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# Why do Research on Commercial Property Management? Somebody HAS To!

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Abstract

This paper identifies some significant gaps in our knowledge of the configuration and performance of the property asset management sector. It is argued that, as many leading academic property researchers have focussed on financial vehicles and modelling, in-depth analysis of property assets and their management has been neglected. In terms of potential for future in-depth research, three key broad preliminary research themes or questions are identified. First, how do the active management opportunities presented, costs of management and the key management tasks vary with market conditions, asset type and life-cycle stage? Second, how is property asset management delivered and what are the main costs and benefits of different models of procurement? Finally, what are the appropriate metrics for measuring the performance of different property managers and approaches to property management? It is concluded that the lack of published materials addressing these issues has implications for educating property students.

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## Why do research on commercial property management? Somebody HAS to!

When posing a similar mocking question about coming from Des Moines, Iowa, it was also clear that Bill Bryson had a deep affection for the place. Starting with a statement of the important – albeit obvious - as an investment class, a unique feature of commercial property is that it requires a relatively substantial (if variable) management input by the owner or user. For many property professionals, one of the attractions of working in the commercial property sector is the tangibility of the assets and the individual's ability to make a difference to the assets and to see this difference. Nevertheless, many of the same property professionals are wary of getting too close. Property asset management remains one of the least glamorous roles in the industry. This also seems to hold true for property academics. To be blunt, in the UK it is difficult to identify any leading academics or researchers, as evidenced by highly rated publications in various research assessment exercises, who specialise in commercial property management. This is seems also to be true for the rest of the world.

Linked to the integration of the commercial property and capital markets, like geography in the 1950s and 1960s, property as an academic discipline experienced a "quantitative revolution" in the 1980s and 1990s. However, whilst often parodied and despite similar changes, broader business management theory as a discipline has continued to mature in terms of its empirical and theoretical depth. Concepts such as Business Process Engineering, Total Customer Service, Customer Experience Management, Total Quality Management *inter alia* emerged from the expanding business management education sector. In contrast, outside of corporate property management, the broader topic of property asset management does not seem to have matured as a subject of academic investigation.

Without wishing to be social outcasts at future property research conferences, it is difficult to deny that the leading property academics have been involved in property market modelling and forecasting, applications of capital market theories to property investment strategies and, perhaps to a lesser extent, property pricing and appraisal. Although it could be argued that property development has suffered from a similar marginalisation, its association with the planning subject area has meant that it has not been neglected to the same extent. As a result, a largely self-perpetuating cycle has emerged whereby a high proportion of new property researchers have been attracted towards property investment theory and practice. Like many other aspects of society and the property sector itself, the property academic research sector has been increasingly affected by financialization. There is an increasing recognition that there is a growing division between property academics who specialise in creating new knowledge about the underlying assets and others specialising in creating new knowledge about the associated financial vehicles and property investment strategies. Broadly, it is research on the underlying assets that has been neglected.

The neglect of property asset management within the academic research community has consequences for teaching the topic. Academic colleagues who deliver modules in property asset management to both undergraduate and postgraduate students are frequently frustrated by their inability to point our students to a body of theoretical analysis, qualitative and quantitative empirical research or even thick description that is relevant to many issues central to *contemporary* commercial property management for portfolio owners. Given the sheer scale of the wealth tied up in commercial property assets often owned and managed on behalf of shareholders and institutional investors, the limited resources allocated to research on their management is perhaps surprising. This paper sets out to outline the nature of the problem – the neglect of property asset management as a subject of academic research. Implicit in this discussion is a problem for higher education. Cohorts of students taking property degrees are simply not being exposed to up-to-date, in-depth analysis of this key element of the operation of property markets. The paper goes on to identify some gaps in our knowledge about property asset management.

A relatively minor aspect of the problem is that commercial property management suffers from a confusion of labels. In this context, the phrase "property asset management" is deliberately used to cover the broad range of operational and/or strategic, routine and/or infrequent and simple and/or complex functions that constitute the management of property assets. In practice, at the portfolio level, it is rare that one individual is responsible for the delivery of all functions relating to the management of property assets. Whilst reiterating that there are no standard terms, "Property Manager" is often used to describe a role concerned with day-to-day functions such as service charge functions, tenant liaison, inspection and monitoring, etc. For large developments with high management intensity e.g. shopping centre, for such managers their workplace may be physically in the asset. In contrast, the role of property manager may not even exist where there is an asset with a single tenant let on a long FRI lease with no owner responsibility for common parts. The term "Asset Manager" is often used to describe someone who the property manager typically reports to. Their main responsibilities may focus on items of managing the property managers, approval of major expenditure, major alterations, implementing acquisition and disposal strategies etc. The asset manager may then report to a "Portfolio Manager" or a "Fund Manager" who also may have approval responsibilities for asset managers' activities and take a more strategic role focussed on asset allocation and fund structure. Even at this stage, it worth noting that there is very little empirical evidence or models of how the delivery of property asset management is structured and evaluation of different possible models.

