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DETERMINANTS OF CAPITALISATION RATES FOR SYDNEY CBD OFFICE BUILDINGS

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INTRODUCTION

The capitalisation rate is a widely understood concept, used daily by valuers to convert income streams into expressions of capital value. As a multiplier, it's role in the valuation process is fundamental with only the slightest change having the potential to significantly affect the final assessment of capital value.

However, exactly which factors determine a capitalisation rate and where practising valuers source such rates are relatively unexplored issues.

In late 1992, a survey was conducted into the determinants and sources of capitalisation rates for prime, CBD office investment property. The results of this survey concerning the relative importance of determinants were detailed in Parker (1994D) and for sources of the capitalisation rate in Parker (1994A).

Year Ending	Dec 1991		Dec 1992		Dec 1993
Vacancy Rate	15.6%	⇑	22.2%	⇓	21.2%
Gross Rent PSM PA	$696		$592		$518
Incentive PSM PA	$265	⇑	$300	⇓	$291
Effective Rent PSM PA	$431	⇓	$292	⇓	$227
Capitalisation Rate	6.75%	⇑	7.50%	⇓	7.25%
Capital Value Index	$6,000	⇓	$4,150	⇓	$3,800
Reported Sales Over $3m:					
Number	16	⇒	17	⇑	34
Total Value	$261m	⇓	$149m	⇑	$461m

Prime Sydney CBD Offices - State Of The Market 1991-93
Source: Jones Lang Wootton

Table 1

The characteristics of the prime CBD office property market in Sydney between late 1991 and late 1992 differed from those between late 1992 and late 1993 as shown in Table 1. Rising incentives, vacancy and capitalisation rates, declining effective rentals, capital values and sales activity confirm the deterioration in the market between late 1991 and late 1992.

Conversely, falling incentives, vacancy and capitalisation rates with rising sales activity show an improvement in certain aspects of the market between late 1992 and late 1993, though effective rents and capital values continued to fall.

It is evident that, in an overall sense, the market deteriorated between 1991 and 1992 but improved between 1992 and 1993.

Given the changes in the market for prime CBD office investment property in Sydney between late 1992 and late 1993, this paper reviews the findings of a practitioner survey conducted in late 1993 relative to those of a similar survey in late 1992, considers whether the sources of the capitalisation rate and the relative importance of the determinants of the capitalisation rate have changed and comments upon the extent to which such changes may be explained by market conditions.

DETERMINANTS OF THE CAPITALISATION RATE

To ascertain those factors which valuation theory suggests are determinants of the capitalisation rate, a comprehensive literature review was undertaken. Notably, this failed to locate an existing, comprehensive list of the determinants of the capitalisation rate in the work of another author. The principal property teaching texts from the UK, USA and Australia were analysed together with a large number of articles from relevant local and international property journals. Summaries of that literature reviewed are contained in Parker (1992A) and Parker (1992B).

It was found that many authors identified the same factors as being amongst the determinants of the capitalisation rate with some authors identifying certain factors not considered by others. Furthermore, the same concept may be identified by several authors but attributed with a different name such that the following paper groups concepts rather than nomenclatures. The authors personal experience, as a property investment operative, was adopted as the arbiter for categorisation of the information found within the literature.

Twelve determinants of the capitalisation rate were identified from the literature, but limitation of space precludes a detailed description of each (for a general discussion of each determinant, see Parker (1992A)). In alphabetical order, rather than any preconceived order of importance, the determinants of the capitalisation rate are summarised in Table 2 with italics denoting the description adopted within the survey questionnaire referred to below.

Of the determinants listed in Table 2, Growth and Risk were found to have the widest range of definitions and commentaries within the literature reviewed. Distiling a succinct definition of each for the questionnaire, which conveyed the most common concepts found within the literature, was particularly challenging. Whilst many practitioners casually justify a change in the capitalisation rate adopted due to the subject being "riskier"or having different "growth prospects", little attention appears to be paid to the underlying reasons for such differences. This is an area which would be worthy of further research as it is possible that practitioners are individually contemplating quite different matters when considering growth and risk in isolation which could lead to inconsistency in both the analysis and valuation processes.

Given the greater buoyancy in the state of the prime CBD office market in Sydney between late 1992 and late 1993, it will be interesting to see if the order of relative importance of the determinants of the capitalisation rate changes accordingly.

