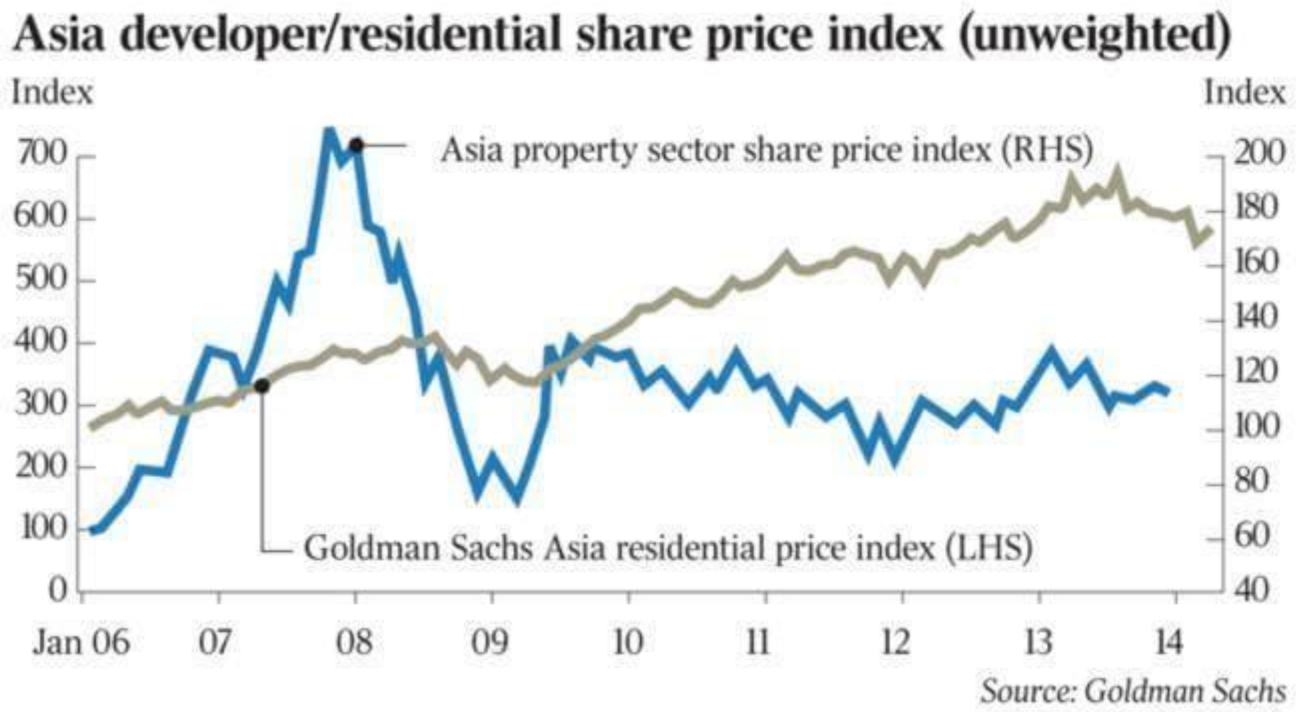
No-man's land leads to Asia



'The maturing markets of Asia appear to be a path out of the current no-man's land'

By **Stirling Larkin**

DAVID Tepper, founder of Appaloosa Management, a hedge fund focused on distressed companies, recently commented that investors appeared to be skittish and that he was nervous about the stockmarket, but now was not the time to sell.

Comments such as these highlight the view that the market is heading into a no-man's land with neither a clear bullish nor bearish sentiment apparent.

A strong candidate for consideration is the Asian real estate market, of which more later.

The no-man's land exists because the once-in-a-75-year reflation measures undertaken by the US Federal Reserve, Bank of England and the Bank of Japan have distorted all natural metrics.

As a result, the Australian ultra-high net worth investment community is trying to make sure its portfolios are both allocated towards growth and simultaneously fireproofed against any number of hazardous scenarios that appear to be looming in the shadows.

