MARKETBEAT

China Outbound Investment Capital Watch

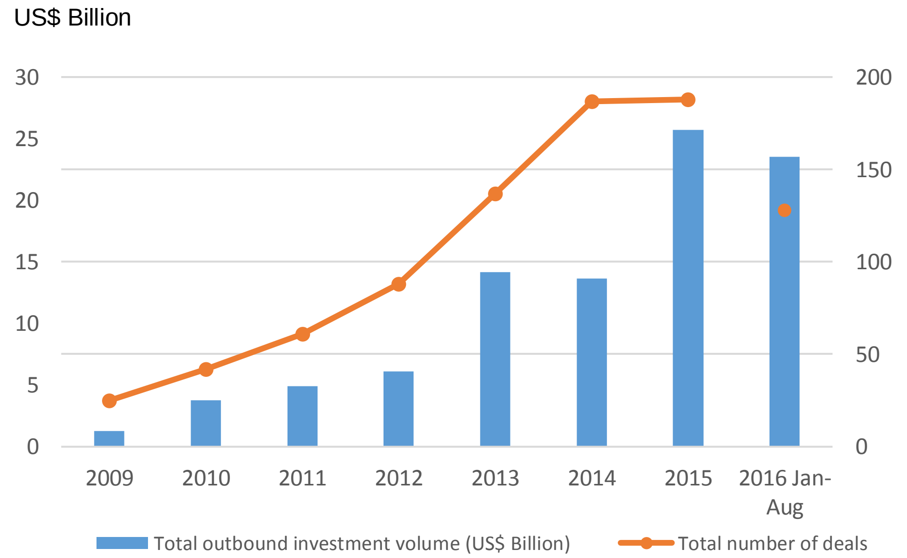
Q3 2016

Market Highlights

- Chinese outbound investment by volume is set to hit a record high in 2016. Already, US$23.5 billion of en-bloc investments have been recorded over the first eight months, nearing the US$25.7 billion invested for the full year in 2015.
- More Chinese investors are looking overseas for opportunity due to limited availability of quality salable assets in Tier-1 cities and further compression of cap rates for core or core-plus assets.
- Another driver for overseas capital deployment is concern over potential RMB depreciation along with record low borrowing rates in mature markets such as the U.S. and U.K.
- DTZ/Cushman & Wakefield forecasts Chinese outbound investment will continue to grow over the short- to mid-term as investors diversify their portfolio on a global scale. Favored investment destinations will likely remain the U.S., Australia, U.K., Germany and France in the near-term. Investors will continue to demonstrate a preference for office assets, with hotels and development sites strong runners-up.

Figure 1

Total Outbound Investment from China (All Property Types, 2009 – Aug 2016)



Source: RCA, DTZ/Cushman & Wakefield research

**Investment volume is calculated based on actual investment dollar value, not asset value.*

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Economic Overview

Q2 saw China match its slowest quarterly growth since 2010 at 6.7%. Despite a slowdown in the national economic growth, there has been robust non-financial outbound direct investment (ODI) at US$118.1 billion recorded over the first eight months of 2016, surging 53.3% y-o-y and eclipsing inbound FDI growth of 4.5% over the same period.

Investment by Asset Class

Office and hotel investments remain the favored asset classes, according to data from Real Capital Analytics (RCA). Over the first 8 months of 2016, office transactions accounted for over half of Chinese outbound deals (en-bloc), followed by hotel investments at 33%.

Office assets have the perceived benefit of relatively stable cash-flow streams thanks to a typical lengthy lease commitment of 10 years or more in developed countries like the U.S. and U.K. Core office assets in mature destinations are also viewed as providing strong resistance to market volatility, thereby being a relatively safe investment option. Hotel assets, on the other hand, although vulnerable to seasonality, on average have offered Chinese investors higher capitalization rates than office or retail assets. Landmark hotels may be attractive to tap into rapidly rising Chinese tourism overseas and offer a degree of prestige.

Investment by Destination

Chinese investors elected mature markets almost exclusively as their destination of choice. By value, 97% of the transacted amount through the first eight months of 2016 was limited to five markets: the U.S., Hong Kong, Australia, U.K. and Canada (in order of preference and according to RCA).

The result of Brexit has in fact triggered an increase in investor interest in the U.K., particularly assets in London, as all investments made in the U.K. so far this year have been in the city. Some Chinese investors view Brexit-related uncertainty and the dip in Sterling's value as a timely opportunity to secure quality assets and leverage the currency advantage. A recent example is Shenzhen-based Vanke's acquisition of Ryder Court in London. The acquisition followed reports that Henderson Group was putting the office property on the block to increase cash reserves as some investors called for redemption. Nonetheless, the U.S. market has been in primary favor this year at a 57% share of Chinese investment volume, thanks to an economic rebound and strengthening dollar.

