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China and European Real Estate

China's emergence as the second largest economy in the world can be seen as the natural consequence of it being one of the largest and most populous countries in the world. Yet this is a new development as it comes in the shadow of different economic policies pursued between 1947 and 1989. What will the emergence of China mean for European real estate market?

Internally China has a rudimentary cash management and finance market which means that each state, quasi-state or private company sits on a large physical holdings of cash. This means that capital investments by companies are not as 'measured' as others around the world might be, the money return metrics of each of these entities is very low indeed. It also means that they are loathe to diversify beyond very straight forward 'safe' cash, treasuries or real estate.

Therefore, Chinese entitties have collected vast amounts of reserves and surpluses to spend within China and around the world. The benefits of the transfer of these reserves and surpluses not within China but around the world is that first, they are non-inflationary in the home environment; secondly, they are diversifying from core enterprises in the home environment; and thirdly, they are integrating with far more competitive capital centres than the home market. All of these factors are positively good for the future of China and of the Chinese people.

In common with any large capital flows from major developing countries, decisions directing these vast capital flows are concentrated in the hands of a small amount of people. This can present both opportunities as well as pitfalls. The benefits are that they can think strategically and intelligently, the pitfalls is that they can become beholden 'group think' or to a cabal of advisers that will only be proved wrong when it is too late to reverse any investment decisions.

European real estate is an open and transparent market that is traded and therefore liquid. It is in vogue as its perceived position between fixed income and equities means that it might be able to avoid the volatility of either with the capital upside of both. This is a natural home for Chinese surpluses and cash reserves. However, this requires intelligent understanding of the market as well as investment management allocation decisions. For example, as important as investment *alpha* is the ability to judge liquidity needs correctly and know how redemption works and have a real time understanding of the oscillating trends of the market in general or each sub-segment in particular. Inflows to European real estate because it is liquid and it is a mature economy are, after all, as important as the underlying occupational demand.

In contrast outflows from China, because the country is developing so swiftly and successfully, will be uneven and unpredictable. Whilst current and predicted capital flows will be impressive the long term sustainability of these should not be counted on. China's growth will mean more internal projects, its contraction will mean less capital overall. In either case European real estate should remain transparent and open to all.

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