

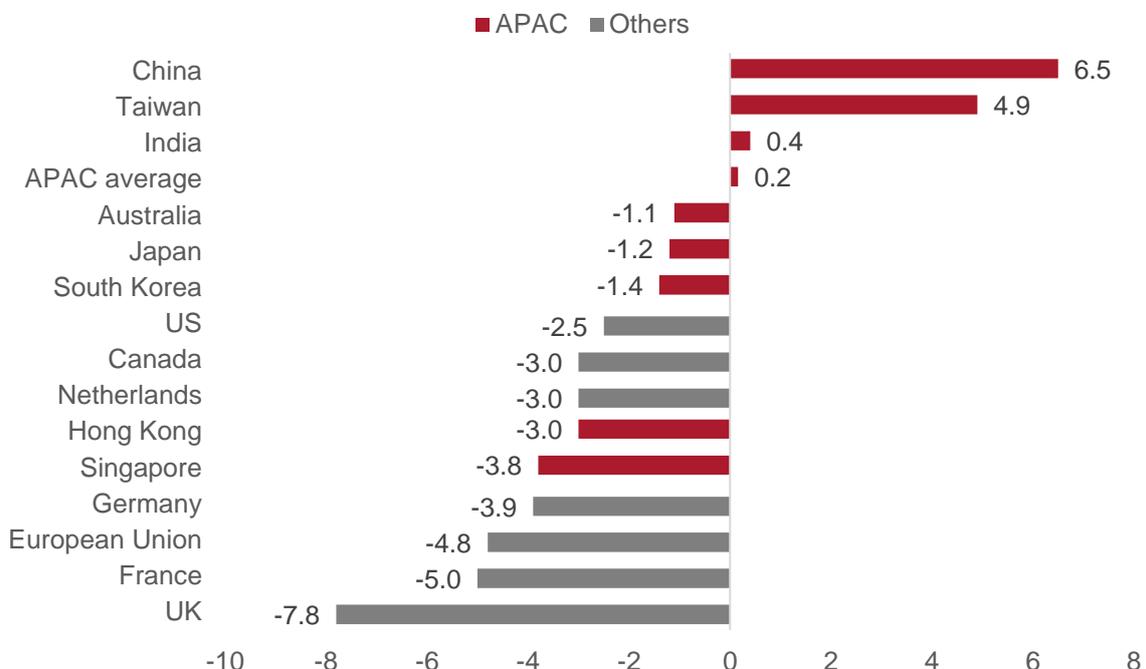
## Phoenix Property Investors' Quarterly Market Update (April 2021)

by Milan Khatri, Head of Research

### Is Asia's slow vaccine roll-out of concern?

- Asia's economy has performed relatively well compared to Europe and North America throughout the pandemic due to strong control of the virus. Global GDP growth data for the year to Q4 2020, showed that most of the top performing countries were from Asia Pacific including China, Japan, Australia, and South Korea (see chart 1).
- The roll out of vaccines appears to have been slow in APAC but many countries are in a fortunate position to take a 'wait and see' approach in view of low COVID-19 cases; for example, there have only been 4,000, 2,150 and 1,150 cases (per million of population) in Japan, South Korea, and Australia respectively<sup>1</sup>. This compares to 94,000 in the US and 63,000 in the European Union<sup>1</sup>.
- Much of Asia has sufficient vaccines ordered to ensure herd immunity from the virus by the second half of 2021 or early 2022. We believe this will support a broader economic recovery as consumer facing industries open-up more extensively e.g F&B, retail, hospitality.

**Chart 1: GDP Growth in the Year to Q4 2020<sup>2</sup>**



**Notes:**

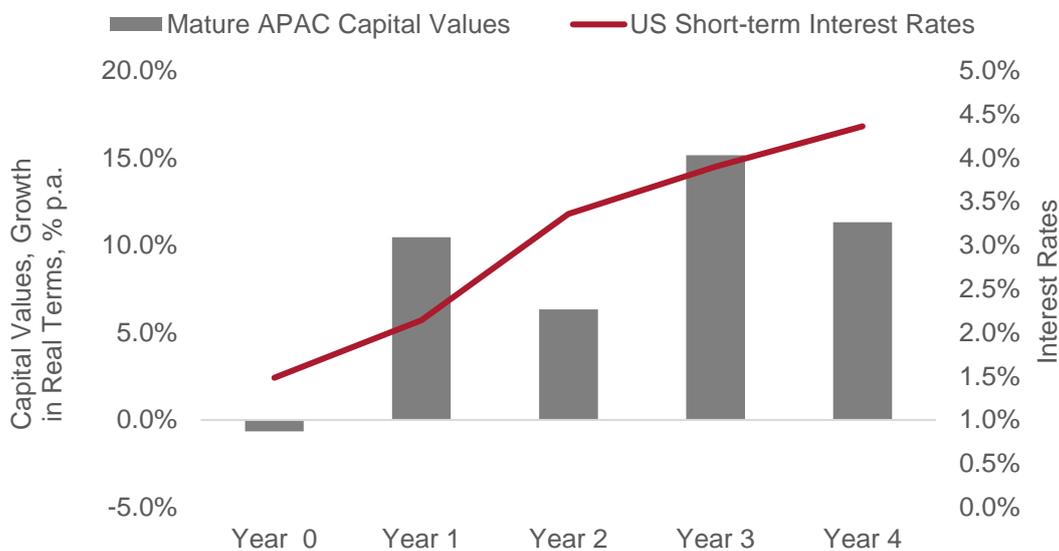
<sup>1</sup> <https://ourworldindata.org/covid-cases> April 2021