SOURCES OF THE CAPITALISATION RATE

Rost and Collins (1990) typify the narrow approach to sourcing the capitalisation rate advocated by the standard teaching texts:

> "The capitalisation rate or Years' Purchase should, wherever possible, be derived from market transactions."

or

> " ... as disclosed by the investigation and analysis of market transactions in respect of comparable properties."

This is particularly problematical in a market characterised by relatively little, if any, comparable sales evidence - as, for example, existed in Sydney between early 1990 and late 1992. In the event of no comparable sales, where is a valuer to look for evidence of prevailing capitalisation rates? The standard teaching texts are notably silent as to the sources of capitalisation rates in a depressed property market.

Alternative Investments - *Equities, bonds, other property investment alternatives, etc* - as competitors for investment funds, relative risk return profiles, etc

Building Itself - *Services, features, reputation, etc* - at its simplest, newer buildings are generally worth more than older buildings which encompasses such issues as depreciation and obsolescence, adequacy and styles of finishes, layout, foyer, etc

Economic Situation - *International, federal, state, city levels* - macro and micro factors, economic stability, prosperity of a country, inflationary and recessionary trends, credit conditions, etc

Growth Prospects - *Potential for income growth and/or capital appreciation* - may be absolute or relative to other types of property or asset classes, etc

Legal Issues - *Freehold/leasehold, restrictive covenants, etc* - traditional title related issues and landlord and tenant as well as contemporary, socio-political issues such as health and safety, environmental concerns, site contamination, etc

Location - *Situation, position, etc* - within the CBD area, street address, adjacent properties and users, views, aspect, evolution over time, etc

Planning - *Zoning, plot ratio, use limitations, etc* - though probably relatively static for CBD offices compared to other classes of property (such as retail or industrial), this may be significant for properties with redevelopment potential

Risk - *The possibility of events not occurring as anticipated* - it is generally agreed that property is a riskier form of investment than a government bond and should be priced accordingly, though definitions and approaches to risk within the texts vary enormously

Sentiment - *Towards property as an asset class* - generally plus sentiment of investors towards particular types of property specifically, general investment market sentiment, etc as well as the role of expectations of the future

Special Characteristics Of Property As An Asset Class - *Long term nature, illiquid, etc* - fifteen factors including hetorogeneity, indivisibility, inelasticity of supply, high costs of transfer, management, perpetuity, imperfect knowledge, decentralised market, government intervention, ability to create special interests, scarcity, etc

State Of The Property Market - *Supply and demand for investors and occupiers* - for the CBD office property subsector specifically, the office sector and for the property asset class generally given prevailing economic, political and social conditions

Tenants - *Security and regularity of income, etc* - not only the covenant of the tenant but also the structure and nature of the lease document (rent review, alienation, user, guarantee provisions, etc) from the viewpoint of both valuation and investment integrity

Determinants Of The Capitalisation Rate

Table 2

Based on practical experience as an institutional property investment operative, the author proposed eight different sources of the capitalisation rate in a recent article (Parker (1994A)), namely:

a. Directly comparable sales;
b. Changes in the market since the last directly comparable sale;
c. Recent sales of other types of office property;
d. Recent sales of all types of office property;
e. Discussions with investors;
f. Discussions with agents;
g. Practitioners own feelings of market levels;
h. Relative position of and movements in other asset classes (eg: equities, bonds, etc).

Whilst each of the above may be recognisable as a potential source of the capitalisation rate, empirical research is required to determine the relative level of importance of each. Based on the traditional textbook approaches, it may be anticipated that directly comparable sales would be considered the most important source but the ranking of the other sources cannot be similarly determined. In the absence of directly comparable sales, the textbook approach is flawed - so where does a valuer then look for sources of the capitalisation rate? Furthermore, as a market moves from a state of limited sales evidence to a state of greater levels of sales evidence, do the preferred sources of the capitalisation rate change? - and, if so, in what way?

