Study: Only select group of property fund managers outperform market

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Only a small group of elite property fund managers are able to consistently lead their funds to gains greater than the market, according to new research co-authored by a professor at Penn State's Smeal College of Business.

In a report for the Investment Property Forum, Shaun Bond, Smeal visiting associate professor of real estate, and consultant Paul Mitchell set out to determine whether real estate fund managers can achieve alpha, or risk-adjusted market outperformance over successive periods of time.

The researchers examined commercial property portfolios in the United Kingdom collected by the Investment Property Databank from 1982 to 2006. They looked at returns relative to a benchmark and on a risk-adjusted basis over successive three, five, and ten year periods to determine whether market outperformance could be sustained.

They found that the evidence of systematic market outperformance and risk-adjusted performance (alpha) is not strong and that only a select group of managers are able to sustain outperformance over an extended period of time.

Over the consecutive three-year periods, before adjusting for risk, they found the strongest evidence of persistent outperformance. The researchers found less evidence of continual performance over the five and ten year periods, with only a select few able to maintain outperformance over the successive ten-year periods.

In interviews with investors and investment consultants, Bond and Mitchell found that most investors view property as a way to diversify their portfolio and seek only beta returns, or those returns in flux with the market.

They did, however, find that "a minority viewed property in a different way, seeing market inefficiency, illiquidity, active management and also disregard of benchmark structures as sources of extra long-term return."

It's this different approach to property fund management that the authors believe leads this small group of investors to continually outperform the market.

Bond states: "Maintaining consistently high levels of alpha is incredibly difficult for most fund managers to achieve, however, one feature that we did note is that mangers using a value strategy appeared better placed to deliver high alpha in subsequent periods."

Mitchell adds: "Doing things differently from, instead of better than, your peers seems to be the key. It will be interesting to see how the 'beta' investors' strategies evolve in a world where market exposure can potentially be attained cheaply through property derivatives."

While the researchers examined property funds in the U.K., Bond says he would expect the results to be similar in the United States.

"U.S. and U.K. funds share the same investment philosophies and approach to investment analysis," he says. "Furthermore, many U.K. fund managers are owned or closely associated with U.S. financial institutions. For U.S. funds directly investing in the U.K., these results show that they will have to choose their strategy carefully if they are to succeed."

"Alpha and Persistence in UK Property Fund Management" is available from the Investment Property Forum (IPF). A summary of the report is available online at www.ipf.org.uk/resources/pdf/r … search_reports/Alpha%20&%20Pers%20Summary.pdf .

This research was commissioned and funded through the Investment Property Forum Research Program 2006-2009. IPF is one of the leading specialist property industry bodies in the U.K. with more than 1,800 members, including investment agents, fund managers, bankers, lawyers, researchers, academics, actuaries, and other related professionals.

Source: Penn State

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