



The Value-Add of Competitive Sets

Why informed market strategy must integrate quantitative and qualitative analysis

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Defining our terms: the benefits of competitive sets for market differentiation

"Investors are driven by asset value. Innovative asset differentiation is most accretive to that value. The mission of the building owner has changed (to become) a true partnership with the tenant to enable individual and collective performance."

– Charles Musgrave, Ivanhoe Cambridge

Charles Musgrave, senior director of leasing investments for Ivanhoe Cambridge in Toronto, admits that this observation isn't news to real estate investors and advisers. Yet achieving that differentiation unquestionably is a matter of innovation. Setting an asset apart from its peers is driven by constant awareness of what else is taking place in your market and then surpassing it. Whether the issue is investment sales, leasing or asset management, market intelligence in this age of fierce competition is key, and the player with the quickest, most accurate intel wins the day.

And therein lies the value of competitive sets. As NAIOP defines them, competitive sets are "a subset of total inventory that enables one to isolate and compare buildings on the basis of similar characteristics rather than simply by location."

To drill down further, competitive sets are aggregations of data that compare assets primed for either sale or lease to their local market peers. The difference between competitive sets and traditional market comps is the depth, breadth, immediacy and accuracy of the data. Indeed, the content of those traditional comps, such as pricing, occupancy or rental rates, is embedded in properly curated competitive sets.

But sales and lease comps are only part of a competitive set and are just one factor in the ability to analyze a property in the local market and make critical adjustments to its position. Equally important, changes in that data also set the stage for more in-depth and meaningful conversations – for example, between potential buyers and their advisers, or between occupiers in search of new spaces and their representatives.

Competitive sets, then, should be used as the baseline for a deep market analysis that can cover a wide array of considerations, including:

- Local market construction pipeline
- Other listings and competitive positioning
- Property amenities
- Walkability
- Access to public transit and highways
- Building health and safety standards
- Sustainability and green features
- Convenience of access and parking for tenants and visitors

Regardless of their depth and breadth, however, data are a commodity – "table stakes," in the words of Spencer Levy, global chief client officer and senior economic advisor at CBRE. Only in the conversations that arise through analysis does data make the leap from commodity to value-add service. As Levy points out, informed human judgment will bring to light the "megatrends in our business that can never be boiled down to data points in an actionable way."

"The problem with ESG is that the data simply doesn't exist to say this is actionable. What makes it actionable is the human judgment side of it."

– Spencer Levy, CBRE



COMPETITIVE SETS IN ACTION

The technology behind competitive sets allows the data to be massaged for the individual user, and in real time. Daniel Levison, CEO of Atlanta-based CRE Holdings, is currently underwriting the purchase of a small (15,000-square-foot), Class B building in a local submarket. On his dashboard, which uses Yardi's CommercialEdge, he can filter the competitive set to profile Class B competitors of the same size within a specified radius. Levison can also broaden that radius for a more comprehensive picture.

"This in-depth approach gives us some additional leverage with the seller."

– Daniel Levison, CRE Holdings

"We aren't competing with all of the buildings in my submarket," he says. "Based on our knowledge of this submarket (the qualitative side of the analysis) plus physically driving my trade market, we can see exactly who we feel are our direct competitors."

With this approach, CRE Holdings can narrow its focus to about 10 direct competitors among all Class B assets in the area. The in-depth analysis offers some additional leverage; it demonstrates to the seller that the \$2.2 million asking price does not take into consideration the cost of upgrades that the next owner will take on.

Moreover, the pricing would require rents of \$24 to \$25 per square foot, while more modern Class B buildings are leasing for \$23 to \$23.50, he notes.

That flexibility in the search parameters carries over to the needs of different disciplines as well. A sampling of other uses includes third-party managers, which can create competitive sets to demonstrate their knowledge when pitching services to owners and lenders, and owners or asset managers planning to file a CapEx proposal with their lending institution.



DRIVERS OF NEED

How competitive sets enhance industry partnerships

The innovation that Musgrave referred to implies a shift in the dynamics of the marketplace, one that demands a clearer understanding on the part of owners, investors and managers of the needs of potential buyers, sellers and tenants. That was a key takeaway from [“Your Building’s Competitive Set,” a webinar hosted by Yardi and Bisnow](#) in July 2021. Turner Levison, a Yardi senior account manager and the session’s moderator, cited Deloitte US real estate leader Jim Berry on the subject:

“CRE owners and operators should shift their mindsets to align with how tenants place strategic bets on their CRE investments,” said Berry. “To do this, leaders should use technology and data at every step of decision-making and execution. They would also need to frequently collaborate, communicate and coordinate with tenants to be in lockstep.”

But why is the call for a change of owner and operator mindsets necessary? And why now?

Because market conditions demand it. Allison Marsales, managing director of office leasing for Cushman & Wakefield in Toronto, notes a shift “in the leadership we interact with.” That decision-making capability has passed from the CEO to the COO and folks on “the operational side, as well as human resources, for the people aspect.”

