REPURPOSING **ON THE RADAR**

A Unique Opportunity at an Exciting Time

2021

EXECUTIVE SUMMARY

As COVID-19 induced lockdowns expose the weaknesses of income-producing properties around the world, a two-tiered market forms as the more resilient prime assets continue to hold their values, while the non-prime assets start to see their values deteriorate. As a result, we are witnessing massive moves to repurpose assets and bring them to relevance in the evolving landscape across the region. There are five demand drivers consisting of both the pull and push factors influencing the Great Asset Repurposing of the Decade:

1. **Uncertainties around occupier demand over the medium- to long-term**
2. **E-commerce disruption rendering retail assets obsolete**
3. **Prolonged weak international tourism impacting hospitality assets**
4. **The growing importance of Environmental, Social and Governance (ESG)**
5. **Emergence of sectors with structural tailwinds**

There are significant advantages of moving towards asset repurposing as opposed to redevelopment. The key benefits include acquiring assets at a discount to the price of the finished product, reduced competition from investors who are only interested in passive strategies and speed to market, which allows for return to more optimised real estate usage in a shorter time.

There are real opportunities for investors and developers to repurpose some of their assets for alternative or mixed-uses. While there is no ‘one-size-fits-all’ approach, location, demand and local infrastructure will inform what is viable. Repurposed uses are likely to range from healthcare, co-working/flex space to residential (including build-to-rent) and logistics based on case studies we have gathered from across the region.

We also expect to see more opportunities to acquire underperforming assets at reduced values from sellers who are either moving away from the vulnerable sectors or seeking to rebalance their portfolios away from brick-and-mortar asset classes of the old economy into the new economy assets. While the viability of repurposing each asset will be different, we believe this is an exciting opportunity for both investors and developers looking for sites with potential to meet a new evolving demand in the market.

INTRODUCTION

COVID-19 induced lockdowns have exposed the weaknesses of income-producing properties around the world. While many structural shifts within the real estate industry have been ongoing for some time prior to 2020 such as the disruption from e-commerce on brick-and-mortar retail, COVID-19 has, in many ways, accelerated these shifts by several years and in some cases crippled those disrupted sectors. We are starting to witness a two-tiered market forming as the more resilient prime assets continue to hold their values, while the non-prime assets start to see their values deteriorate as functional obsolescence takes hold.

As property incomes and market values come under pressure, asset owners who have been slow in repurposing underperforming assets pre-COVID are now jumping on the bandwagon.

Across the region, we are witnessing massive moves to repurpose assets and bring them to relevance in the evolving landscape.

The most cited cases of asset repurposing involve the conversion of office and hospitality assets into living sectors such as build-to-rent or residential projects, and older industrial assets into business parks and data centres to extract more values. Retail and hospitality sectors have been greatly impacted by COVID-19 due to lockdowns and border closures, with low foot traffic into malls and all-time low tourist arrivals. There has been plenty of activity in recent times to convert these asset classes into living-sectors, offices and industrial spaces, all more resilient than their current uses during the pandemic.

The property cycle also comes into play, as asset owners have diverse views on what is hot and what is not in various territories across the APAC region. For instance, since COVID-19 has had limited impact on the office sector in Seoul and Tokyo, asset owners are actively looking for opportunities to convert hospitality assets into offices and co-working spaces. However, the same sector is not in favour in other markets such as Kuala Lumpur and Shanghai. A structural oversupply of the office market has led office landlords to explore conversion opportunities of older office stock into senior living, residential apartments, and even specialist hospitals in these places. Meanwhile, in Australia, the sustained strength of the industrial and logistics sector is leading investors to seek out creative ways to add to their portfolios, particularly in urban in-fill areas where they can cater to rising demand for last mile logistics facilities. This is leading to the retail and leisure assets being acquired with a view to repurposing.