Even defining the scope of property asset management can be tricky and the boundaries are far from clear-cut. Often building upon introductory courses in economics, law, construction, financial maths, management theory and urban planning, there tend to be four main building blocks in most property courses at higher education institutions – appraisal, asset management, development and investment. Whilst there are overlaps between all the blocks, it is often particularly difficult to draw boundaries around property asset management. Obviously, the strategic task of fund or portfolio investment management is concerned with construction and ongoing rebalancing of investment portfolios, their investment performance measurement and, where appropriate, the creation and administration of fund investment vehicles. Major refurbishment can be interpreted as just another type of property development and appraisals will be central to any financial analysis of the rationale for capital expenditure decisions. Clearly, whilst property asset management is a core service of property professionals and, consequently, a core component of property education, defining the scope of property asset management is difficult.

However, some aspects related to commercial property management have proved relatively fertile. Corporate property strategy and management has continued to mature as a sub-discipline. The growing importance of sustainability has meant that policies, barriers and opportunities for improving the environmental performance of the existing stock has focussed attention on the potential contribution of property asset management. Improving the performance of public sector property assets has also remained a relatively important policy area and the body of knowledge in this area has continued to grow. Nevertheless, there are glaring gaps and potential opportunities for researchers.

Often, one of the first pieces of knowledge that we attempt to transfer to property students is that property assets are heterogeneous. This knowledge is usually conveyed in an appraisal module. However, it is also of central importance for property asset managers. Property assets vary in terms of their lease terms (what and how many lease events can occur?), age (demand for renovation, maintenance, repair), technology (specialist skills and knowledge, complexity), services required (cleaning, security, landscaping, maintenance, repair etc) and tenant characteristics (nature of business, default rates). Table 1 presents this distinction in the form of two extremes. This diversity of assets is augmented by differences between different market sectors (retail, industrial, office and leisure) within which there are established and emerging specialist sub-sectors such as data centres, health clubs' serviced offices *inter alia*.

In effect, as well as requiring different levels of management responsibilities to owners, property assets also vary in the (real) options that they offer owners. One of the key decisions of owners is whether, when or how to exercise these options. Of course, many of these options can also be viewed as asset risks. Perhaps put glibly, in a buoyant market they present opportunities whilst in a depressed market, they are risks. However, we know very little about diversity in asset management intensity, diversity in required skill-set and knowledge base and, presumably, diversity in management costs. There seems to be a knowledge void here on *measuring* the size, scope and nature of these risks and options and the relationship between asset management requirements, risk and performance. Robust research could help to provide a deeper of the understanding of the extent to which property asset management sits at the nexus of risk and return in commercial property portfolios.

**Table 1 The Relationship Between Asset Characteristics and Active Management Opportunities**

| *Adding value?* | ***'Straw-asset' 1 Low Beta*** | ***Optionality*** | ***'Straw-asset' 2 High Beta*** | ***Optionality*** |
|---|---|---|---|---|
| *Improve tenant mix? Surrender premiums?* | Single tenant | Low | Multiple tenants | High |
| *Is the scope for re-gearing leases?* | Long unexpired lease term | Low | Short unexpired lease terms | High |
| *Can onerous lease terms be changed?* | No onerous lease terms | Low | Onerous lease terms | High |
| *Can quality of tenant be improved?* | Low tenant credit risk | Low | High tenant credit risk | High |
| *Can building be improved?* | High quality building | Low | Low quality building | High |
| *Is there scope for increasing quantity of space?* | Site at maximum development density | Low | Site at low development density | High |
| *Is there scope for changing the use of space?* | Site at highest and best use | Low | Alternative uses are viable | High |
| *Can the layout be improved?* | Configuration of building is inflexible | Low | Configuration of building is flexible | High |
| *Does the L have control?* | FRI lease | Low | Landlord responsible for repairs etc | High |
| *Can the L affect the service charges?* | No service charge | Low | Many services delivered by L | High |
| *Is there scope for additional revenues from advertising?* | Public has no access to building | Low | Public are commonly on the premises | High |
| *Is there demand for new space or uses?* | Static or declining local economy/property market | Low | Dynamic local economy/property market | High |
| | **Few opportunities for entrepreneurial property asset management** | | **Numerous opportunities for entrepreneurial property asset management** | |

