

September 2020



# TRADING PRIVATE REAL ESTATE #1: LIQUIDITY

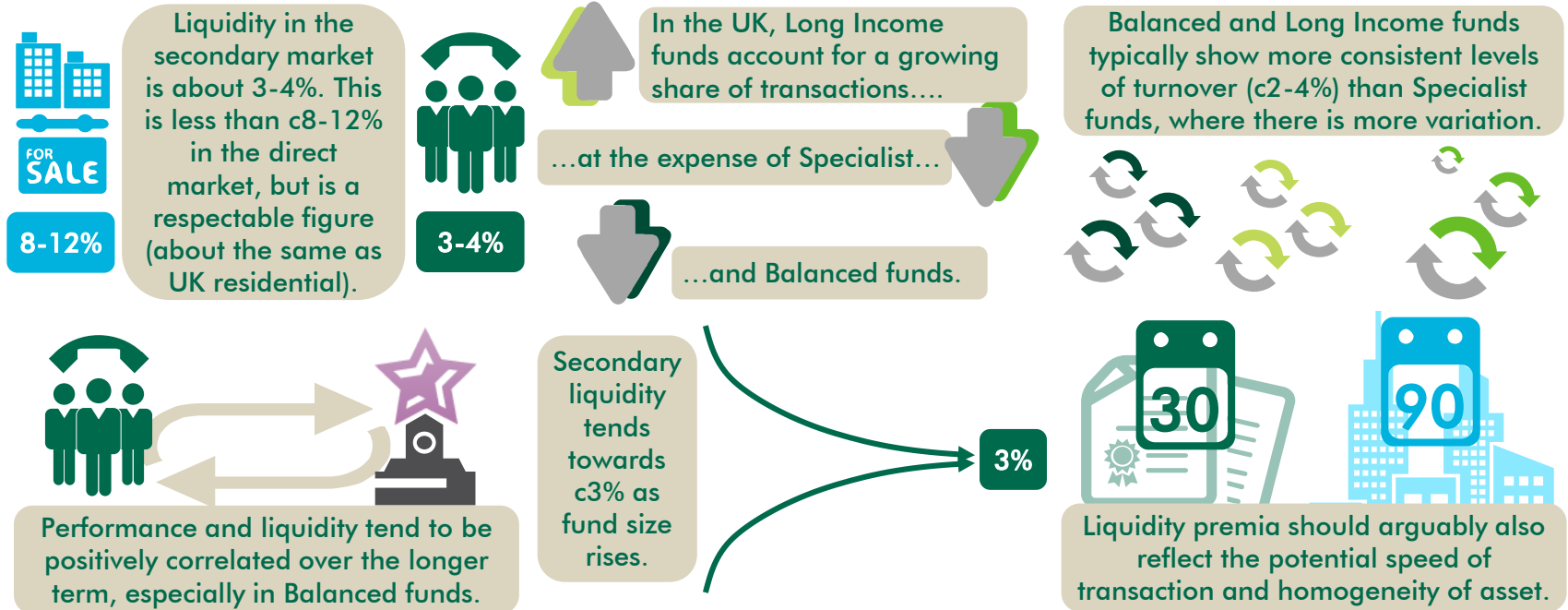
PropertyMatch®

IN ASSOCIATION WITH

**DOMINIC SMITH**  
SENIOR DIRECTOR, UK RESEARCH

**CBRE**

# LIQUIDITY & PERFORMANCE: KEY FINDINGS



Source: CBRE Research, PropertyMatch.

## BACKGROUND

This report on Liquidity aspects of the secondary market in private real estate funds is the second in our initial series.

Launching alongside this report are companion pieces looking at Pricing and Strategy.

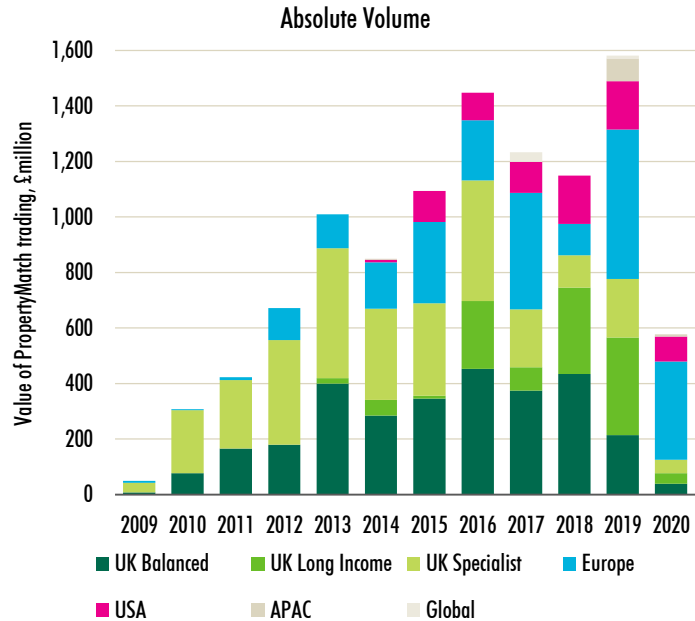
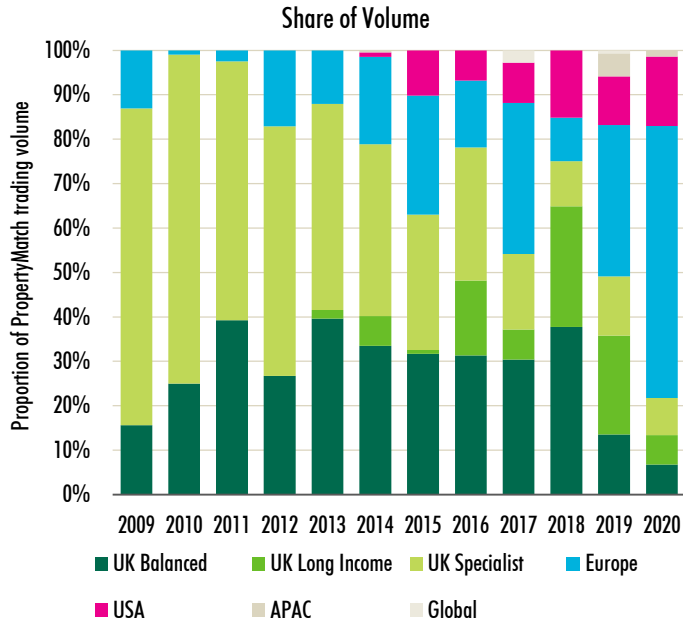
All draw on PropertyMatch's unique dataset of £10bn+ of deals and pricing information over ten years.

Further reports will follow in Q4 2020 on these and other aspects of the market, and regular pricing indices will be launched in 2021.



# PROPERTYMATCH TRADING VOLUME, 2009-2020

UK Balanced and UK Specialist funds have seen liquidity decline in the last couple of years; UK Long Income and European funds have picked up the slack. This is attributable both to a shift in investor focus and growth in the PropertyMatch international platform.



