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Shojin - UK real estate opportunities

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Why is this a good time to invest in the UK

To begin with, the UK has a severe supply demand imbalance. For probably the last 25 to 30 years, they've just not been building enough homes. So every year, you have about half a million people graduating from universities. 10 to 20% of them would like to get on the housing ladder, but they're unable to do so simply because there's not enough housing being built. And each year, these numbers just keep adding up. Now the government is providing support at the lower end to help young people buy the first property through things like the Help to Buy scheme and the 95% mortgage. Because of this type of support and the severe supply demand imbalance, that actually makes the UK very attractive as a place to invest into real estate development. But it's not just the lower end of the market. Once these people start buying, it actually frees up homes for others to buy and move into family homes and for older people to move into things like retirement apartments.

So, all up and down the spectrum, there is a shortage. The other area that it's probably worth considering though is that the UK's moving towards more of a rental model. So this is something that's already been happening in places like the US and Europe for a long time. In the UK, we had this obsession with buying our own property, but that's now slowly starting to fade not just because people can't afford to buy, but actually because young people prefer some sort of social mobility. So that's creating demand for all rental buildings, enabling young people to not tie into a long-term commitment. So if you imagine yourself as a 21-year-old coming out of university, do you really want to buy a place and take on a mortgage and be stuck in one place? The chances are not... You might want to actually explore different cities both in the UK and abroad. So, it has really opened up this market for all rental properties both towards for young people but then also in the retirement space.

What are some of the specific opportunities that you can highlight?

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ladder. There's not enough stock there, but there is a lot of demand. So really building anything in any of the major cities or commuter zones or even the coastal areas. These all have fantastic demand. So that's the first one. The second one I would say is that the UK is rapidly becoming a rental market. So something that's already been happening in the US and in Europe for quite a while. It's starting to happen in the UK where people want to rent their place and then pretty much change their apartment like they might be changing their cars every few years because they need change. When they graduate from university, they might be in a studio or one bed. They then get a partner. They might move into a two-bed. They might think of having kids. They might move to a three-bed. They might have more kids, and they want a garden. They move into a family home.

And then obviously that at some point the kids move out and go off to university. They might want to start downsizing and eventually moving into some sort of retirement living. So people's needs change throughout their life, but the UK doesn't have the right kind of rental stock to meet these needs. So that is a huge area of opportunity. For example, in the UK, we have a serious problem in residential property being that really we don't have any kind of senior living product. So like they have in the US, they have retirement villages and things like that. We don't have that in the UK, and we don't even build many apartments for the elderly or retirees. So what this ultimately means is that a lot of older people end up staying in the house where they probably raise their children. And you've got this elderly couple rattling around in maybe a four or five-bedroom house.

The problem with that is that without them moving anywhere, there's nowhere for people with young families to move to. So young families end up getting stuck in smaller properties and apartments, which in turn means that the lower end of the market, the first time buyers are also stuck because there's not enough property being released. So we need to unlock the entire chain, and that's by building enough of the appropriate type of properties, especially on the rental side. So certainly at the upper end, building more retirement apartments, retirement villages, and then kind of trickling all the way down to first-time buyer homes at a more affordable price point. But then also building more rental properties so that even if people aren't necessarily looking to buy a property, they have the right kind of housing for their needs. Again, whether it's when they're starting off in life, when they graduate from university all the way through to having families, all the way through to retirement.

What does Shojin do in this space?

Shojin's core role really is to identify the right type of opportunities and find the gems in the market. So I'd say we reject more probably about 90% of the things we see because oddly enough, we don't have much competition. So we focus on providing equity and mezzanine for real estate developers. And because there aren't many firms providing this type of funding, we get to see a lot of the deal flow. And what that means is that we get to cherry-pick the projects where we feel that the risk is very, very low while the return is quite high. Now this is quite important because it's almost like finding outliers in the market. Our market is simply not efficient. So risk does not equal return. So people can be earning 15, 20, 25% per annum, but actually, your risk isn't significantly higher than something where you are earning maybe 5% per year. And that's the key thing. We are looking for those real gems.

How do you decide which projects you do or do not invest in?

Well, we carry out a lot of due diligence on any project that we move forward with. So we have what we call a three stage due diligence process. We'll initially assess projects at a high level and really figure out if it's a kind of project we like, the price point, the developer's background, a whole number of kind of key items. And once we're satisfied with that, we will make an offer to fund but subject to deeper due diligence. And that's really when things get interesting because we then do a deep dive into every aspect of the project. So there's probably about 200 odd items that we ultimately assess. And that includes really kind of quirky things like what's the access to the site like. Is it okay for trucks to get in, or will they have to break deliveries down into smaller loans? Things that could have an impact on the timing or the cost of the development.

But there's so much we look at way more than any senior lender ever would because we're in the equity position. So we go into all of that detail. And once we're satisfied with the bulk of that, we will start the third stage due diligence which is the legal work while we continue finishing the rest of the due diligence work. So then in parallel, the legal work happens. We get all the third-party surveys done as well, which then really are used to make sure that things are aligning with the way we are thinking about, things like cost consultants or valuation consultants. So all of these things are then done independently of us to make sure that what we're saying is aligned with what the independent experts are saying. So once you've gone through all of those phases of due diligence, and it still passes everything, you know you've got a pretty solid project there. ■