SURVEY ASSUMPTIONS

To determine the relative importance of the identified determinants of the capitalisation rate and the sources of evidence currently being used for the valuation of CBD office property in Sydney, a questionnaire was devised for completion by a panel of practising valuers. It was decided to approach valuers rather than investors for survey purposes for a variety of reasons including the following:

- there are relatively few major portfolio investors in the Australian property market and, of those, even fewer who specialise in commercial property;
- of those investors, their objectives and investment philosophies vary widely between groups which may be likely to impact upon their respective approaches to the valuation of commercial investment properties, which would serve to detract from a focus on the capitalisation rate;
- there are numerous valuers in Sydney who specialise in the valuation of CBD commercial investment property;
- valuers are experienced in valuing to a standard definition of open market value and, if a standard definition of open market value can be adopted, a closer focus on the determinants of the capitalisation rate, rather than any other extraneous issues, may be achieved from respondents.

To maintain the focus on the capitalisation rate within the questionnaire, respondents were asked to make a series of assumptions by basing their responses on a hypothetical building with the following characteristics:

- a prime, CBD office property, fully leased to several tenants (such that no discount for bulk or single tenant risk is required);
- let at rentals which do not require an adjustment to reflect market levels through the capitalisation rate and with no shortfall in the recovery of outgoings;
- let on long, standard institutional leases with conventional review patterns;
- no extraneous problems such as limited car parking, onerous outgoings, etc.

Theses assumptions were designed to remove the need to consider many of the problems facing valuers in practise within the current market and which may be addressed wholly or partly by adjustments to the capitalisation rate. By removing the need to consider such factors, it was hoped that valuers would focus more closely on the respective roles of the identified determinants.

PRACTITIONER SURVEY

In November, 1993 a questionnaire was forwarded to 33 respondents, each of whom had been previously confirmed to be practising valuers of CBD office property in Sydney. Of these, 22 were anonymously returned giving a response rate of 67% which is considered statistically satisfactory.

The respondents were asked to complete a series of qualifying questions, in order to establish their appropriateness to provide responses concerning capitalisation rates for CBD office valuations. The individual practising experience of the respondents ranged from 5 years to 25 years, with an average of 17 years, confirming that the respondents were all experienced valuers. All respondents were professional members of the AIVLE with 3 also being professional members of the RICS. Consistent with such experience and seniority within the industry, the sample contained numerous office holders within both the AIVLE and the RICS which further reinforced the professional standing of the sample.

The total sample had completed over 2,000 investment valuations in the previous year (averaging 91 such valuations per respondent) of which 412 or approximately 20% were of CBD office property, averaging 19 per respondent. The valuations undertaken by the respondents ranged in capital value from $200,000 to $600 million though the majority fell in the range of $5 million to $500 million.

The respondents are clearly, therefore, regularly involved in the valuation of a large number of high value CBD office properties. As such, they are ideally situated to answer, with authority, questions on matters concerning the capitalisation rate for such properties and their views should be indicative of those of many valuers of such properties in Sydney.

SURVEY RESULTS

Following return, data from the 22 anonymously completed questionnaires was collated and analysed. The results concerning sources of the capitalisation rate and the relative importance of the determinants of the capitalisation rate, respectively, are set out below.

Sources Of The Capitalisation Rate

The 1992 questionnaire listed the eight potential sources of the capitalisation rate, given above, which were repeated in the 1993 questionnaire with the addition of a ninth alternative, "Discussions With Other Valuers". This was added as it was suspected that, in a period of limited sales activity, practitioners may seek a second opinion either from colleagues internally or fellow valuers in other firms.

Respondents were asked to rank each source of the capitalisation rate, for prime office investments in the Sydney CBD in the current market, by annotating the survey form with 1, 2, 3, etc next to each determinant in descending order of importance. For each of the years, current meant November 1992 and 1993 respectively.

A full discussion of the 1992 rankings is contained in Parker (1994A) which also alludes to the discussion of the 1993 rankings and comparative analysis given below. The rankings provided by respondents in both the 1992 and 1993 surveys were attributed with the same simple 1, 2, 3, etc scoring method with the totals summed and the resulting ranking given in Table 3.

1992	1993
1 Directly comparable sales.	1 Directly comparable sales.
2 Recent sales of other types of office property.	2 Recent sales of other types of office property.
3 Recent sales of all types of office property.	3 Changes in the market since the last directly comparable sale.
4 Changes in the market since the last directly comparable sale.	4 Recent sales of all types of office property.
5 Discussions with investors.	5 Discussions with investors.
6 Relative position of and movements in other asset classes.	6 Respondents own feelings of market levels.
7 Respondents own feelings of market levels.	7 Relative position of and movements in other asset classes.
8 Discussions with agents.	8 Discussions with agents.
	9 Discussions with other valuers.