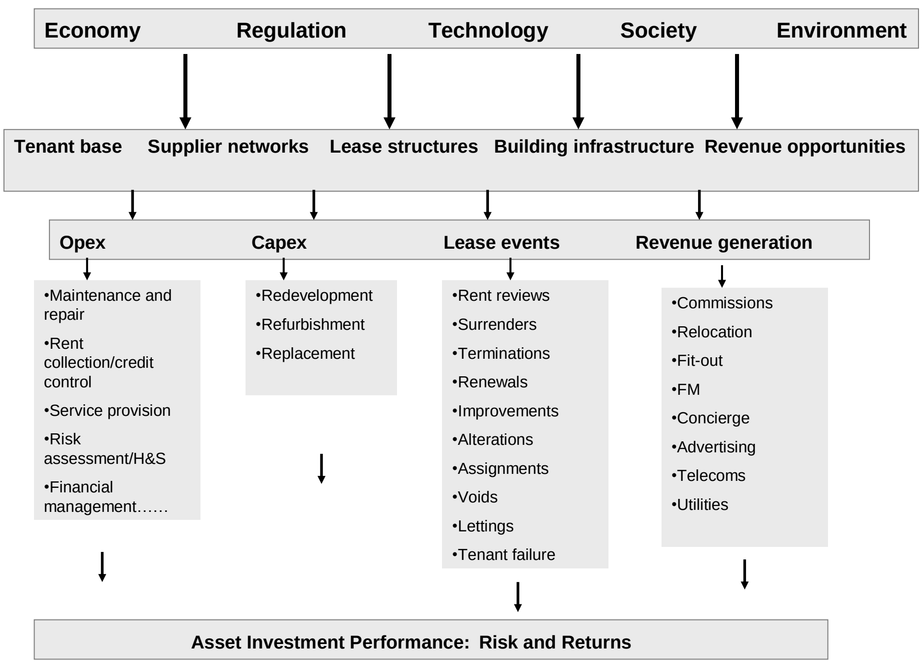
In turn, different assets require different levels of management and different specialist management functions during their life cycle. This is illustrated in Table 2. In the initial letting stage, management will tend to be intensive. Buildings will tend to require identification and resolution of construction defects, marketing, analysis, evaluation and approval of plans to alter and fit-out. In addition, managers will be required to procure the range of facilities management services for the building to operate. Once tenanted, the focus and intensity of property asset management will change to more routine functions such as rent collection, rent reviews, periodic maintenance etc. However, as buildings get older, they tend to require substantial capital expenditure to counter the effects of depreciation and assignments, surrenders and lease expiries will be more likely. In essence, the functions of property asset management change as assets become older. After buildings are let, there may be little that asset managers can do in the early years to influence financial performance. This is likely to be primarily determined by market conditions and initial leasing strategy. However, as leases and buildings mature, the decisions and activities of the asset management team become more important.

## Table 2 Management Intensity and the Property Asset Life Cycle

| Management Task | Market introduction | 'Youth' | Maturity | Decline |
|---|---|---|---|---|
| | | | | |
| Snagging | | | | |
| Fitting out | | | | |
| Marketing | | | | |
| Letting | | | | |
| Services procurement and contract negotiation | | | | |
| Fitting out | | | | |
| Service delivery and monitoring | | | | |
| Rent collection | | | | |
| Maintenance | | | | |
| Repairs and replacement | | | | |
| Rent reviews | | | | |
| Tenant failure | | | | |
| Asset disposal | | | | |
| Assignments, expiries, surrenders and dilapidations. | | | | |
| Re-lettings and renewals | | | | |
| Refurbishment and redevelopment | | | | |
| | | | | |
| Relative cost of management? | High | Low | Medium | High |

Similar to models of the property development process, the property management process could also be modelled in terms of events and tasks (lease events, financial management, procurement etc), stakeholders (tenants, public, owners, occupiers, contractors, professionals) and structural drivers (technology, economy, social, regulation). How these variables are transmitted to the financial performance of the asset is rarely evaluated. Figure 1 tries to provide a simple descriptive model of the different 'layers' of factors focussing on the how structural changes are transmitted to property asset managers' activities which are, in turn, transmitted to asset performance.

**Figure 1 From Macro to Micro in Property Asset Management**



The nature of the business models for property management services does not seem to have been analysed with the same rigour as many other business sectors.

A key decision for the owner of property assets is how to structure their procurement and delivery of property asset management - whether to deliver in-house, outsource to property management service providers or, more commonly, some combination of these two options. Apart from drawing upon the mainstream outsourcing literature in the management discipline or, perhaps more closely related, from corporate property management, we are rarely able to offer our students more than anecdotes about the different approaches to structuring the delivery of property asset management in the commercial property sector and to explain why it is structured in these ways. The knowledge gap is not just in *explanation* and *evaluation* of different approaches but also in basic *description* of different delivery models. In the UK, the standard, but not universal, model for most large investment organisations *seems* to be to outsource property management functions (however defined) to property services companies such as JLL, CBRE etc and to retain asset management 'in-house'. Within this group, often in an effort to procure specialist expertise in a specific function (e.g. lettings, rent reviews), sector (e.g. retail warehouse) or geographical market (e.g. City of London), some investors use multiple providers. We think that a fairly small proportion of large investment organisations deliver most property management functions 'in-house'. However, it seems to be rare for an organisation to outsource all functions or to deliver all functions.