As a result, “the mission of the building owner has changed,” states Musgrave. A role that was once limited to the owner has evolved to become “a true partnership with the tenant to enable the individual and collective performance of the owner’s tenant partners.”

Driven by these changes, conversations are now taking place that never would have just a few years ago. Not surprisingly, many of those new conversations revolve around health and wellness protocols. Where fitness centers or food service once topped the list of sought-after building amenities, the focus is now on social distancing and lessons learned during the pandemic.

Health and wellness are closely linked to sustainability and have accelerated as priorities since early 2020. Once assumed to be strictly the province of the tenant or the employee, wellness has become a major focal point for investors, particularly larger institutions, which prominently feature environmental, social and governance (ESG) protocols in their mission statements.

Further, sustainable performance has extended its reach into all asset types; it’s not just for office anymore. As Levy noted during the webinar, “The rules are changing.”

Although it was once enough to “slap an ENERGY STAR® sticker on your door,” he stated, green performance today must be measured and documented. Ironically, as ubiquitous as the conversation about health protocols and green initiatives has become, the

sustainability movement has not advanced sufficiently in either consistency or use to be documented in a competitive set.

“The problem with ESG is that the data simply doesn’t exist to say this is actionable,” Levy says. “What makes it actionable is the human judgment side of it.” By way of example, he notes that 70% of buildings in Chicago are LEED-certified; that dilutes the value of certification as a point of comparison. “So how do you compare, unless it’s through a qualitative analysis?”

But ESG’s time as a measurable—and therefore actionable—item will come, he predicts: “This is a major topic that will have a significant impact on our industry. In the meantime, it is one of the qualitative conversations that will be triggered by changes in the competitive sets movement. Too much is at stake, Levy says, for sustainability discussions not to continue their advancement, not only from the health perspective but also from the perspective of investments and returns.

Levy offers two examples. One offshore investor he works with owns a 10 million-square-foot portfolio and calculated that compliance would cost \$2.5 million. The other, with a much larger portfolio, said that if he didn’t comply, he would risk much greater damage when investors forced him to perform a detailed environmental analysis, take a lower price or both.

There is also the consideration of how rapidly evolving work patterns have changed the conversation about asset value. Much has been written about the new give-and-take between the safety and convenience of remote work on one hand, and on the other, the long-anticipated return to the workplace, where culture and collaboration can fully thrive. For owners, managers and corporate tenants alike, the shared challenge is to transform the office into a lifestyle brand supporting the needs and preferences of its population.



DATA MEETS EXPERIENCE

Data meets qualitative market experience

A greener strategy and a larger commitment to a corporate tenant's lifestyle focus are both drivers of change as a buyer or renter chooses one building option instead of another. New construction in the pre-leasing stage can have the same effect. The real-time data delivered in competitive sets will provide proof of market changes. That quantitative part should spark further discussion on the qualitative reasons for the change—the “what” that drives the “why.”

“The data element is the bedrock of a competitive set,” observes Turner Levison. “The qualitative component necessitates a boots-on-the-ground understanding of your market, tenant preferences and the softer things that are harder to refine into rows and columns on a dashboard.”

Those changes work as alerts, he says, to initiate a conversation with your sales or leasing broker. Changes in the data could mean the user has to revisit rental rates or take a closer look at what prospective buyers in that submarket are looking for. It could indicate the need to revamp marketing strategies.

To a large degree, the quantitative aspect of competitive sets is limited by the rules of the Appraisal Institute, which carefully guards the wall between market knowledge and confidentiality. Appraisers are “the foundation on which our business is built,” says Levy. “But if you can’t move beyond the limitations of what an appraisal requires, you’ll limit your ability to see value where others do not. Qualitative analysis, then, becomes central to overcoming those restrictions.



TECHNOLOGY ENHANCES DISCUSSIONS

Technology enhances qualitative discussions

"A building that's structurally identical to the next is still different," says Levy, "or you might have two neighborhoods that look identical, but one is a ghost town and the other is the red-hot Arts District in Los Angeles. What are the points of differentiation there? You have to be able to understand what and why."

Part of the value-add of competitive sets is the support that will prompt those qualitative discussions and analyses of differentiation. Turner Levison notes that Executive Updates from CommercialEdge track the changes in data and can flag the items on the dashboard that are actionable. "The alerts tell you that something is changing in the trendline that you need to think about and discuss," he says.

As that information supports those qualitative discussions, so the intel is in turn supported "by 500-plus CommercialEdge researchers watching over

virtually every market in the country, 24/7 and 365 days a year," he says.

The curation process behind those dashboards is a heavy lift, says Daniel Levison, understandably so since the accuracy and timeliness of the data are "obviously critical." He recounts the example of a building he was analyzing in Charlotte, N.C., which was for him an unfamiliar market. Levison worked with a local broker to provide intimate market knowledge and used competitive sets for the "table stakes" data. It was a one-two punch, he says, that saved him from days of driving around unfamiliar city streets.

The time element he refers to is critical in a transactional environment that demands speed to market. The ability to sift the relevant data to have meaningful, actionable analysis is what competitive sets are all about.

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