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HD **Sinking Yields in Asia Spur a Property-Buying Shift; Investors Are Modifying Their Strategies and Taking on More Risk**

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Commercial real-estate yields in Asia are the lowest in the world, forcing investors to pay top prices for the highest-quality buildings, take on more risk or consider property investments outside of their regions for the first time.

Yields for centrally located office buildings are just 2.2% in Taipei, 2.8% in Hong Kong and 3.5% in Tokyo and Singapore. By comparison, they are 4.7% in New York and 3.8% in London's West End, according to CBRE Group Inc.

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Pension funds, sovereign-wealth funds and other institutional investors have been willing to accept such low returns because they look attractive in a low interest-rate environment. But it also means that buyers are exposed to a loss in value if interest rates rise and demand for such low yields cools.

Yields have fallen so far in Taiwan that financial regulators last year instituted a new rule that limits domestic insurance companies' investments to properties that offer a rental yield of 2.875% or above. Authorities also have allowed insurance companies to buy real estate outside the country's borders for the first time.

Investors are modifying their strategies. Terence Loh, executive director at China-focused investment fund CDH Investments, said he has been investing in development projects in cities such as Beijing, Hangzhou and Xi'an rather than buying existing buildings. "The risk-reward is more compelling," he said.

Yields are an important measure of commercial-property values because lower yields typically mean higher prices. They are calculated by dividing the annual income by the price.

Traditionally, yields in Asia are lower than they are in Europe and the U.S. because often there are more buyers chasing fewer properties. Pension funds, sovereign-wealth funds and other institutional investors favor fully leased, well-located buildings and there are fewer of these in Asia. Also, many of these investors, until recently, have been reluctant to venture outside the regional markets they know best.

But lately yields in Asia have fallen to unusually low levels, along with the rest of the world. Buyers can tolerate smaller yields partly because they can borrow at lower costs and the lower returns still look attractive compared with the debt market.

Yields also have been falling in many countries because the annual incomes of properties aren't keeping up with rising prices. Prime office rents in Beijing and Shanghai, for example, have stayed flat over the past two years, according to CBRE, while those in Hong Kong and Taipei rose 2.3% and 1.1%, respectively, in the past year.

In some Asian cities, including Taipei and Beijing, yields are at or near historical lows, according to CBRE. In **Hong Kong**, they are at similar levels to the last major **property** boom in 1997. In Tokyo, the yields are at their lowest levels since 2005, CBRE says.

In Taipei, for example, Mercuries Life Insurance Co. Ltd. in April bought almost 8,000 square meters of retail space in the podium at Taipei TiT Tower Square for 3.95 billion New Taiwan dollars (US$131.5 million), with a rental yield of 3%, according to Real Capital Analytics, a real-**estate** data **firm**. The seller, Homax **Group**, acquired the same **property** in June 2011 at a price of NT$2.8 billion for a yield of 4.5% at the time.

In Singapore, a **group** of local companies in May bought a 93% stake from Keppel REIT in the Prudential Tower in the city's central financial district for 512 million Singaporean dollars (US$409.3 million). The deal boasted a 3.5% yield, according to Real Capital. By comparison, Keppel REIT in 2011 bought the Ocean Financial Centre, also in the heart of Singapore, for S$2.0 billion in a deal that offered a 5.3% yield, Real Capital says.

Investors have started to leave their comfort zones to find higher yields. Some have targeted Australia. Yields are at 6% in Sydney's and Melbourne's main office districts. Singapore-based real-**estate company** Hiap Hoe **Group** bought an office building in Perth for 90 million Australian dollars (US$84.8 million), at a yield of 8.3%, according to research by **property firm** JLL.

Other investors are seeking distressed properties, hoping to boost yields by increasing revenue. Gaw Capital Partners, a **Hong Kong**-based private-equity real-**estate firm**, earlier this year paid US$30 million for the Hyatt Regency Osaka in hopes of turning around a **hotel** that lost US$10 million in the year ending March. "We saw a lot of quick fixes that we could do and cost-cutting that would make the **hotel** cash-flow positive right away," said Christina Gaw, managing principal and head of capital markets at the **firm**.

Some real-**estate** experts say investors are willing to accept low yields because they feel that **property** incomes are poised to rise after years of stagnation, especially in Japan as it emerges from a long slump. They point out that **commercial property** often benefits from rising inflation because it allows landlords to raise rents. "Investors are going into Tokyo with the expectation of rising rents," said Alistair Meadows, international capital **group** head at JLL.

But others say investors accepting low yields are walking a thin line. Many of them have been trying to boost returns by adding leverage, a risky formula that exposes investors to default if rents or values decline.

Also, if interest rates rise faster than inflation, owners could get squeezed, especially if they have floating-rate debt, experts say. "These tight [yield] rates will have a very small margin of error," said Nicholas Wilson, research manager for capital markets in Asia Pacific, at JLL.

Esther Fung in Shanghai and Aries Poon in Taipei contributed to this article.

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