KENSHO INVESTMENT GROUP

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CEO Insight: Diversification is the order of the day

Decoupling and deglobalization mean that property markets are no longer moving in international harmony. Investors need to broaden their investment strategy and in doing so there is no way around Japan.

In contrast to the poor mood among market participants in the US and Europe, the participants at the Japan conference at the MIPIM property trade fair in Cannes in March were unanimously optimistic. For example, Laurent Jacquemin, Head of Asia-Pacific Real Estate at French AXA Investment Managers and CEO of its Japan subsidiary, emphasized that the Japanese market "continues to work". AXA has been one of the most active players in Japanese residential property in recent years. Its investments are doing so well that the French company is now expanding its residential spectrum to include other forms of living space. In addition to flats, Jacquemin is now looking also at retirement homes, student residences, and hotels for long-term stays.

AXA is one of the few European property investors to consistently abandon the previous standard strategy of "one-size-fits-all" investments at an early stage. Since the Great Financial Crisis, the property markets in most industrialized nations have moved in lockstep, allowing investors to largely ignore country-specific characteristics and follow the same pattern everywhere. However, the pandemic has intensified the trends toward decoupling and deglobalization. This means that what applies to Germany or the USA does not automatically apply to Japan or Asia. National markets are developing a stronger momentum of their own, meaning that diversification must become a more important part of a global investor's investment strategy. More capital should be channeled to those markets that are developing conspicuously positively.

And Japan has long stood out in this respect. AXA recognized this early on and reacted quickly, as did many foreign investors operating out of Singapore. German investors have held back almost completely so far, in my opinion partly because some prefer to ignore the hard economic facts rather than abandon their negative attitude towards Japan in general (more on this in my CEO Insight from March). Hard economic facts mean that the key interest rate in Japan is in a range of 0.0% to 0.25% and the 10-year bond yield is 0.85%, far below the level in Germany. As a result, the property markets in Japan and Germany are completely decoupled from each other.

Please allow me to quote what financial journalist Koko Shinoda said in her contribution to the discussion at the Japan conference of MIPIM 2024: “Despite its low growth rate, Japan’s fundamentals remain stable. After all, Japan boasts the largest, most liquid, and highly developed real estate market in Asia.”

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“In terms of investment, it ranks as the third-largest globally. Foreign investors can secure loans relatively easily, with leverage of up to 70%, and benefit from the very weak yen. Last year, one in three buyers of large transactions were foreigners (list of the Top 20 transactions in 2023). If we include Japanese corporations backed by foreign capital, the ratio becomes even higher.”

Ms Shinoda continued: “Among the assets, the residential sector, Japan’s huge housing market is solid. But what stands out is the hotel sector. According to the Nikkei newspaper, last year’s hotel transaction volume in Japan reached 471 billion yen (2.9 billion euro), up 128% from the previous year. Some investors may think: ‘Let’s borrow cheaply, buy cheaply, and then let‘s sell when the inbound tourists are back and yen become high.’ But, unfortunately, there is nothing left to buy nowadays. You can patiently collect small hotels through the network in Japan, or look into regional cities. Bulk buying is possible only if you have a strong foothold in Japan for many years with a long-term strategy.”

Japan's investments in foreign real estate assets also underline the viability and maturity of the market. Japan's Government Pension Investment Fund (GPIF) and the Dutch APG Asset Management have just launched a joint investment program. The focus is on infrastructure in developed markets with sectors such as sustainable energy, fiber optic networks, and transport. The GPIF is the world's largest pension fund and is wholly state-owned, while the majority of APG is owned by ABP, the largest public pension fund in the Netherlands. Together they manage assets totaling over 2 trillion euros. The cooperation proves that foreign investors seek and respect Japanese investors for their expertise and capital strength.

No matter how you look at it: in today's global environment, property investors need to diversify their investment strategy according to national markets. If you want to fulfill your yield targets, you cannot avoid identifying the strong markets and exploiting the higher yield opportunities there. Japan has long been an obvious choice for this and is still such an obvious choice that one wonders why more European investors are not as active in Japan as the French investor AXA.

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