



IFC-National Bank of Belgium Workshop on "*Data needs and Statistics compilation for macroprudential analysis*"

Brussels, Belgium, 18-19 May 2017

What is 'commercial property'?¹

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¹ This paper was prepared for the meeting. The views expressed are those of the author and do not necessarily reflect the views of the BIS, the IFC or the central banks and other institutions represented at the meeting.

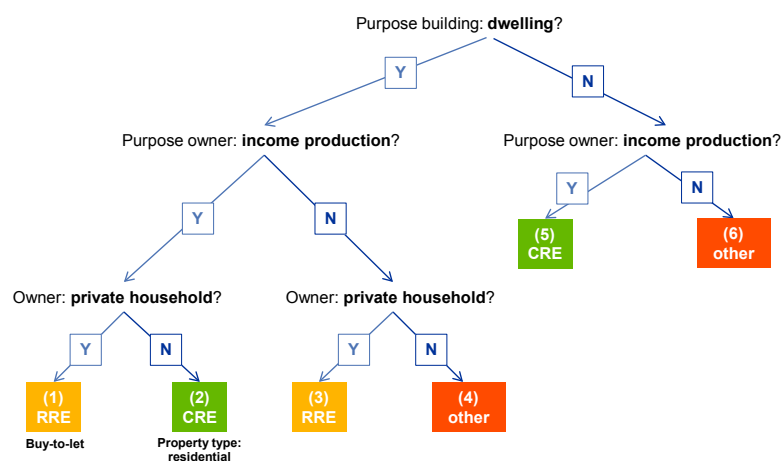
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Definitions of commercial real estate

Before considering commercial property price indicators, it is necessary to define 'what is commercial property?' Property represents one of the most significant, non-financial assets owned by households, firms, and governments. However, the use of property and its economic role changes depending on the entity that owns and uses it. In the European context, Dierick and Point (2017) discuss the delineation of residential and commercial property for the application of the European Systemic Risk Board (ESRB) recommendation on data gaps in the real estate field.¹ They highlight that these definitions are to be seen for the specific purpose of financial stability monitoring and macroprudential policy-making. It is duly and therefore rightly noted by them that the definitions in the recommendation do not coincide with the ones used in the Capital Requirements Regulation (CRR) and analytical credit database (AnaCredit) Regulation.

Figure 2 of Dierick and Point (2017), in particular, provides an overview of the categorisation in the form of a decision tree. First differentiating between residential properties (dwellings) and non-residential properties, the second level is whether or not the owner's purpose is 'income production', followed by a third level, in the case of dwellings, whether or not the owner is a private household. This figure is reproduced here as is.



(4) and (6) are outside the scope of the Recommendation because they are less relevant for financial stability and macroprudential policy
(4) includes, for example, certain forms of social housing
(6) includes, for example, certain public infrastructure (bridges and roads without toll), religious buildings, corporate headquarters

¹ Dierick, F., and Point, E. (2017), 'Closing real estate data gaps for financial stability monitoring and macroprudential policy in the EU,' *IFC Bulletin*, 46; ESRB (2016), 'Recommendation of the European Systemic Risk Board of 31 October 2016 on closing real estate data gaps (ESRB/2016/14),' *OJ*, C 31.

The internationally agreed definition of commercial real estate and the relation of the ESRB definition to it

Only very recently has an international definition of what constitutes commercial property in the first place been agreed – a harmonised breakdown (including selection criteria) according to property types like office or retail is still lacking. Eurostat prepared a complete system in the form of building blocks for different definitions according to the varying uses in macroeconomic and macroprudential policies. This work has been approved by the Inter-Secretariat Working Group on Price Statistics (IWGPS)² and will be elucidated in early 2018 as part of a ‘statistical book’ publication (in the context of the G20 Data Gaps Initiative) on commercial property price indicators. The building blocks are presented in the following table.

Activities	Assets		Residential properties (buildings together with the land on which they are situated)	Non-residential properties (buildings together with the land on which they are situated)
	Selling and renting of real estate	Rental housing Residential properties rented at market rents	<i>of which</i> Owned by household	Investment properties Non-residential properties sold at market values or rented at market rents
Construction of buildings	Residential buildings under construction on own account for sale, or on a fee or contract basis	<i>of which</i> For use by owner-occupiers	Non-residential buildings under construction on own account for sale, or on a fee or contract basis	
Own use	Owner-occupied housing Residential properties used as residences (dwellings)		Corporate properties Non-residential properties used in the production of goods and services (other than real estate) sold at market prices	
Non-market	Social housing Residential properties rented below market rents		Other non-residential properties Non-residential properties used in the production of goods and services sold below market prices or provided for free	

Typically, rental housing and investment properties are considered as ‘commercial property’. The boxes shaded in grey are those building blocks which could form the broadest possible definition of commercial property, i.e. also including buildings under construction and corporate properties that are used in the production of (other) goods and services but moreover ‘buy-to-let housing’, i.e. if a private household acts as a landlord. On the other hand, even rental housing might be excluded from a user (rather than owner) point of view, leaving investment properties, only, in the narrowest definition of commercial property.

² Members of the IWGPS are UNECE, ILO, IMF, OECD, Eurostat and World Bank (current chair).

How does the definition in the ESRB recommendation relate to this new international standard? First of all, the express aim of the building blocks is two-fold:

1. Every property goes into one and only one building block, i.e. every property appears exactly once somewhere (technically speaking, it is a partition).
2. Since it is appropriate to use different measurement approaches depending on the specific analytical objective, the building blocks can be flexibly grouped.

Then, by looking at the decision tree is it evident that number³ (2) is 'rental housing', while number (5) is 'investment properties'. Together with 'non-residential buildings under construction' – which are left out of the decision tree – these form commercial property for the sake of the ESRB recommendation. How 'residential buildings under construction' which are not for use by owner-occupiers, i.e. future rental or buy-to-let housing, shall be treated for the purpose of the ESRB recommendation remains unclear, though.

Number (1) refers to rental housing that is owned by households ('buy-to-let'). 'Owner-occupied housing' is equivalent to number (3). There is a vague relation of number (4) to 'social housing' and of number (6) to 'corporate properties' as well as 'other non-residential properties', which is not further elaborated (presumably for the reason that these three classes are not considered as commercial property).

It is undoubted that a decision tree helps a lot in the grouping of properties in one or the other class. The value might still be increased, though, if the new international standard would be incorporated and, thus, help in harmonising the approaches to measurement of commercial property price and associated indicators.

Conclusions and final remarks

The purpose of this note has been to discuss the definition of commercial property and set the ESRB recommendation in perspective to global efforts in this field. As such, this note necessarily fails short of providing the full background to the new international standard and this has to be left to the 'statistical book' publication on commercial property price indicators in early 2018 by Eurostat.

The evaluation here should also have been non-judgemental. Whether or not the definition applied by the ESRB recommendation is best for financial stability was out of the scope of this discussion. To reiterate this point, the buildings blocks are thought to be flexible enough to accommodate different definitions according to the varying uses of indicators in macroeconomic and macroprudential policies.

³ In what follows the numbers relate to Figure 2 of Dierick and Point (2017), i.e. according to the ESRB definition.