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# Information Explosion and Commercial Markets

By Wayne E. Etter

**T**echnology makes information about the commercial real estate market increasingly available. Because information is fundamental to this market, what will be the impact of the information explosion? Consider information's role in the economic concept of efficient markets.

In an efficient market, all relevant information is known and understood by market participants. Accordingly, in such a market it is impossible to earn an abnormally large profit or experience an unusually large loss because assets' market prices incorporate completely all relevant public information.

The opposite condition characterizes an inefficient market, however. Market participants are not equally well informed and, therefore, some market participants make decisions with incomplete information. As a result, exceptionally large profits and losses may result.

Why would all relevant information be known by the participants in some markets and not in others? The answer is that participants can obtain information easily and at low or no cost in some markets while information in other markets is difficult and expensive to acquire. These differences are illustrated by comparing the U.S. Treasury securities market with the commercial real estate market.

## U.S. Treasury Securities Market

All U.S. Treasury bonds of a particular issue have the same interest rate and date of maturity. Furthermore, except for the interest rate and the maturity, all U.S. Treasury bonds issues are similar in their terms, conditions and credit risk. Although Treasury bills differ from bonds, all Treasury bills are homogenous except for the maturity date. While buyers may prefer a certain issue of Treasury bonds or bills for portfolio reasons, they do not need to consider each issue's credit quality or otherwise analyze terms and conditions.

The U.S. Treasury securities market responds principally to broad economic forces that affect the United States and global economies. The market is dominated by large securities firms that maintain research staffs to analyze the market. They regularly announce prices and yields at which they are willing to buy and sell securities. To compete for the business of institutional and individual investors, many firms publish market analyses. In addition, many investment advisory services sell their analyses to libraries, institutional investors and individuals.

Because the necessary economic data are readily available and numerous investors own U.S. Treasury securities, the total cost of collecting and analyzing information about this market, even though it is a large amount, is spread over many investors. Thus, this information is generally available at little or no cost. Market participants can obtain a great deal of information with a small out-of-pocket cost.

Because most of the information sources generally agree with the other sources, an investor need consult only a reasonable sample of the available information. If there should be a difference among these views, say, in the expected direction of U.S. Treasury security prices, those investors who believe that prices are going to decline will sell securities while those who believe that prices are going to rise will buy. The actions of the buyers and the sellers will eventually cause the difference between the two views to disappear as either sellers will have nothing left to sell or buyers will run out of funds.

## Commercial Real Estate Market

In contrast, each parcel of commercial real estate is unique. Even two identical commercial buildings are of necessity on different sites and, therefore, not the same. An owner of one of the two identical buildings should carefully investigate and evaluate the second building before buying it.

The two buildings could be in the same state but still be subject to different governmental regulations and taxing jurisdictions because they are located in different cities. These two buildings could be in the same city but be in different market areas, so the supply and demand for space would not be the same for each building. And, even if they are within the same market area, factors such as the differences in each property's ingress and egress or in the surrounding traffic pattern could make a difference.

The list of possible differences between the two properties could include items such as the existence of easements on one of the properties and the differences in surrounding land uses. For a potential investor to evaluate all these points means that substantial, costly information about each particular property must be collected.

Furthermore, the local market's basic supply and demand conditions must be analyzed for each property. As a result, supply and demand information has to be collected and analyzed separately.

The cost of data collection for a specific property is high, and much of the collected data cannot be used to analyze other

properties in the market area because of property characteristic differences such as being another type of land, too distant to be comparable or some other peculiarity that distinguishes the subject property from others. Therefore, much of the data collection cost cannot be spread over other properties to reduce the per-property cost.

Often, a specific commercial property in the market has a limited number of interested buyers. In the commercial property market, data collection and analysis cost is paid by those investors with an interest in purchasing the property. This information is not shared with other investors.

### A Role for Market Research

**W**ith the growing supply of publicly available commercial real estate information, will this market come to resemble the U.S. Treasury securities market? This seems unlikely because the cost of collecting the necessary data to make a commercial property investment decision is high, and no benefit accrues to the collector if the data are given to the public. Because so few investors are interested in a specific property, investors-at-large without an interest in that property would not pay for the data. Thus, the only reason for collecting the necessary data is to support a specific transaction. A firm might possess the information

and use it to an advantage, but the information's cost will be borne by the specific parties to the transaction.

Certainly, basic information about rental rates, occupancy and the supply of unleased space for a particular type of property obtained from a public source could contribute to any investor's knowledge about a local property market, but the uniqueness of each property should limit the role of these data in the investor's decision. The free data are useful and interesting for some purposes, but they cannot be the basis for a thorough investment analysis because all commercial properties are not alike; they require individual analysis.

This suggests a continuing role for the real estate market research firms, real estate consultants, real estate appraisers and commercial real estate brokers in the commercial real estate transaction. Investors considering the purchase of a commercial property will continue to need estimates of the supply and demand for particular types of properties within particular market areas, property-specific financial feasibility studies, property value estimates and the expertise of knowledgeable real estate brokers to carry out the transaction. □

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