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The Financialization of the Property Sector: the Case of the Swiss Pension Trusts (1994-2005)

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PROPERTY SECTOR FINANCIALISATION: THE CASE OF SWISS PENSION FUNDS (1994-2005)

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Abstract: *This paper deals with the Swiss Pension funds investments in property. Between 1994 and 2002, about 15% of Swiss pension funds' wealth was invested in property. As far as their investment policy is concerned, pension funds have two choices. First, they can directly own, and have management responsibility for, the properties in their portfolios. Alternatively, they can buy shares in mainly Zurich-based investment vehicles. In the first case, pension funds behave as both investors and managers, and this requires staff with the relevant expertise along with knowledge of property markets. Investments have a regional focus and are assessed internally by the funds. In the second case, pension funds are merely investors and investment appraisals and comparisons are made on the basis of market criteria such as yield, diversification in relation to risk and liquidity. In this case, property investments focus solely on the country's main urban areas.*

Key words: pension funds, capital mobility/ liquidity, property, regions, Switzerland

* This research is part of a project on the impact of pension funds on the Swiss economy which is being funded by the Fonds National Suisse pour la Recherche Scientifique (FNSRS).

PROPERTY SECTOR FINANCIALISATION: THE CASE OF SWISS PENSION FUNDS (1994-2005)

INTRODUCTION

The actions of property market players are widely responsible for the way the built environment develops and evolves. Pension funds in Switzerland have grown hugely over the last twenty years and they are now one of the property sector's main financers and players. An appreciation of the way pension funds are organised, the channels through which their investments are made and the reasoning behind their decisions has become indispensable for understanding developments in the Swiss property sector. Historically, pension funds were spread right across Switzerland and a significant share of their funds were traditionally invested in accommodation for company workers. Their closeness to, and involvement with, both the company and its employees began to loosen after 1985 with the rapid growth that occurred in the wake of occupational pension schemes becoming more widespread (such schemes are the so-called "second pillar" of the Swiss pension system).[1] Since then, the task facing pension funds in terms of having to manage the huge funds at their disposal has become much more sizeable. For the *registered pension funds* only, these funds peaked at SFr445bn (of which SFr56bn was in property) before the burst of the stock market bubble in 2000, but they still amounted to SFr403bn (of which SFr60bn was in property) in 2002.

Furthermore, pension funds have become integral players in certain economies (the United States, Canada, United Kingdom, Japan, the Netherlands and Switzerland) and their regional impact is significant (Martin and Minns, 1995; Clark, 2000 and 2003). The increase in funds has been accompanied by another phenomenon, the financialisation of activities which is tied in with the growth of institutional investors. This has impacted on the entire way in which the economy and society have developed. Briefly, financialisation means the continuous assessment of economic activities by financial markets (Orléan, 1999); an assessment process which involves supervisory bodies (for example those regulating financial markets), channels (stock markets and financial centres), players such as financial institutions and advisers, and the space and time factors that are specific to the finance industry. Risk and return are the exclusive assessment criteria. However, these seemingly self-evident terms do not have the same meaning in the real, non-financial economy. For example, the concept of a "satisfactory" or "unsatisfactory" return depends on the basis on which comparisons and calculations are made along with factors like the time horizon used in the appraisal process. During the 1990s, the growth in stock market prices made investment in shares very attractive since financial markets continuously assessed returns and, when markets were liquid, offered investors the possibility of being able to make quick disposals. Since the heavy fall in share prices at the start of 2000, property investment has again become attractive for financial markets. (From the financial industry's perspective, the mistake was not to have lost money after investing in shares, but to have turned in a worse performance than one indicated by the general stock market index or to have used a diversification strategy turning out badly.) A comparison over fifteen or twenty years could be made between the performance of a market investment portfolio and direct investments made in the real economy which avoided going through financial market channels. However, such a comparison is not "financial", since one

[1] The Swiss pension system is often referred to as the "three pillars". In addition to the middle pillar represented by occupational pension schemes there is the first pillar (state provision) and the third pillar (individual pension plans).

of the stages of the investment decision bypasses financial markets. Such comparisons can only be made in exceptional circumstances. Given that they have different meanings according to whether the context is that of the real economy or of financial markets, there is thus "return" and "return".

Furthermore, financialisation gives rise to a "mechanised" form of investment management. This favours certain types of space (financial centres) to the disadvantage of others (areas specialising in traditional, industrial or tourist industries which are either outdated or have fallen out of fashion). It also favours certain types of players (large companies and financial players) at the expense of others (SMEs, small savers etc.) along with certain types of investments (comparable and large-scale projects) as opposed to other projects (those which are small-scale, venture capital, etc.). While Engelen (2003) examines the effects of financialisation on the economy, his analysis takes no account of the property market. Furthermore, although major economic geography studies associated with Clark (http://urban.ouce.ox.ac.uk/) have looked at how some of the funds have played a part in regenerating urban centres, this group has only looked indirectly at the consequences of financialisation. In view of a whole series of measures taken over the last few years and which are aimed at financialising the property sector, the purpose of this study is to examine property market issues surrounding financialisation. These include the impact of pension funds on property investment in Switzerland; the extent to which it has become financialised and the effects of this process. It also involves answering questions about the types of investment that are favoured (commercial developments as opposed to housing or communal as opposed to individual living spaces) and whether the path followed by institutional investors favours certain types of spaces at the expense of others.

