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Global Demographics and Their Real Estate Investment Implications

M. Leanne Lachman

THE PAUL MILSTEIN CENTER FOR REAL ESTATE

About ULI

ULI—the Urban Land Institute is a nonprofit education and research institute that is supported by its members. Its mission is to provide responsible leadership in the use of land to enhance the total environment.

ULI sponsors education programs and forums to encourage an open, international exchange of ideas and sharing of experiences; initiates research that anticipates emerging land use trends and issues and documents best practices; proposes creative solutions based on that research; provides advisory services; and publishes a wide variety of materials to disseminate information on land use and development. Established in 1936, ULI has more than 29,000 members in 80 countries representing the entire spectrum of the land use and development disciplines.

About This Report: This ULI and Paul Milstein Center for Real Estate Issue Paper contributes to ULI's ongoing discussion of World Cities Forum topics.

The purpose of the first forum, held in 2005 in London, was to create both a timely and timeless urban agenda that cities around the world can use to improve their prospects for success. People attending offered numerous ideas, noting the need to do the following things:

- Promote tangible services; assure a secure and clean environment;
- Think beyond municipal boundaries and adopt a regional perspective; reinvent and design for change;
- Acknowledge the city's unique identity; build on assets, including history, culture, and the physical environment;
- Make environmental issues a top priority; work toward sustainable communities, not just buildings; optimize stewardship of natural resources; educate and incentivize rather than just regulate;
- Establish a property rights system and create market transparency to encourage investment; provide mixed-income housing throughout neighborhoods rather than segregate housing by income;

- Be open to immigration and different lifestyles; foster economic mobility to offer residents of all classes opportunities for success; attract talent with an environment of intellectual stimulation and creativity;
- Use the public realm to foster community pride; provide ample open space as common ground for all citizens;
- Provide infrastructure upfront as a framework for development;
- Link transportation and land uses; address congestion through a variety of solutions, not just through additional road construction; and
- Be progressive not reactive; consider the legacy for future generations; engage all stakeholders; and think globally and implement regionally and locally.

The next World Cities Forum will be held September 12–15, 2006, in Shanghai, China.

Richard M. Rosan
President

This paper is available on the ULI Web site at www.uli.org/policypapers/issues and on the Columbia Business School Web site at www2.gsb.columbia.edu/departments/realestate/pubs/publications.html.

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The Paul Milstein Center for Real Estate, launched in 2001, is an endowed center of excellence that enriches and expands the reach of Columbia Business School's MBA Real Estate Program. Led by Chris Mayer, Paul Milstein professor of real estate, the center's mission is to provide an educational bridge between academia and its many constituencies by fertilizing research and dialogue; developing events that stimulate discussion among students, alumni, and industry professionals; and producing high-quality educational materials that strengthen the curriculum and can be included in external publications.

Building on the program's reputation for excellence and its existing strengths in real estate finance and investment management, the center offers new opportunities for educational leadership, program innovation, and outreach. The center has developed a roster of activities that includes:

- **Career Mentoring Breakfasts:** Distinguished real estate leaders meet with small groups of MBA students to share insights on building a winning career path, the current job market, and the state of the industry. Breakfasts are headed by mentors from all segments of the industry and such not-able firms as Tishman-Speyer, Merrill Lynch, Shorenstein, Fisher Brothers, and Lazard Frères, among others. Career mentors include many alumni and members of Columbia's Real Estate Forum.
- **Columbia Real Estate Forum:** The center hosts an off-the-record annual meeting of industry leaders at which issues of strategic importance to the real estate industry are discussed candidly. During the year, forum members attend breakfast sessions led by faculty experts.
- **Discussion across Disciplines:** Three times a year the center brings together 25 Columbia professors and invited non-Columbia scholars from a variety of disciplines to participate in an author-led discussion of real estate themes raised in a recently published academic work.

Chris Mayer
Director, Columbia Business School MBA Real Estate Program and the Paul Milstein Center for Real Estate

About the Author

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Providing considerable research assistance for this paper were Deborah Brett of Deborah L. Brett Associates in Plainsboro, New Jersey, who helped on demographics; and Marc A. McGehan, a second-year MBA student at Columbia Business School, who helped on global real estate investments to date.

Global Demographics and Their Real Estate Investment Implications

Summary

Today's institutional real estate investors are expanding their horizons—to global markets and then to core and value-added foreign properties, not only to opportunistic plays. When buying in mature, stable countries, investors assume that moving down the risk scale is safe; however, population and labor force trends suggest that demand for real estate is eroding as Europe, Japan, and South Korea edge toward markets based on “replacement needs only.” Simultaneously, American, Canadian, and Australian demographics continue to support new development, as do those of Asian emerging markets. Short-term real estate options are abundant around the world; but over the next five to 20 years, those who believe that demographics are destiny will find the greatest number of attractive opportunities in the United States and India.

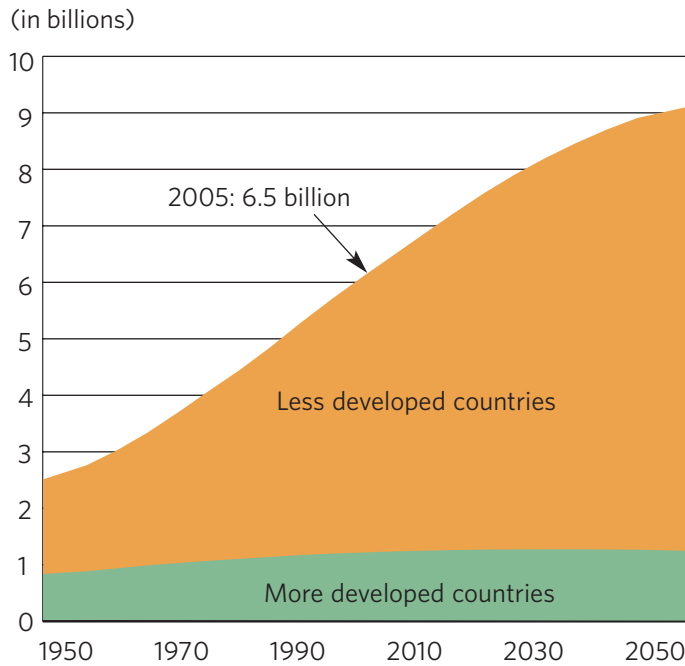
Introduction

Thanks to global real estate securities funds, international commercial mortgage-backed securities products, and global commingled vehicles making high-quality equity investments, opportunity funds are no longer the lone players on the international real estate stage. Global investment is gaining traction among core and value-added investors seeking diversification, so a review of the demand side of the equation is timely. Which countries will have strong future needs for Class A properties? And where is demand likely to decline?

