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Time for Real Values on Commercial Property

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This page shows the article as it originally appeared in the newspaper. The article itself can be read on the following page.

Commercial Property

Valueless Greater Clack? Rejected

Time for real values on commercial property



The article discusses the current state of the commercial property market, highlighting the challenges faced by investors and the need for realistic valuations. It mentions that the market has been sluggish and that there is a need for more transparency and realistic pricing. The article also touches upon the impact of economic factors on property values and the role of government in regulating the market.

Valueless: Greater Clack? Rejected

Inducements kept secret for competitive advantage

The article continues to explore the complexities of the commercial property market, focusing on the issue of secret inducements and their impact on competitive advantage. It discusses how such practices can distort the market and lead to unfair competition. The article also mentions the need for regulatory changes to address these issues and ensure a fair and transparent market.

This is the article's web address for reference.

<http://www.irishtimes.com/newspaper/archive/2007/0328/Pg046.html#Ar04600>

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Time for real values on commercial property

One of the major transparency problems in the commercial property market is the use of inducements and the openness (or not) with which they are disclosed, writes

Lorcan Sirr

The recent letting by Shelbourne Development to Dolmen Stockbrokers of space in the newly refurbished 75 St Stephen's Green was apparently one of the first lettings in several years to happen without the use of inducements.

Whether this is entirely true depends on whether or not a landlord paying for a fit-out of space for a tenant is considered an inducement.

But the disagreement over whether or not the yields being quoted for the sale of the building were accurate or not highlighted some ongoing issues in the commercial property market as a whole. In particular, it brought home the question of transparency in the market.

The Irish commercial real estate market is, in reality, fairly transparent. According to Jones Lang LaSalle's *Global Real Estate Transparency Index 2006*, Ireland is joint 15th (with Austria) out of the 56 countries mentioned.

That puts us in the second tier out of five, behind such countries as Australia, the United States, Sweden, and even South Africa. (Vietnam came last, in case you were wondering.)

Not too bad, all-in-all, but when yields are so low and the sums of money involved so huge, any improvement on 15th could well be financially advantageous to all concerned in the long term, and commercial property investment is all about the long term.

A new question on Jones Lang LaSalle's *Global Real Estate Transparency Index 2006* concerned the availability of information regarding properties for sale or lease, on which we could undoubtedly do better.

And that's the point, for one of the major transparency problems in the commercial property market is the use of inducements, and the openness (or not) with which they are disclosed.

As inducements have a direct impact on the amount of net income generated by a property, the disclosure or lack of disclosure - in other words, transparency - can have a significant impact on the true value of a property. This is particularly pertinent when the building in question is being used as a comparable to value other property.

Inducements are prevalent in the Irish commercial property market and, being designed to fit the individual tenant, can take many forms.

They are often to be found as rent-free periods, periods of staggered or stepped rents, premium payments to tenants, break clauses, contributions by landlords to the costs of any fit-out for tenants, or indeed the acquisition by the landlord of new tenants' existing lease on another property.

All very well then, and when inducements encourage a struggling market, or indeed simply fill empty space, they are very welcome.

After all, buying one tin of beans in your local supermarket only to receive another one free is a form of inducement, and we happily live with them every day.

The problem is, if your local supermarket was for sale, the inventory will describe in detail all remaining stock after the buy-one, get-one-free offer. It's possible to work out the net cost of the customer inducement.

In the commercial property market, these inducements are very rarely disclosed, nearly always being the subject of confidentiality agreements, and as they have an intrinsic financial value - a year's rent-free is, on the face of it, a year without rent for a landlord - not disclosing them is effectively masking their existence to interested parties.

A potential purchaser or a valuer arrives on the scene and has to second-guess the real financial value of the income stream based upon nothing more than personal knowledge, experience and contacts or those of his or her surveyor.

As the value of the income stream will be a major determinant of the capital value of the property, then it is vital that accurate financial information is acquired and analysed.

The problem lies in the sourcing of this information.

Valuers look at similar recent deals and

analyse the rents and prices quoted, but again accuracy is difficult as alongside the inevitable confidentiality clauses, many leases are structured to protect the landlord's long-term and reversionary interest by keeping the headline rent as high as possible.

Information is garnered from other valuers, but eventually everybody is a competitor, and many agents are landlord-oriented, and are also unwilling to create a situation where they reveal information only to have this used as evidence against them at some later date in a rent review or arbitration.

Valuers, of course, are aware of the prevalence of these inducements and the over-enthusiastic use of rental figures, and make very competent attempts to incorporate them into their valuations. But they are only attempts, and their success at analysing the hidden element of a commercial property transaction truly is partly science and partly art. Inter-firm competition, client confidentiality and a paucity of real evidence makes accurate valuation difficult.

A large degree of the reliability of comparable information is dependent on having faith that the figures being acquired

are indeed true and accurate. In many instances the comparables are to an extent "true", but are they always accurate? And when so much money is at stake surely there is a better way of ensuring more accurate values are determined?

What is really needed is more transparency in the market.

The so-called "free market" is not really free in the world of commercial property due to the lack of reliable and accurate information.

One system to improve transparency is by means of a central commercial property transactions databank. This could be established on a statutory footing, but there are already successful private sector examples in places, such as Scotland and Connecticut.

In this the true and accurate details of each and every commercial property transaction would be compulsorily recorded.

Inducements would be acknowledged and accounted for in each and every transaction.

Figures would be broken down into the essentials, such as true price per square metre, recording and value of any inducements, and capital value and hence yields derived. Details, such as location, would be necessary in order to be able to track yields and rents in specific areas, but

access could be restricted to specific groups.

This would not be a tool to enable the Revenue Commissioners to chase the occasional forgetful investor, but an instrument that would aid valuers – and the market in general – to come to terms with reassessing the valuation, and potential overvaluation, of commercial property in Ireland. This would initially create a two-tier system of accounted-for and non-accounted-for valuations.

But, coupled with modern valuation techniques over a period of, say five years, when most commercial properties would have had a rent review, this would bring about a gradual realignment of market values, creating in the meantime a more sound economic basis for the market. Many interests would – in some ways, understandably – be natural objectors to this, but thinking strategically, transparency ultimately makes everybody a winner, including the market itself. And as the world of real estate becomes increasingly global, it is especially important not to deter international funds through opaque habits.

● Dr Lorcan Sirr is a chartered surveyor and senior lecturer in the Faculty of the Built Environment, Dublin Institute of Technology

Transparency ultimately makes everybody a winner, including the market itself. And as the world of real estate becomes increasingly global, it is especially important not to deter international funds through opaque habits



75 St Stephen's Green, Dublin 2: the 9,402.3sq m (101,206sq ft) building has seven floors ranging from 596-1,586sq m (6,435-17,072sq ft) and was refurbished by Shelbourne Development. The recent letting of space in the modern office block to Dolmen Stockbrokers was apparently one of the first Dublin lettings in several years to happen without the use of inducements