FIVE **KEY DRIVERS** of Change and Adaptation

1. Uncertainties Around Occupier Demand over the Medium to Long-term

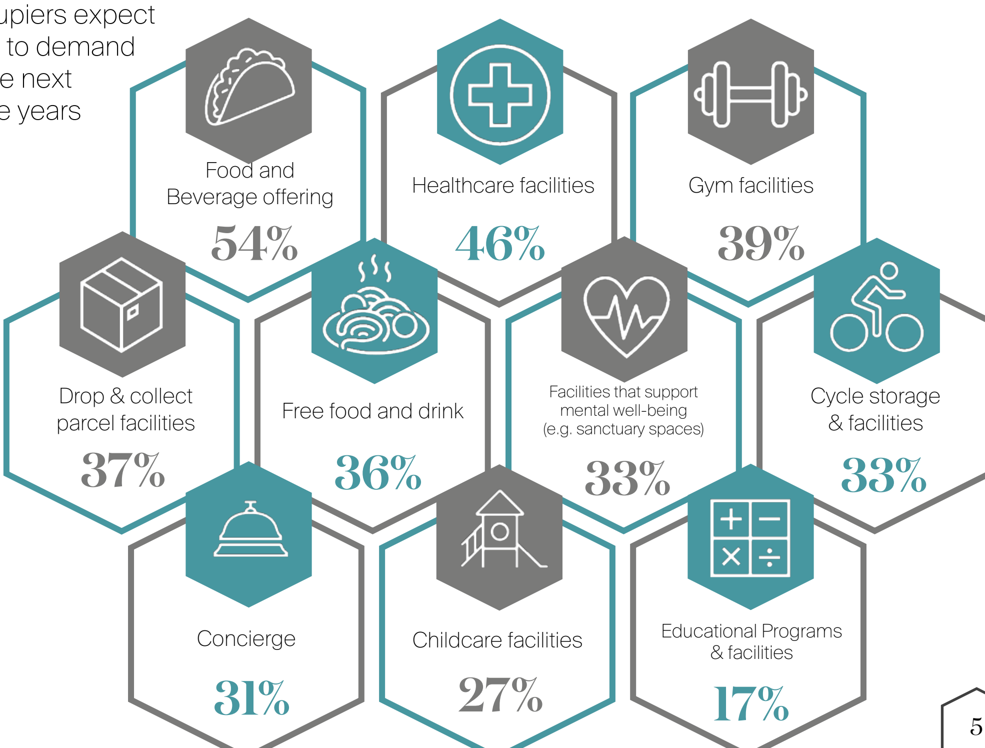
One big push factor in driving asset repurposing is the uncertainties around occupier demand assessment. 75%[1] of the significant global occupiers surveyed by Knight Frank indicate that COVID-19 will have a long-lasting impact on their real estate over the medium- to long-term.

Landlords, particularly those holding older assets, are especially vulnerable. With the adoption of hybrid working models possibly leading to a reduction in occupiers' footprints, quality is likely to come into focus, driving a flight-to-quality trend.

The shift towards more collaborative spaces and more health- and wellness-centric buildings have also resulted in a compression of a building's life cycle and an accelerated rate of obsolescence. For instance, according to (Y)OUR SPACE, healthcare and fitness facilities are the top amenities that occupiers have identified in the next three years, which could possibly pivot pure office buildings to include more such amenities moving forward. As it could be difficult to reposition existing assets, some may choose to tap into government incentives to repurpose the buildings to mixed-use developments.

1 Survey results are based on Knight Frank's (Y)OUR SPACE - 2021 report, which covers occupier trends & the changing workplace. It draws on responses from almost 400 international businesses with a combined headcount in excess of 10 million, providing unique insight into the workplace strategies and real estate needs of global companies. The survey was conducted between December 2020 and February 2021.