Demographics drive real estate demand over the long term. In this paper, which is largely based on 2005 data, the time span is 45 years—to 2050—but the greatest focus will be the short and medium term (from now to 2025). Both population and labor force growth are essential drivers of property markets, along with rising personal and national incomes. Without users who can afford new space, there is no point in constructing buildings, so demographic and economic expansion is essential to maintaining dynamic property markets—for all land uses. The same is true for consumer markets that attract multinational companies selling cosmetics, soft drinks, cameras, razor blades, or batteries.

Several mature economies that have been considered safe havens for real estate investment are facing serious growth reversals, and some emerging economies are moving rapidly onto the world stage. Consequently, a reevaluation of medium- to long-range plans for property investment may be appropriate. To that end, this paper focuses first on expected socioeconomic patterns of change in key regions of the world¹, then turns to current institutional real estate investment behavior. The final section makes geographic recommendations as

Figure 1. World Population, 1950-2050



Source: United Nations Population Division.

to short- and medium-term investments by property type.

Global Socioeconomic Change

According to United Nations demographers, the world's population growth—from today's 6.5 billion people to 9 billion in 2050—will occur almost entirely in less developed regions. Among mature economies in the aggregate, as illustrated in Figure 1, population will remain flat at best. However, that masks two totally different dynamics. Most developed countries will be losing substantial portions of their populations as deaths far exceed births, but there will be exceptions: the United States, Australia, Canada, and the United Kingdom all will continue to grow over this 45-year period, largely as a result of their longstanding policies supporting expansion through immigration.

The world's population currently increases by just over 1.1 percent annually—faster than America's 0.9 percent growth rate. Six countries account for half the global expansion: India, China, Pakistan, Bangladesh,

Nigeria, and the United States. Among the most populous countries, as shown in Figure 2, the United States is expected to remain third through the middle of this century. India will displace China as the most populous and will have four times as many people as the United States, but America's ranking will hold. China's population will actually decline between 2025 and 2050, thanks to the country's policy allowing only one child per family, which has been in place for over 20 years. China's working-age population will reach about 1 billion in 2015 and then drop steadily.

Russia and Japan will no longer be among the ten

Figure 2. Most Populous Countries, 2005 and 2050

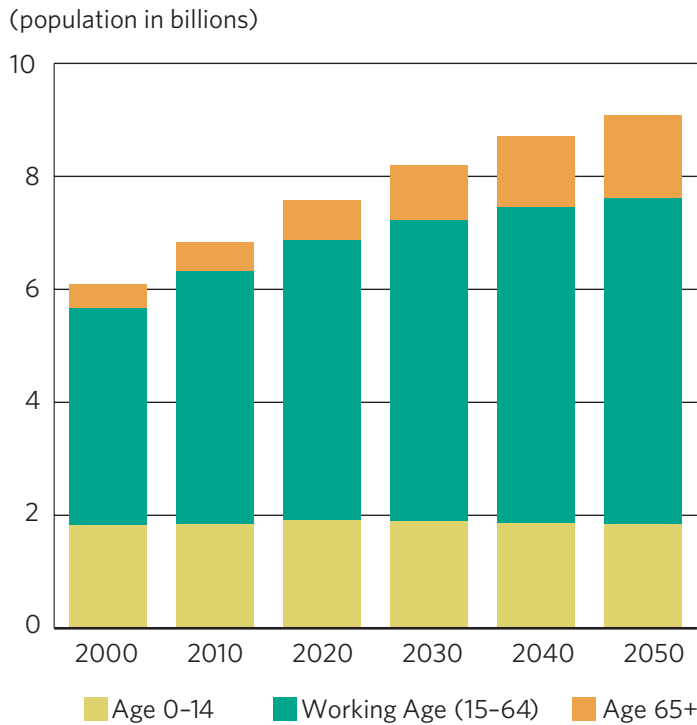
(in millions)

2005			2050	
Country	Population	Rank	Country	Population
China	1,316	1	India	1,593
India	1,103	2	China	1,392
USA	298	3	USA	395
Indonesia	223	4	Pakistan	305
Brazil	186	5	Indonesia	285
Pakistan	158	6	Nigeria	258
Russian Federation	143	7	Brazil	253
Bangladesh	142	8	Bangladesh	243
Nigeria	132	9	Dem. Republic of Congo	177
Japan	128	10	Ethiopia	170

■ Replaced by 2050 ■ Added by 2050

Source: United Nations Population Division.

Figure 3. Expected Global Workforce, 2000-2050



Source: United Nations Population Division.

most populous countries by 2050, and the Democratic Republic of the Congo and Ethiopia will move onto the list. With Japan gone, the United States will be the only currently mature economy in the 2050 top ten.

Broadly speaking, the world will have sufficient labor. The global working-age population is likely to expand by nearly 50 percent between now and 2050, as shown in Figure 3. The problem is that, absent a drastic change in immigration policies, there will not be enough new workers in Europe or Japan. By 2050, the proportion of the world's population that is of working age will decline slightly because of decreases in fertility and subsequent aging of a smaller population. China will account for much of the percentage drop.

To a far greater extent, work will be sent where labor resides, rather than laborers moving to economically developed countries in order to work. This has been the modus operandi in manufacturing for 30 years, as steel, clothes, lingerie, toys, computer parts, and other products have been produced in one low-cost country after another. Now, thanks to

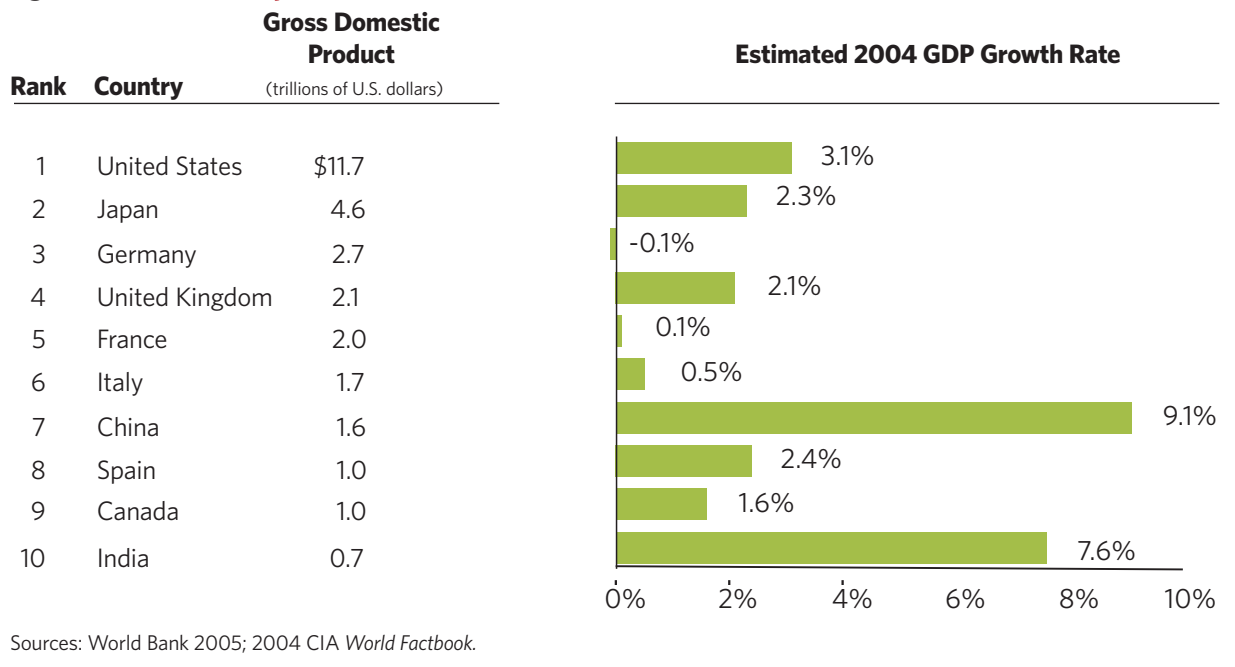
the Internet, business processing is being sent offshore, and many companies are experimenting with the use of multiple research and development locations in different time zones so projects can be worked on continuously on a “follow the sun” basis. The “offshoring” trend will accelerate—of necessity as employers seek access to both skilled and trainable laborers.

