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THE WEEKLY UPDATE ON THE INSTITUTIONAL MARKETPLACE

Japanese Return, Cautiously, to US Market

After playing a minor role for the past few decades, Japanese investors are poised to once again ramp up their presence in the U.S. real estate market.

While overseas capital has been pouring into U.S. commercial properties during the current cycle, Japanese firms have been largely absent, with a few exceptions such as **Mitsui Fudosan** and **Mitsubishi Estate.**

Now, brokers and investment managers are reporting a sea change in attitudes among Japanese pension funds, developers and others seeking to improve their yields and diversify their portfolios. That's led to an uptick in property purchases in the U.S., as well as investments in real estate vehicles and companies, that market pros say may be only the beginning.

"We are seeing a lot more activity today than we have in many years in terms of Japanese institutional interest in U.S. real estate," said **Jason Kern,** chief executive of the Americas at **LaSalle Investment** of Chicago. In the last 12-18 months, he said, a number of Japanese entities have made their first investments in both LaSalle's latest value-added fund and an open-end core vehicle.

Japanese investors were a substantial force in the U.S. market through the 1980s. But after being burned by falling values during the savings-and-loan crisis, and then going through a deep recession at home, they have generally steered clear.

That picture has begun to change. Japan accounted for 4.3% of foreign investment in U.S. commercial real estate in 2016, up from a mere 1.8% the year before, according to **Real Capital Analytics.** And the first two months of this year saw Japanese purchases surge to $843.3 million, from $187.9 million in the same period in 2016.

The biggest deal so far this year was in January, when **Mori Trust** took its first step into the U.S. market. It paid $673 million for an 825,000-square-foot office complex at 10 St. James Avenue and 75 Arlington Street in Boston's Back Bay submarket. **Newmark Grubb** brokered the sale for **Liberty Mutual.**

Meanwhile, **Unizo Holdings,** which has been active in the U.S. since 2013, recently stepped up its pace. The firm, formerly known as Jowa Holdings, has spent nearly $845 million on five Washington office properties since July.

The increased Japanese interest in U.S. real estate "is being driven by limited opportunities to grow their portfolios within their home market," said **Lucy Fletcher,** a managing director at **JLL's** global capital-markets group. That's partly due to low yields on assets in Japan amid a negative interest-rate environment.

But this time around, Japanese buyers are proceeding cautiously, Fletcher said. "What we've seen this cycle is a very different approach," she said. "They are sending research [staff] in first . . . before they make a play. They are laying the groundwork for what we believe will be some significant acquisitions."

Among those looking across the Pacific are two of Japan's largest institutional investors, **Government Pension Investment Fund of Japan** and **Japan Post Bank.** In the past year, both have set new allocations for alternative assets, with substantial portions targeting real estate. Pros expect them to focus largely on the U.S. due to the size and stability of its market.

"New capital allocators to commercial real estate from Japan, such as GPIF and Japan Post, have crafted a careful way forward based on research and long-term objectives," said **Christopher Ludeman,** global president of capital markets at **CBRE.**

Last month, Tokyo-based **Mitsui & Co.** agreed to acquire a 20% interest in Los Angeles fund shop **CIM Group** and to invest in its vehicles. The total investment is estimated to be between $450 million and $550 million. In announcing the deal, Mitsui said "U.S. real estate [is] expected to remain as the largest and most attractive segment in the alternative investment market."

Institutional investors new to the U.S. market will likely favor stability over yield, at least initially. "They are looking for more core, stable, bond-like investments," said **Junichiro Muto,** head of the capital-advisors team at CBRE Japan. "They are going to be very, very conservative. They are not going to take on big risks."

So far, many Japanese firms are "putting their toe back in the water," said **Tom Landry,** a managing partner at **TA Realty** of Boston, which is majority-owned by Mitsubishi Estate subsidiary **Rockefeller Group.** "They are starting with fund investments just to become a little more educated, but they will eventually run the gamut from separate accounts and club funds to direct investments." ❖