# THE SIGNIFICANCE OF REAL ESTATE IN ASIAN PENSION FUNDS

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## Abstract

Pension funds are major institutional investors, with over $30 trillion in assets. Typically, real estate accounts for 5-10% of their portfolios in the developed markets. Importantly, pension funds in Asia are significant players, with five Asian pension funds in the top ten pension funds globally. However, Asian pension funds typically have low levels of real estate in their portfolios; often having no real estate. A number of critical drivers are now seeing an environment of pension fund reform in Asia, eg: rapid demographic change. This is seeing pension funds in Asia reviewing their strategic asset allocations to meet future obligations; this includes assessing the level of real estate in their portfolios. This paper will highlight this changing pension fund environment in Asia and the activities of various pension funds in Asia strategically increasing their levels of real estate. This includes case studies of South Korea's National Pension Scheme, Malaysia's Employees Provident Fund and other Asian pension funds, as well as interviews with leading pension funds in Asia to assess the implementation of their changing real estate strategies. Enabling strategies are also identified to facilitate other pension funds in Asia to increase their real estate allocations. These increased levels of real estate in Asian pension funds will see significant benefits across all sectors of the real estate industry in Malaysia and Asia.

## INTRODUCTION

Pension funds have taken on increased importance in recent years, with their long-term investment horizon and their need to select assets to match their long-term liabilities. Globally, pension fund assets were over $30 trillion in 2011. Whilst many of the leading pension funds are based in the mature US/European economies, pension funds in Asia are significant contributors to this global pension fund context. This sees pension funds in Japan (Global Pension Investment Fund: #1 globally) and South Korea (National Pension Scheme: #4 globally) amongst the world's leading pension funds.

Pension funds have typically tended to be conservative investors; typically focused on fixed income assets and their domestic markets. Importantly, real estate has been an attractive asset for pension funds in many countries. The investment characteristics of high quality, income-producing real estate, its low risk and portfolio diversification benefits sees real estate as a secure long-term asset; well-placed to meet the future long-term liabilities of pension funds. This has seen numerous pension funds in the US, Canada, Europe and Australia being long-standing investors in commercial real estate; developing multi-billion dollar real estate portfolios via a range of real estate investment vehicles as an essential element in their strategic asset allocations. This includes leading pension funds such as CalPERS and CALSTRS in the US, CPP Investment Board and the Ontario Teachers Pension Scheme in Canada, and ABP and the British Telecom Pension Scheme in the UK/Europe. This has seen indicative levels of real estate in their portfolios of 5-10%; with some major pension funds having significantly higher allocations to real estate in their portfolios. In Asia, real estate currently does not make up a significant level in most pension fund portfolios.

However, there are deficiencies in many of the pension schemes in Asia; particularly concerning significant under-funding and the ability to meet future long-term financial liabilities. This has been the catalyst to considerable reform in the pension systems in Asia; particularly concerning improved pension fund coverage rates and suitable asset allocations to manage risk and deliver higher returns to meet these future long-term liabilities of Asian pension funds. These substantive pension fund challenges and reforms for Asia highlight the potential added-value role that real estate can play in pension funds in Asia.

As such, the objectives of this paper are:

- to highlight the significant opportunities for pension funds in Asia to increase their real estate exposure
- to highlight the leading pension funds in Asia that are effectively including real estate in their portfolios
- to survey Asian pension funds and leading real estate professionals in Asia regarding real estate in Asian pension fund portfolios
- to identify effective strategies for the inclusion of increased levels of real estate in Asian pension fund portfolios.

## PENSION FUNDS IN ASIA

### *Asian pension fund context*

Asia has some of the largest pension funds globally, including Japan's Government Pension Investment Fund (#1 globally), South Korea's National Pension Scheme (#4 globally), Japan's Local Government Employee's Fund (#7 globally) and Malaysia's Employees Provident Fund (#9 globally). This sees Asia as having five of the top 10 pension funds globally and eleven of the top 50 pension funds globally. Table 1 lists the major pension funds in Asia, with representation across most major countries in Asia.

