

JAPANESE US REIT FUND – AN UPDATE

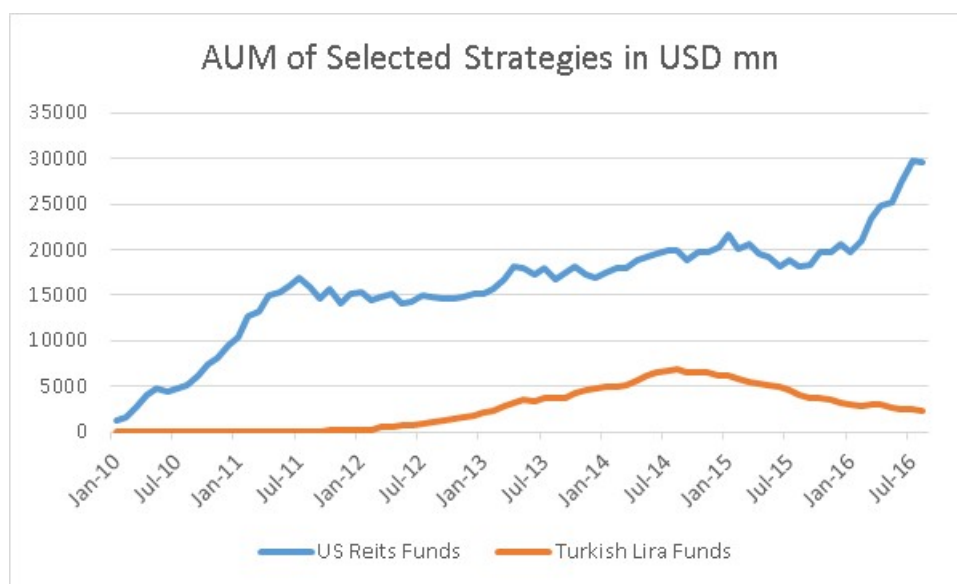


Russell Clark's
Market Views

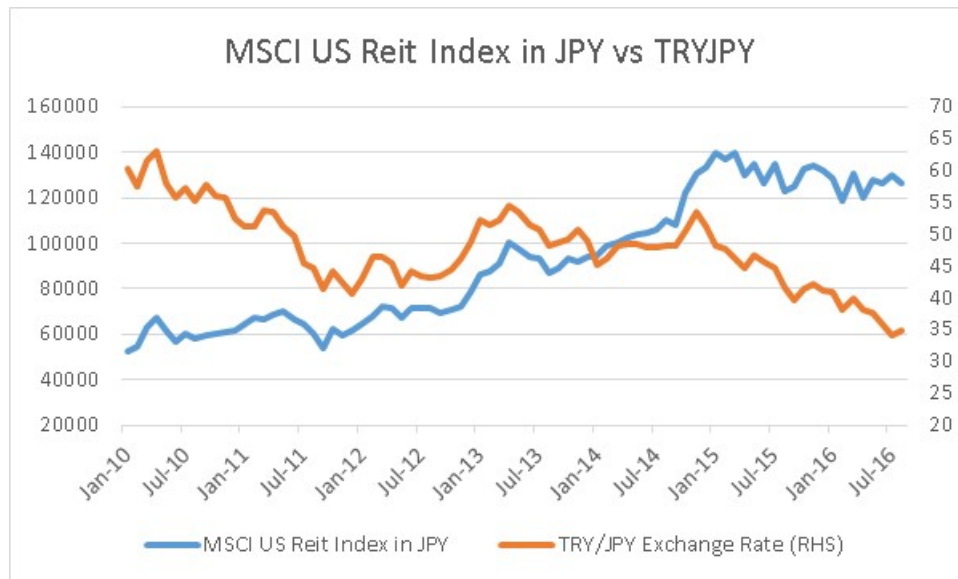
“If Japanese investors just cease adding capital to these funds as they did in 2012 and 2014, it would precipitate significant selling of US Reit holdings to pay dividends.”



In 2015, we released two market views about Japanese investors being short Yen via fund products. One was [long Turkish lira \(TRY\) and short Yen \(JPY\)](#), while the other was [long US Reits \(Real Estate Investment Trusts\) unhedged](#). Both of these assets classes are relatively concentrated, the two largest TRY funds account for 80% of assets, while the two largest US Reit funds make up 50% of assets. This year we have seen Yen rally significantly. While the size of the Turkish lira funds (Amundi European High Yield – TRY Course and Nikko Pimco High Income Sovereign Fund – TRY Course) have shrunk dramatically, the US Reit funds (Shinko US Reit and Fidelity US Reit Fund) have increased.