A list of the world's largest economies as of 2004, shown in Figure 4, places Japan second only to the United States, followed by Europe's four most populous countries. China is in seventh place, and India is tenth. After this list was compiled by the World Bank, China's National Bureau of Statistics indicated that the country's gross domestic product (GDP) was nearly \$2.0 trillion in 2004, not the \$1.6 trillion it had previously reported. With that change, China is tied with France for fifth place in the world—and is gaining steadily on the United Kingdom and Germany, as the growth rates on the right side of the chart make clear.

American economists are comfortable with annual GDP growth of 3 or 4 percent. After languishing for many years, Japan's GDP is back in the 2 to 3 percent growth range. That country is showing marked improvement partly because Tokyo functions as a key financial center for Southeast Asia, partly because Japanese companies are offshoring work to more dynamic Asian countries, and partly because Japanese firms are investing heavily in regional businesses. Nonetheless, healthy economic growth in the United States, Japan, the United Kingdom, and Spain pales in comparison with the expansion in China and India.

As *Business Week* observed in its “Chindia” issue last August 22, “For the past two decades, China has been growing at an astounding 9.5 percent per year, and India by 6 percent. Given their young populations, high savings, and the sheer amount of catching up they still have to do, most economists figure China and India possess the fundamentals to keep growing in the 7 to 8 percent range for decades.”² *Business Week* predicted that India will move ahead of Germany and be in third place within 30 years

Figure 4. World's Ten Top Economies in 2004



and that China will overtake the United States and have the world's largest economy by 2050. If that happens, China will recapture a global position it held 200 years ago.

Asian progress is truly spectacular. For many years, people predicted that this would be the Asian century, but no one thought it would happen in the first five years! Yet, Thomas L. Friedman's book *The World Is Flat* is subtitled *A Brief History of the 21st Century*.

Prospects for Mature Economies

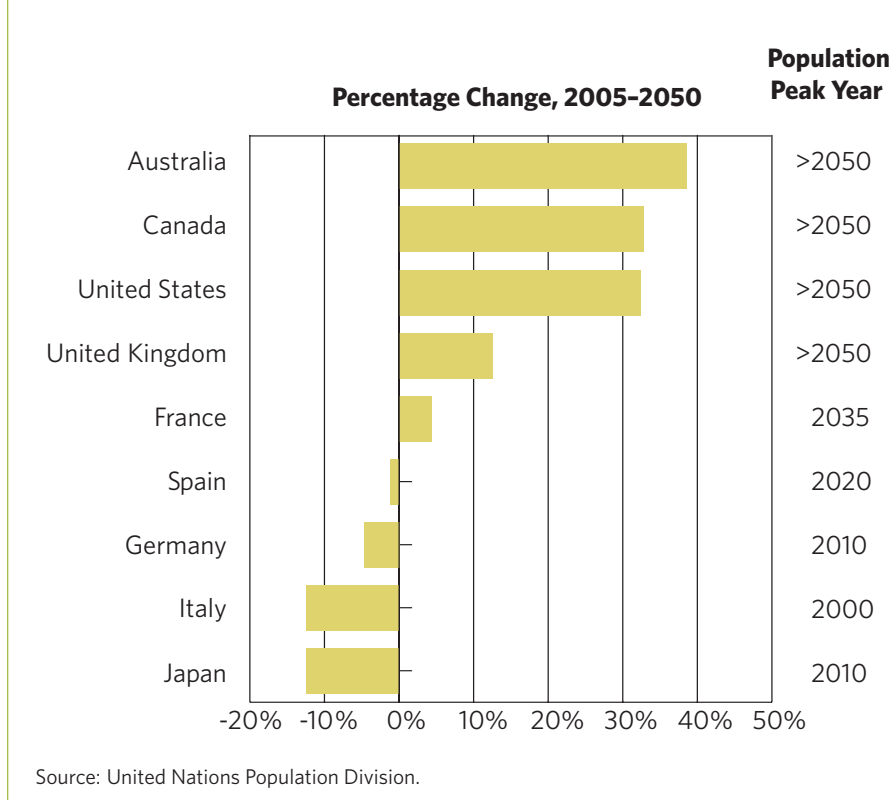
For Japan and continental European countries, the prospects are far less exciting. In fact, as illustrated in Figures 5 and 6, most of their population and labor force changes will be negative between 2005 and 2050. As shown on the right side of Figure 5, Italy's population peaked six years ago. Japan's and Germany's numerical peaks will occur in 2010—just four years away. Spain's population peak is anticipated in 2020, though the Spanish government is trying to deal proactively with immigration to enhance labor force and demographic growth. France is not projected to switch to negative population change until 2035 because its birthrate is one of the highest in Europe—thanks to the expanding Muslim community. Also, the French government

is offering benefits to encourage families to have more children.

Australia, Canada, and the United States have the highest projected growth among the mature economies—and will still be expanding in 2050. Growth will continue in the United Kingdom as well, but not at the vibrant rates of its younger spin-offs. As mentioned, the key to continuing population growth in each of these countries is their long-standing encouragement of immigration. Immigrants tend to arrive as adults, enter the workforce quickly, and subsequently produce more children on average than the native-born residents. As subsequent generations are financially successful, birthrates fall. Hence, ongoing immigration is essential for countries with mature economies to maintain net population and labor force growth. Equally important is assimilation of immigrant families into the culture of the receiving country so they believe their children and grandchildren will have even greater economic opportunities. That motivates employees.