Pension funds in Asia have tended to be conservative in their asset allocations; largely focused on domestic fixed income assets. For example, recent major asset allocations include:

- Government Pension Investment Fund (Japan): fixed income (77%), stocks (22%)
- National Pension Scheme (South Korea): fixed income (71%), stocks (22%), alternatives (6%)
- Government Pension Fund (Thailand): fixed income (77%), stocks (17%), real estate (4%)
- Employees Provident Fund (Malaysia): fixed income (72%), stocks (27%).

This asset allocation focus on low-yield fixed income assets clearly presents potential difficulties in meeting future obligations for an aging population in Asia.

*Drivers for pension fund reform in Asia*

A range of important factors have highlighted major deficiencies in the current adequacy of pension funds in Asia and have been key drivers for pension fund reform in Asia in recent years. These factors include:

- Changing demographics: aging population; declining fertility rates; early retirement ages
- Structural change in the economic environment: economic growth; increased urbanisation and industrialisation; reduced focus on agriculture
- Costs and deficiencies of the previous defined benefit pension systems
- Ability to meet future long-term liabilities with current low yield asset allocations; eg: significant fixed income asset exposure
- Impact of the GFC on pension fund asset performance
- Growth in the funds management sector in Asia.

In particular, the changing demographics in Asia have significant implications for the ongoing financial viability of current pension schemes in Asia. Table 2 clearly highlights the future impact of the changing demographics with an aging population in Asia. Significant increases in the old-age dependency ratios over 2005-2050 in all countries in Asia are evident; particularly for Hong Kong, Japan, Singapore, South Korea and Taiwan, as well as major increases for China and India.

Also, deficiencies in the previous state pension systems in Asia have been highlighted; particularly the costs and inadequacies of the often generous defined benefit schemes in Asia compared to that seen in many OECD countries. Often the overall adequacy of the retirement income from pension fund schemes in Asia is insufficient from the current low coverage rates; eg: China (17%), India (6%), Philippines (14%), Thailand (21%), Indonesia (11%), with only Japan (75%) and South Korea (60%) having substantive coverage rates. This is further compounded by some pension schemes often allowing withdrawal of funds before retirement, access to lump sum payments seeing the risk of participants outliving their financial resources, and some pension schemes not always being automatically adjusted for increased living costs.

Overall, this sees most Asian countries as not adequately prepared for this rapidly aging population over the next 20 years; resulting in unsustainable and financially-constrained pension fund schemes in many cases. The lack of well-functioning pension fund systems with high levels of coverage is further highlighted by the pension fund sustainability indices for Asia shown in Table 2. Of the 44 countries surveyed, this sees Asia as having some of the countries with most need for pension system reform globally (4 in top 5); eg: India (#2), China (#3), Thailand (#4) and Japan (#5). Only South Korea (#22), Taiwan (#31) and Hong Kong (#38) rate with a lesser need for pension system reform.

*Pension fund reform in Asia*

Key recent pension scheme reforms have included:

- regulatory changes seeing a shift from defined benefit to defined contribution schemes (eg: Hong Kong, Taiwan, South Korea, Japan, China); this has seen an increased focus on improved asset management to deliver better returns

- introduction of new pension fund systems to improve national coverage rates (eg: NPS in India), and recognition that some of the older pension fund systems are now out-dated (eg: Singapore, Japan)

- regulatory changes to asset allocations to balance the current focus on domestic low-yielding fixed income assets versus the need for assets to be delivering higher risk-adjusted returns (eg: Japan, Taiwan, South Korea). This has seen strategic asset allocation shifts in the areas of:

    (1) reduced levels of domestic stocks and fixed income assets

    (2) increased diversification via international stocks, in both mature and emerging markets

    (3) increased levels of alternative assets (eg: infrastructure, private equity, real estate)

    (4) increased use of external fund managers

    (5) increased use of experienced investment managers in-house

    (6) review of portfolio rebalancing timeframes

    (7) establishment of separate risk management companies for more efficient asset management (eg: South Korea).

Importantly, these reforms have seen many pension fund systems in Asia strategically reviewing the way their assets are managed post-GFC and in the context of meeting future long-term liabilities. This potentially has significant implications for real estate in Asian pension funds and how this real estate exposure is managed effectively.