Figure 2

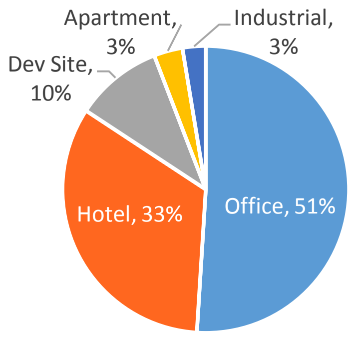
Economic Indicators (Year-on-Year Growth)

	2015	2016	Past 12-Months
GDP Growth (Q2)	7.0%	6.7%	▼
ODI Growth (Jan–Aug)	18.2%	53.3%	▲
FDI Growth (Jan–Aug)	8.7%	4.5%	▼

Source: China Statistics Bureau, Ministry of Commerce

Figure 3

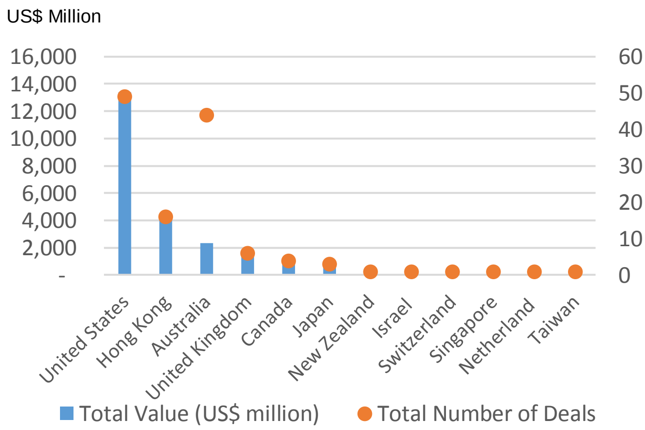
Chinese Outbound Investment by Asset Class (Jan – Aug 2016)



Source: RCA, DTZ/Cushman & Wakefield research

Figure 4

Chinese Outbound Investment by Destination (Jan – Aug 2016)



Source: RCA, DTZ/Cushman & Wakefield research

OUTLOOK

Based on strong investment activity seen over the first eight months of 2016, DTZ/Cushman & Wakefield forecasts Chinese outbound real estate investment volume (en-bloc) will surge 37% in 2016 over last year. The forecast suggests a record US$35 billion in overseas Chinese property investment by year's end. The flood of outbound capital has just begun, as further growth in available funds and capital allocation overseas is anticipated.

This year's clear trend of outbound capital finding its way to mature markets and gateway cities seems set to continue over the mid-term as investors seek stability and steady returns. As the Chinese investment community becomes increasingly experienced in overseas property management and operation, they will likely expand their horizon to growing markets, opening up a broader playing field. Ahead, the mode of investment will see diversification, and intending investors will increasingly look to alternatives such as investing through funds or consider forming joint ventures with local firms with operational experience in those markets.

The U.S. and Australia will remain a key focus, with the U.K., particularly London, continuing to attract Chinese investors provided that the current exchange rate advantage remains intact and that the Brexit referendum result remains the status quo or can be settled without major economic disruption. On the other hand, assuming successful resolution of outstanding issues within Europe or at least no further major disruption, Germany and France will continue to remain attractive to Chinese investors.

Chinese capital will likely continue to play a part in supporting healthy gateway markets globally for some time to come. Recent transaction evidence and investor sentiment would point to greater sophistication of China's outbound investment community. Investors are increasingly conscious of, and factoring in, exchange rate volatility, local regulations – including debt and taxation policy – and market stability, and are becoming acutely aware of political risks so as to make informed calls.

Significant Investment Transactions, Jan – Aug 2016*

PROPERTY NAME	REGION/COUNTRY	INVESTOR	TYPE	PRICE (US$million)	SIZE (SQ M)	DATE
Strategic Hotels & Resorts Inc	Washington DC, San Francisco, etc, U.S.	Anbang Insurance Group	Hotel	6,500	7,571 rooms	May 2016
285 Avenue of the Americas	Manhattan, U.S.	China Life JV RXR	Office	1,650	162,484	May 2016
Mass Mutual Tower	Hong Kong, China	Evergrande RE Group	Office	1,606	32,091	Jan 2016
Dah Sing Financial Centre	Hong Kong, China	Everbright Group	Office	1,285	37,171	Feb 2016
Salesforce Tower	Manhattan, U.S.	Hong Kong Monetary Authority (HKMA)	Office	1,150 (49% of share)	111,000	Aug 2016
Bentall Centre Tower I, II, III, IV	Vancouver, Canada	Anbang Insurance Group	Office	1,000	134,843	May 2016
One New York Plaza	Manhattan, U.S.	China Investment Corp	Office	700 (49% of share)	236,431	May 2016
One Harbour Gate (East Wing)	Kowloon, Hong Kong, China	Cheung Kei Group	Office	580	25,000	July 2016

Source: DTZ/Cushman & Wakefield, Real Capital Analytics
**Deal value over 500 million USD*

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