In Europe and Japan, the prospects for labor force expansion are especially troubling. Japan, Italy, and Germany have already peaked in terms of labor force, which United Nations demographers define as the national population between ages 15 and 64. In five years, the workforce will peak in Spain and France. Meanwhile, the U.S. labor force is expected

Figure 5. Projected Population Change in Selected Mature Economies



several important observations. The most startling was that all real estate sectors in continental Europe will evolve into “replacement markets” over the next couple of decades. This is not an easy concept to grasp.

In simple terms, replacement demand results only from one of three factors: demolition of old buildings, fires that devastate structures, or physical or functional obsolescence. In a stagnant economy, neither job growth nor an increase in household numbers generates new demand, so replacement needs are the only justification for new construction. That results in very modest activity—akin to treading water.

to expand by 23 percent between now and 2050. At midcentury, the United States will have the highest proportion of people who are of working age among the mature countries listed.

As working populations shrink, dependency ratios rise. Italy’s population 65 and older will increase by 44 percent between now and 2050, while the potential labor force will decline by 32 percent. European budgets will be severely tested by soaring dependency ratios—the proportion of children and retirees to workers. The situation is exacerbated by the fact that many Europeans have been accustomed to retiring in their early to mid-50s and do not look kindly upon proposed policy changes that would extend retirement ages for them or their children. They also expect a broader and deeper social safety net than Americans have ever had.

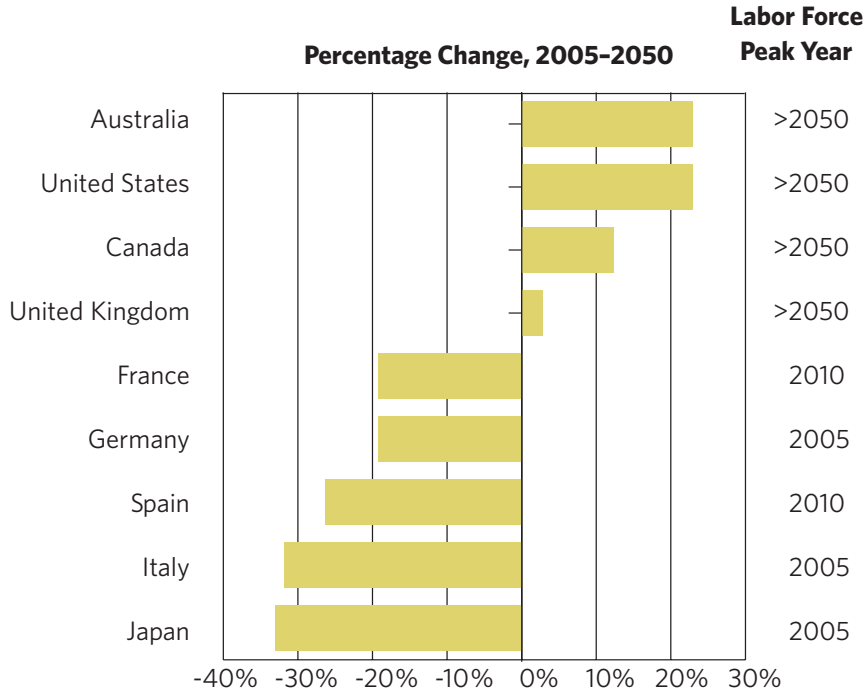
Real Estate Implications of Demographic Contraction

In September 2004, the European Public Real Estate Association issued a report³ on demographic contraction in Europe’s property markets that made

A structural transition to replacement demand is already visible in some European office markets, particularly in Germany. When office job growth is limited or nonexistent, any development of additional inventory produces higher vacancy rates and weaker rents. In Europe, offshoring of business processes is just beginning to accelerate, with work being transferred electronically to eastern European countries, to India, to Central and South America, and elsewhere. Offshoring started as a cost-saving strategy, but meager or negative labor force growth creates a second reason, pushing outsourcing to become more widespread. The effect will be further erosion of office demand.

Labor force reduction has a devastating impact on office markets. As the need for space drops, inventories have to shrink to maintain rent and price levels. For people investing in European and Japanese office buildings, this is a critical point: new development must be accompanied by removal of at least an equal amount of high-quality space. The location need not be identical: for instance, a new suburban project could replace a building torn down closer to the city center. Without net new

Figure 6. Projected Labor Force Change in Selected Mature Economies



Source: United Nations Population Division.

demand, though, there cannot be additional supply—only replacements.

The situation is better in eastern Europe—e.g., Poland, the Czech Republic, Romania, and Estonia. The demographic trends in these countries are actually bleaker than those in central and southern Europe because their fertility rates have been even lower. However, because of stagnation under Soviet rule, eastern Europe has catch-up demand for modern office, industrial, retail, and residential space. Also, jobs in places like Poland and the Czech Republic are shifting from basic industries to services—a transition that generates office demand. And eastern Europeans are beneficiaries of outsourcing from Germany, Austria, the Netherlands, and other European countries.

For retail properties, demand growth relies on income gains, total population increases, or both. Continental Europe's population will decline more slowly than the labor force, so weak demand for store space will not be noticeable as quickly as the lack of office demand. Also, most of Europe wants additional modern, automobile-oriented shopping

facilities, so retail development is likely to continue for some time. Nonetheless, older people do not spend as much on consumer goods, a factor to keep in mind when considering investment in countries with an aging population.

Because growth in the number of households will persist longer than population expansion, the European Public Real Estate Association report suggests that “European housing demand has approximately ten more years of growth potential, but will turn into a replacement market, just like the office and retail markets.”⁴

Overall, the medium- to long-term real estate prospects in mainland Europe and Japan are sobering.

The same is true of consumer demand for most types of products, with the exception of pharmaceuticals and others items needed by the elderly. Recognizing this, Japanese companies like Toyota have been developing products for the seniors' market—from vehicles that accommodate wheelchairs to hydraulic home elevators and orthopedic mattresses. Markets will be strong for housing for the elderly at all income levels, and for a broad range of assisted and communal living facilities.

In the slowing mature economies, real estate investors are well advised to maintain short time horizons. It will take residents and investors a long time to come to grips with the notion of replacement markets, which are very susceptible to oversupply problems. While people struggle with the new realities of stagnant supply and demand, outsiders are well advised to focus elsewhere. Because the point at which growth turns negative will vary from country to country, investors should monitor economic and demographic trends when considering whether to acquire or sell property investments.

For medium- to long-term investing, a focus on countries with growing populations and economies is far more promising. For institutional investors, the most comfortable locations will be the United States, Canada, Australia, and the United Kingdom—all places with large inventories of high-quality commercial real estate, transparent markets, readily available debt, investor-friendly legal systems, title insurance, and large public real estate companies. What's not to like?

Investors with higher risk tolerance should consider some of the dynamic emerging markets. India and China/Hong Kong are the largest, but global investors are increasingly active in Mexico, Chile, Malaysia, New Zealand, Costa Rica, and Dubai as well. Transparency is steadily improving, and title insurance is now available in many emerging markets.