Sources Of The Capitalisation Rate
Prime CBD Office Property, Sydney

Table 3

In is interesting that the top two sources of the capitalisation rate, directly comparable sales and recent sales of other types of office property, are the same in both years. This is, of course, entirely consistent with the approach advocated by the textbooks considered above. In late 1992, the limited availability of office market sales meant that a first place ranking for directly comparable sales was a surprising finding. By definition, it may have been expected that recent sales of other types of office property or of all types of office property may have achieved primacy given the very limited availability of directly comparable sales. However, the increased level of sales activity in the ensuing year makes this order of sources a more logical choice in 1993. Of the relevant sales in the CBD office sector in Sydney in the year to late 1993, many are challenging to devalue by the capitalisation of income method, such that the primacy of directly comparable sales still remains a little surprising.

The reversal of third and fourth places is notable with changes in the market since the last sale overtaking recent sales of all types of office property in the order of importance in 1993. It may be that the respondents were viewing changes in the market in the context of the increased level of recent sales activity. In a period like 1992 when sales, per se, were few, the respondents may have been expected to consider any and every office sale in the whole Sydney CBD market. Perhaps the higher level of sales activity within the subsectors in 1993 allows the respondent to focus more closely on particular subsectors of the Sydney CBD office market, leading to a reduction in the need to consider data from beyond the prime subsector and a decline in the importance of all types of office sales as a source of the capitalisation rate.

Such an approach would be consistent with the increase in importance of changes in the market since the last comparable sale. As sales activity accelerates within certain subsectors of the Sydney CBD office market, value trends will become more apparent. The analysis of even limited sales evidence in a subsector will, therefore, show the respondent not only that the market is moving but also by how much and in what direction. Given the vital significance of such information in the valuation process, it is not surprising that changes in the market achieved a higher ranking in 1993 than 1992.

The continued dominance of the top four sources is worthy of note. The fundamental propensity to rely on comparable evidence advocated in valuation theory is clearly evident in valuation practise, surviving through periods of both limited and increased sales activity, with the relative order of importance moving slightly to reflect the transition from one period to another. By definition, the analysis of comparable sales should diminish in significance in periods of limited sales activity and rise in periods of greater sales activity but this is demonstrably not so.

It is quite remarkable that, even during periods when the reliance on comparable sales may be expected to be most under threat, it still continues to dominate the valuers approach to sourcing a capitalisation rate. The principle alternatives to reliance on comparable evidence continue to remain the bottom four (or five) sources of the capitalisation rate, despite their apparent greater relevance in periods of limited sales activity. The apparent reluctance to attach greater importance to alternative approaches was disappointing.

Of the four (or five in 1993) non-sales evidence based approaches to sourcing the capitalisation rate, discussions with investors continued to be the most important. It would seem eminently logical, in a market characterised by limited sales activity, to speak with those most likely to generate such activity about the levels at which they would be inclined to do so. It is, in some ways, surprising that this does not rank higher as a valuers opinion of the level of market value is of limited substance if there is no market activity at that level. In a market characterised by limited sales activity, seeking the views of investors (who, ultimately, are a significant component of the market) as to the speed and direction of movement in the market would seem a logical step in sourcing the capitalisation rate.

Discussion with agents ranked in 1992 as the least important source of evidence of the capitalisation rate. It may have been anticipated that the increased level of sales activity during 1993 may have led to agents being considered a relevant source of capitalisation rate information. Such a situation does not, however, appear to have transpired. It is interesting that, in 1993, the only group that a practitioner would consider less important as a source of capitalisation rate information than agents was fellow valuers.

Whilst discussion with valuers in other firms may give rise to a variety of problems (such as confidentiality, etc), it is difficult to believe that valuers would not discuss appropriate capitalisation rates with their valuer colleagues within the same firm. As noted in Table 2, imperfect knowledge is a special characteristic of the property market but the degree of imperfection has rarely been examined (see, for example, Brown (1991)). It may be, simply, that the question was ambiguous or, which is a much more complex and significant issue, that the flow of information between practising professionals is even more restrained than was previously thought. In either case, this is an area which would be worthy of further attention.