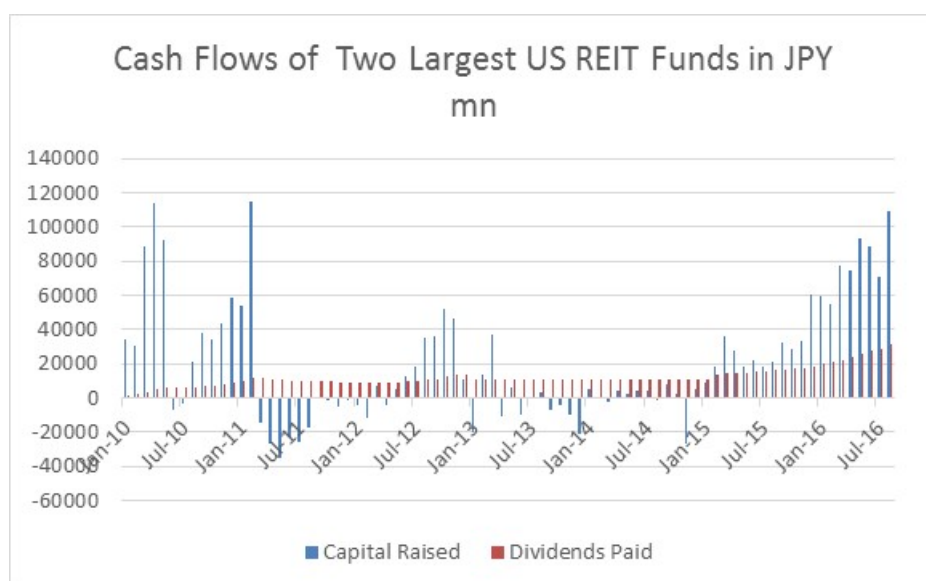


The contrasting fortunes of Turkish lira funds and US Reit funds in Japan are undoubtedly connected to the divergent performance of these assets. The Turkish lira has been very poor, while US Reits have performed well.

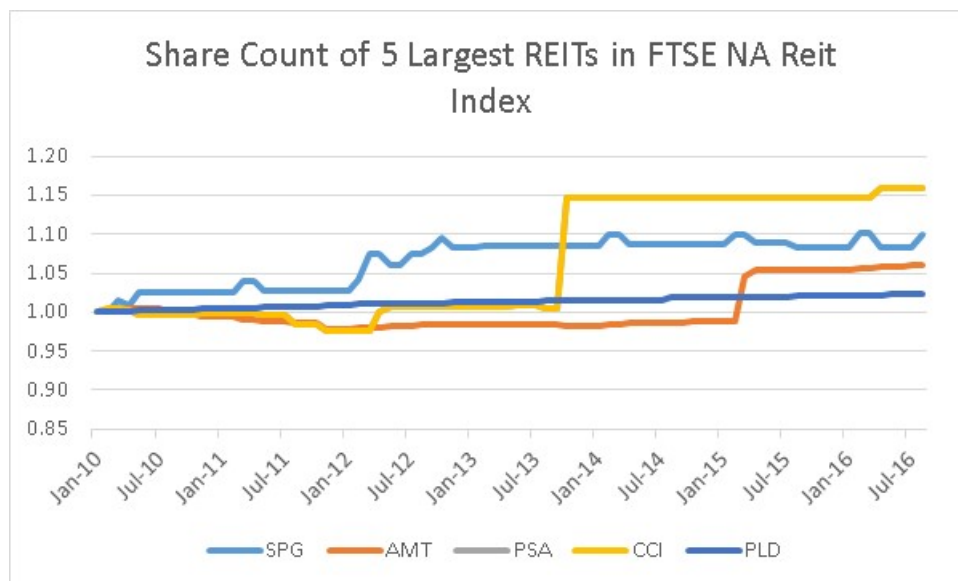


While the US Reit funds and the Turkish lira funds are very different assets, they both offer Japanese investors very high dividend yields as the main selling point for Japanese yield hungry retail investors. The typical dividend yield of the largest Turkish lira funds and US Reit funds is 25%.

US Reits do not offer 25% dividend yields, and the Japanese US Reit funds are not leveraged. Instead, they commit to maintaining these dividend yields from capital. Fortunately, for these funds they have been able to raise enough funds and realise enough capital appreciation to grow their funds' assets significantly. The problem is that with increasing share count, and large yields the two largest funds are paying out 64bn JPY (640m USD) a month. Since 2015, a period of significant capital raising, they have on average raised 80bn JPY a month. If Japanese investors just cease adding capital to these funds as they did in 2012 and 2014, it would precipitate significant selling of US Reit holdings to pay dividends.



It is also interesting that US Reits, in contrast to the trend for most US corporates, have generally been issuers of shares, some quite dramatically. In general terms, Japan based US Reit funds use the FTSE North America Reit Index as a benchmark. According to the index provider, the top five stocks in this index are Simon Property Group, American Tower Corp, Public Storage, Crown Castle Intl and Prologis.



Reits have various tax advantages, as long as they pay out the majority of their income as dividends. This means that to grow assets, they need to issue shares to buy assets. The Reits above are typical in that share count has a tendency to rise over time. It seems to me that for the Reits to grow, they need to be able to find buyers of new shares at ever higher prices, while Japanese based US Reit funds need to find new investors to not become sellers of Reits to meet dividend commitments. This strikes me as particularly unstable.

INFORMATION

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 Investor Relations: Alain Zakeossian, Carol Brown
 Email: info@horsemancapital.com
 Telephone: +44 (0)20 7838 7580
 Website: www.horsemancapital.com
 Business and registered address: Horseman Capital Management Limited, 9 Chester Close, London SW1X 7BE, United Kingdom. Registered in England and Wales - Company number: 04034280

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