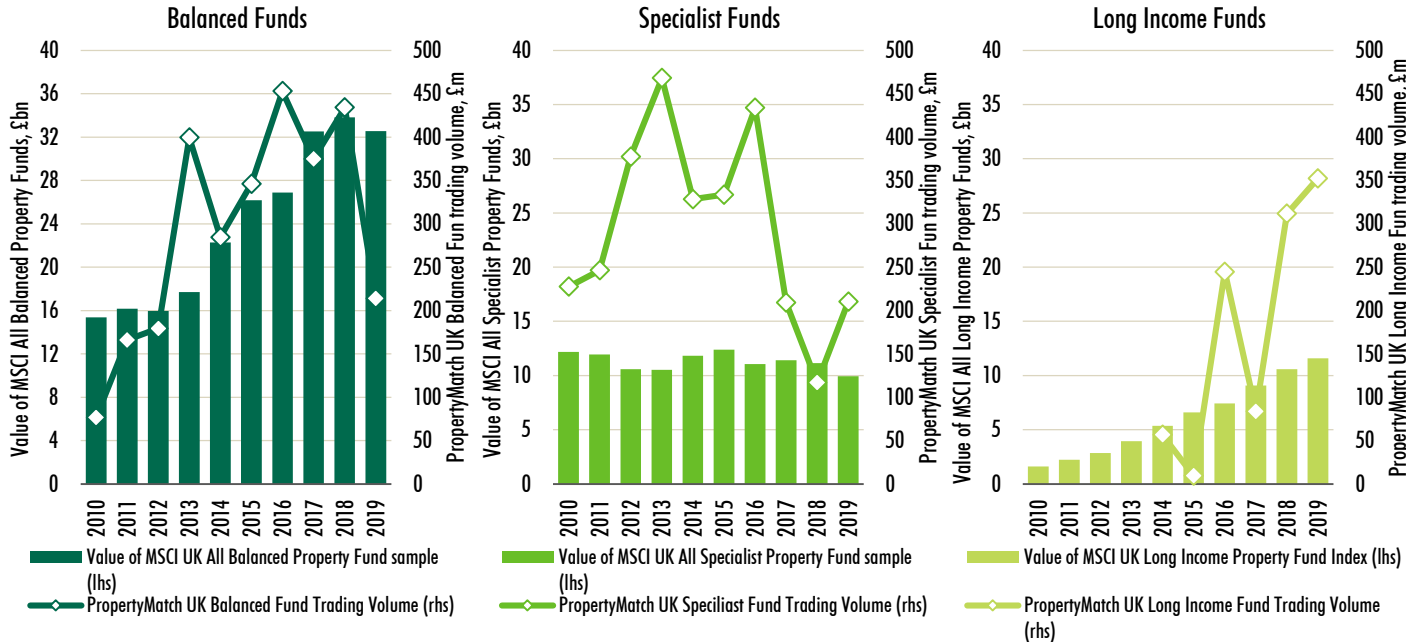
PropertyMatch has traded over £1bn in six of the last seven years. As clients' focus has become increasingly global, so the share of non-UK funds has grown, peaking at just over 50% of 2019 volume. European trades account for the majority of non-UK volume.

Within the UK, the share of volume accounted for by Long Income funds has grown rapidly over the last few years, at the expense of Balanced and Specialist funds, so that in 2019 Long Income funds were the single largest grouping in the UK, at just over £350m. Balanced fund volumes trailed off to just over £200m, having been at or around £400m in the previous six years.

Source: CBRE Research, PropertyMatch. Note: 2020 covers the period for H1 2020 only.

# PROPERTYMATCH LIQUIDITY, UK FUNDS, 2009-2019 (1)

Complete data on the size of the Private Real Estate fund Universe is not available. We can probably conclude that the mix is roughly 60-20-20 Balanced-Specialist-Long Income at the end of 2019 – with the Long Income share gaining at the expense of Specialist.



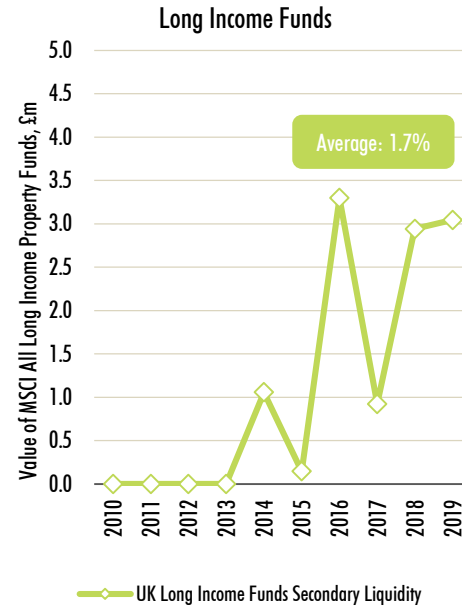
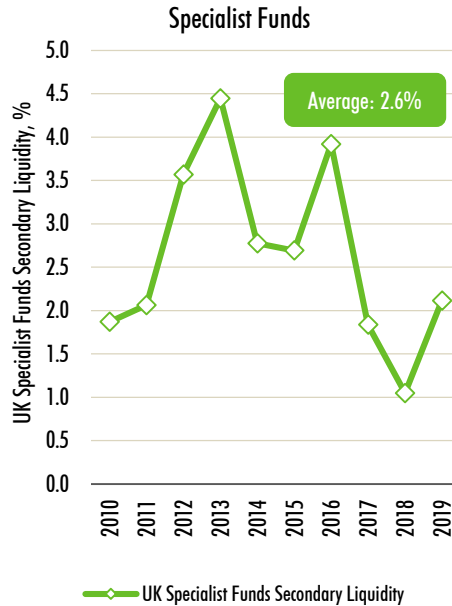
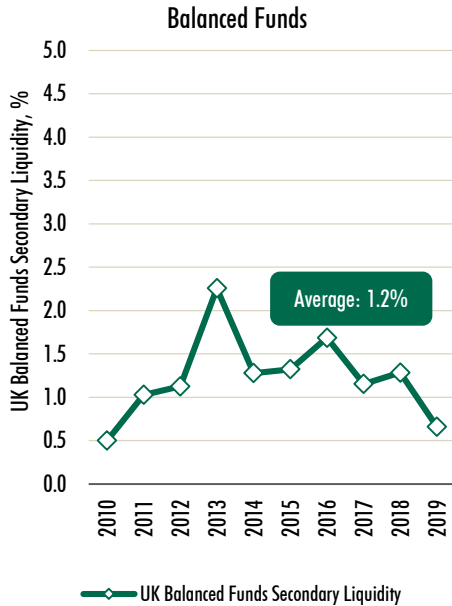
Establishing the rate of turnover of the fund groupings is problematic. It requires knowledge of the value of the respective universes. Data on this can be obtained from the MSCI / AREF UK Quarterly Funds Digest. However this may understate (because not every fund is a contributor) or overstate (because some funds listed are not tradeable) the Universe.