There is very little published knowledge on how the delivery of property asset management is structured, the perceived rationales for different structures and there is certainly no empirical research evaluating the effectiveness of the different models. With regard to property asset management delivery, we find ourselves unable to address three key questions with the authority that can be drawn from empirical evidence. How do investing organisations procure and deliver property asset management functions? What are the costs and benefits of different models? How effective are the different models of delivery? The growing globalisation of property markets has meant that many occupiers and investors increasingly need to solve the problems of procuring and delivering effective property asset management in non-domestic markets where principal-agent problems and information asymmetries are enhanced.

In addition to the standard investment management tactical and strategic allocation decisions common to all investment portfolios, property investors have the opportunity to improve investment returns (create alpha) by entrepreneurial and innovative management. Conversely, a relative lack of entrepreneurial or innovative skills can produce relative underperformance. Since the delivery of property management is often organised in an hierarchical structure, it is difficult to generalise about the skill set and knowledge base. However, typically core skills have been associated with administration and co-ordination closely associated with communication and negotiation. The core knowledge base has consisted of landlord and tenant law, contracts and procurement procedures and building technology and services. This application of this knowledge base is often triggered by the wide range of events linked to the delivery of services, management of the landlord and tenant relationships and problems with the physical condition of the actual building.

However, as we have seen, it is widely recognised that the ownership of property assets presents many opportunities to add value by entrepreneurial activities and innovations. Commonly acknowledged ways in which owners can change both the income and expenditure profile are by changing the building (improve/refurbish, replace, extend, reconfigure), the use (intensification or switching), the tenants, the leases and the services (expand or re-organise). Problems related to principal-agent, incentivisation and contract design are at the heart of the effective delivery of property asset management services. To what extent do the organisational structures used for the delivery of property asset management services incentivise entrepreneurial actions by managers? To what extent do the organisational structures used for the delivery of property asset management services *disincentivise* entrepreneurial actions by managers? Principal-agent problems are central to these issues but they have rarely been analysed in these terms. Does the property asset management profession attract individuals with the skill sets and personal attributes associated with engagement in entrepreneurial activity? Is there a structural conflict between the skill sets required for the co-ordination and administration roles relative to the exploitation of opportunities to enhance value?

Whilst investing organisations seem to justify their decision on structuring property asset management in terms of rationales rather than evidence. There have been no published empirical investigations of the relative performance of property asset managers. Whilst the investment performance of fund managers is benchmarked and can be attributed to their relative stock selection and portfolio strategy skills, there are no analyses of how effectively the underlying assets have been managed. This is probably because such an exercise is not straightforward. The basic research question here seems to be "All else equal, are there statistically significant differences in the financial performance of different property asset managers?" The ideal experiment would be to give a sample of identical assets to a range of property asset managers and measure the total returns (taking into account costs, expenditure etc) achieved over a fixed holding period. Whilst such an experiment is not feasible, envisioning it helps us to appreciate the number of potential confounding factors that need to be controlled for.

Due to asset heterogeneity caused by variations in location, age, lease structures, construction, tenants etc, disparities in property asset manager performance may occur due to differences between portfolios over which the property asset manager has no control.  In addition, it is also important to control for the time-varying risk preferences.  For instance, in market downturns, "flight from risk" effects may mean that the values of higher risk and more management intensive (short unexpired lease terms, weak tenant quality, older buildings) assets may fall faster relative to prime assets.  As a result, the performance of property asset managers who manage higher than average amounts of secondary property may be poor because of investors increased risk aversion rather than their intrinsic performance as property asset managers.  Controlling for confounding factors, randomness and time-varying risk preferences presents major challenges in estimating whether there are statistically significant differences between property asset managers in terms of income and capital growth.

To sum up, it seems reasonable to argue that much of the published material about the operation of the property asset management sector is become increasingly obsolete.  There seems to be opportunities for researchers interested in property management to provide description, analysis and evaluation of contemporary approaches to delivering and procuring property asset management.  Since producing methodologies for measuring the relative performance of property asset managers itself presents significant challenges; robust, evidence-based evaluation of different models of property asset management is likely to be difficult.  Whilst certain types of property assets are likely to throw up opportunities for entrepreneurial activities, other assets are likely to require a larger focus on administrative, technical and organisational skills and knowledge.    The research questions are implicitly focussed on identifying the best models to incentivise property asset managers to add value and to assess whether the right skills are being deployed in the right assets at the right time.  Clearly, there is a large research agenda here.