Amenities APAC occupiers expect staff to demand in the next three years



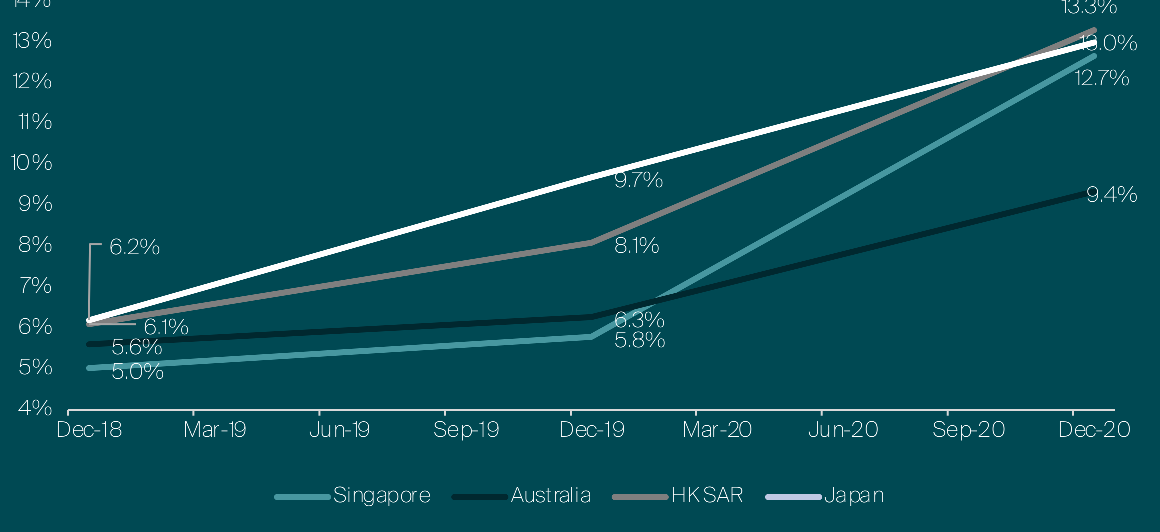
Source: (Y)OUR SPACE - 2021

2.

E-commerce Disruption Rendering Retail Assets Obsolete

Many retail market observers had forewarned the incoming disruption that e-commerce would bring to physical stores, but many would have only expected these challenges to impact discretionary goods such as electronics and books, while non-discretionary consumer staples would remain resilient. However, COVID-19 and its resultant lockdowns ensure that nearly all forms of retail need to have an online presence. Even if the lockdowns across the region are eventually eased, changes in consumer behaviour will likely outlive the pandemic. Footfalls at physical retail stores might not recover to the pre-pandemic levels with consumer spendings shifting towards necessities and away from discretionary items in the near-term. This profound shift means that retail properties, especially those that were struggling before the pandemic, may never regain their pre-COVID values.