It's hard to find this balance.

These techniques traditionally rely upon these common metrics, which are telling us that nearly all asset classes appear frothy, mispriced and, most worrying of all, calm. This calmness is a worry because reliable research shows each major crash of the past 30 years was pre-empted by a period of low to little volatility.

This suggests that in tranquil times people become complacent and cavalier in their attitudes towards debt and risks.

This in itself is not necessarily a bad thing but what it says to the global investor is they cannot rely on traditional tools to gauge whether the typical business and investment cycles match up with current valuations.

UHNW investors are particularly sensitive to these mismatches because their portfolios commonly hold a disproportionate allocation towards one specific asset class or subset.

This might surprise a lot of people as they are led to believe that diversification is the key to successful investing.

They are told this is the only model to build wealth but forget that even John Maynard Keynes often argued that it was possible to build wealth by closely following a few companies or investments.

In Australia, UHNW portfolios are often concentrated in residential and commercial real estate assets or the retail sectors, particularly in the textiles, clothing and footwear industry.

However, to ensure these portfolios are positioned for growth but can still weather bad times, it appears timely to explore broader opportunities within these same asset classes.

The strongest opportunity for these Australian investors appears to be Asian real estate.

The Australian UHNW investment community has found a good play in Asian real estate and this investment subset has allowed them to find new ways to employ their existing acumen throughout wider geographies.

This market has matured significantly since the dark days of the 1997 Asian financial crisis and presents astute Australian investors with more robust opportunities that can be managed far better than ever before.

According to Cameron Clarke, an Australian pioneering in this region, Asian property investment is being driven by increased land availability, respective yield and an improved efficiency in value adding that has not been seen before.

Cameron believes “the Singaporean and Malaysian real estate investment trusts market remains solid, with high-yielding towers leveraging not only the residential sales component but also higher-yielding luxury retail brands that are soaking up the available commercial spaces in these markets”.

He argues that the development of aged care and industrial assets in mainland China is important and provides the example of Malaysia’s construction of Asia’s first transnational high-speed rail system linking Penang, Kuala Lumpur and Singapore representing a unique opportunity to invest in commercial and residential assets around station nodes.

This new degree of value adding across Asian real estate bodes well for direct off-the-plan residential investment opportunities in the established markets of Singapore and Hong Kong as well, where land had been starved.

According to Geoff Gedge, a director of the SILC Group and former chief executive of the Property Funds Association of Australia, "As Australia has become a hotspot for Asian property investors, so are Asian centres increasingly becoming popular for Australian investor funds."

While there is no fixed focus on any particular Asian country, what is emerging is a strong focus on what Gedge refers to as "emerging Asian cities". These are in Bangladesh, Malaysia, China, Bali and India and even some South American centres.

In line with Cameron's comments, Gedge believes a number of Singaporean and Hong Kong-based fund managers are establishing investment funds based on this concept and are looking to offer these investments to Australian investors.

These funds would seek to invest primarily in social infrastructure and other growth property areas within developing emerging Asian cities and are focused on the growing middle classes, which are enjoying increased disposable incomes. There appears little doubt that as the region matures, bilateral investments become more viable, attractive and manageable for both Asian and Australian investors.

The most important portfolio technique to focus on with these investments is the management of foreign exchange exposures. Investors need to be acutely aware about whether their investments are made on a currency hedged or unhedged basis and, in both circumstances, what this means for their investments and risk management.

The smart money knows there is a trend emerging and they are positioning accordingly.

This trend is being driven by European, North American and other Asian investors.

Now appears the time for Australian investors to not only follow this trend but in many instances, lead it.

As Warren Buffet famously said: "Wide diversification is only required when investors do not understand what they are doing."

For many Australian real estate investors uncertain of their next move, the maturing markets of Asia appear to be a path out of the current no-man's land.

Stirling Larkin is chief investment officer of Australian Standfirst
www.australianstandfirst.com