Implications of Comparative Demographic Profiles

The age/sex diagrams arrayed in Figure 7 illustrate the problems and opportunities facing investors as they look ahead to 2025, and then all the way to midcentury. In these charts, each horizontal line is the percentage of men and women in five-year age cohorts, rising from babies and toddlers at the bottom to seniors who are 85 or older at the top. Men are on the left, women on the right. The boxed area highlights each country's potential workforce—the population between 15 and 64 years of age.

The U.S. diagrams provide a good baseline. On the 2005 chart, the baby boomers are in the 40 to 59 age brackets. Further down at ages 10 to 30, it is clear that the size of the baby boom echo is nearly the same as that of the parents' group. (Over time, as immigrants filter into their age cohort, the echo boom numbers will become at least as large as the boomers.) Unlike continental European countries, America is replenishing its workforce, as shown in the boxed area of the 2025 diagram.

Additional implications of the American charts include the following:

- The baby boomers encompass four age brackets, so they will not all retire at once. Press reports often suggest that once the first boomers turn 65 in 2011, the majority of the labor force will switch to dependence on pensions and

Social Security, and there will be a severe shortage of experienced employees to perform the country's work. In 2011, though, the youngest baby boomers will only be in their mid-40s; and generation X and the echo boomers are rising beneath them. So, in an absolute sense, there will be no shortage of workers—as long as the United States maintains its immigration levels, which is assumed in these projections.

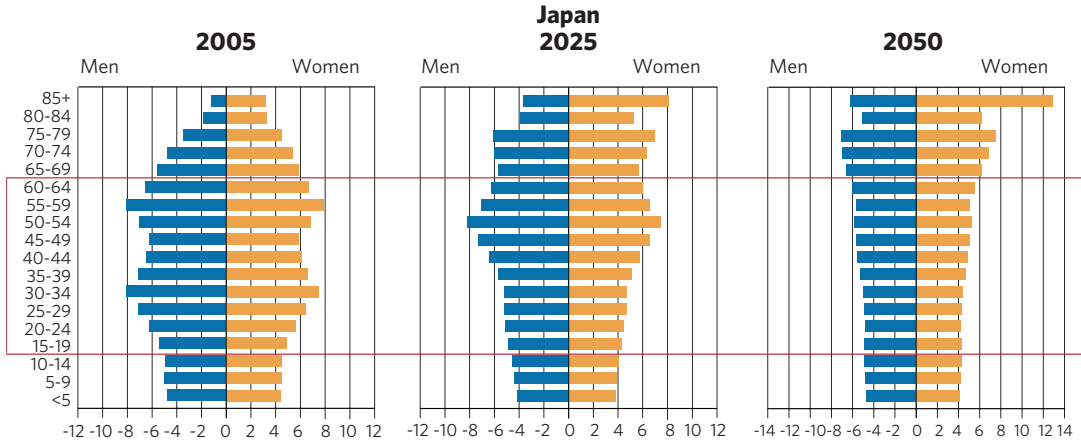
- People are expected to live a long time, so the number of older Americans grows steadily. (The reason the top bar gets particularly wide is that it includes all ages above 85; so as more people live to 95 and then beyond 100, the cohort gets larger.) The dependency ratio—the proportion of seniors and children to workers—will rise. Consequently, more political conflicts among age groups can be expected as older people focus on Medicare, middle-aged people worry about retirement savings, and young people advocate spending on their children's education. As each age group becomes roughly equal in size, consensus will be harder to reach. The political decision-making challenges ahead will be formidable.
- America will have plenty of growth at all age levels to support residential and retail real estate of every kind, as well as warehouses, offices, labs, hotels and resorts, schools, hospitals, sports complexes, and any number of other property types.
- When steady population growth combines with affluence, the result is deep, diverse, and dynamic real estate markets, which is promising for long-term investment.

Above the U.S. charts in Figure 7 are diagrams for Germany and Japan, two affluent countries with population numbers that are beginning to decline sharply. The last three charts depict the population changes in India, China, and Mexico, countries with rapidly growing populations of modest income, but with sharply expanding middle classes and buoyant consumer prospects.

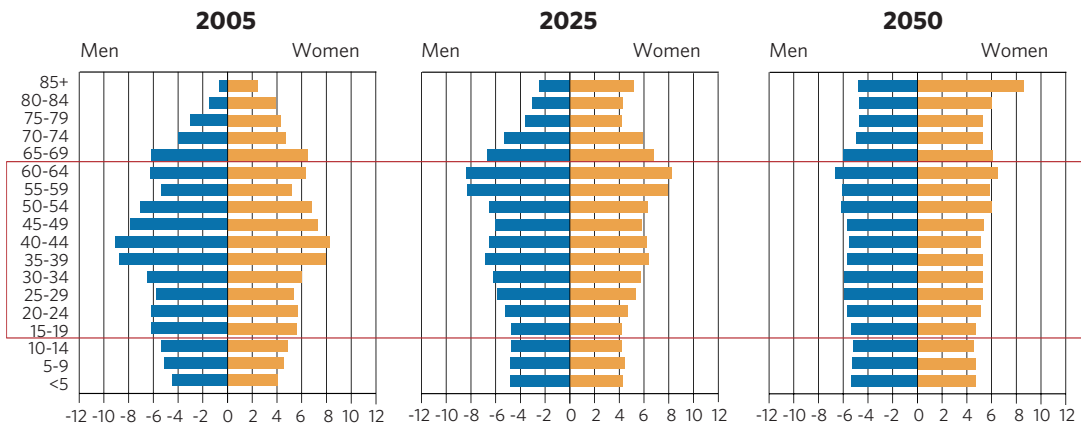
Japan's demographic prospects are disconcerting. The country not only has almost no immigration, but also birthrates are expected to remain low, the labor force is withering, and the elderly population—especially females—will expand dramatically. The population loss will accelerate, with a 10 percent drop between 2025 and 2050; this is

Figure 7. Population Profiles, 2005-2050

Mature Economies with Populations Peaking by 2010
Population Percentage by Gender