Online Retail Share of Total Retail Sales

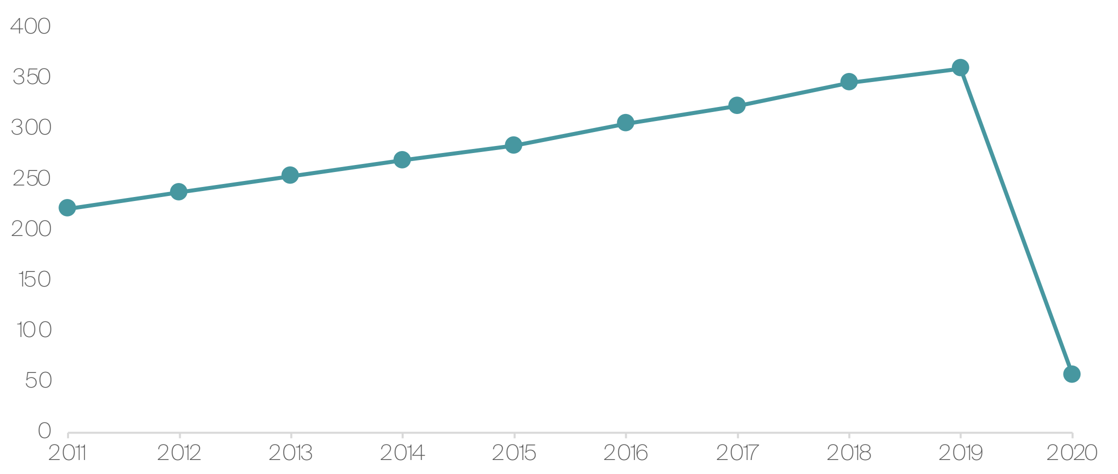


Source: Euromonitor, SingStat, ABS, Statista

3. Prolonged Weak International Tourism Hitting Hospitality Assets

While staycation became the only form of "holidaying" in 2020 for many, it remained a fraction of the tourism demand generated in pre-COVID times. For many major tourism destinations in APAC, the lack of international travel has had devastating consequences. International tourist arrivals for the APAC region slowed to a trickle in 2020, plunging by 84%. Tourist arrivals in Hong Kong and Singapore declined by 94% and 86% year-on-year in 2020. During pre-COVID within the APAC region, mainland Chinese tourists made up around half of inbound arrivals in South Korea, Vietnam, Japan and Thailand, while they account for up to 80% in Hong Kong.

Hotels naturally took the hit with occupancies across the region averaging between 20-30% throughout 2020, leading to significant declines averaging more than 50% in revenue per available room (RevPAR) for most major hotels in Asia-Pacific.



Source: UNWTO

4. The Growing Importance of ESG

Environmental, Social and Governance (ESG) factors have, for the longest time, been seen as desirable by many investors and assets owners globally. However, as institutional investment criteria evolve further and ESG requirements become more of a necessity rather than a vanity, the real estate sector, being one of the largest contributors of greenhouse gases, need to itself evolve to stay relevant. A study conducted by the World Green Building Council has shown that buildings with the highest local green certifications can command price premiums of as high as 20% when compared to transactions of similar conventional buildings without green ratings.

With these in mind and looking ahead, the relevance of ESG will definitely grow in importance among asset owners. With the focus on sustainability and constant drive to reduce downtime, repurposing of the buildings rather than demolitions is becoming the preferred option both socially and economically. The approach to repurpose the non-ESG compliant stock also leads to mixed-use developments, which provide for better live-work environments and unlock a property's unrealised potential by switching to sectors that have a better long-term growth prospect. This is also reflected in Knight Frank's recent Attitudes Survey, where 46% of private bankers, wealth advisors, and family offices in Asia surveyed indicated that their ultra-high-net-worth clients are more interested in ESG investments in late 2020 compared to a year before.

5. Sectors with Structural Tailwinds

While the pandemic has not entirely negatively impacted the real estate sector, traditional commercial sectors such as office, retail and hospitality have received the short end of the stick. The industrial sector is an obvious winner, as the boost in e-commerce consumption has bolstered the demand for logistics space and data centres, while the greater importance placed on life science has increased the need for high-spec biomedical manufacturing facilities. Recent examples have been BioNTech setting up its regional headquarters (HQs) and a vaccine manufacturing facility in Singapore which is expected to be completed by 2023. These are the significant pull factors that have drawn asset owners to the repurposing journey to extract higher value from underperforming asset classes.

INVESTOR OPPORTUNITY

A Creative Approach to Raising Asset Performance

Advantages

Favourable entry price

- Acquire assets at a discount to the price of the finished product
- A way for local players to access stock in competitive markets where prices have been driven up in recent years

Opportunity for differentiation

- Reduce competition from other investors who are only interested in passive strategies
- Opportunity to generate alpha through active asset management expertise

Lower costs versus redevelopment

- A complete redevelopment tends to incur significant costs
- Keeping intact some physical parts of the assets while repurposing them for other uses can reduce construction and renovation costs
- Less architectural, engineering, legal and professional fees incurred overall

Speed to market

- A redevelopment can be a lengthy process
- Adaptation to new circumstances may call for faster processes to react to new environments
- Repurposing assets can be significantly quicker, allowing for return to more optimised real estate usage in a shorter time

Maximise value

- A good location or having strong complementary uses with surrounding real estate can keep the asset optimised
- Market values for certain segments of the real estate market have changed, thus making more financial sense to repurpose to capture the upside

