarter with several deals already announced.

HONG KONG: Market remains tenant favorable

- The recent Omicron outbreak has worsened the near-term outlook as businesses delay decision making and reopening plans with the mainland get further pushed back.
- A record amount of vacant space alongside strong supply in the decentralized areas in 2022 (with limited pre commitments), means the market is likely to remain tenant favorable in the near-term.

CHINA: Leasing weakness in H1 reduces rental growth

- Shanghai's strict lockdown to manage the COVID-19 outbreak has heavily impacted leasing activity in the market. Demand for the full year will probably conclude 20% short of initial forecasts, dampening rent growth prospects.
- In Beijing, where conditions are slightly better, only select submarkets like Lize, Guomao and Finance Street saw decent take-up in Q1.
- In both markets, investor interest has dampened, and we expect liquidity to be constrained in the next few months.

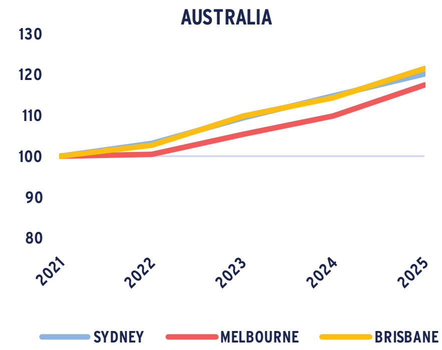
SOUTH KOREA: Favorable fundamentals support rental growth

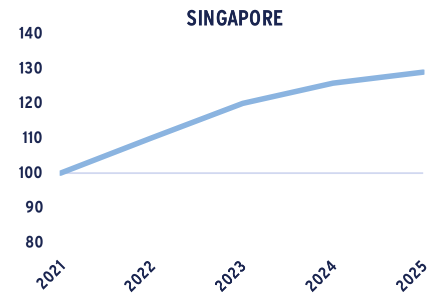
- Occupier markets continue to expand, benefiting the three-core as well as outer lying submarkets like Bundang, Magok and Pangyo Tech Valley. CBD and YBD have both reached single digit vacancy, while in GBD vacancy rates have dropped below 1%.
- With supply in 2022 falling to its lowest level in more than ten years and better than-expected demand, rents are expected to grow > 3% p.a. in the near-term, higher than typically seen in Seoul office.

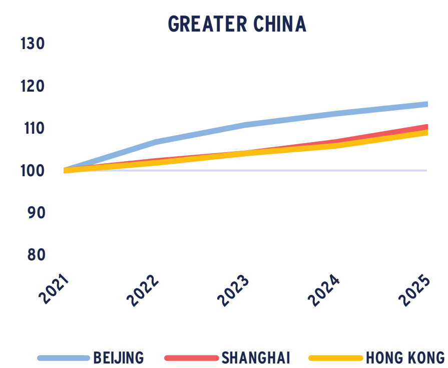
JAPAN: Upcoming supply risks

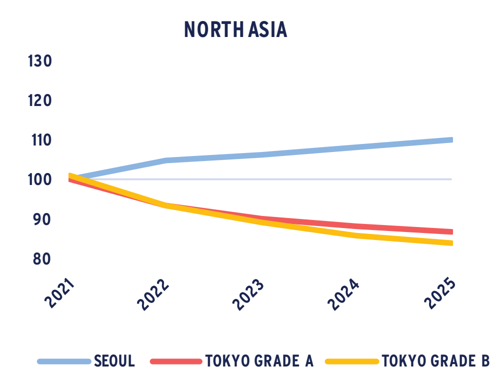
- Tokyo: While there is evidence of demand supply rebalancing in Q1, this is expected to be short-lived. More vacant Grade A space is expected to be returned to the market in the coming months as larger firms concretize their hybrid working plans and reduce their requirements. Grade A in 2022.
- With more vacancy expected in H2, and strong supply levels from 2023 to 2025, prospects for a rental recovery are weak.

