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TRANSCRIPT

Building the Foundation for the First Real Estate Indexes

Featuring: ***René Veerman****, Head of Real Estate, MSCI with* ***Rupert Nabarro*** *and* ***Ian Cullen****, Co-Founders, IPD*

René:

Today we are celebrating 40 years of indexes, together with Rupert Nabarro, Founder of the Investment Property Databank, predecessor of MSCI real estate. Thank you very much for joining us, Rupert. Rupert, would you mind telling us a little bit about when you first started in the real estate industry, your first role, and what investing in real estate looked like at the time?

Rupert:

I certainly had no background whatsoever in real estate industry and I trained and practiced as an urban economist, and was thus interested city markets, housing markets, transportation markets, labor markets, and also real estate markets. And they were very difficult to work in because there was never any proper information about them. And I was an economist and what I wanted was price information, which in this case, meant information about rents, and rent security, and rental growth. I wanted to know the relationship between income rents and yields, thus how capital values were determined. And I wanted to know what the rates of return were in different markets for different types of property. And it was an entrepreneurial effort. This information was lacking. The information had been provided for stock markets in the 1930s, for fixed interest markets in the 1950s, and I realized it was an urgent need to provide it in real estate markets as well.

René:

Rupert, what initial challenges did you face when you set-up IPD?

Rupert:

The first problem was that MSCI doesn't have a data collection problem. It merely goes onto a stock exchange and buys data from it. In our case, we had to create the data set ourselves. And I guess, the perception we had at the beginning was the place that the data set existed was in the records of the major investors. And my job in starting a service was to approach the major investors. You have to be very rich to work in the real estate market, so they weren't all that large number of them. But I had to approach these investors and persuade them to let me have access to their records. And with the promise of how it pulled the information, they would be anonymized and they would benefit from the public good of having better information about the market. So, that was one problem. The second problem was that real estate is extremely heterogeneous and you had to have very large samples of data in order to be able measure it. The stock exchange, few hundred companies dominate it and even the largest countries in real estate, you need to deal with some thousands of properties to get any chance of being able to represent an accurate picture of what's happening in each market. And the third problem was you need a great deal of information about each property. Each property, by definition is different, and if you wish to explain the differences, you've got to actually say what it is in terms of leases, and location, and building type, and tenant type, and a whole range of other things. So, we had to collect about a hundred pieces of information about each property from the records of existing investors, without computers and with no register which told you where the properties were. So, it was a really very, very big operation and we needed capital to do this, and then we needed to employ a team of researchers we trained to go out and collect the data. That was the data problem, but there were other problems as well. The first was that the market didn't have anything like a proper set of information, but that didn't mean it couldn't operate. It could operate in the format of a coffee house market like 18th Century stocks and shares were traded in. And the participants in the market were unused to using data, they were antipathetic to it. And they'd made use at all of models, so we had to show them that we could produce better data and information they held about the market in their heads. And they weren't easy people to persuade. That was the second problem, how to get the thing in use.

René:

Okay, so, Rupert, do you think, with IPD, you've achieved what you set out to do?

Rupert:

Yeah, we did achieve a lot. We allowed much wider markets to operate, statistics allowed better understanding of markets. We were a big support in the globalization of real estate, although, of course, the globalization is much more talked about than actual, but the extent that it was globalized, I guess it was greatly helped by the fact that IPD was able to produce statistics for a whole range of merkets. On the whole, we approached the market authorities in different countries. We showed them what we had done, or they had been to see us. And we formed partnerships and it road its way forward, and by 2010, I think we were operating in 33 countries, which was about the limit of what we had the capability of doing, because there are certain circumstances where it becomes extremely difficult. You [inaudible].

René:

Thank you very much, Rupert, and thank you for helping us celebrate 40 years of indexes, obviously initiated by you, yourself, by setting up the Investment Property Databank in 1985. The first index that we count went all the way back to 1980, that's the UK index. So, it's been a real pleasure to have you with us as we celebrate this significant milestone. Thank you very much.

Rupert:

Terrific. Thank you to you, too.

René:

I have, with me, Ian Cullen, Co-Founder and happily retired now of Investment Property Databank. Ian, thank you so much for joining us. Can you talk us a little bit about how you started in the real estate industry and what that industry looked like when you started?