What the data does show is the stabilisation in value of Balanced funds, the decline of Specialist funds and the rise of Long Income funds over the last few years, so that in very rough terms they might be said to account for 60%, 20% and 20% respectively of the total Universe.

Source: CBRE Research, MSCI / AREF, PropertyMatch.

## PROPERTYMATCH LIQUIDITY, UK FUNDS, 2009-2019 (2)

Liquidity can be estimated at 1.2% for Balanced, 2.6% for Specialist and 1.7% for Long Income funds. However, this likely understates the true position thanks to probable over-statement of the size of the Universe (particularly Balanced funds).



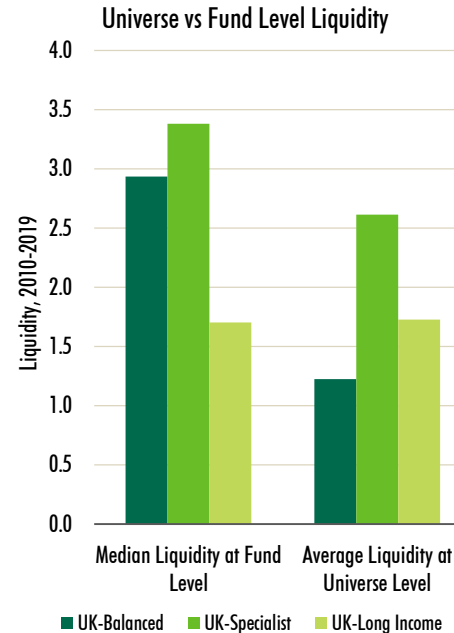
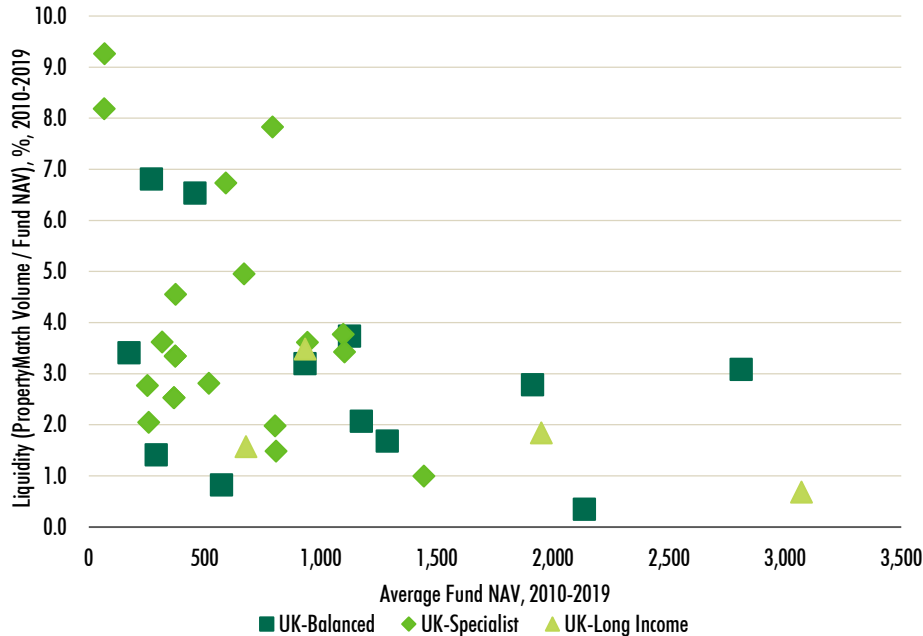
By dividing PropertyMatch trading volume by MSCI data on the value of the various Universes, it is possible to arrive at estimates of market liquidity for the three UK fund categories.

Over the last ten years (six for Long Income), Specialist funds have been most liquid (2.6% of value traded on average each year) though this has been on the decline. Long Income follows at 1.7%, though this is arguably trending upwards. Balanced funds trail at 1.2% - but here it is likely that the figure understates the truth because the MSCI Universe of Balanced funds contains a number of entities that are not tradeable on the secondary market.

Source: CBRE Research, MSCI, PropertyMatch.

## PROPERTYMATCH LIQUIDITY, UK FUNDS, 2009-2019 (3)

At the fund level, turnover as a proportion of net asset value is higher than group level estimates. It is reasonable to assume that overall, annual liquidity is likely in the order of 3-4%.



Rather than looking top down, a better way to estimate liquidity may be bottom up. For those funds that have been traded in the 2010-2019 period, and that contribute to the MSCI / AREF UK Quarterly Funds Digest it is possible to compare trading volume and net asset value.

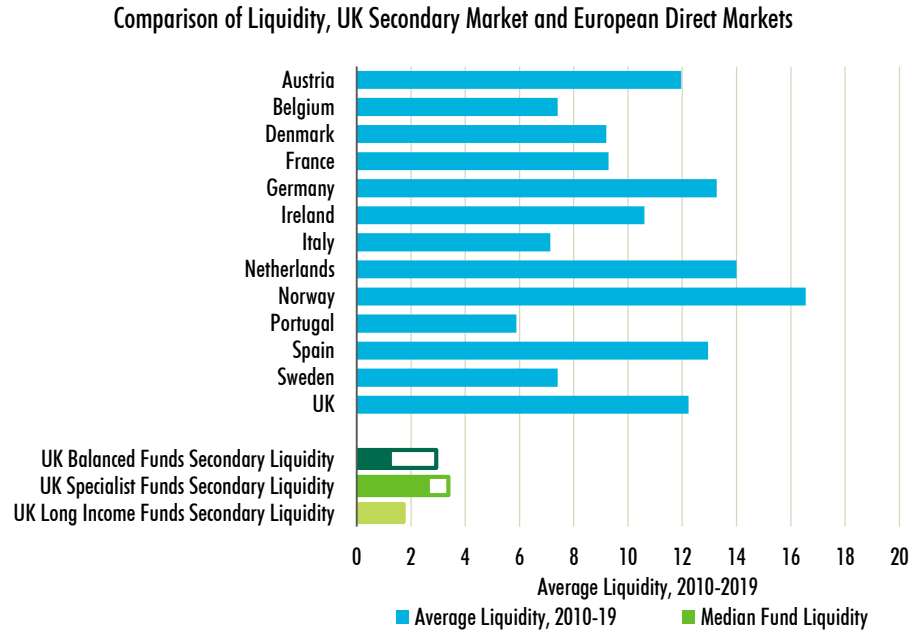
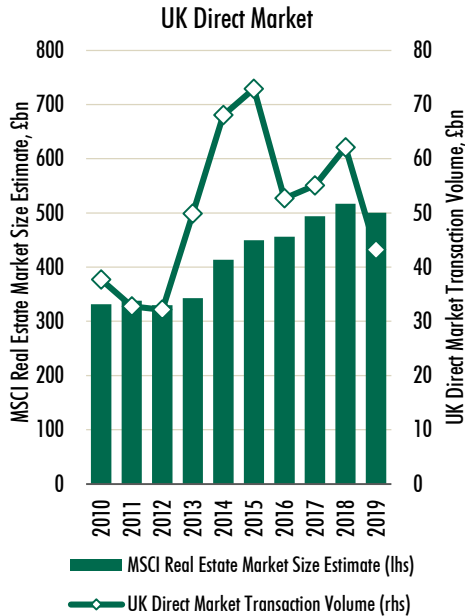
On this measure, the median liquidity figure is unchanged for Long Income (1.7%), but higher for Balanced (2.9% versus 1.2%) and Specialist (3.4% versus 2.6%).

