

Invest in Japan? Certainly, Mr. Abe

Dr. Leonard Meyer zu Brickwedde, founder and president of Kenzo Capital Corporation, has witnessed — and played his part in assisting — a significant change in the Japanese real estate market over the last ten years, a change marked by the establishment and growth of an institutional share. We asked Dr. Meyer about Japan's real estate market and his company's work to bring long-term oriented core investors from Europe into this young but "fair and transparent" market.

What is your background in the Japanese real estate industry?

I have lived in Japan since 1993. I came first as a banker for Germany's HypoVereinsbank and from 1997 worked as a branch manager for the same bank. I started to get interested in what would become the Japanese real estate market in 1997 or 1998, when I anticipated that Japan too would have institutional investors and that the Japanese real estate industry would move away from a market dominated by corporate ownership. In 1999 I was able to convince the bank to begin financing real estate on a non-recourse basis. Until then you could only finance real estate if you financed companies and took the real estate as a security. That was not what we wanted to do. We wanted to finance purely as a project, meaning we would finance the real estate with the security being only the real estate and the cash flow from the property. In March 2000 we completed our first financing transaction on a non-recourse basis through an investment done by Babcock and Brown. Other transactions followed. In 2004 I joined the Hypo Real Estate Group, a new company that was a spin-off of the real estate business of HypoVereinsbank, and in 2008 I decided to start my own company, Kenzo Capital Corporation.

What were the features of the Japanese real estate market in those early days?

In 2000, when the first investors came

in, it was a market for opportunistic investors. The market needed liquidity to get started again, for prices to recover [after the collapse of the asset price bubble in 1991]. It was also necessary to build a more transparent market. In 2001, J-REITs (Japanese Real Estate Investment Trusts; listed on the Tokyo Stock Exchange) were introduced, and these greatly increased transparency in the market. J-REITs have to be totally transparent with everything they do. When they buy a property, they have to tell the public or the investors what price they bought it for, what the occupancy is, what the average rent is, what the costs are and what the net income is, so that everyone knows at exactly what investment return they have bought that property. From around 2006, and with this new transparency,

I was convinced that the market was ready for long-term oriented investors. In Germany we have many large core investors of this type, those who invest in property not to take the opportunities in market cycles but instead to benefit from the ongoing cash flow over a long time.

Which is where Kenzo comes in...

I established Kenzo as a platform, meaning we provide investment advisory and asset management for these investors. We have also established our own fund — a German fund to which institutional investors subscribe. We have a clear concentration: one, the Japanese market; and two, European investors, who are predominantly German. The advantage that we have,

German Prescience in Yokohama

The first institutional investors in the Japanese real estate market in 2000 were companies like GIC, Babcock and Brown, and Lone Star. Predating even these investments, however, was a closed-end fund of Deutsche Bank which in 1987 constructed a large building in Yokohama called the German Center for Industry and Trade. Located in the Hakusan High-Tech Park, the building, a home to many high-tech German and international companies, is today known as the German Industry Park. The initial investors were wealthy private clients of Deutsche Bank. In 2008 the fund was closed after the building was sold to a fund of Deka Immobilien, one of Germany's two largest open-ended real estate fund managers.

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– Dr. Leonard Meyer zu Brickwedde

and what investors realize about us, is that we understand the market here. Besides myself, all the staff are Japanese; everyone has built up experience in this market for overseas decision makers, and knows what it takes to do business in one legislation and to communicate with people in a totally different legislation and totally different environment. Two [staff members] have also conducted real estate business abroad for Japanese decision makers. So we have this experience, and with myself, I know the environment under which our investors have to work: the supervisory environment, the legal environment. We may have to discuss, for example, how a TMK (specified purpose company; an investment vehicle) or GK (anonymous partnership) structure in Japan compares with something that is possible under German law.

What particular issues do overseas investors in Japanese real estate face?

The most important thing to be successful in this market is to find a local team in whom you can trust. If you make a quick decision and choose the wrong partner, when you come to all the specialities of the market you can feel pressured to make an investment and make the wrong decision. Other than that, the market has no additional risk. The market is very fair and transparent. If you deal with the right partners, you can be very successful. Including my years with Hypo Real Estate, I have done with my team in total between 7 and 8 billion euros of financing, and we have earned good returns while not losing money due to a defaulting transaction. That's not my success; that's the success of my team. I knew that I could only be suc-

cessful if I found a team I could totally trust; if I do not force them into a transaction; if I just trust that they will find the right transactions and do them not because there is a bonus at the end. You find people here who are trustworthy and who see I just want to do business, who say, once the loan is repaid that's my reward, not the bonus.

How would you describe the health of the real estate market in Japan today?