Challenges

Policy and land use restrictions

- Typically constrained by policies and restricted land use/zoning, but areas with gentrification themes tend to have more flexible guidelines on the change of use
- Some markets such as Hong Kong and Singapore have more robust incentive schemes to allow change of land use to repurpose assets to promote gentrification

Making financial sense

- Given office and retail tend to have higher capital values than residential and logistics, financial viability is always a stumbling block to repurposing
- Hefty upfront capital expenditure is not available to core funds

Lack of development expertise

- Lack of operational capability amongst asset owners may result in slow adoption of asset repurposing

CASE STUDIES

Asset Repurposing from Around the Region

Wisma KFC

Location	Kuala Lumpur, Malaysia
Asset Class	Office -> Hotel
Conversion Metrics	175,292 square feet (sq ft) of net lettable area (NLA) -> 430 room
Year of completion	To be announced (TBA)
Owner	Royal Group
Rationale for repurposing	Traditional office spaces are facing high volumes of incoming supply and a 'flight-to-quality' trend that is putting downward pressures on both rents and occupancy in Kuala Lumpur City.
Asset Analysis	Formerly the main office of Kentucky Fried Chicken in the 1990s, the asset had been left vacant since 2017. In 2019, the 22-storey office building was sold by Employees Provident Fund (EPF) to Singapore-based property developer and manager, Royal Group for RM130 million (US$31 million). EPF also submitted plans to the city council of Kuala Lumpur on 1 November 2019 seeking planning permission to convert the long-vacant office building into a 430-room luxury hotel.

Menara HLX (formerly known as Menara HLA)

Location	Kuala Lumpur, Malaysia
Asset Class	Office -> Co-working & Co-living spaces
Conversion Metrics	385,215 sq ft (no change to NLA)
Year of completion	2020
Owner	Tower Real Estate Investment Trust
Rationale for repurposing	Heightened competition amid a prolonged office glut due to high incoming supply of office space and weak occupational demand, continues to impact occupancy and rental levels.
Asset Analysis	Since 2014, the aging Menara HLX (formerly known as Menara HLA) had been experiencing rising vacancies due to the supply growth momentum of new buildings and limited demand growth. In 2019, with occupancy level reaching 34%, Hong Leong Group launched its innovation exchange, the HLX, together with the Malaysian Digital Economy Corporation (MDEC). A one-stop centre connecting the corporate and start-up community, the HLX strives to accelerate innovation and boost Malaysia's start-up ecosystem. Spanning 250,000 sq ft, HLX comprises of working spaces, electronic gaming academy, a data centre, innovation labs, event space, living space, gym, and F&B outlets.

RETAIL

Auburn Redyard Centre

Location	Sydney, Australia
Asset Class	Retail/Leisure ->Logistics
Conversion Metrics	4.82 hectare land holding
Year of completion	TBA
Owner	Charter Hall (recently acquired from Reading International)
Rationale for repurposing	To cater to rising demand for last mile logistics facilities in a supply-constrained inner-West market. Rental and capital growth prospects are considered to be far better with the change of use.
Asset Analysis	The scheme has just been bought by Charter Hall for AU$90 million (US$66 million). The company intends to repurpose the asset into a last mile logistics hub. The completion of the M4/M5 Link Tunnels in 2023 as the last stage of the WestConnex project will further enhance the attractive location characteristics of the site and significantly reduce travel times to Port Botany and the airport.

Homemaker Prospect

Location	Sydney, Australia
Asset Class	Large format retail -> Industrial
Conversion Metrics	25,770 square metres (sqm) -> unknown
Year of completion	Planned for conversion (timing unknown)
Owner	Dexus
Rationale for repurposing	To cater to rising demand for industrial space in Western Sydney. Long term rental and capital growth prospects are considered to be better with the eventual change of use to industrial.
Asset Analysis	The scheme was purchased by Dexus for AU$65 million (US$48 million). The asset owner intends to convert the asset to industrial use. Large-format retail centres such as Homemaker Prospect that are close to major road interchanges offer strong potential for warehouse and logistics operations.

