

THE WALL STREET JOURNAL.

REAL ESTATE

Buy Commercial Property for the Income, Study Says

Commercial real estate is a good investment for income not, as most investors believe, rising property prices, according to a new study.



By Laura Kusisto

Commercial real estate is a good investment for income not, as most investors believe, rising property prices, according to a new study.

Over the course of a seven-year holding period, apartments and industrial, office and retail space all generated unlevered returns in the roughly 7% to 9% range, according to a new study by Mark Eppli, a professor of finance at Marquette University, and Charles Tu, a professor of commercial real estate at the University of San Diego. The study was commissioned by the National Multifamily Housing Council Research Foundation.

But most of those returns came from the income generated by the property, not capital

appreciation, which measures the value of the property over time but subtracts money spent on upgrades.

Some property types, such as office buildings, suffered capital depreciation over the seven-year holding period because office landlords spent significant amounts of money outfitting new tenants' spaces.

Apartment buildings delivered the best returns on capital, at 1.97%, and total returns of 9.05%, partly because landlords sometimes need do little more than slap on a fresh coat of paint. Industrial space offered the best returns on the income properties generate, at 7.96%.

“Investors underestimate the cost of capital improvements when they purchase buildings,” Mr. Eppli said.

Researchers, like Wall Street, often tend to focus on shorter return periods, but Mr. Eppli said it is important to consider longer periods, when most commercial real estate types fare better. Retail delivers the best return on investment for those looking to make a quick buck, but, beyond a one-year holding period, apartments are the best investment, the researchers found.

Write to Laura Kusisto at laura.kusisto@wsj.com