**Table 1: Leading pension funds in Asia**

| Pension fund | Country | Global rank | Total assets (2011) |
|---|---|---|---|
| Government Pension Investment | Japan | 1 | $1,432B |
| National Pension Scheme | Korea | 4 | $289B |
| Local Government Employees | Japan | 7 | $190B |
| Employees Provident Fund | Malaysia | 9 | $146B |
| Central Provident Fund | Singapore | 10 | $145B |
| National Social Security | China | 14 | $130B |
| Pension Fund Association | Japan | 16 | $125B |
| National Public Service | Japan | 21 | $104B |
| Public School Employees | Japan | 31 | $78B |
| Employees Provident | India | 42 | $60B |
| Organisation of Workers | Japan | 46 | $54B |

Source: P&I (2011)

**Table 2: Demographic factors in Asia: 2005-2050**

| Country | Population | Population over 65 | Old-age dependency ratio* | | Pension sustainability index |
|---|---|---|---|---|---|
| | | | 2005 | 2050 | |
| China | 1,329M | 7.7% | 11% | 39% | #3 |
| Hong Kong | 7M | 12.0% | 16% | 58% | #38 |
| India | 1,169M | 5.0% | 8% | 21% | #2 |
| Japan | 128M | 19.7% | 30% | 74% | #5 |
| Singapore | 4M | 8.5% | 12% | 59% | #17 |
| South Korea | 48M | 9.4% | 13% | 64% | #22 |
| Taiwan | 23M | 10.0% | 13% | 63% | #31 |
| Thailand | 64M | 7.8% | 11% | 38% | #4 |

Sources: Allianz (2008, 2011), OECD (2012)

*: percentage of population aged greater than 65 years compared to population aged 15-64 years.

## REAL ESTATE IN PENSION FUNDS IN ASIA

*Current status*

While real estate is an important asset class in many pension fund portfolios globally, the level of real estate exposure in Asian pension funds has typically been lower than that seen in the US, Canada, UK, Europe and Australia. This has largely been due to their focus on domestic low yield assets; particularly fixed income assets. As such, real estate has often been considered as a relatively new asset class by Asian pension funds and real estate investment has also often been seen as the domain of the country's sovereign wealth fund which can take on potentially more illiquid assets with higher risk levels to generate higher expected returns.

*Japanese pension fund attitudes to real estate*

A major survey was conducted in Japan in 2010 by the Association for Real Estate Securitisation to assess Japanese pension fund investments in real estate. Key findings included:

- 34% of pension funds included some type of real estate in their portfolio; this was down from the peak level of 42% in 2007
- average 1.1% allocation to real estate in portfolio; compared with 23% Japan stocks, 17% foreign stocks, 31% Japan bonds, 11% foreign bonds, 7% alternatives
- the 2010 allocation to real estate of 1.1% was below the 2.4% peak allocation seen in 2007
- main reasons for investing in direct real estate were portfolio diversification, stable cash flow, improved rate of return
- main reasons for **not** investing in direct real estate were low liquidity, unfavourable market conditions, lack of understanding of direct real estate.

*South Korea: National Pension Scheme*

South Korea's National Pension Scheme (NPS) was established in 1988, having approximately $289 billion in assets in 2011. NPS is the 4th largest pension fund globally and the 2nd largest in Asia. NPS includes real estate in the alternative asset allocation, along with private equity and infrastructure.

With a previous focus on domestic fixed income assets, the expected growth of NPS to $2 trillion by 2043 has seen NPS recently undergoing the process of diversifying their investment portfolio. By 2015, the goal is to have less than 60% domestic fixed income, less than 10% international fixed income, more than 20% domestic stocks, more than 10% international stocks and more than 10% alternative assets. In 2011, the NPS portfolio comprised domestic fixed income (67%), international fixed income (4%), domestic stocks (17%), international stocks (6%), alternative assets (6%).The NPS alternative asset sector has increased significantly since 2006; increasing from 1% to its current level of 6%, via a range of local and international external fund managers and acquisitions.