G: Corp Pulse Mall

Location	Pune, India
Asset Class	Retail -> Office
Conversion Metrics	0.3 million sq ft -> 0.45 million sq ft (Built-up area)
Year of completion	2020, Ready for fit-outs
Owner	G: Corp
Rationale for repurposing	Poor business economics as a retail asset on account of competition and mall design.
Asset Analysis	As a retail mall, the property was facing poor financial economics. Since the catchment is strong on connectivity and other commercial market prospects, this asset has been repurposed from retail to office use. As progress, over 25% of the property has already been leased.

HOSPITALITY

Ootopia Hong Kong

Location	Kowloon and Hong Kong Island, Hong Kong
Asset Class	Hotels -> Co-living & serviced residence
Conversion Metrics	Total GFA of 3 premises: 48,000 sq ft, over 150 rooms
Year of completion	All opened in 2019
Owner	ARCH Capital and Wanderwonder Hospitality
Rationale for repurposing	Investors like ARCH Capital (private equity-backed fund real estate manager) targeted hotels for conversion into co-living spaces as the tourism industry struggles with the effects of months of social unrest and the coronavirus pandemic, while capturing the growing trend of a sharing economy. From investors' perspectives, co-living premises provide risk-adjusted returns than traditional real estate investments.
Asset Analysis	Oootopia is a branded co-living serviced residence backed by Hong Kong-based ARCH Capital and Singaporean-based Wanderwonder Hospitality. The Oootopia Kai Tak and Oootopia Tai Kok Tsui were both converted from the former Bridal Tea House Hotel, a chained boutique hotel. The co-living brand expanded its footprint rapidly to three premises within the same year.

JC Mandarin Plaza

Location	Shanghai, The Chinese Mainland
Asset Class	Hotel -> Office & Retail
Conversion Metrics	58,195 sqm -> 55,000 sqm
Year of completion	Estimated 2021
Owner	Shanghai Baohua Group
Rationale for repurposing	In order to adopt an asset light business model, the seller Jinjiang Co.,Ltd. sold JC Mandarin Hotel, an old hotel asset with poor operating performance to recycle capital. The buyer, Baohua Group, has transformed it into a high-end commercial complex to fill the new supply gap in the core CBDs.
Asset Analysis	The former Shanghai JC Mandarin Hotel, one of the city's oldest luxury hotels dating back 30 years was sold to Shanghai Baohua Group in 2014 for RMB2.118 billion. Baohua together with Gensler have worked on the transformation of this hotel to a Grade-A office building with a retail podium since 2016. So far, they have secured office leases with several principal tenants including SHANGXIA and Dior.

HOSPITALITY

Le Méridien Seoul

Location	Gangnam-gu, Seoul, South Korea
Asset Class	Hotel -> Residential (expected)
Conversion Metrics	Not available
Year of completion	Under Planning
Owner	Wealth Advisors – Hyundai Engineering and Construction Consortium
Rationale for repurposing	Repurpose the asset into luxury residential to fully utilise one of the most core locations in Seoul GBD area. Recent Covid-19 and imbalance of supply and demand in Seoul's residential market have pushed for this asset repurposing.
Asset Analysis	The hotel opened as a Ritz-Carlton Hotel back in 1995 and renovated into Le Méridien Seoul in 2017. It was one of Korea's the most luxurious hotels but due to the opening of other newer, more prestigious hotels in Seoul, it couldn't maintain its top status. The hotel is in one of the best locations in Seoul GBD (Gangnam) area and recent Covid-19 and imbalance of supply and demand in Seoul residential market boost this repurposing. The new owner bought it for KRW700 billion (US$620 million) and is expected to put it under planning process.