OFFICE RENT INDEX (2021 - 2025F)
2021 =100









Source: JLL, Q1 2022

Logistics

AUSTRALIA: Competition for assets to result in continued cap rate compression

- After increasing by 8% to 10% p.a. in the last two years, the rent cycle in Melbourne and Sydney is expected to extend for the next three to five years (3.0% to 3.5% p.a.) supported by continued occupier demand and higher land values.
- Because of favorable rental prospects and the continued investor interest, the rising debt cost environment is unlikely to trigger a repricing in the sector. We forecast yields to continue to compress in the near-term.

SINGAPORE: Healthy demand environment

- Business Parks: Demand for well-located and newer spaces continue to be sought by growing industries, widening the rental gap between prime and sub-prime buildings.
- Logistics: Demand for warehouses remained healthy in Q1 as food, pharma and semiconductor firms increased their storage requirements. Near-term supply is low, and demand is expected to remain strong, causing upward rental pressure.

HONG KONG: Investment pace slows in Q1

- Expansion of online retailers offset the weakening external trade sector. Amid the low supply environment, vacancy rates are expected to continue to remain low, supporting rental growth.
- The industrial sector saw the highest level of investment activity compared to other sectors, but volume dropped about 30% over the quarter with just two enbloc deals completed. We expect volumes to increase in the coming months as pandemic related risks ease off.

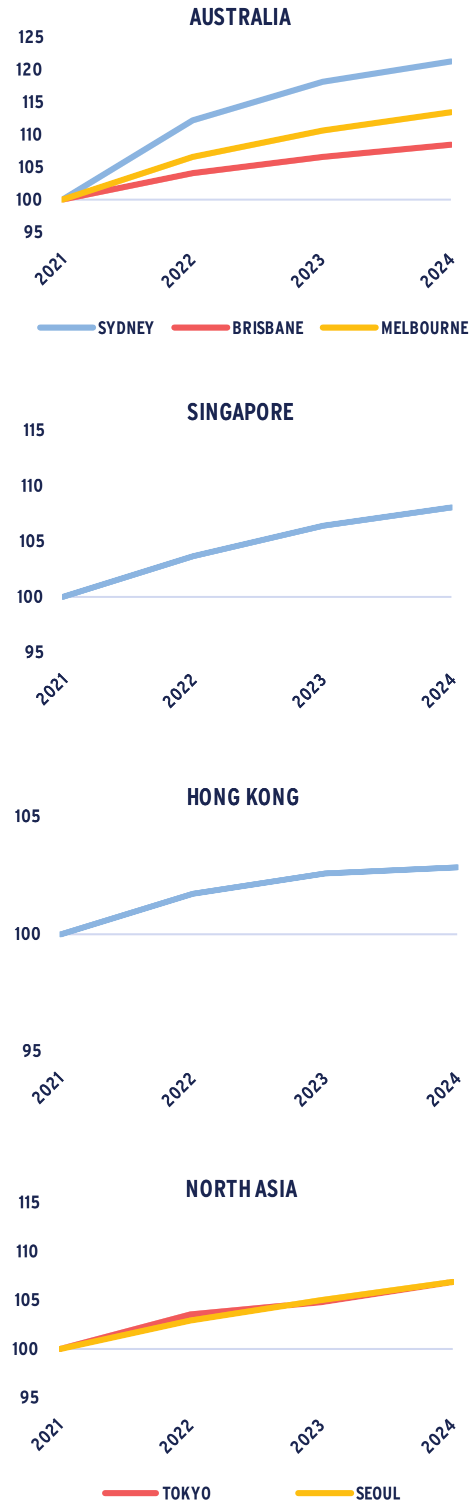
SOUTH KOREA: Construction delays lower near-term supply risks

- There is evidence of pent-up demand with low vacancy rates (2.7% as of Q1 222) restricting take-up in existing facilities. Construction delays have resulted in new supply for 2022 contracting by 10%. More occupiers are committing to leases in projects still under construction. Pre-lease rates for 2022's supply stands at 25%.
- With low vacancy rates and supply risk less of a concern than initially thought, the market remains landlord favorable in 2022. Landlords are also further embedding the rising operating costs into CAM fees, pushing rents up further.