The changing position of the remaining two potential sources of capitalisation rate information proved to be quite surprising. In 1992, the relative movements in other asset classes was considered more important than the respondents own feelings of market levels. In 1993, these rankings were reversed which may be interestingly considered in the light of the increased volume of sales activity.

Perhaps the lack of sales evidence in 1992 lead valuers to have greater confidence in looking at movements in other capital markets than in their own feelings about the subsectors of the property market. This would be consistent with an increased level of activity in 1993, leading valuers to be more confident about their own views and less reliant on other capital markets for indicators as to direction.

Alternatively, the relativity with other capital markets might be an issue considered primarily by investors, which contributes to the investors views on capitalisation rates. Accordingly, in discussions with investors, the respondents may be implicitly assimilating the result of a consideration of capital markets activity such that direct attention to such factors is of less importance.

Conversely, the decrease in importance between 1992 and 1993 may simply mean that the relative position of and movements in other asset classes are no longer an important consideration in sourcing capitalisation rates. If this is the case, it is arguably a retrograde step as property is an integral part of the capital markets, regardless of the level of sales activity, with any movement away from such a position regrettable.

Given the nature of this type of research, it is not possible to arrive at definitive conclusions. Inferences and commentary can, however, be logically drawn from and made upon the findings as preliminary conclusions. It is only through further, more detailed research, working from such initial studies as these, that a greater understanding of how valuers source capitalisation rates will arise.

In summary, the findings over the two years begin to polarise the sources of the capitalisation rate into comparable sales related and non-comparable sales related groups. In both periods of limited and increasing sales activity, the respondents were most comfortable with sourcing capitalisation rates from the former, despite how limited the comparibility may be. In neither periods has the latter moved ahead of the former. The continued prominence of the former over the latter, despite the relative lack of comparable sales, is a simple but extremely significant finding for the future of the valuation profession in Australia.

Determinants Of The Capitalisation Rate

Each respondent was asked to attribute a simple point score to the respective determinants (as listed and with the same descriptions as given in Table 2) from 1 (least important) to 5 (most important), with the respective point scores collated and totalled to give the rankings detailed in Table 4. This approach was designed to overcome the common response that all determinants were important, with the acknowledgment that some may be marginally more important than others. The same survey approach was adopted in 1992 allowing the resulting rankings for the two years, as given in Table 4, to be capable of direct comparison. In both years, respondents were encouraged to add other determinants which they considered relevant in order to make the list more comprehensive.

1992		1993	
1	Tenant	1	Tenant
2	State of the property market	2	Growth
3	Growth	3	State of the property market
4	Risk	4	Location
5	Location	5	Building
6	Building	6	Economic situation
7	Legal	7	Risk
	Alternative investments	8	Legal
	Economic situation	9	Sentiment
	Sentiment	10	Characteristics of property as an asset class
11	Characteristics of property as an asset class	11	Alternative investments
12	Planning	12	Planning

Determinants Of The Capitalisation Rate
Comparative Rankings 1992-1993

Table 4

Over the course of the twelve months between surveys, there have been some fascinating changes to the order of importance of the determinants of the capitalisation rate. Notably, only the top and bottom determinants occupy the same ranking in each of the two years, with the intermediate determinants changing considerably.

Although respondents were provided with definitions of each determinant, it should be noted that their responses may reflect their individual assessment or interpretation of what the determinants may encompass rather than the definition proposed. This may be most prevalent for those determinants for which there may be some conceptual overlap (such as State Of The Property Market and Sentiment) or for which there is a range of equally valid definitions (such as Growth and Risk). Such a factor cannot easily be removed and whilst drawing respondents attention to the problem may reduce its impact, it is not possible to ensure that the resulting ranking purely reflects the order of importance of determinants solely and precisely as defined.

The three most important determinants are, interestingly, common to both 1992 and 1993 but in a slightly different order. The tenant, or the security and regularity of the income stream, continues to be the most important determinant which is consistent with press reports concerning the greater attention being paid by investors to the cash flow of a property (see, for example, the "Australian Financial Review", 29th March 1993 and 22nd April 1993).