As UK Long Income liquidity is likely constrained by a dearth of sellers, it seems reasonable to assume that all groups' true liquidity is likely around the 3-4% mark.

Source: CBRE Research, MSCI, PropertyMatch.

# PROPERTYMATCH LIQUIDITY, DIRECT MARKET COMPARISON, 2009-2019

Unsurprisingly, turnover in the direct market is quantifiably higher than in the private real estate secondary market. Our estimates of each are wide ranging – at say 8-12% versus 3-4% – but they are intended to demonstrate the orders of magnitude.



MSCI also produce estimates of the size of investment markets in all countries they operate in. CBRE tracks investment market volume in these markets. By combining the two it is possible to estimate turnover in the direct market over the 2010-2019 period, for comparison with that of the private real estate fund market.

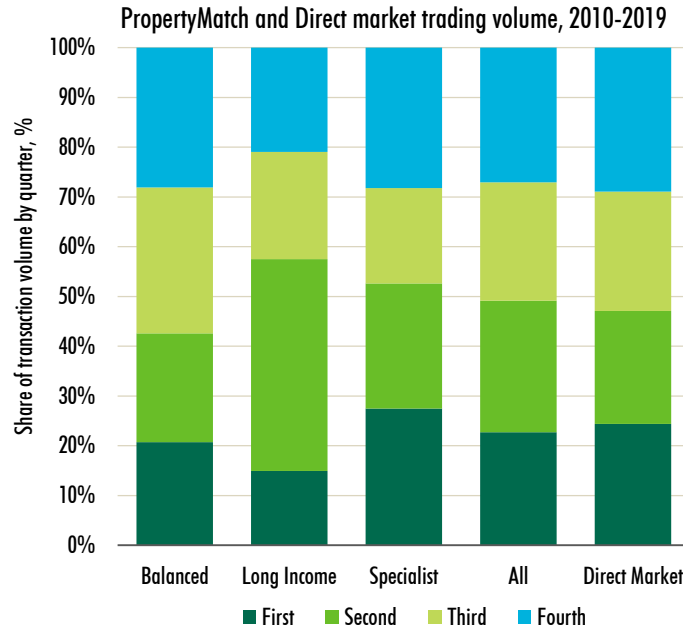
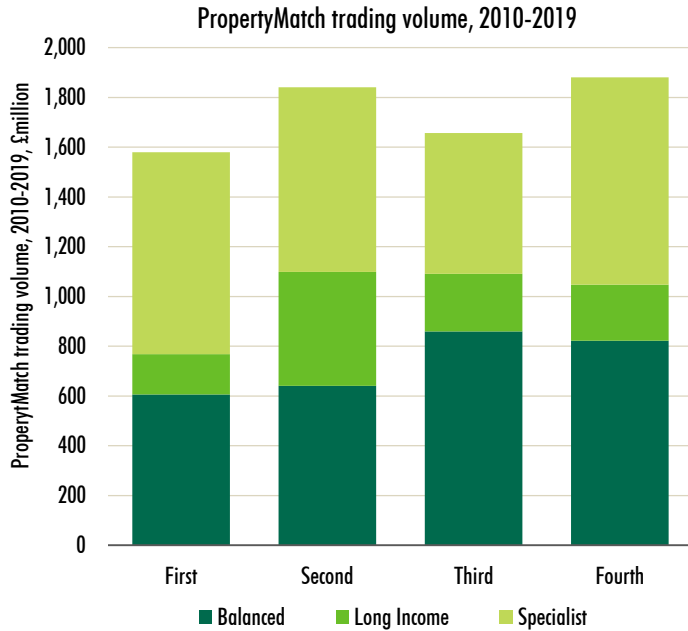
As would be expected, the direct market is more liquid; typically 8-12% of a country's commercial real estate is transacted each year, versus the 3-4% turnover seen in the secondary market for private funds.

Source: CBRE Research, MSCI, PropertyMatch.



## PROPERTYMATCH LIQUIDITY, SEASONALITY, 2010-2019

The secondary market for private real estate funds is, if anything, slightly less seasonal than the direct market; 51% of PropertyMatch transactions occur in the second half versus 53% for the direct market. It appears to be consistently active.



The direct commercial property market in the UK shows some seasonality; in the 2010-2019 period 53% of transactions by value occurred in the second half of the year, and 29% in the fourth quarter. The figures for PropertyMatch are lower at 51% and 27% respectively.

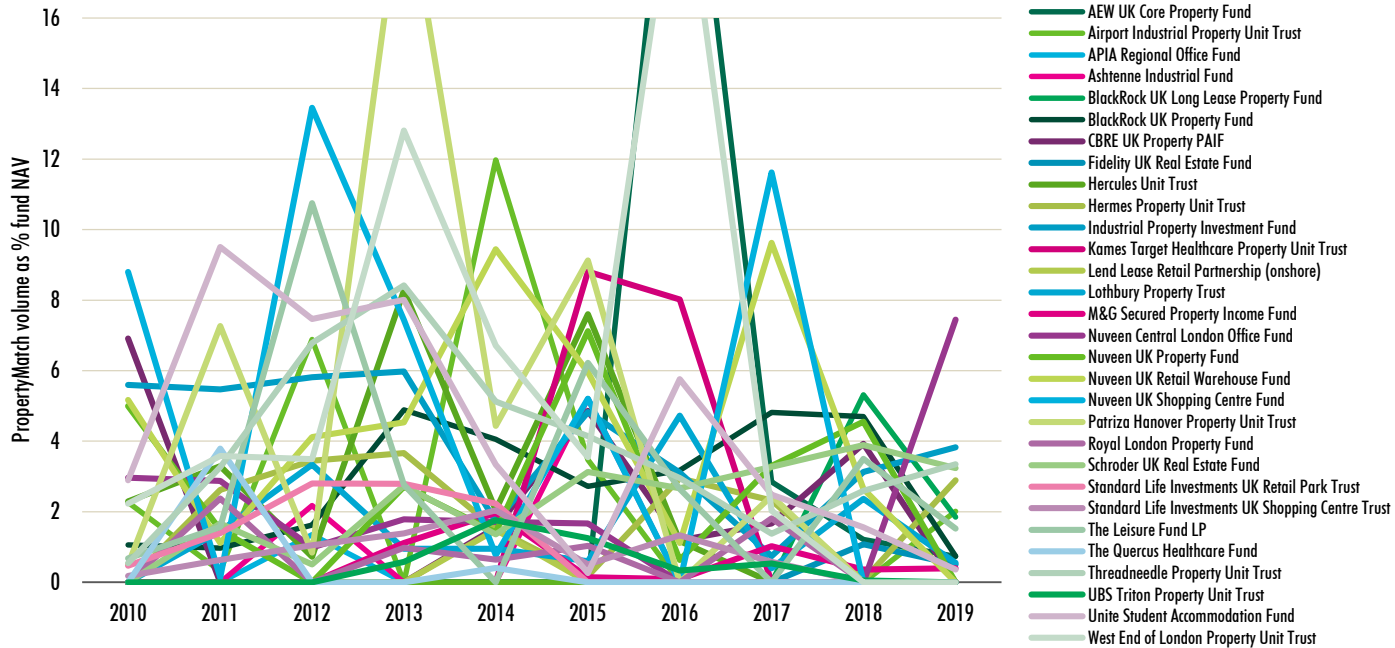
Within the secondary market for private real estate funds, Balanced and Long Income funds exhibit the most seasonality, albeit in opposite directions: 57% of Balanced fund transactions by value have occurred in the second half of the year, compared with just 43% for Long Income funds.