BizMiiX Yodoyabashi

Location	Yodoyabashi district, Osaka CBD, Japan
Asset Class	Hotels -> Office
Conversion Metrics	Nine-storey Steel Structure, Total GFA of 1,821.56sqm.
Year of completion	Conversion completed in December 2020 (Original Completion January 2017)
Owner	MIRAI Corporation (J-REIT)
Rationale for repurposing	The Yodoyabashi area has had strong office demand on the back of limited new supply. Changes in office demand had been observed since the declaration of the state of emergency in April of 2020 from the perspective of office layout, participating in online meetings and nee for arranging teleworking environment. On the other hand, hotel occupancy in the area had been stagnating due to significant decline of overseas tourists.
Asset Analysis	The hotel originally had been operated as a Hotel WBF Yodoyabashi-Minami. However, the tenant/ operator's bankruptcy has triggered the conversion aiming to convert into high value-added, serviced office property which will be favoured in post-COVID-19 market.

Big Box

Location	Singapore, Singapore
Asset Class	Warehouse-cum-retail -> Business Park 1 Venture Avenue, Singapore
Conversion Metrics	1.4 million sq ft -> 1.5 million sq ft (gross floor area, GFA) 1.0 million sq ft -> 1.1 million sq ft (NLA)
Year of completion	Estimated to progressively complete from Q4 2021 onwards
Owner	Perennial consortium
Rationale for repurposing	Repurpose the asset into a business park to tap into the decentralisation strategy due to lack of popularity for the retail warehousing concept
Asset Analysis	The original retail warehousing scheme has proven unpopular in Singapore. The former owner could not sustain the enterprise with the mall being sold by a liquidator. The new owner bought it for S$118 million (US$87 million) and had the zoning changed to business park, which is more resilient during the pandemic. It plans to lease the space to potential tenants from TMT, biomedical sciences and financial institutions.

The Repurposing Assessment Checklist

Key Considerations	Questions to ask about the asset
Market profile	Do the best tenants in the market shun your building?
Rental Income	Are your rents underperforming the general market by a large percentage of at least 20%?
Government Regulations	Are there any incentives by government for you to repurpose the building?
Operating Expenses	Are your utility costs and other operating expenses growing at an unsustainable rate due to low energy efficiency?
Investment Trends	Do likely buyers display a preference for your competitors' building?
Risks	Are you running the risk of obsolescence if you do nothing about the current property?
Economic Characteristics	Is your property less marketable than your competitors' buildings?
Discounts	Will the market price your asset at a discount to your competitor's assets as yours is deemed riskier?
Value	Is the utilisation maximising the highest and best use of the property?
Opportunity	Does the repurposed property fulfil an underserved segment in the location?

ASSET STRATEGY – Evaluate, Calibrate, Collaborate

Like many sectors, real estate is undergoing a seismic shift, driven by consumer behaviour and global demographic trends. The onset of the pandemic has accelerated these changes. Most acute of all is the rapid adoption and proliferation of e-commerce, driving growth in the industrial, logistics and data centre markets while simultaneously contributing to the steep decline in physical retail.

The expansion of the living sector, on the other hand, is driven mainly by global demographic changes: urbanisation, ageing populations, greater accessibility of higher education and more. This asset class, propelled by non-cyclical trends, has proven to be a lucrative alternative for many investors.

Last - but by no means least - is the pandemic's impact on the office sector as office workers adapt to hybrid working models, with many demanding spaces that prioritise quality over quantity. As occupiers focus on best-in-class products, flexibility, ESG, and talent-attraction will be critical considerations.

For many investors, the events of the past 18 months have necessitated a new plan for their investment strategies. While some have fled to safe havens in a defensive strategy, others choose an active approach by adapting their assets through repurposing and repositioning to meet the most significant demand within an evolving landscape.

One approach to gathering traction is capital partnering. Owners who pair up with experts in the growing alternative sectors will excel as they circumvent the issues of international travel restrictions as well repurposing assets to sectors previously unfamiliar to them.

Ultimately, the biggest challenge for global investors will be understanding the nuances in each market and adapting their strategy accordingly. Whether this means refurbishing an asset to cater to occupier demand or fundamentally changing its use, engaging with experts on the ground ensures income security and portfolio longevity.

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