As Table 1 shows, the market for prime CBD office property in Sydney weakened between late 1991 and late 1992. Accordingly, in a deteriorating market a consideration of the State Of The Market ahead of Growth is relatively logical. Though Growth ranked third in 1992, by 1993 it had surpassed the State Of The Property Market in importance which may suggest a subtle trend towards the positive by respondents. Such events as the significant rise in the level of sales activity, the Olympics announcement, the positive trend in economic indicators, decreasing prime vacancy rates and the upturn in the sentiment surveys may all have contributed to valuers now paying greater attention to the upside of the current market, contributing to a greater focus on the future than on the past - whereas in 1992 the prospects of Growth may have been submerged beneath concerns over the lingering negative aspects of the State Of The Property Market.

Such an argument would be consistent with the fall in importance of Risk. Although illogical and theoretically incorrect, risk tends to be associated with negative events and declines, rather than positive events and improvements. Therefore, an office investment with stronger growth prospects may be expected to have fewer disadvantageous aspects or lower risk. Accordingly, as Growth rises, Risk may be expected to fall in importance as a determinant and the drop from fourth in 1992 to seventh in 1993 is resultingly unsurprising.

Both Risk and Growth are challenging to define and intuition would suggest that they may have opposing characteristics. As referred to above, it may be that the definitions of Risk and Growth adopted in the questionnaire were inappropriate and, whilst reflecting the consensus of text book views on each, do not reflect that understanding of each which is common amongst practitioners. Further research in a discursive forum would be worthwhile to investigate these issues, as the roles of Risk and Growth in the selection of the capitalisation rate may be of fundamental importance.

The proposition of possible links between such determinants as the State Of The Market, Growth and Risk is intuitively appealing, with a movement in one having an impact on each of the others. Apart from suggesting such possible links, it is not feasible from this survey to ascertain any more about the nature of the relationship.

Contrary to the traditionally taught principle that the three most important factors in property valuation are "location, location and location", Location ranked fourth in importance in 1993, up from fifth in 1992. One argument for not ranking first could be that the CBD office area of Sydney is relatively small, such that Location is less significant than it might be in larger markets. The literature, however, would not support such a view. Accordingly, while Location is important and consistently ranks highly, it is not as important as certain other determinants.

Building continues to follow Location in importance as a determinant and remains within the top 50% in order of importance. Given that vacancy rates continued to be high in late 1993, providing tenants with a choice of properties to lease, the continued importance of such factors as the building fabric, services and finishes within the investment might be logically anticipated.

In 1992, the determinants ranking from seventh to eleventh all scored between 25 and 29 points, such that their ranking was determined solely on the basis of an individual point. This suggests that the respondents viewed these factors as of very similar levels of importance. In 1993, Economic Situation rose from this grouping to sixth place which may be attributable to the more positive economic news during 1993 attracting greater attention to this variable. With the fall of Risk to seventh place, these form the only changes in the seventh to eleventh ranking determinants in 1993, with such determinants scoring between 64 and 78 points which is a marginally wider range than in 1992. Interestingly, in 1993 the range for eighth to eleventh places was 69 to 78 which is considerably narrower than in 1992 indicating that respondents continued to find many of these mid-ranking determinants of near identical levels of importance.

Legal continues to be a mid-ranking determinant which is surprising as it may be considered something of a given, like Planning, which could therefore be expected to be of less importance. Sentiment may have been anticipated to have risen in importance and achieved a higher ranking in 1993, consistent with the positive economic and other news in the property market, but this did not transpire. The Characteristics Of Property As An Asset Class continues to be a low ranking determinant which, with Planning, may be argued to be taken as given information within the CBD office valuation process, though Planning could be expected to receive a cursory confirmatory check.

Within this mid-ranking group, the only determinant to have clearly fallen in importance is Alternative Investments. This is consistent with the comments above concerning the decrease in attention given to the performance of other capital markets when the property market is enjoying an increase in activity. It was suggested, above, that as activity returned to the property market, attention to the other capital markets diminished which is arguably also apparent in the ranking of determinants of the capitalisation rate.