Overall, these figures suggest that the market is never regularly inactive.

Source: CBRE Research, Property Data Limited, PropertyMatch.

# PROPERTYMATCH LIQUIDITY, FUND LEVEL, 2010-2019

Discerning patterns across the range and variety of funds traded via PropertyMatch is difficult. Analysis will necessarily focus on UK Balanced funds; these are often larger and more stable, have been traded the longest and have performance data available.



The chart shows UK fund level trading volume via PropertyMatch over the last ten years as a proportion of NAV (for those funds for which NAV history exists in the MSCI / AREF UK Quarterly Funds Digest).

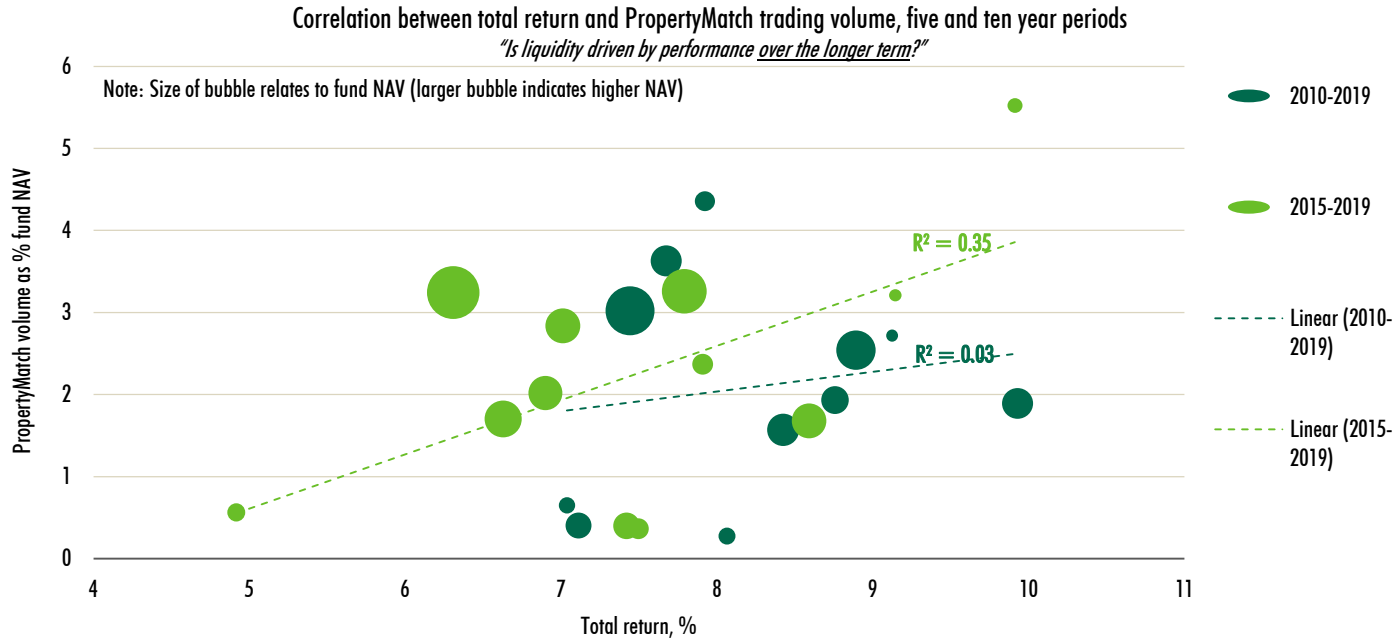
The purpose of the chart is not to allow identification or assessment of patterns at the fund level – except perhaps the broad impression that most funds usually see trading volume within the 1-4% range identified earlier – rather it is to show the noise within the sample.

In order to try to discern patterns and relationships with other factors, it is necessary to homogenise our area of study somewhat.

Source: CBRE Research, MSCI, PropertyMatch.

# PROPERTYMATCH LIQUIDITY & PERFORMANCE, UK BALANCED FUNDS, 2010-2019 (1)

For UK Balanced funds, there appears to be a reasonable relationship between performance (total return) and fund level liquidity via PropertyMatch over a five year period. This suggests that generally, better performing funds have greater secondary liquidity.



The chart compares, for the last five and ten years collectively, fund total return and trading volume (as a proportion of NAV) of 11 UK Balanced funds. (Those that have been traded via PropertyMatch and for which performance history exists in the MSCI / AREF UK Quarterly Funds Digest).

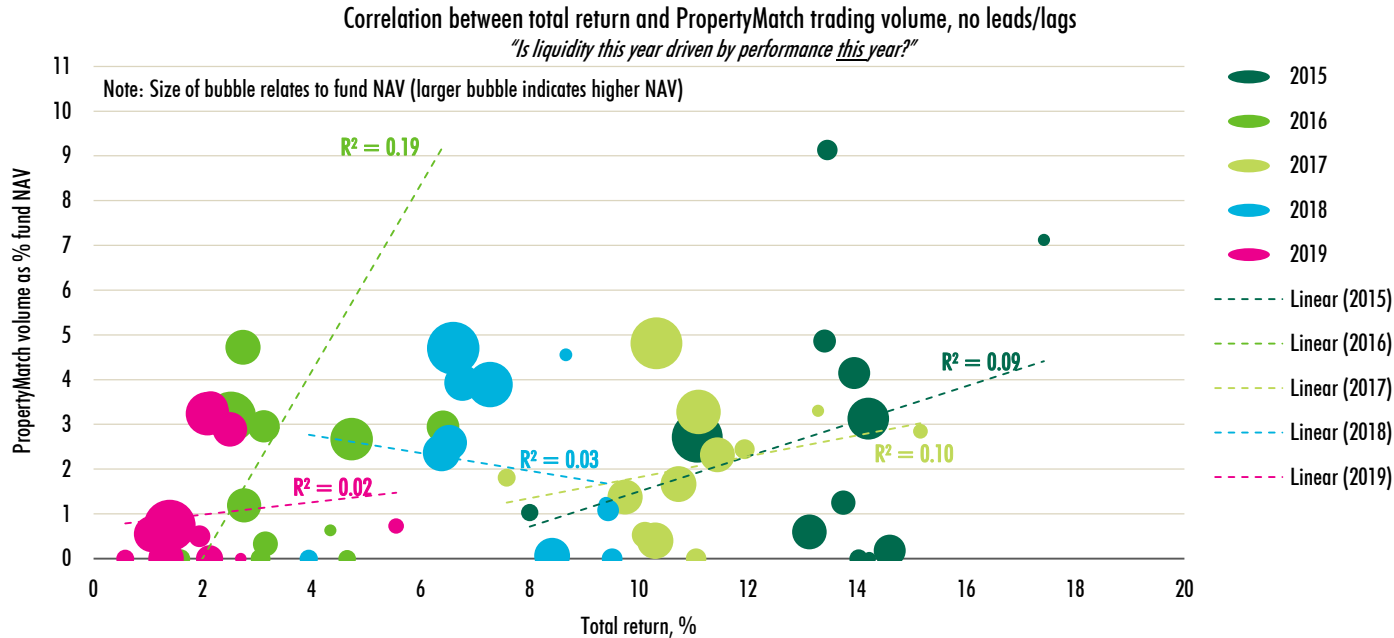
A strong relationship between performance and liquidity would indicate that the performance was driving liquidity.

