PATRIZIA
INVESTMENT COMPASS

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CONCENTRATION OR COMPETITION –
where does the journey go for the global real estate investment management industry?

In today's environment, real estate is one of the most sought after asset classes from institutional investors. Consequently assets under management in the industry have grown significantly since the global financial crisis, as reported in the different market surveys like the ANREV/INREV/NCREIF fund manager survey. Based on this survey, assets under management of the top 100 fund managers have more than doubled, increasing nearly 12% p.a. on average since 2009. At the same time, noticeable M&A activities were observed in the industry in an environment becoming ever more global, especially with regard to capital sourcing.

For institutional investors this gives the impression that market concentration has significantly increased during this time. Looking at the cumulative market share, based on global assets under management for the top 100 over the last six years, the feeling of increased concentration seems to be contradicted. In 2009 assets under management were more concentrated within the top 100 players as in 2015. However, an increase in concentration can be observed during the last three years. As this analysis only captures the top 100 market players and 162 fund managers responded to the survey in 2015, further analysis is required to look closer at this market development. Analysing the competitive situation in a given market, different concentration measures can be used. The most common measures are the concentration ratio (CR) and the Herfindahl-Hirschman Index (HHI) (see box for calculation method). Looking at the overall results of the 2015 ANREV/INREV/NCREIF fund manager survey, 162 managers responded, representing assets under management of 1.78 trillion. Of these 1.78 trillion the top 100 managers account for round about 1.73 trillion or a little more than 97%. This gives a first indication about the missing market share, if the analysis is focused on the top 100. The following analysis concentrates on the top 100 and assumes two scenarios for the missing market share: 3% as indicated by the missing 62 companies in the 2015 survey and 10% to account for the fact that possibly some larger players are missing in the survey. The development of the averages between the upper and lower bound estimation of the HHI in each of the two scenarios for the global real estate investment management industry over time are reported in Figure 1 as are the CR4 values, confirming the concentration pattern seen in the top 100.

CONCENTRATION MEASURES

1. Concentration ratio (CR)

The most widely used concentration ratio is the "CR4", measuring the cumulative market share of the largest 4 firms (k =4):

$$CR_4 = \sum_{i=1}^{k} s_i$$

with s_i=market share of firm i

2. Herfindahl-Hirschman Index (HHI)

The HHI sums up the squared market shares of each single firm competing in the market:

$$HHI = \sum_{i=1}^{n} s_i^2$$

with n=number of firms in the market

The difficulty with both measures when applying them to the real estate investment management industry is that information about the size of the whole market is required. As the size and the absolute number of players in the global real estate fund management industry is unknown, one has to make an assumption about the missing market share as a first step and calculate the CR and an upper and lower bound of the HHI as a second step.

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DEVELOPMENT OF CONCENTRATION MEASURES FOR THE GLOBAL REAL ESTATE INVESTMENT MANAGEMENT INDUSTRY OVER TIME

CR$_4$ (missing market share)

	3%	5%
2009	23.86%	22.34%
2010	18.99%	17.78%
2011	21.19%	19.84%
2012	18.48%	17.31%
2013	20.08%	18.80%
2014	19.28%	18.05%
2015	19.40%	18.17%

As often with such type of analysis, the devil is in the details, and a closer look at the market situation on a regional basis and for different product types is useful to better understand the current market developments, as the overall results for the market do not indicate any significant market concentration within the global real estate fund management industry. Looking at the cumulative market shares of the respective top 100 investment managers of the assets under management in the different global regions, it becomes obvious that on a regional level higher concentration can be seen in all three major regions, i.e. Europe, Asia and the US. This suggests that there are some noticeable regional market players to be found in Europe, Asia and the US who are not competing in the same intensity for assets under management on a global scale as they do right now in their respective regions.

With more than 800 employees in more than ten countries, PATRIZIA Immobilien AG constantly analyses the different real estate markets and helps institutional and private investors make knowledgeable decisions.