Interestingly, none of the respondents in 1993 added further determinants of the capitalisation rate to the list. Overall, the range of scores in 1992 was 24 to 35 compared to a significantly wider range of 60 to 108 in 1993. This would appear to suggest that respondents found it easier to distinguish determinants in order of importance in the market of 1993 than in that of 1992. Perhaps the increased level of market activity has contributed to the greater ease with which respondents can distinguish between determinants.

The total point scores also indicate that, as the level of importance increases, so does the gap between scores. This may be attributable to a combination of the scoring system and the consistency of responses showing certain determinants to be always well ahead of others. This is significant for the lower scoring determinants where the combined effect is that respondents attribute almost identical levels of importance to the determinants with only very slight adjustments between the two surveys. It would appear that the top five (or possibly seven) determinants may be contributing the majority of the decision on capitalisation rate selection such that almost half of the determinants may be potentially disregarded with possibly little impact on the decision. Such a concept and proposition of proportionate importance is considered further in Parker (1994E).

The broad groupings of determinants in 1992 and 1993 also suggest that it may be possible to propose a hierarchy of determinants that is relatively consistent over time (as discussed in Parker (1994B)). Further research into the possibility of a nexus between proportionate importance and such a hierarchy could be potentially fascinating and contribute to a greater understanding of the capitalisation rate determination process.

In summary, not only the differences but also the similarities in the results of the relative importance rankings between 1992 and 1993 are significant. The similarities in the findings confirm that there are only twelve determinants of the capitalisation rate and, whilst each determinant has a differing degree of importance, consistency within a hierarchy of relative importance over time is discernible. The differences confirm that, whilst the determinants may vary in importance over time, when considered in relation to changes in the underlying property market, such variations may be explicable. The significance of such findings in the context of forecasting cannot be understated.

CONCLUSION

Given the paucity of research into factors driving capitalisation rates, the above findings on the relative importance of the determinants and sources of the capitalisation rate are particularly significant. It is found that there have been not only changes in the relative importance of determinants between late 1992 and late 1993, but also in the sources of the capitalisation rate with such changes capable of interpretation as reflecting movements in underlying property market conditions.

To find directly comparable sales as the primary source of capitalisation rates during periods of limited sales activity was surprising. It would seem that such a response is so deeply ingrained into the valuers subconscious that it continues to be reiterated, literally, without thinking. The significance of this for the continued adoption of traditional techniques despite limited applicability and the apparent unpreparedness by respondents to embrace anything other than traditional approaches, are issues which should increasingly concern both the individual practitioner and the profession as a whole.

Conducting the capitalisation rate survey annually is now beginning to provide some interesting findings concerning determinants, both at points in time and over time. The identification of twelve determinants of the capitalisation rate, to which no additional determinants have been added by practitioners, is significant as is the finding that their relative importance can be identified at a point in time and varies over time.

Overall, a similarity in the annual rankings is emerging with certain determinants consistently of high, low or mid-range importance. Within each band the order of relative importance changes between years but a hierarchical framework can be identified. It would, therefore, appear that the top ranking determinants are carefully and specifically considered whilst the mid-range determinants are more cursorily reviewed, apparently as a group. The repetitious proximity of scores for the mid-range determinants in each year reinforces the concept of practitioners mentally juggling a series of determinants of near identical importance within the capitalisation rate decision.

A disappointing finding, from both it's relative importance as a determinant and it's significance as a source of the capitalisation rate, was the low ranking of movements in other capital markets. Whilst valuers have been found to have an awareness of the prevailing direction of the economy and the capital markets, these are of a far lower level than their awareness of property market directions (Parker (1994C)). There has previously been argued to be "a disconcerting insularity among valuers regarding the role of property in the capital markets" (Parker (1992C)) which appears to have strengthened between 1992 and 1993. The property market may have idiosyncratic features, but it is still a fundamental component of the aggregate capital markets and economy. It can only be to the detriment of the valuation profession that this is so persistently disregarded.

Whilst professed integration with the property markets may provide practising valuers with a powerful defence against other professions who may claim to provide a similar service, this is arguably not enough. The trend over the last few years to unitise property for trading as a financial instrument has brought the property market and the other capital markets irreversibly closer together. To continue to view property in isolation is to refuse to adapt to changing conditions, which is a classic Darwinian symptom of a genus facing extinction. The choice, therefore, for the valuation profession should be clear.

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