For the last five years there is a reasonably strong positive correlation, but not over ten years. This may indicate that as the market has matured, a relationship between performance and secondary liquidity has evolved.

Source: CBRE Research, MSCI, PropertyMatch.

# PROPERTYMATCH LIQUIDITY & PERFORMANCE, UK BALANCED FUNDS, 2015-2019 (1)

For UK Balanced funds, there appears to be no relationship between performance (total return) and fund level liquidity via PropertyMatch in that year.



The chart compares, for the last five years, fund total return and trading volume (as a proportion of NAV) of 11 UK Balanced funds. (Those that have been traded via PropertyMatch and for which performance history exists in the MSCI / AREF UK Quarterly Funds Digest).

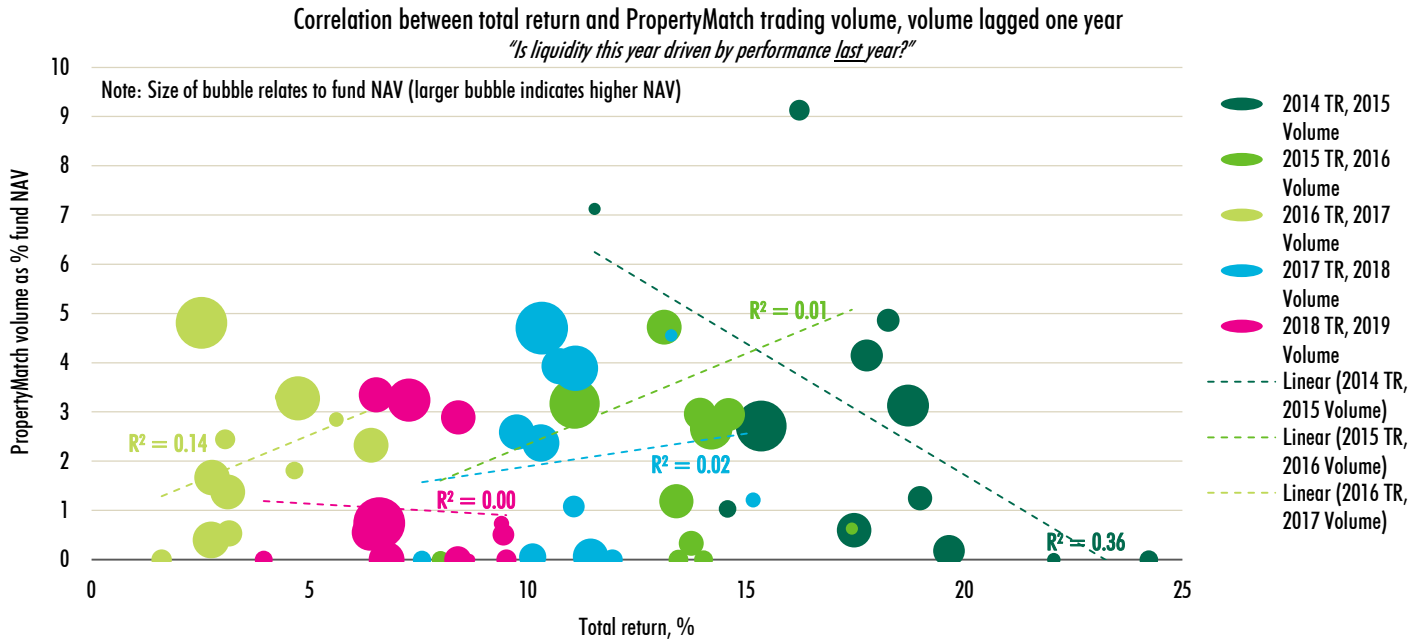
A strong relationship between performance and liquidity would indicate that the current year's performance was driving liquidity.

In all five years there is a positive correlation, but it is extremely weak (the strongest R<sup>2</sup> is just 0.19) indicating that there is no causal link between fund level liquidity and performance in that year.

Source: CBRE Research, MSCI, PropertyMatch.

# PROPERTYMATCH LIQUIDITY & PERFORMANCE, UK BALANCED FUNDS, 2015-2019 (2)

For UK Balanced funds, there appears to be no relationship between performance the previous year (total return) and fund level liquidity via PropertyMatch. Investors are not “buying last year’s winners”.



The chart compares, for the last five years, fund total return in the preceding year and trading volume (as a proportion of NAV) of 11 UK Balanced funds. (Those that have been traded via PropertyMatch and for which performance history exists in the MSCI / AREF UK Quarterly Funds Digest).