There is much more money going into real estate, first of all from the Japanese side. The J-REITs mainly get their money from the private sector; from the retail market. The total assets under management of all the J-REITs together has grown to 11 trillion yen. Three years ago Japan also invented a private REIT, meaning there are a number of companies, mainly large developers, who have introduced a REIT where they say, we will never go to the stock market with this REIT, we'll keep it private. This is something that has attracted the Japanese pension funds and life insurance companies, because they do not want to be exposed to the stock market price, which is just about de-

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mand and supply. If there is no supply, all of a sudden the price goes up, and if everyone wants to sell, the price goes down, but of course basically real estate is not something you can trade every day. If the stock market tells you that the price of the stock is at 80 while the building is still worth 100, that is not what pension funds and life insurance companies want, and that is why they have invested heavily in private REITs. These REITs have almost the same legal structure as J-REITs, but the issuer of the REIT promises not to go on the stock exchange, but instead on a regular basis to return the net asset value of your investment. From the Japanese side, this is very important. The market is new. The United States market started in the 1950s; the German real estate market started fifty years ago; the U.K. market is old. But the Japanese real estate market until 2000 was corporate

owned. Only now do we have institutional investment, and total investment is still I would say less than 30 trillion yen. 11 trillion yen of that is assets under management of the J-REITs and the other maybe 19 or less than 20 trillion yen is private managed funds. So that's still comparatively small. [Prime Minister] Abe has been suggesting to the pension funds and life insurance companies to do more money in risk investments. Risk investments means of course first of all stock, but it also includes real estate. Pension funds and life insurance companies will also increase their holdings in real estate, so that's an example of growth.

How does the Japanese real estate market compare in terms of attractiveness with markets overseas?

Foreign investors are also interested in this real estate market. I mean, how many markets do you have that you can still invest in as a core investor? Germany, England, still maybe France, America... but I do not hear from core investors that they are concretely looking to southern Europe or other countries. What happens then is that the investment returns go down because the prices go up, because everyone is competing for properties in the same few markets. So investors have to look for alternatives, and the Japanese market is a very strong candidate.

What is the outlook for the next few years?

I'm very positive about the next few years with regard to real estate and to the Japanese economy generally. I think that Abenomics will be successful. The mistake Mr. Abe made was to speak about the third arrow as something that also could be achieved very quickly. He raised expectations on the third arrow too much, and people were disappointed when nothing happened. As someone who has lived in Japan for many years I know that such structural changes cannot happen overnight. They cannot happen in fourteen months. Mr. Abe is not only supported by the general population; there is also a shoulder-to-shoulder

working together between the government, the Bank of Japan, Keidanren, the companies.... The Japanese elite is sticking together and that's a big difference, and that's why I'm positive about Abenomics and also the future growth from here.

What impact will the 2020 Tokyo Olympics have on all this?

The Olympics will just be an add on. The positive thing I see about the Olympics is that they will give Tokyo and Japanese society a younger feel, because the Olympics are always connected with young people going somewhere. When I'm in Europe or Germany I keep hearing that Japan is an aging society, a dying society. Yes, Japan is aging, but Tokyo is not aging. Tokyo is still growing, Fukuoka is growing, there are other centers that are growing.... And with Mr. Abe, for the first time we have a Japanese prime minister saying we will change the aging trend; we will stop the population shrinking and we will be 100 million people by the year 2050 and not 85 million. This also takes time, but if you support the family enough, if you make it attractive for young families to have more than one child, it can also be achieved. What I'm positive about with Abenomics is that it's a paradigm change in many respects. In the past, we always had a Bank of Japan Governor who said, "yes we will fight deflation, but we are a shrinking population so it's a natural thing that we have deflation." Who trusts in such a statement? To say you want to fight something but at the same time announce you may not be successful! Mr. Kuroda was the first one who said, "without compromising, we will fight it; we will achieve this and we will do x and if x is not enough we will do

epsilon, and if that is not enough then we will do even more." The Olympics will make Tokyo even nicer. They will improve certain aspects of the infrastructure. But the most positive aspect of the Olympics is that they will change the perception of the city. The Olympics will make Tokyo sexy.

What is the significance of Japan hosting MIPIM this year? What are your expectations of the conference?

[Hosting MIPIM] is a great example of how Abenomics is moving down from the administration into industry. It follows up on all the many statements made by Mr. Abe to "invest in Japan." It's an example of how Abenomics and the third arrow are now materializing. I go to two events in Europe every year. One is MIPIM, the other is a similar event held in Munich called Expo Real. Both are large real estate conventions attracting about 20,000 people. The former takes place in March and the latter in October, so they are a good distance apart. On both occasions I see most of our investors. Everyone goes to these events to have meetings. In the case of MIPIM Japan, everyone knows that from Wednesday morning to Thursday evening his schedule will be filled. You might have one meeting with someone and find out together that you need a third person. This is no problem, since the third person is most likely also there, because the whole industry has come together. Business is people; it's not just paper and phones and laptops. So much misunderstanding can be created by communication over the Internet. People need to see each other from time to time. ▣

Interview by Alex Hendy, The Japan Journal

MIPIM Japan: German Investors to Meet Japanese Experts

Dr. Leonard Meyer zu Brickwedde will moderate a pre-MIPIM Round Table Meeting on May 19 engaging representatives of the Japanese real estate elite and German real estate investors. The meeting is sponsored by the Ministry of Land, Infrastructure, Transport and Tourism and will be hosted by the German Chamber of Commerce.