<sup>2</sup> Source: OECD, National Statistical offices, April 2021

## What do higher bond yields mean for APAC's real estate market pricing?

- Globally, financial markets are anticipating an economic recovery as vaccines have shown a pathway out of the pandemic.
- Bond yields have jumped since November last year by over 50 basis points on expectations that short-term interest rates will need to rise, and this is despite pronouncements by central bankers that interest rates will stay low for many years<sup>3</sup>.
- To better understand the potential impact of rate hikes on APAC real estate, we examined the past three cycles for US interest rates. The data suggests that capital values tend to RISE as short-term rates go up (see chart 2).
- In recent decades, rising interest rates have been accompanied by stronger economic growth and higher employment; thus, despite rising interest rates, real estate capital values have moved higher.
- Asia's economic growth cycle is closely tied with US growth; the current cycle is likely to be no different and will be supported by the rolling out of vaccines globally into 2022.

**Chart 2: US Interest Rate Upcycles and Mature APAC Capital Values<sup>4</sup>**



**Notes:**

3. See the most recent projections from the U.S. Federal Reserve where even by 2023, the median view of central bank members is for no change in interest rates relative to the current position:

<https://www.federalreserve.gov/monetarypolicy/files/fomcprotabl20210317.pdf>

4. Source: National Statistics data, OECD, Mar 2021. Figures show the average of three US interest rate cycle upturns (1993-1997, 2003-2007 and 2014-2018) and the path of APAC office capital value growth during these years in Tokyo, Seoul, Sydney, Melbourne, Hong Kong, and Singapore. Year 0 marks the low point of the US interest rate cycle.

## The future of office demand in APAC: How is it different to the US and Europe?

- There is a lot of speculation about work from home, and its potential impact on occupier demand for office space. For Asia, evidence for 2020 shows RISING grade ‘A’ office demand in many major cities (e.g. Shanghai and Tokyo), which contrasts starkly with falling demand in similar cities in the US (such as New York and Los Angeles).
- Why did demand for grade ‘A’ office in major Asian cities increase in 2020?
  1. **Quicker return to the office:** The number of people back in their office (rather than working from home) has been relatively high in APAC, varying in late 2020 from 40%-100% across major cities<sup>5</sup>.
  2. **Expansion of office using industries:** In 2020, unemployment rose modestly in APAC, and office using industries added jobs even as consumer facing industries retrenched; technology, financial and business services firms grew employment by c. 1% in APAC’s mature economies<sup>6</sup>.
  3. **Upgrading to higher quality offices:** Firms have used the pandemic as an opportunity to upgrade their office space. Phoenix estimate<sup>7</sup> that major APAC cities have low amounts of grade ‘A’ office space per capita compared to US and Europe. As more grade ‘A’ space becomes available, pent-up occupier demand in strong locations becomes evident.
- We expect frequency of homeworking to increase in Asia. However, we believe that robust growth of office using industries, and a flight to quality from poorer office space (to attract employees and enhance their in-office experience), will benefit grade ‘A’ and good quality grade ‘B’ offices.
- As a result, we see investment opportunities in both the upgrading of existing stock (e.g. grade B offices), or development of new grade A assets, as the economic recovery progresses across the region

If you would like more detail on the questions above and Phoenix Property Investors’ market views please get in contact ([ir@ppinvestors.com](mailto:ir@ppinvestors.com)) and we would be happy to help.

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*Notes:*

5. *Colliers, Oct 2020*

6. *Data covers Japan, Korea, Australia, Hong Kong, and Singapore.*

7. *Source: Cushman and Wakefield, JLL, Colliers, OECD, National Statistical Offices, Phoenix calculations, March 2021*

**Disclaimer:**

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