JAPAN: Modern stock limited, still good demand for Grade B facilities

- Supply and demand balance for new stock remains tight with strong expansion demand from e-commerce firms, retailers, and manufacturers. About 65% of the new supply expected in 2022 has already been pre-leased.
- A large proportion of older stock exists, but vacancy in these assets is elevated. While rent growth potential is minimal, these assets are affordable on a per square foot basis and could benefit from value-add upgrades.

LOGISTICS RENT INDEX (2021- 2024F)
2021 =100



Source: JLL, as of Q1 2022

Retail

AUSTRALIA: Gaining traction among investors again

- Growing retail sales sets a positive picture for Q1. Spending has been driven by discretionary categories such as clothing and footwear, café and restaurants as well as department stores.
- Rents have stabilized across most retail subsectors in Australia (except for large-format retail or neighborhood malls which have been increasing). Incentives are likely to remain stable for 2022 with a broader rental recovery expected by 2023.
- Investors are viewing the asset class more positively today alongside several encouraging developments such as reopening of international borders, employees returning to office, and strong labor market conditions. Transaction volumes for the quarter were up 10% compared to the same period last year, with prime CBD assets seeing compression of around 10 to 20 bps.

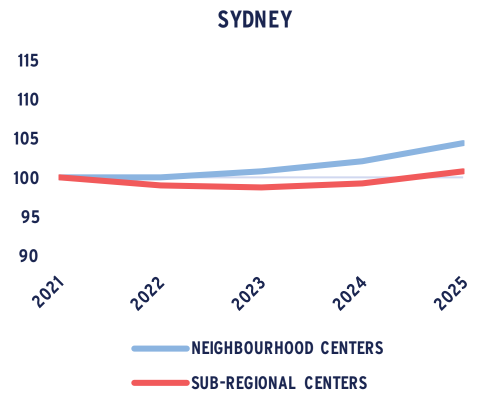
SINGAPORE: Turning a corner, better fundamentals ahead

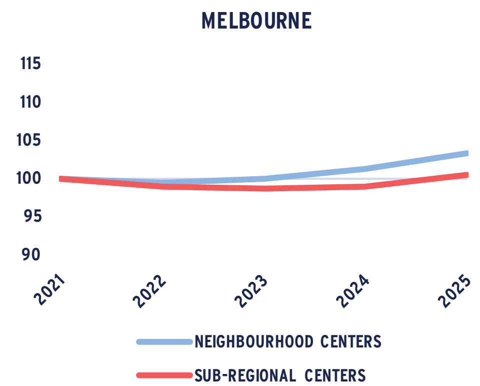
- In Q1, the recovery of the sector was slow, but leasing momentum is expected to gain pace from Q2 onwards as all social gathering restrictions were lifted as of end April 2022.
- Average rents today for suburban retail are 15% to 25% cheaper from where they were at year-end 2019. Improving fundamentals and more affordable rents could give landlords an impetus to raise rents.
- Positivity among investors is already building – using the public market as a leading indicator, the retail REIT market had a surge in trading volume and increase share price since the start of the year.

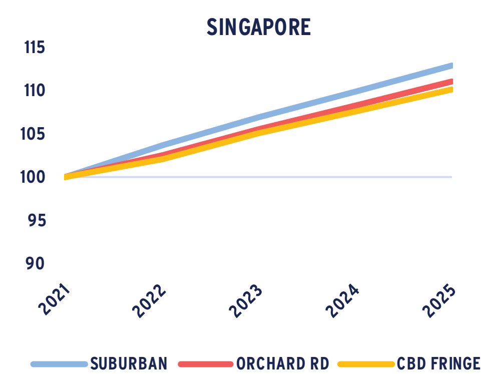
HONG KONG: Expect Improvement in Q2 2022