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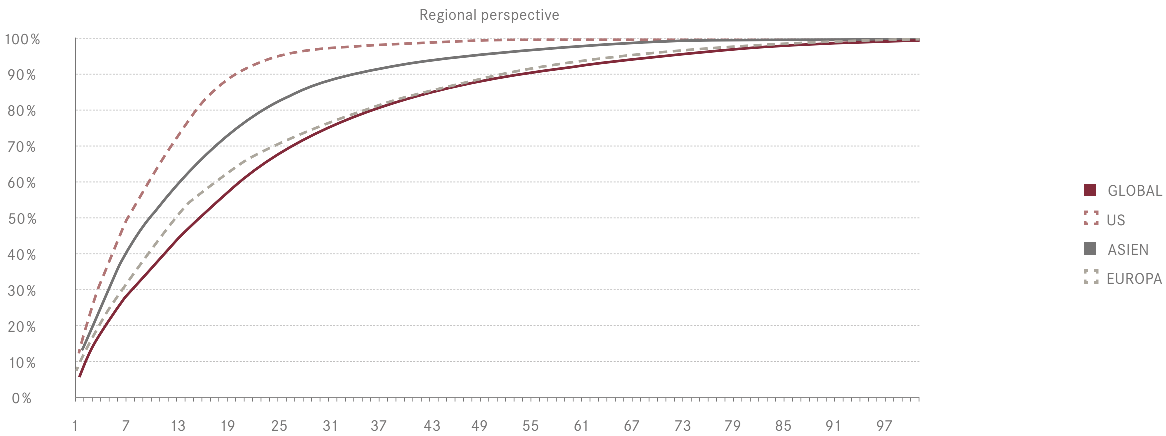
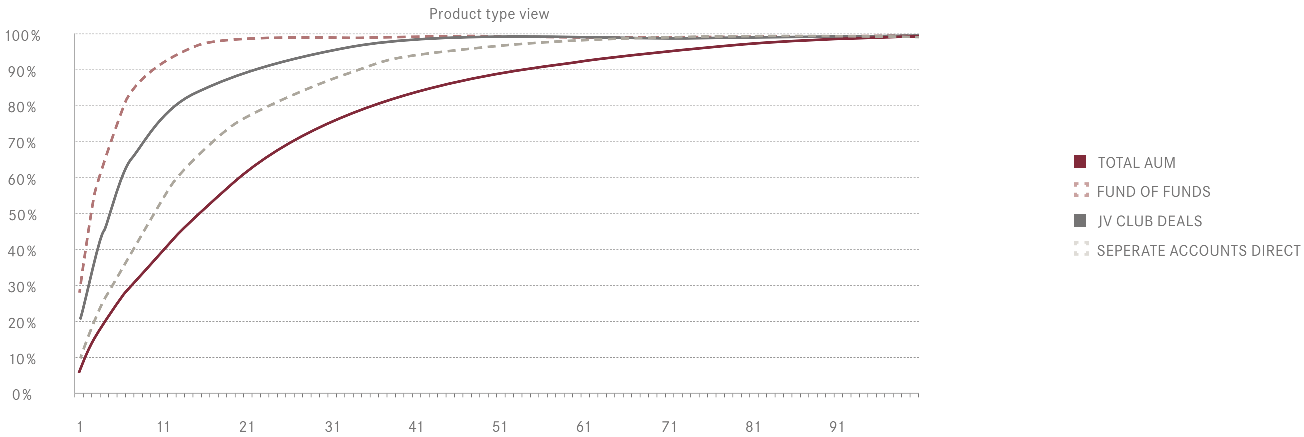
CUMULATIVE MARKET SHARE BY REGION AND PRODUCT FOR THE RESPECTIVE TOP 100 FUND MANAGERS IN 2015

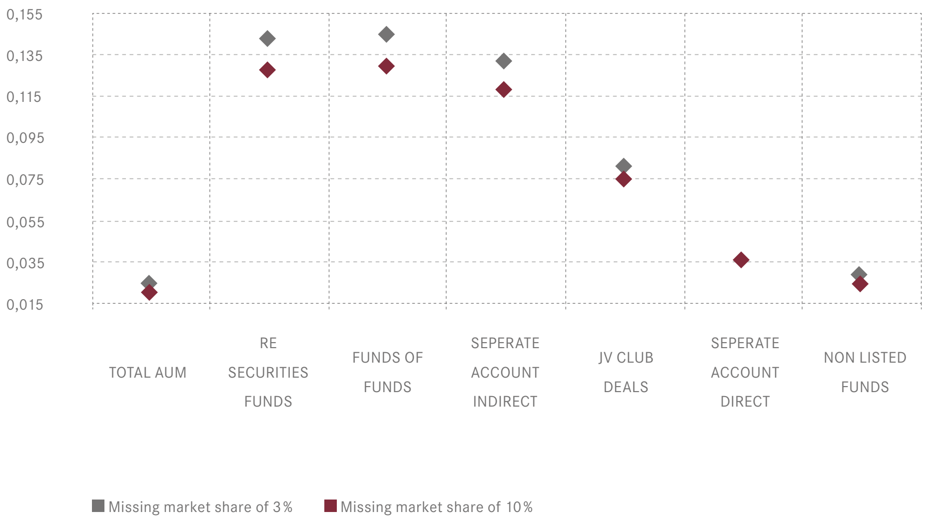




Source: PATRIZIA, based on INREV data

A much stronger market concentration can also be found when looking at different product types. Assets under management in the fund of fund segment, in separate accounts and in the area of club deals and JVs are much more concentrated in comparison to the overall assets under management in in the global real estate investment management industry.

HERFINDAHL-HIRSCHMAN-INDEX APPROXIMATION BASED ON ASSUMPTIONS OF MISSING MARKET SHARE FOR DIFFERENT PRODUCT TYPES ON A GLOBAL SCALE



Source: PATRIZIA, based on INREV data

These structural differences are largely due to the fact that these segments require a special skill set on the side of the investment manager. In addition, the time consuming process of the development of knowledge and trust is a crucial success factor, especially in the area of separate accounts as well as with club deals and JVs, requiring specialised staff and reporting systems.

Due to the costs associated, these resources are not available to every investment manager in the industry. The higher concentration in these segments is therefore the logical consequence of these barriers to entry. In addition, one has to keep in mind that the data of the ANREV/INREV/NCREIF fund manager survey give a more or less complete picture of these segments compared to the overall market. The estimations with the missing market share of 10 % will therefore not be closer to the actual concentration level, pointing to a moderately concentrated market in these product types. In addition one has to keep in mind that the survey is looking at the assets under management and is therefore in general backward looking.

Current fund raising activities as well as not fully invested funds do not show up in the results yet, as do the changes resulting form current regulatory changes.

Given the very competitive environment in the real estate investment markets, it can be expected that it will take something between three and five years before all of the current fund raising and closing activity is fully reflected in the surveys about assets under management, making the effects and costs associated with current regulatory changes visible. Going forward, the ongoing changing regulatory environment will ultimately lead to increasing concentration, especially in the segments outlined above. It will be less the case in the general indirect fund market, as service providers can help in this segment delivering the infrastructure needed to comply with the national and international regulations.

As more capital will be channelled towards real estate in the coming years and as the globally active institutional investors increasingly demand tailor made reporting solutions, it can be expected that segments like separate accounts or club deals and JVs will see substantial growth going forward.

Ultimately these developments will result in a more concentrated market, but it will take some time, before this development becomes clearly visible in the market data.