Germany



Mature Economy with Growing Population
Population Percentage by Gender

United States

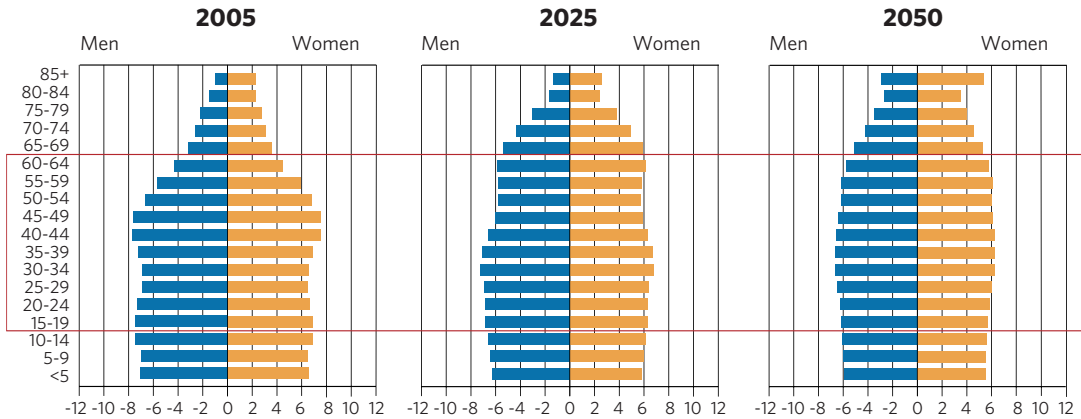
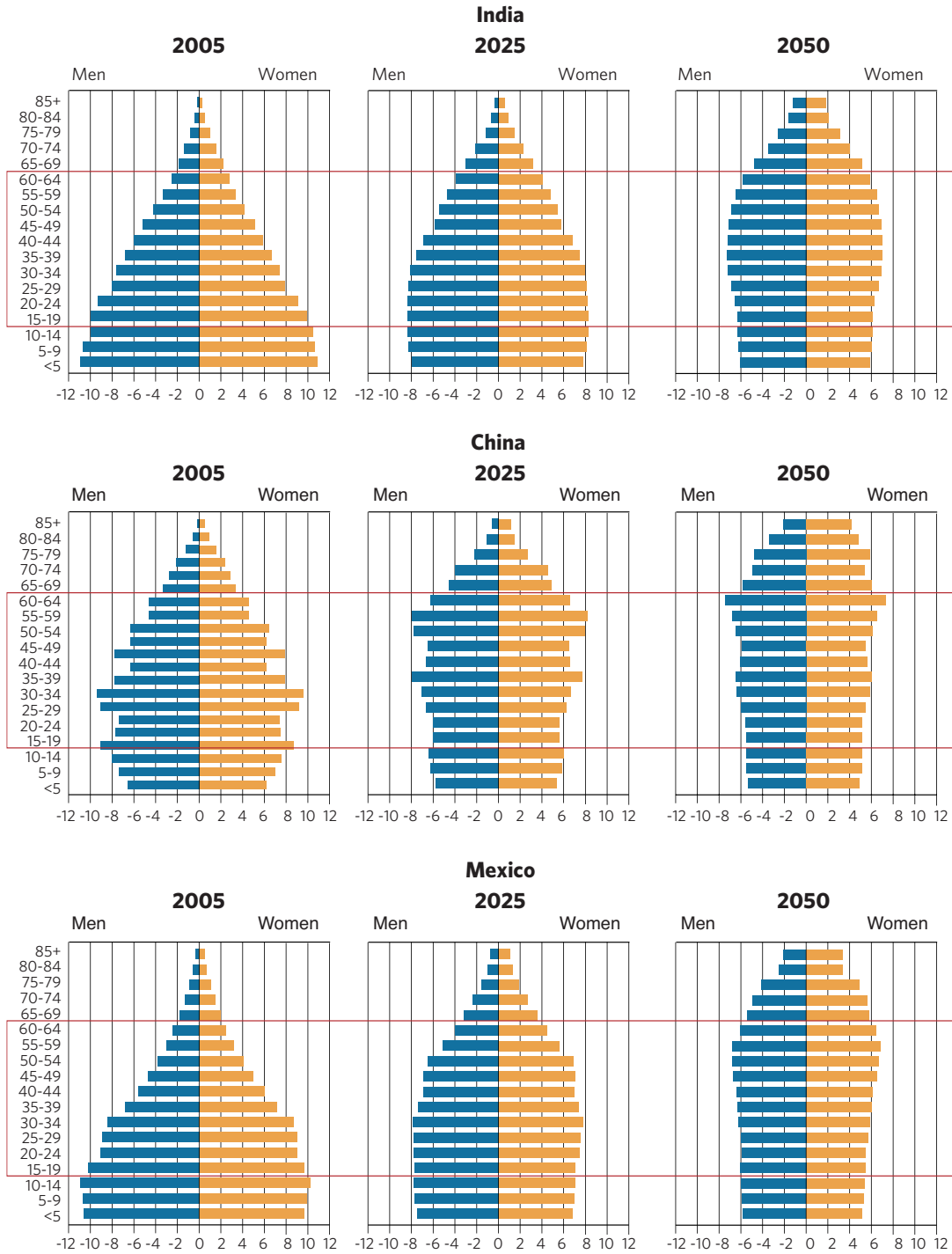


Figure 7. Population Profiles, 2005-2050

continued

Emerging Economies with Growing Populations
Population Percentage by Gender



Note: Red box indicates working-age population.
Source: United Nations Population Division.

four times the rate of decline projected between 2005 and 2025. By midcentury, when Japan's median age will top 52 years, it looks as though the diagram could topple to the right from the sheer weight of older women! The difference between the number of elderly men and women partly relates to life expectancy patterns and partly harkens back to the loss of men in World War II. Japan will certainly be trying to keep people working well past 65. As mentioned earlier, Japan already is outsourcing work to other Asian countries.

Although not depicted in Figure 7, South Korea's population is aging much faster than Japan's. The country's median age is expected to rise from 35 in 2005 (almost eight years less than that of Japan) to 54 years in 2050—a year and a half higher than the projection for Japan. The explanation is probably a combination of low birthrates, as in Japan, and high levels of emigration of young families to destinations throughout the world, with the result that many Korean children eventually join the workforces of other countries. Though South Korea will have modest population growth between now and 2025, a nearly 10 percent population decline is expected between 2025 and 2050. South Korea is likely to be another job exporter, and therefore will not demonstrate strong office or industrial real estate demand over time.

Germany's profile is similar to that of South Korea, but slightly less dramatic. The labor force will decline sharply as a proportion of the population, and the dependency ratio will become almost as severe as that of Japan, though more of the dependents will be children. The median age will rise from 42 years in 2005 to 47 years in 2025 and then will remain flat through midcentury. Population loss will be modest. Germany's chart in Figure 7 can be considered representative of continental Europe because all the countries have similar profiles with only minor variations. Birthrates have been particularly low in Italy and eastern Europe, so their labor-force contractions will be more severe, but France's more positive labor-force profile provides a bit of balance.

U.K. diagrams, also not presented in Figure 7, are closer in appearance to those of the United States, albeit with a lower population growth rate going forward. Australia and Canada have much smaller aggregate populations but have demographic profiles very similar to that of the United States, and

both continue to solicit immigrants to maintain their workforces.