Importantly, real estate accounts for 25% of the domestic alternative asset exposure and 36% of the international alternative asset exposure. From an initial focus on domestic retail property, NPS has undertaken significant international real estate investment in the office sector since June 2009. This is part of NPS's stated strategy of acquiring more commercial properties in the major global cities to secure stable income sources as part of their long-term investment strategy. In particular, NPS has acquired six major office properties valued at $3.6 billion since June 2009, with core office properties in London (3), Tokyo, Berlin and Sydney; see Figure 1 for property specifics.

In 2011, NPS continued this strategy with major property acquisitions in major cities including Paris, Seoul and Melbourne (eg; via Rockspring, Pramerica and Townsend), as well as issuing significant mandates (over $650M) in four value-add/ opportunistic/distressed funds with leading real estate fund managers (Invesco, Cornerstone, Colony, Tishman Speyer); additional funds have also been earmarked (over $500M) in this area of higher risk real estate. Overall, this has seen over $5 billion invested in real estate over 2009-2011 by NPS, with real estate now accounting for over 2% of their total assets.

Clearly, South Korea's National Pension Scheme sees real estate as a key component in NPS's ongoing overall investment strategy and in its alternative asset allocation, with the alternative asset sector expected to increase to over 10% by 2015. This proactive real estate strategy by NPS is expected to see an increased real estate portfolio at both the domestic and international levels in the future.

*Malaysia: Employees Provident Fund*

Malaysia's Employees Provident Fund (EPF) has approximately $146 billion in assets and is the 9th largest pension fund globally. The asset allocation for EPF has largely been fixed income (72%) and stocks (27%).

Since 2010, EPF has developed an international real estate strategy; seeing its first real estate investments outside Malaysia. This $1.5 billion international real estate mandate, jointly with RREEF (50%) and ING RE (50%), has seen major office property acquisitions in London; several being jointly with KWAP. EPF has also taken a 20% stake ($640 million) in a joint venture mixed development in Singapore with GuocoLand.

This sees international real estate as a key element in EPF's real estate agenda; with real estate now accounting for 2% of EPF's assets. This is part of EPF's overall strategy of increased overseas investments, increasing from 13% in 2012 to an expected 30% by 2017; requiring government approval to its maximum international asset allocation mandate.

*Thailand: Government Pension Fund*

Thailand's Government Pension Fund (GPF) has approximately $16 billion in assets. The 2012 asset allocation for GPF is domestic fixed income (67%), international fixed income (9%), domestic stocks (8%), international stocks (9%), real estate (4%), alternative assets (2%).

In addition to its domestic real estate portfolio, GPF has recently allocated 2% to international real estate, initially focused on US/ Europe core/core-plus real estate investments. This will see the real estate allocation of GPF increase to 7.5%, with the domestic fixed income allocation reducing to 65%.

*Other Asian pension funds*

Other Asian pension funds are also now considering real estate in their portfolios, as part of their investment strategy to diversify risk and increase their exposure to the alternative asset classes. This includes Toshiba Employees Pension Fund ($9B), Korea Teachers Pension Fund ($9B) and Taiwan Labour Pension Fund. In several cases, they are considering real estate in their portfolios for the first time.

HSBC HQ, London
$1,275M

Sony Centre, Berlin
$768M

Aurora Place, Sydney
$626M

KDX *Toyosu Grandsquare*, Tokyo
$367M

88 Wood St, London
$292M

40 Grosvenor Place, London
$282M

Source: Real Capital Analytics (2012)

**Figure 1: Recent global property acquisitions by South Korea's National Pension Scheme**

Overall, these examples have clearly highlighted the lesser allocations to real estate seen in Asian pension funds, compared to many pension funds in the US, Canada, UK/Europe and Australia. This has seen most Asian pension funds focused on fixed income assets. The ability for this conservative style of asset allocation to meet future liabilities has raised major concerns and has been the catalyst of recent pension fund reform in Asia. The proactive role of South Korea's National Pension Scheme and Malaysia's Employees Provident Fund has also highlighted the ability of some Asian pension funds to effectively integrate real estate into their asset allocation via both a domestic and global real estate investment strategy. The performance of real estate in these pension funds will be watched closely by other Asian pension funds and real estate fund managers seeking their real estate mandates. Moving forward, similar strategies will need to be adopted by other pension funds in Asia to ensure the ability to meet long-term liabilities in an effective manner.