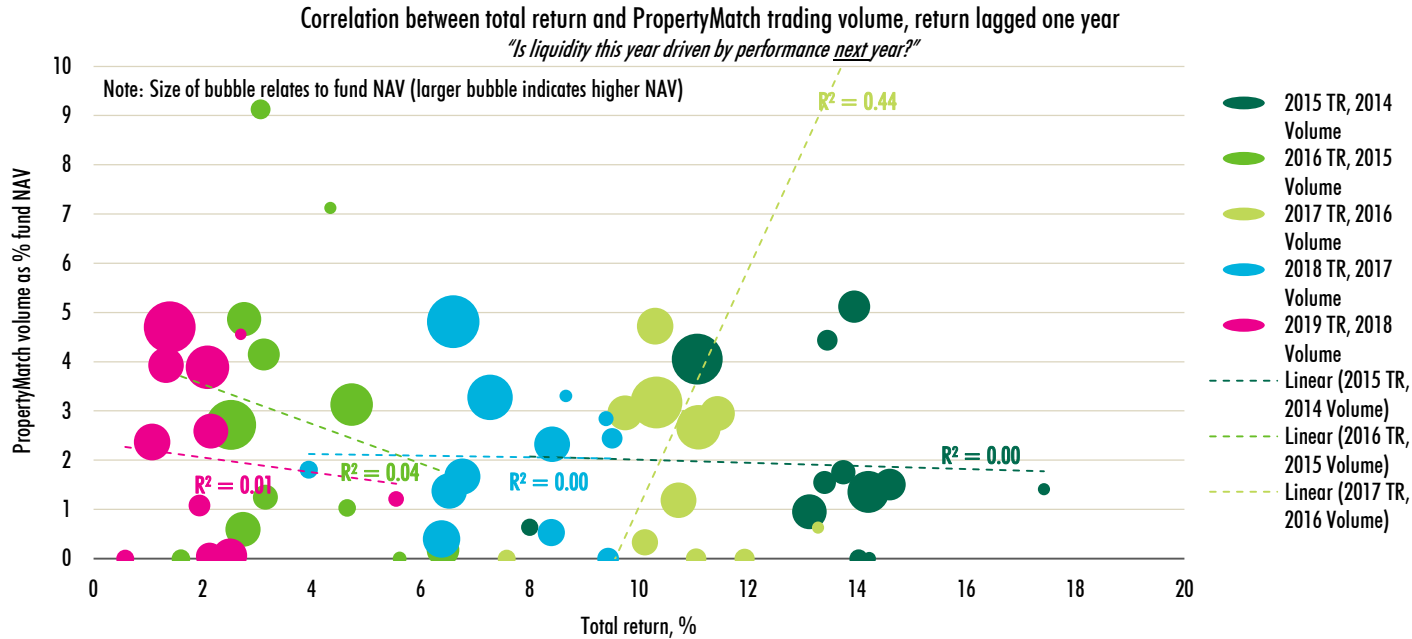
A strong relationship between performance and liquidity would indicate that the previous year’s performance was driving liquidity.

In three out of five years there is almost zero correlation, indicating that there is no causal link between fund level liquidity and performance in the prior year.

Source: CBRE Research, MSCI, PropertyMatch.

# PROPERTYMATCH LIQUIDITY & PERFORMANCE, UK BALANCED FUNDS, 2015-2019 (3)

For UK Balanced funds, there appears to be no relationship between performance the following year (total return) and fund level liquidity via PropertyMatch. Investors are not “buying next year’s winners”.



The chart compares, for the last five years, fund total return in the following year and trading volume (as a proportion of NAV) of 11 UK Balanced funds. (Those that have been traded via PropertyMatch and for which performance history exists in the MSCI / AREF UK Quarterly Funds Digest).

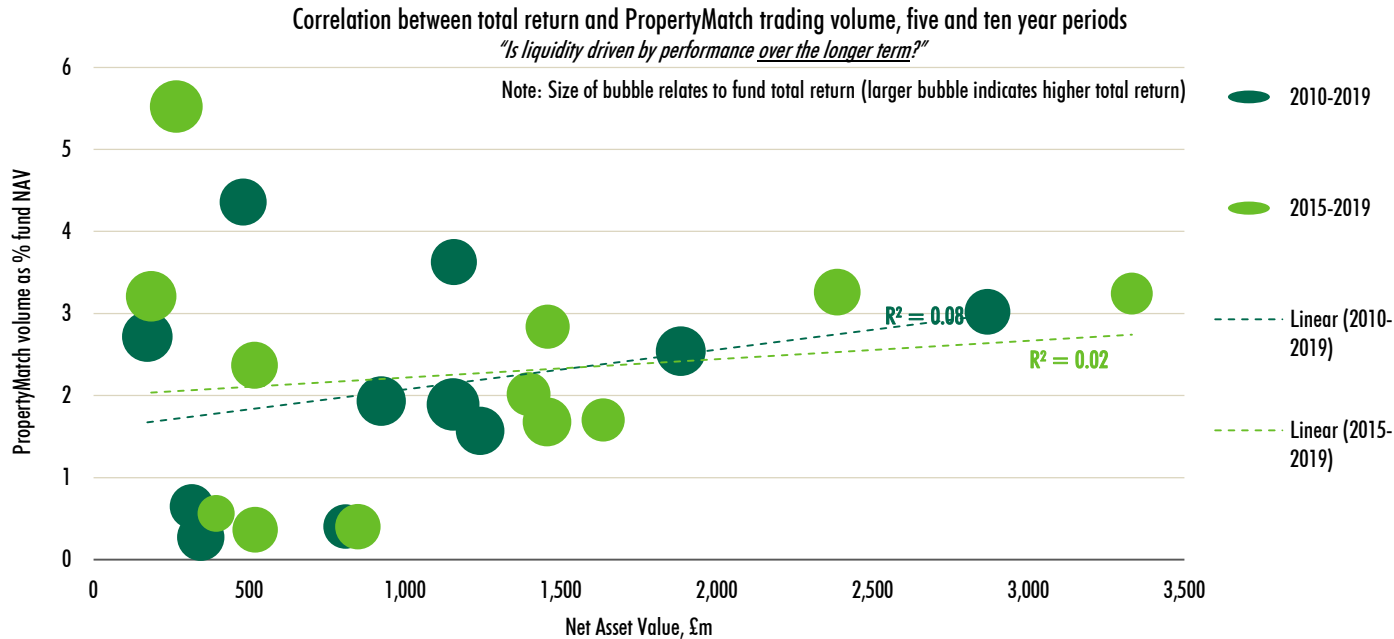
A strong relationship between performance and liquidity would indicate that the previous year’s performance was driving liquidity.

In four out of five years there is almost zero correlation, indicating that there is no causal link between fund level liquidity and performance in the prior year.

Source: CBRE Research, MSCI, PropertyMatch.

## PROPERTYMATCH LIQUIDITY & SIZE, UK BALANCED FUNDS, 2010-2019

For UK Balanced funds, there appears to be no relationship between size (measured by NAV) and fund level liquidity via PropertyMatch over five and ten year periods. If anything, there is a “fan” shape showing liquidity coalescing around 3% as size increases.



The chart compares, for the last five and ten years collectively, fund size (NAV) and trading volume (as a proportion of NAV) of 11 UK Balanced funds. (Those that have been traded via PropertyMatch and for which NAV history exists in the MSCI / AREF UK Quarterly Funds Digest).