Turning to emerging countries, the 2005 Indian and Mexican diagrams reflect the age/sex pyramid shape that was traditional before birthrates fell in the developed world and life spans expanded so significantly in the latter half of the 20th century. Today's pyramid shapes are expected to change dramatically in both India and Mexico over the next 20 years. With rising per-capita incomes and a larger middle class, fertility rates will decline, the median age will rise, and there will no longer be a base for a true pyramid. Mexico's pyramid is projected to slim down enough to make Weight Watchers proud as the median age soars from 25 years in 2005 to 43 years in 2050. This is the result of a steady loss of young people to the United States over the past 20 years: many of the migrants' children will bolster America's labor force, not Mexico's.

By midcentury, India will have 1.6 billion people, and 220 million more workers than China. Figure 7 shows that the workforce growth will be staggering. No wonder India is concentrating on importing jobs! The country will generate enormous demand for high-quality real estate of all types—residential, retail, and industrial space, warehouses, hotels, and office buildings.

Despite its much higher population, India currently has fewer people over 85—in absolute numbers—than the United States. As its median age rises from just over 24 to almost 39 over the next 45 years, the older population will expand, but India will not have to worry about its dependency ratios for a long time.

China's diagram is completely different. It has fewer children, so there is no pyramid shape. In 2050, China will be the one country with a lot of old men as well as old women—only one of the social challenges that lie ahead. The shrinking labor force between 2025 and 2050 will create competitive issues with other Asian countries. Nonetheless, the absolute number of men and women in each age cohort is very large.

India and China are extremely diverse countries with respect to geography, topography, climate, infrastructure needs, and economic activities. Both have multiple formal languages, as well as diverse dialects. In the case of India, though, English was selected as the language of education, a decision

that is serving the country well in attracting technology and business processes, with call centers serving English-speaking countries. China, by contrast, has largely been attracting manufacturing processes, where language skills are less critical. India and China each view the other as its most serious competitor, and both are investing heavily in education—from elementary through graduate schools.

Real Estate Investment Observations

Commercial real estate's \$14.5 trillion investible universe⁵ is heavily concentrated in the mature economies, as reflected in Figure 8. In fact, the ranking of commercial real estate markets by country closely parallels Figure 4's list of world economies. America contains one-third of all high-quality commercial property (about \$5 trillion worth), and two-thirds is in the top five countries—the United States, Japan, Germany, the United Kingdom, and France. The 15 countries specified in Figure 8 account for 88 percent of global commercial real estate value. The only emerging markets with enough high-quality real estate to qualify for the top 15 are Hong Kong/China, South Korea, and Mexico, each of which contains less than 2 percent of global value.

Institutional real estate investment has risen steadily in recent years, and, as monitored by LaSalle Investment Management, so has cross-border direct investment in property⁶. Cross-border investment rose 21 percent between 2003 and 2004, as shown in Figure 9, and LaSalle reports that investment rose at that same rate for the first half of 2005 over the comparable 2004 period. Interregional investment is rising faster than intraregional investment, indicating clearly that global investors are venturing beyond their familiar territories.

Not surprisingly, over half of global direct real estate investment occurs in North America, and more than one-third is in Europe. Among cross-border transactions, Europe attracts two-thirds of the activity because there is considerable back-and-forth investing among European Union countries. More interesting is the doubling of cross-border investment in the Asia-Pacific region—to 12 percent of the total in 2004—as transparency and liquidity have improved. Logically, this is where the most future growth is likely to be seen, though the U.S. market will continue to capture at least its fair share.

Figure 8. Largest Commercial Real Estate Markets

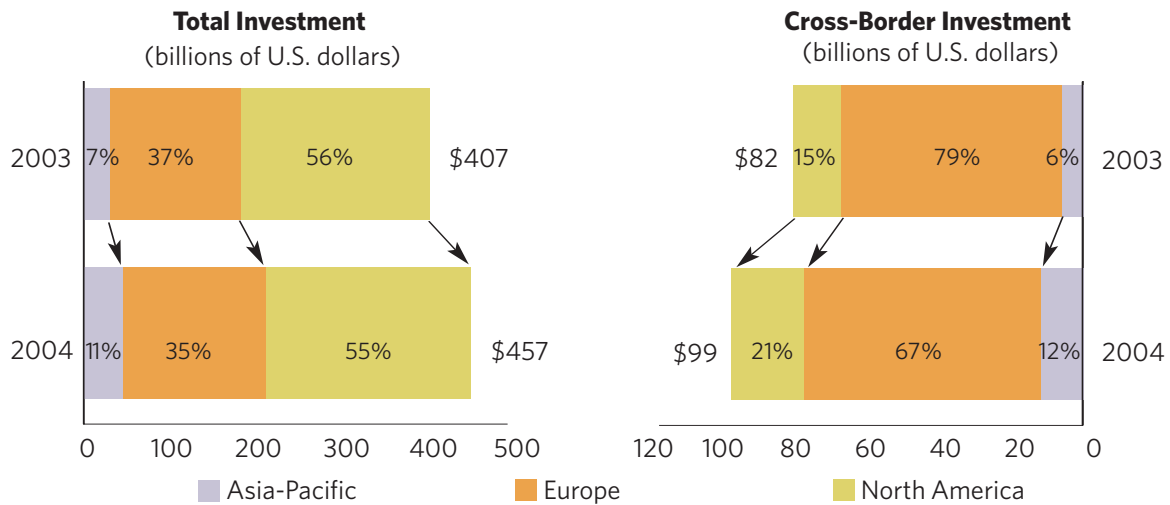
Country	Real Estate Value (billions of U.S. dollars)	Percent of Total
United States	\$4,997	34.42%
Japan	1,966	13.54
Germany	1,075	7.40
United Kingdom	1,039	7.15
France	791	5.45
Italy	657	4.53
Canada	396	2.72
Spain	378	2.60
Hong Kong/China	288	1.98
South Korea	237	1.63
Australia	232	1.60
Netherlands	229	1.57
Mexico	200	1.38
Switzerland	144	0.99
Belgium	137	0.94
34 other countries	1,754	12.08
Total	\$14,519	100.00%

Sources: European Public Real Estate Association, World Bank Organization, FTSE Group.

Whereas opportunity funds were among the earliest and most aggressive global investors, Jones Lang LaSalle emphasizes that the market is “now seeing a wave of interest in global real estate from core and value-add North American investors including REITs, institutions, and private equity groups, which are looking for strong risk-adjusted returns in more established locations such as London, Paris, and Tokyo.”⁷ In 2004, 45 percent of interregional investment was by core and value-added investors (the Private, Institution, and Public Listed categories in Figure 10). Opportunity funds, which generally use much higher leverage, are in the Unlisted category and account for one-third of 2004's interregional investment.