## ASIAN PENSION FUND SURVEY AND INTERVIEWS WITH LEADING REAL ESTATE PROFESSIONALS

*Survey of Asian pension funds*

A survey was distributed to a number of the major pension funds in Japan, South Korea, Thailand, Singapore, Malaysia, Taiwan, Philippines, India and China. Most pension funds considered that they had less knowledge and less familiarity with real estate as an asset class compared to the other major asset classes, with real estate considered as an alternative asset class. The contribution by asset consultants to their real estate allocation decision-making was considered as important or essential.

The most important reasons (in priority order) for having real estate in a pension fund portfolio were:

(1) portfolio diversification benefits

(2) access to global real estate markets

(3 eq.) lower risk for real estate

(3 eq.) liquidity provided by REITs

(3 eq.) enhanced returns.

The main factors influencing selection of real estate fund managers (in priority order) were:

(1) manager's understanding of client needs

(2) legal structure of the fund

(3 eq.) alignment of interests

(3 eq.) fund's organisational stability

(4 eq.) manager's local expertise

(4 eq.) corporate governance issues

(5) fund's previous performance.

Specific risk management strategies identified as important for real estate in a pension fund portfolio were:

- established exposure limits
- managing illiquidity risk via asset-liability management, cash management and longevity management
- real estate sector and geographic diversification
- good tenant ratings and tenant relations
- asset management strategy
- experienced real estate management team.

This range of strategies was across the strategic level, portfolio level and at the individual property level.

This survey identified several key strategic issues for real estate in Asian pension fund portfolios. Overall, pension funds in Asia are positive regarding their view on real estate, with the benefits of real estate in a portfolio clearly recognised; particularly the portfolio diversification benefits. They generally have established separate real estate teams in the pension fund asset management structure and rely strongly on asset consultants in their strategic real estate investment decision-making, with real estate generally classified as an alternative asset class, along with infrastructure and private equity. Their criteria for selecting real estate fund managers sees alignment of interest and understanding of pension fund requirements as high priorities.

However, they also recognise that they have less knowledge concerning real estate compared to the other major asset classes; reflecting real estate being a relatively new asset class in Asia for many pension funds. This lack of a fuller understanding of real estate as an asset class is seen as an impediment to making substantive real estate investment decisions by many pension funds. They also clearly recognise the need for improved real estate market information and transparency to facilitate the real estate investment process by Asian pension funds. With many countries in Asia seeing a shift from defined benefit to defined contribution schemes, these real estate issues will take on increased importance as it will see a strategic shift to an increased emphasis on asset performance and higher levels of asset management skills by pension funds in Asia.

*Interviews with leading real estate professionals in Asia*

Interviews were also held with twelve leading real estate professionals in Asia regarding real estate in Asian pension fund portfolios. These leading real estate professionals in Asia were in the areas of institutional real estate, real estate funds management, real estate asset consultancy, real estate advisory and real estate professional services; each having considerable interaction with Asian pension funds regarding their real estate investment decision-making. These interviews focused around five key strategic aspects concerning real estate in Asian pension funds.

**#1: Why are there generally low levels of real estate in Asian pension fund portfolios?**

Three key issues emerged from these interviews as to why there were generally low levels of real estate in Asian pension fund portfolios. These issues were:

- Lack of familiarity by pension funds with real estate as a credible asset class. This sees the lack of a fixed allocation to real estate in the portfolio, a lack of real estate experience at the investment decision-making level, as well as under-resourced internal real estate teams. This has been further compounded by the traditional view by Asian investors that investing in real estate was for capital growth, not for the stable income stream it produces, with real estate also seen as having higher risk

- Liquidity issues, seeing the pension fund portfolio with high allocations to fixed income assets and cash; this is often influenced by government regulatory constraints in the asset allocation process

- Lack of available institutional-grade core and core-plus real estate assets in many of the less developed Asian markets. In many cases, a significant amount of this high quality real estate in Asia is securitised already in listed real estate developer portfolios. As such, the domestic real estate markets are often considered to be too small to support decent pension fund allocations to real estate. This has seen both direct and listed real estate only at the investible asset class level in most Asian markets in the last ten years.