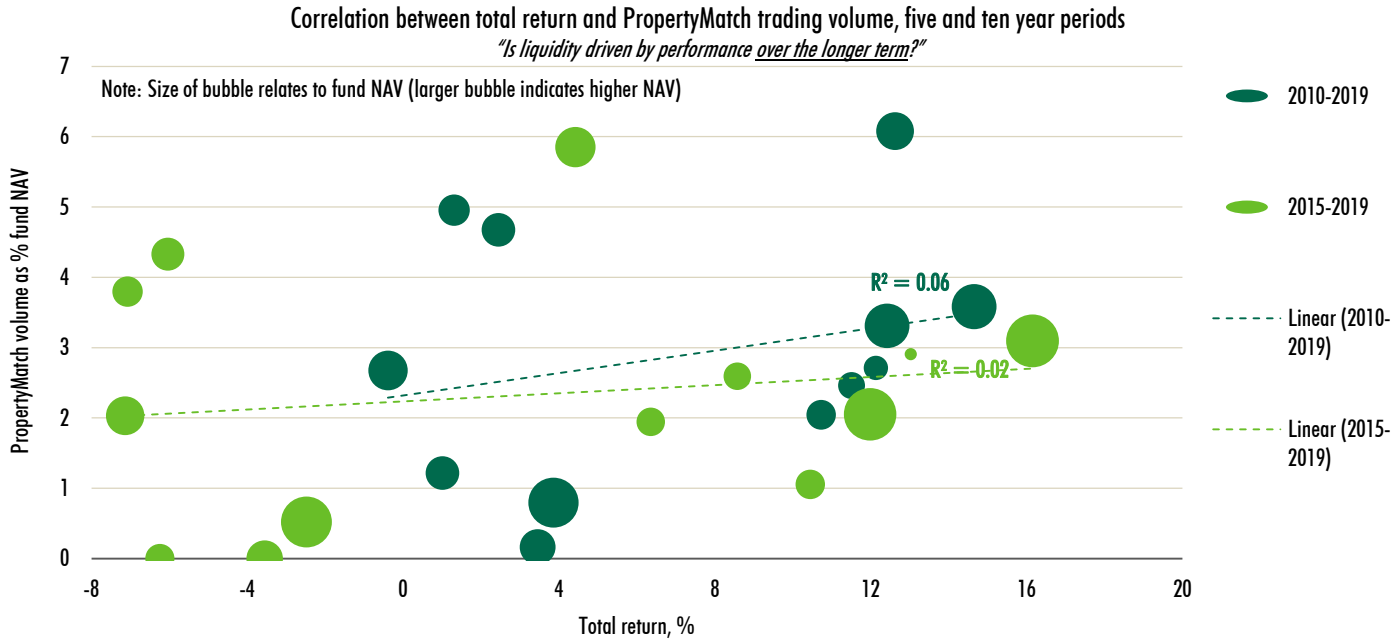
A strong relationship between size and liquidity would indicate that the performance was driving liquidity.

The data shows there is no linear relationship between size and liquidity. If anything, as size increases liquidity tends to narrow to around 3%, from an earlier range of 0-6% for smaller funds.

Source: CBRE Research, MSCI, PropertyMatch.

# PROPERTYMATCH LIQUIDITY & PERFORMANCE, UK SPECIALIST FUNDS, 2010-2019 (1)

For UK Specialist funds, there appears at first glance to be no relationship between performance (total return) and fund level liquidity via PropertyMatch over the five and ten year periods.



The chart compares, for the last five and ten years collectively, fund total return and trading volume (as a proportion of NAV) of 13 UK Specialist funds. (Those that have been traded via PropertyMatch and for which performance history exists in the MSCI / AREF UK Quarterly Funds Digest).

A strong relationship between performance and liquidity would indicate that the performance was driving liquidity.

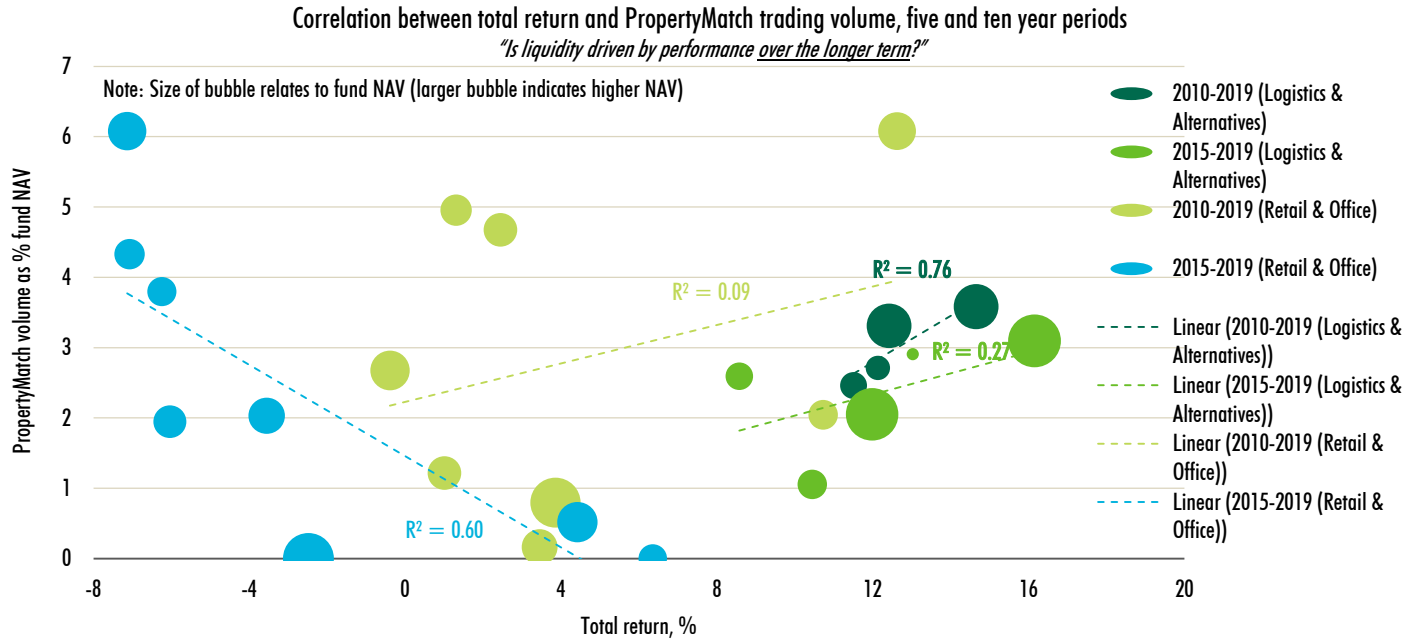
In neither case does a correlation exist, suggesting no relationship between performance and secondary liquidity.

Source: CBRE Research, MSCI, PropertyMatch.



# PROPERTYMATCH LIQUIDITY & PERFORMANCE, UK SPECIALIST FUNDS, 2010-2019 (2)

However, if UK Specialist funds are categorised by sector type, it is possible to observe much stronger relationships between performance (total return) and fund level liquidity via PropertyMatch over both the five and ten year periods.



By splitting the funds up along sector lines – grouping the better performing Logistics & Alternatives and the weaker-performing Retail & Office – it is possible to discern relationships between performance and liquidity over the longer term.

There is a strong positive correlation over ten years and a weaker positive correlation over five years between performance and liquidity in the Logistics & Alternatives funds grouping.

The Retail & Office grouping actually shows a strong negative correlation between performance and liquidity in the last five years; volume in weak funds may have been driven by opportunistic buying at sharp discounts.

Source: CBRE Research, MSCI, PropertyMatch.



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