Listed or public companies deserve special mention. Europe, North America, and Asia-Pacific all have large numbers of publicly traded real estate companies that attract both individual and institutional investors. Figure 11 shows the countries in which more than 1.0 percent of the commercial real estate inventory is securitized and listed publicly. An estimated 30 percent of Australian commercial real

Figure 9. Global* Direct Real Estate Investment, 2003 and 2004



* Global refers to Asia-Pacific, Europe, and North America.

Sources: Jones Lang LaSalle, LaSalle Investment Management, Property Data (U.K.), KTI.

estate is held by listed companies, for example, and the proportion in Hong Kong and Singapore is nearly as high. The U.S. share is about 7 percent, the U.K. share is 4.6 percent, and Japan is just below that. This means there are many options for those who want to invest in real estate through stock markets.

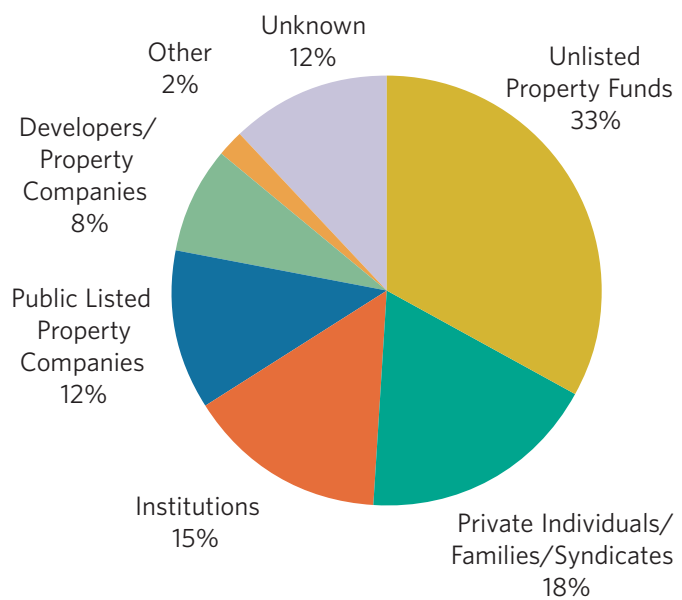
For European real estate investment, listed companies are a relatively safe way to play going forward: they are liquid, so owners can sell easily when the replacement demand issue becomes obvious. In the Asia-Pacific region, publicly traded property companies are attractive for different reasons: they offer an immediate point of entry into real estate, an opportunity to learn about diverse markets, and—thanks to their liquidity—lower risk than direct investments.

Figure 12 offers a few recommendations for short- and medium-term property investments in Europe. Except for the office category, one can be fairly sanguine about Europe in the short run. However, when thinking about real estate investment and development prospects five to 15 years hence, it is hard to erase the images of negative labor force and population

growth shown in Figures 5 and 6. Caution is in order for the medium term.

Europe will continue to need state-of-the-art logistics facilities at crucial transportation hubs.

Figure 10. Interregional Property Investors, 2004



Sources: Jones Lang LaSalle, Property Data (U.K.), Real Capital Analytics (United States).

Figure 11. Levels of Real Estate Securitization

Country	Percentage of Real Estate Listed on Stock Exchange
Australia	30.24%
Hong Kong/China	27.46
Singapore	25.98
Luxembourg	12.48
Sweden	9.90
Canada	7.49
United States	7.18
Netherlands	6.49
New Zealand	5.61
Austria	5.14
United Kingdom	4.59
Japan	4.23
France	3.47
Switzerland	3.07
Spain	2.94
Belgium	2.90
Finland	1.61
Norway	1.58
Poland	1.47
Denmark	1.09

Source: European Public Real Estate Association, September 2005.

Tourism will receive more and more government support because it brings in foreign exchange, is able to employ older people, and uses in-place infrastructure; this means hotel investments will be fine. “Targeted retail” is a proxy for “highly selective locations and types of stores,” probably heavily oriented to the tourist market.

As summarized in Figure 13, non-Japan Asia holds far more promise. Retailers are flocking to this region. Fast-food restaurants are always the first in, which is ironic because Asian countries have wonderful street food. Nonetheless, the world has a taste for Pizza Hut, KFC, McDonald’s, and Starbucks. Grocery stores follow behind fast food providers. (The top five global retailers—Wal-Mart, Carrefour, Royal Ahold, Metro, and Tesco—all sell through the hypermarket or supermarket format, and all are expanding in Asia.) Every big shopping center real

Figure 12. Real Estate Investment Opportunities—Europe

Short Term	Medium Term
Public Securities	Public Securities
Warehouses	Warehouses
Retail	Targeted Retail
Hotels	Hotels
Office—Eastern Countries	—
Corporate Holdings	Retirement Housing

Source: Lachman Associates.

Figure 13. Real Estate Investment Opportunities—Emerging Asia

Short Term	Medium Term
Public Securities	Public Securities
Retail	Retail
Warehouses	Warehouses
Build-to-Suit Office	Office
Infrastructure	Infrastructure
	Hotels/Motels
	Residential

Source: Lachman Associates.

estate investment trust is nosing around Asia, trying to find joint venture partners.

India and China represent mammoth housing markets, but locals will probably dominate that business until it becomes easier for foreigners to own land. Asia seems perfectly suited for prefabricated housing, kits that households can assemble themselves, and large condominium or co-op communities.

Warehousing is an immature market in Asia, but it is growing rapidly. AMB and ProLogis are active, catering to companies using modern logistics. With global production expanding steadily, there will be continuing demand for distribution facilities.

Becoming involved in Asian real estate investments outside Japan and South Korea could prove very productive. India is a place with overwhelming demand, increasing openness to foreign property investment, democracy, and a basically English legal

system that is likely to be compatible for American and European companies. Retailers, manufacturers, hotel operators, and other *users* of real estate may do well in China, but *investors* are likely to be better off in India.

Notes

1. Although demographic data are highly predictive, no one can anticipate 45 years of socioeconomic events—from economic dislocations and wars to pandemics or medical breakthroughs that alter death rates. Even so, recognition of unknowable externalities should not prevent analysis of the information at hand.

2. *Business Week*, August 22/29, 2005, p. 54.

3. Dirk Brounen and Piet M.A. Eichholtz, “Demographic Contraction and European Property Markets: Consequences for the Demand for Office, Retail, and Residential Space,” European Public Real Estate Association research report, September 2004.

4. *Ibid.*, p. 15.

5. Fraser Hughes and Jorrit Arissen, “Global Real Estate Securities—Where Do They Fit in the Broader Market?” European Public Real Estate Association, September 2005. This estimate excludes residential property.

6. Jones Lang LaSalle defines *cross-border* as “‘inter-regional’ (either or both purchaser and vendor originate from outside the region in which the transaction occurs) and ‘intra-regional’ (either or both purchaser and vendor originate outside the country in which the transaction occurs but not outside the region).”

7. Jones Lang LaSalle, “Global Real Estate Capital Travelling Further to Return Stronger,” June 2005, p. 5.