**#2: Why is real estate important as an investment for Asian pension funds?**

The strong portfolio diversification benefits provided by real estate was a key factor in the comments by all of the leading real estate professionals in Asia. Other aspects included stable income streams from core properties, less volatility, competitive returns in the longer term, and inflation-hedging; making it suitable for liability matching and fitting the nature of a pension fund's portfolio to meet future obligations. Real estate was clearly seen as a key element in the alternative investment classes portfolio in Asian pension funds by these real estate professionals.

**#3: Do you see Asian pension funds increasing their real estate allocations?**

All real estate professionals interviewed saw Asian pension funds increasing their real estate exposure in the future. Importantly, they saw this being done in different ways and over different timeframes, with pension funds in South Korea, Malaysia and Thailand seen as being more proactive in implementing their real estate strategy.

In some cases, it was still seen to be in the early stages, as they positioned their real estate strategies and portfolios. Evidence was being seen of increased real estate activity, but it was being done selectively. Quality stock availability was also seen as a key issue, with REITs often considered part of the equity portfolio and not part of the real estate portfolio. Direct property and core property funds were seen as popular options in the near future for increasing this real estate exposure.

**#4: What strategies will Asian pension funds use to increase their real estate exposure?**

A diverse range of real estate products were seen to be likely to be used by Asian pension funds as their strategies for increasing their real estate exposure. This was clearly influenced by the size and experience of the pension fund and included:

- direct investment via issuing a mandate with the real estate fund manager

- use of unlisted real estate funds

- REIT mandate

- JV with developer; with the pension fund retaining a monitoring role.

Importantly, this real estate exposure was seen to be both local and global, using a combination of private and public real estate investment products. Partnering with existing real estate managers was also seen as a key element, with these managers increasingly offering real estate products reflecting a closer alignment of interest with the pension fund; eg: low leverage or all equity funds. The need for a clearly articulated real estate investment strategy by the pension fund was seen as essential.

**#5: What can the real estate industry do to increase the levels of understanding of real estate as an asset class by Asian pension funds?**

A range of initiatives were identified in these interviews to increase the level of understanding of real estate as an asset class by Asian pension funds. These initiatives included:

- actively promoting a better understanding of real estate as a credible asset class; via real estate industry organisations (eg: APREA), other related industry bodies, engaging with asset consultants, and producing additional empirical research on the added-value of Asian real estate in a portfolio. This increased understanding should cover both domestic real estate and international real estate
- engaging with pension funds to establish increased levels of client trust and confidence through long-term impartiality and transparency
- greater transparency in the availability of reliable real estate information and performance data for both unlisted and listed real estate; this includes more direct real estate performance benchmarks for the Asian real estate markets (eg: IPD) and improvements in the reliability of valuations. Lack of these real estate performance benchmarks in Asia were considered to be a key concern for pension funds
- access to more core real estate products and a validated track record of these products performing well in Asia
- lobby governments to relax the regulatory restrictions on real estate levels in pension funds in several Asian countries.

## STRATEGIES FOR ENHANCING REAL ESTATE IN PENSION FUND PORTFOLIOS IN ASIA

Given that many pension funds in Asia have low levels of real estate in their portfolios, their lack of experience and understanding of real estate as an effective asset class needs to be increased. This was clearly highlighted in this survey of Asian pension funds and the associated interviews with leading real estate professionals in Asia. Importantly, this will see an enhanced understanding of the validity of real estate as an important asset class for pension funds in Asia. The following are some effective enabling strategies for increased real estate exposure in Asian pension funds; within the context of their portfolio risk profiles.

