Taking Treasury into China

Conglomerate company sees opportunities in commercial property, logistics and waste management in China

By Mark Godfrey

If taste in Chinese art is anything to go by then Treasury Holdings know what's hot in China. Contemporary artists Zhang Zhihong and Xie Dongming add colour to the reception area at Treasury Holdings' China headquarters on the 10th floor of the Treasury Building on Huashan Road in the world's largest construction site, Shanghai.

"We are very into art," says Steve Priddis, Retail Asset Management Director in an interview with the Irish Network China. Treasury's adeptness at understanding China was shown in how it foresaw a current craze for environmental sustainability in China. That was a headline grabbing 50/50 joint venture deal with the Shanghai Industrial Investment Company in 2005 to build the "world's greatest eco city" on an island off Shanghai.

The Dongtan Island project has however been a slow starter. It is on hold "for a while," says Priddis. Treasury will play "whatever part is appropriate," in the island says Steve Priddis when construction finally commences, as expected, in early 2008. The "world's greatest eco city" with energy saving sustainability of futuristic buildings of chrome and glass staring upon the hooded cranes and other migratory birds who live among the green reeds and mudflats that jut out into the East China Sea.

The 4.2 million square metre island development was phase one of Treasury's China strategy, a deal signed after three years of careful and tedious research and checking. Treasury's carefully guarded reputation for high design standards – it has its own Treasury Design subsidiary - and an environmental conscience landed the project.

While waiting for Dongtan to take off the firm has moved onto its plan B for China. Buying and building commercial properties, the original phase two of Treasury China's growth plan, has now become phase one, says Priddis. The firm has already assembled portfolio of assets worth RMB7 billion (EUR700 million) in China by mid 2007.

Treasury aims to become the number one foreign developer in China – but in standards, not scale. It's not necessary to trump the spend and presence of Singapore's Capital Land or Hong Kong's Henderson, both huge developers in China, says Priddis. "We are more specialized, growing organically and steadily."

Vacant space is rare at Central Plaza, overlooking the well-manicured People's Square in the centre of Shanghai. Treasury bought the 13 year old skyscraper, set in the heart of the city's business and shopping district, from a Hong Kong developer. Recent refurbishments, including a glassy lobby dropping more light onto the heaving footpaths outside are part of Treasury China's model of "taking assets and putting value into them for tenants," says Priddis.

In moving into China Treasury is riding a wave of strong demand for commercial property in China, particularly from foreign retail and financial services companies testing a local market that's become increasingly liberalised since China joined the WTO in 2001. Property prices in China's 70 large- and medium-sized cities jumped by 9.5 percent year-on-year last month, according to Jones Lang LaSalle, despite frequent government efforts to curb lending and tighten rules on speculation by foreigners. Pre-leasing rates for top-office products in Beijing have doubled in two years to 50 percent, says David Hand, Managing Director for Jones Lang LaSalle Beijing. "For high-quality retail shopping centers, we are seeing rates of 80 percent and higher."

What Treasury has to add to properties that local Chinese peers lack is good taste – and designers. Local mall projects lack the sophistication in design and management that Treasury has honed in ventures around the world. International players like Treasury and Hong Kong counterparts base rents on revenues, still rare in Chinese. China needs international savvy to run its malls, says David Hand. "You don't put a hamburger joint next to Louis Vuitton but that happens in China."

Quality design and construction are often lacking in Chinese property. "Developers are often from provincial cities and they cut corners," says Paul O'Driscoll, a partner in Investors Asia, which advises real estate investors in China. A quick-buck approach to property management hands the initiative to foreign developers. Treasury, says Priddis competes with local developers by minimising maintenance costs for tenants. Unlike most, who take a fee from the maintenance. "Unlike other owners we don't make money from maintenance. If we are competitive on rent and on operation costs we will succeed."

Better design is also in the company's commercial interest in China, says Priddis. "People spend too long these days in offices, adding a green belt around the F&B areas keeps tenants happier – and they stay." Treasury hired retail architects Benoy to design an extension to another of its Shanghai properties, the Hongqiao City Centre, a 173,000 square metre property spliced into 90,000 square metres of retail and a 33 floor office tower. Treasury bought a 77,500 square metre adjacent site on Zunyi road site to add two 26 storey office towers.

The deal is proof of how thoroughly Treasury does its homework. Treasury plucked for City Centre because the project fits well with a local government master plan to redevelop the area, says Priddis. Treasury's green-friendly refit and extension to the property also nicely assuaged increasing government worries about environmental sustainability of the country's new buildings. Increased footfall will come with a new metro station being built. An expansion of nearby Hongqiao Airport to handle flights from Hong Kong and Taiwan will put the district compete with flashy Pudong on the opposite side of town.

Treasury's in-house legal and financial brains had to work harder however to get their heads around the money side of China's real estate scene, a murky mess of state owned and private developers vying for market share but both dependent on backing from state banks. Chinese banks walk a tightrope between approving loans and suffering NPL rates.