Ian:

So, I started in 1969 when I finished my master's degree at University College and got a research job in urban planning and urban studies, University College. And that morphed in the mid-'80s to helping Rupert form IPD. And that lasted through the transition to MSCI ownership in 2012, I stayed on until, as I just said, 2019. And I decided 50 years was probably enough. But 50 years ago, as you can imagine, the real estate sector was an incredibly different place. It was something like a West End coffee house market. It spoke a private language. It was absolutely and totally opaque in the UK, with the motto essentially being, "Trust me with your money. I can't explain anything about performance, but we'll look after you." And it took us 20 years to notice that. But that was the situation, if you like, at the outset.

René:

Thank you, Ian. Can you maybe talk a little bit about the creation of index and portfolio analysis services, and how they began to be used by the industry?

Ian:

The initial trigger of this exercise was certainly a piece of happenstance. A bright Australian over for a gap year working for [inaudible] firm in the West End [inaudible] thought it might be a good idea if their specialism, which was making a lot of money out of buying and selling farms to various organizations and individuals, if they could stamp their leadership in that market with an index in their name, an index at farm prices, and they approached Rupert. And Rupert approached me, and we talked about this, and we built a farm-price index for [inaudible], and that predated [inaudible] IPD. But it contained the kernel of the idea which became IPD, because we set that not very cleverly and thought, "Well, if something like that can be done for that fraction of an institutional portfolio," which, at that time, was probably way less than 5%, in other words that percentage of their real estate which was agriculture, "then why not apply that same model to the remaining 95%?" The miles and miles of shops and offices and industrial sheds, which were held as investments within their real estate sectors as well. So, IPD was formed to do just that.

René:

Thank you, Ian. So, what was the reaction from the industry and especially the more transitional investors to indexes and benchmarking appearing on the scene?

Ian:

Everyone is pushed into new directions in one way or another, and it would be naive of me and basically wrong to say that they all grasped this with open arms from day one. And the big push didn't come from us, clearly. A bunch of losers in Kentish Town weren't even proper real estate people at all were never going to move mountains. But what did move mountains was deregulation of stock markets in the early '80s. Because at that point, this coffee house was sort of given an ultimatum. Institutional investors, pension funds, insurance companies, traditional estates even, could look elsewhere than UK real estate to diverse [inaudible] portfolios. They could buy Far Eastern Equities, they could buy German bonds, anything and everything to mix into their portfolios. And private language, and a "I'll look after your money. Don't ask me for any information" was not going to be sufficient thereafter. So, in fact, I think I, personally, was surprised by the pace with which they did jump onto this bandwagon. And new research activities were formed left, right, and center, research teams were set-up in the institutions. They espoused indexes and measurement very quickly. Nah, that doesn't mean to say there was no adverse pressure. And I guess you probably find in the sentiment of your clients today, just as I did for years and years and years, that the fullback position was then, possibly, and still today, that actually stock picking is all that it's really about. And that is not a denial of the importance of data. You can use data to help stock picking. But the idea of strategy formation and measuring strategy and assessing the impact of strategy on bottomline performance is at least shining a light at an alternative to stock picking as a means of delivering performance. And it was not right at the beginning of my career that I went down, I think it was in Southampton that this pension fund was based and their real estate management was inhouse. And they'd done very well and I thought that this [inaudible[, but I made the mistake of asking the question of why so much of the asset base was within, I don't know, 50, 70 miles of Southampton. This was a pension fund, you could invest in stocks anywhere. And the boss just said, "I won't buy anything. I can't visit and come back in a day because I've got to see it, I've got to [inaudible] myself, and I don't like staying in hotels. End of story." Now that's hardly a flag waving for the importance of data, but it's real, and now your research teams will probably still demonstrate that in the attribution of performance, stock selection is generally more important than asset allocation. Being able to identify the individual property is probably still a wee bit more important than your spread across markets and sectors.

René:

Thank you very much, Ian, and thank you very much for being with us today to help celebrate our 40 years of indexes. Thank you.

Ian:

And all the very best to you for the next 40 years.

René:

Thank you.

Ian:

Or more, many more.

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