**(1): Use of different real estate investment vehicles**

Direct real estate is an important element in the real estate portfolio; however, liquidity concerns, fund size constraints and management issues often prevent significant levels of direct real estate in the pension fund portfolio. As such, other significant real estate investment vehicles available to pension funds in Asia include listed Real Estate Investment Trusts (REITs) and unlisted private real estate funds; reflecting the rapid growth in funds management in Asia in recent years. These real estate investment vehicles have different real estate investment characteristics (eg: differing levels of liquidity, risk, diversification), as well as providing exposure to both domestic and international real estate markets. Both are considered key elements in a real estate investment portfolio for pension funds. The larger pension funds will also consider separate accounts and club deals to achieve better alignment of interests.

**(2): Real estate risk management procedures**

Pension funds need to consider a range of internal risk management procedures to establish increased levels of real estate in their portfolios. This involves establishing a clearly articulated real estate investment strategy, including:

- real estate types (eg: core) and real estate sectors prioritised
- increased use of experienced real estate professionals; often seeing an in-house real estate investment section established, as well as the use of external fund managers and asset consultants
- increased strategic involvement with the pension fund's investment committee; eg: transparent and timely reporting on real estate performance
- use of risk sharing strategies, including joint ventures and co-investment with other major pension funds, sovereign wealth funds and real estate investors; South Korea's National Pension Scheme has used this strategy effectively, with alignment of interests being a key factor in the success of this strategy
- focus on existing asset enhancement and tenant retention, as well as further real estate acquisitions
- prioritising environmental and sustainability issues in the overall real estate strategy
- increased use of asset consultants (eg: Mercer, TowersWatson) for independent strategic real estate advice.

**(3): Improved levels of real estate information**

A key contributor to the lack of understanding of real estate as an asset class by pension funds in Asia has been the general lack of real estate information available; particularly in comparison to the other major asset classes. This was clearly highlighted in this Asian pension fund survey and real estate industry interviews. This is a key area needing to be addressed by the real estate industry in Asia to enhance the integrity of real estate as an asset class in Asia and facilitate substantive real estate investment decisions by Asian pension funds. It will also play an important role in correcting some potential misunderstandings about real estate by some pension funds; this includes aspects such as real estate being a volatile asset class. This will take on further significance as many pension schemes in Asia move away from being defined benefit to being defined contribution, with this shift seeing an increased emphasis on asset performance and effective asset management.

Key aspects needing improvement are the availability of direct real estate performance indices for Asia, the provision of added-value real estate analytic services to facilitate real estate investment decisions for both unlisted and listed real estate in Asia, and the improvement and standardisation in valuation procedures by the Royal Institution of Chartered Surveyors (RICS) and the International Valuation Standards Committee (IVSC).

All of the above initiatives will actively contribute to the enhanced integrity and understanding of real estate as an important asset class for pension funds in Asia, as well as facilitating increased levels of real estate in pension fund portfolios in this current environment of reform and strategic reassessment of asset allocations within the Asian pension funds.

## REAL ESTATE AND ASIAN PENSION FUND IMPLICATIONS

This paper has highlighted the potential for increased real estate exposure in pension fund portfolios in Asia. The proven international experience of real estate being an important asset class for pension funds has been clearly highlighted, including the range of real estate investment vehicles available to effectively achieve this real estate exposure.

The previous focus of pension funds in Asia on low yield fixed income assets has seen major concerns over pension funds in Asia being able to meet their substantial future liabilities; particularly with an aging Asian population. This has proven to be a catalyst to reassessing Asian pension fund asset allocations and has highlighted the potential value-added contribution that real estate can make to these increasingly important portfolios. This strategy has already been recently adopted by several pension funds in Asia, including South Korea's National Pension Scheme and Malaysia's Employees Provident Fund.

Real estate is an important asset for pension funds to include in their portfolios using a variety of real estate investment vehicles. This has been further confirmed by this survey of Asian pension funds and interviews with leading real estate professionals in Asia. It is expected that real estate will also become an increasingly important asset class for Asian pension funds in future years; particularly as pension funds in Asia increase their understanding of the integrity of real estate as an asset class. Given their significant levels of assets under management, such positive actions by Asian pension funds in increasing their real estate allocations will also see a stimulus to all major sectors of the real estate industry in Asia, including real estate funds management, real estate asset management, valuation and real estate professional services. This will further benefit the ongoing development and sophistication of the real estate industry in Asia and internationally.

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