Real estate loans account for 16 percent of outstanding local currency loans. A system of auctions for state-owned land while intended to increase transparency, hasn't been kind to foreign developers buying land. "They need a contract to bring money in but if there's an auction for the land," says Paul O'Driscoll.

Treasury's China operation is keeping high standards, and playing safe, says a Shanghai-based real estate sales manager who prefers to remain anonymous. "They regularly walk away from deals with risk potential. If there's a mega project but six people living there with land rights, they'll walk away."

Good connections have also helped Treasury in China, where favouritism from local government means local developers get first call on credit: 70 percent of real estate financing comes from banks. Treasury has gotten access to deals by working with state owned companies such as SIIC. Finding good local partners is crucial, particularly in getting land in China, says O'Driscoll. "It is difficult to do, a lot of people in the market a long time and couldn't close deals." Compared to Eastern European counterparts Chinese state owned companies are more efficient. "They get land parceled up quickly."

Treasury will also have benefited from ties to the ultimate dealmaker in China, Li Ka Shing the Hong Kong tycoon whose Hutchinson Ports company partnered with Treasury to on Bremore, a joint venture port operation in Ireland. This, and the willingness to diversify into logistics may be a key to Treasury's success in China, which sorely needs better freight handling facilities.

Treasury's Beijing Logistics Park, a 122,000 square metre warehousing depot set to open in 2009, is located near Beijing's new airport terminal, the world's largest when it opens next year. The need for logistics space is being driven by manufacturers, retailers and distributors outsourcing logistics operations. "This triggered a strong growth in demand for well-located building plots in reputable logistics areas such as Beijing Airport …," says David Hand.

Dongtan Island, with its lanterns and Chinese bridges and weeping willow trees could be a template of how to reconcile environmental sensitivities with Shanghai's insatiable needs for space. But the project, if it's completed, may only be a taste of things to come for Treasury, whose growing waste management business may be an even better fit for polluted Chinese inland provinces which need clean energy more than office blocks. "We will eventually bring its other divisions in," says Priddis who points out that Treasury also has 97 patents for ethanol fuel blends.

The Chinese art hung in the lobby is also for the eyes of local officials. Another sign of the company's commitment, Treasury has a full time staff member running a charity funding education and health projects for Chinese children. "Authorities are concerned about the temporal nature of the property deals here…One of our advantages is that we are long term players, not here to get rich quick. We're not playing the market, we are coming for a long term holding and management of that property."

Cash, art and buildings purchased are signs of the company's intent by Treasury's co-founder and Shanghai resident Richard Barrett. The Ballina native traveled around China in the late 1990s to find a fit for Treasury. "Barrett is the sharpest tool in the shed but very principled," says a Beijing real estate source who has dealt with him. "His living in Shanghai and basing three of Treasury's global directors here in China shows how serious the group is."

Treasury remains modest players in China compared to Singaporean developers like Capital Land and Hong Kong-based Henderson or Swire but its expertise puts it in the ranks of US giant developer Hines, which built Park Avenue and Microsoft Tower in Beijing, or Japan's Mori, the group behind the eye-catching new International Financial Centre in Shanghai.

The company's Irishness could ultimately be its trump card over foreign competitors. A summer shot of the Cliffs of Moher coats the company's glossy, bilingual book produced for Chinese clients and officials. "We're not a giant American and we're not a bank here to rape and pillage the country," says Steve Priddis.

The arrival of other large Irish developers in China may depend on the domestic economy. German developers after all backed out when the domestic economy tightened. The landmark Kempinksi hotel and Sunflower Tower in Beijing were both built by Holzmann, a German developer which collapsed, sucked down by Germany's economic woes.

Small time speculators buying apartments in China's key cities will be first to feel the heat. "China is only for big boys now, says Paul O'Driscoll. "There's no point coming in with five or ten million euros, you need a plan." Smaller investments are less flexible by Chinese laws on investment and foreign exchange. "How will you get your money out? It's worth emulating Treasury Holdings but who has pockets deep enough to?"
Perhaps only investment banking firms Merill Lynch and Goldman Sachs, both finding a vocation in buying up and untangling the bad loans left by China's real estate failures.

Treasury meanwhile shows no sign of slowing. The company's swelling staff count means it is planning to expand into the 11th floor of its flagship building, which counts among its tenants Sony BMG. The sign of the occupancy potential of a good building, there's a Starbucks on the ground floor. Treasury is "looking at other buildings because we see potential growth in them." The firm is in advanced negotiations in Shanghai and is looking at "various opportunities" in Beijing. "An awful lot is being presented to us in [eastern coastal city of] Qingdao."

Malls here remain chaotic and office blocks badly managed but China is getting sophisticated fast, says Priddis. "I'm irritated by too much talk of how difficult it is to do business here. China will take ten years, evaluating USA and do it in five years by cutting out the bad practice in other, more mature markets."

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