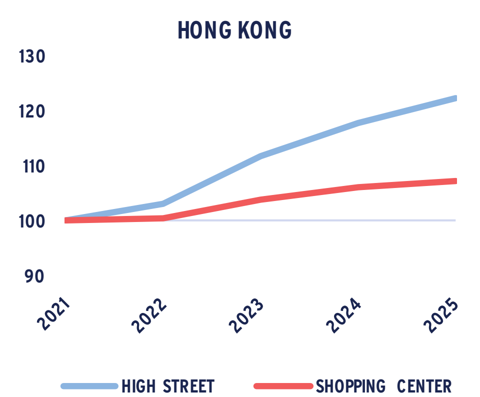
- Widespread disruption amid the fifth COVID wave derailed the city's retail recovery. Vacancy rates in both high street retail and prime malls further increased during the quarter. Some landlords offered shorter and more flexible lease terms to support occupancy, while the government introduced a rent enforcement moratorium, allowing tenants in certain sectors to delay rental payments for up to three months.
- As the city's social restrictions ease in Q2, we expect some positivity in leasing to come through. AEW Research understands that retailers are getting more positive, and are willing to do inspections.
- As the border reopening with the mainland and other countries remain unclear in the near-term, the retail recovery will be dependent on local spending. The government-issued consumption vouchers to all local residents is expected help. Already, the first few weeks since measures were relaxed in late April, there was evidence of a sharp increase in shopper traffic and revenge spending.

RETAIL RENT INDEX (2020 - 2025F)
2021 =100









Source: JLL, as of Q1 2022

Multifamily

JAPAN: Migration trends start to normalize in Q1

- Net migration trends are normalizing in 2022 after two years of disrupted city migration.
- Q1 net migration numbers for Tokyo showed substantial improvement from 2021, with more people entering the city for education or employment opportunities. Meanwhile cities in Greater Tokyo or regional areas that recorded stronger migration numbers in the last two years are starting to see a pull back.
- Leasing demand, especially in Tokyo 23 Wards, are expected to see healthy momentum in 2022 which will support near-term rental growth.

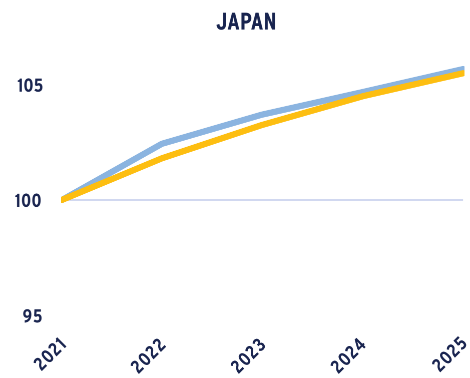
AUSTRALIA: Positive tailwinds, improvement on tax legislation needed

- Better economic conditions and the return of high levels of migration and students are driving sharp increases in the demand for rental housing. In the last 12 months, traditional rents have risen by 15 to 20% within high density areas in capital cities.
- The build-to-rent sector's development pipeline is expanding quickly. With several projects completing this year, the BTR concept and performance will be tested and verified. Recent studies based on completed BTR projects have shown that they command a 20% rental premium to traditional rental projects.
- AEW believes that fundamentals are positive, but further improvement and clarity on tax legislation for foreign investors are needed to encourage investment.

CHINA (TIER 1): Demand falls in Q1

- Leasing demand for the multifamily sector in Shanghai and Beijing has slowed in Q1. While some of the effects are seasonal, the COVID outbreaks and strict lockdowns have dominated the disruption.
- Investor interest in the sector has also waivered under the current conditions, with only one multifamily deal concluding in Q1 in Beijing.

MULTIFAMILY RENT INDEX (2021 - 2025F)
2021 =100



Source: AEW Research, as of Q1 2022

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Natixis Investment Managers may decide to terminate its marketing arrangements for this fund in accordance with the relevant legislation

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