In order to examine these issues, this paper discusses the channels used by Swiss pension funds for financing the property sector and how they have evolved and developed since 1994. The research is based on an analysis of data collected by the Swiss Federal Statistics Office (SFSO)[2] together with private sector data (surveys by Ernst & Young, Lusenti, Robeco and Swissca conducted between 1997 and 2003). Around twenty semi-structured interviews were carried out with players in the sector in the spring of 2005. In addition, a panel of 13 experts met twice: first in the autumn of 2004 in order to check the hypotheses and to identify relevant information sources and providers, and secondly in the autumn of 2005 in order to give critical viewpoints on the researches content and results.

The first section provides a brief outline of the importance of pension funds in the Swiss economy and in the country's property sector. Then the two financing channels used by pension funds for property finance are discussed. One channel can be described as direct and non-financialised while the other is indirect and financialised. Both differ strongly from each other with regard to players involved, spatial organisation and investment criteria. Two criteria appear to be decisive in determining the way investments are divided between the two channels. First, a minimum critical mass in terms of property management skills is needed at all stages of the process (from project management skills at the construction stage to tenant management skills at the operational stage). This is something which the smaller funds are generally unable to achieve. Secondly, there are the ever-present specifics of local property markets (in terms of regulation, organisation, lack of openness) which require in-depth, specialised knowledge of the local and regional contexts of these markets and which limit the

[2] These cover *registered pension funds*, in other words funds which ensure the compulsory benefits set out in the federal law governing occupational pension schemes (abbreviated to LPP in French and BVG in German). Registered funds make up most of the total wealth of the second pillar represented by occupational pension funds, with a share in excess of 90% from 1994 to 2002 (91.6% of the figure of SFr440.5bn for 2002) as well as accounting for virtually all the numbers covered by these schemes.

degree to which property activities can be financialised and centralised. The third section concentrates on financialised channels by looking at financialisation within the economy and the property sector from a theoretical perspective on how the financialisation process operates (in the light of a whole series of measures that have been taken towards greater financialisation). Then, having looked at the operational and spatial processes at work within these channels, a number of limits to property sector financialisation are highlighted. The fourth and final part concludes by emphasising the nature and impact of the current financialisation process on pension funds' property investments.

1. The importance of pension funds in the Swiss property sector

Along with securities, property has always been a major part of pension funds' assets. In 2002, the funds' wealth in terms of property was estimated at nearly SFr60bn, almost all of it invested in Switzerland. This represented nearly 15% of total wealth (estimated to be over SFr400bn). However, these overall figures conceal major differences in both fund management methods for property and the size of pension funds. Despite a fall in the share accounted by property in the total wealth of occupational pension funds (even though stock market difficulties at the start of the new millennium saw property coming back into favour) amounts increased by around SFr18bn between 1994 and 2002.

TABLE1: PROPERTY INVESTMENT PATTERNS OF REGISTERED SWISS PENSION FUNDS BETWEEN 1994 AND 2002 (SFR MILLIONS)[3]

	1994	1996	1998	2000	2002
Total land and property	**42,071**	**46,636**	**50,290**	**56,141**	**59,885**
(Switzerland and abroad)	17%	15%	13%	12%	15%
Total wealth	**247,010**	**304,540**	**383,476**	**445,911**	**403,551**
	100%	100%	100%	100%	100%

Source: SFSO

Based on the work of Clark (2000 and 2003), the concern here is with the operational aspects of pension funds' asset management. Swiss pension funds use both internal and external management and the funds' boards are the top decision-making bodies. The boards are responsible for determining and controlling the strategic allocation of the fund's wealth along with the choice of in-house and outside managers. The boards are joint bodies, made up of an equal number of employee and employer representatives.[4] Few funds manage their entire asset portfolio in-house. In the first place, the management approach adopted can depend on the class or sub-class of assets. In-house management mainly concerns property owned in Switzerland, mortgages and liquid assets, while outside management is more often used for securities (shares and bonds), investments on alternative markets and, to a lesser degree, property owned abroad. Secondly, size[5] is to a large extent the main determinant of funds'

[3] Research is based on data from registered pension funds, which is why the figure differs from those given on the first page.

[4] Art. 51, para. 1, of the Occupational Pension Funds Act (referred to as LPP in French and BVG in German). As to the numbers of board members, this can vary.

[5] Although modest (representing less than 2% of total property investment) the property investments of collective funds are excluded, since their management is structurally devolved. Apart from collective foundations, whose strategic asset allocation decisions are determined externally through being devolved to an investment foundation, other administrative structures remain free to define their strategic asset allocation and to choose the institutions to which they want to delegate this management.

margin for manoeuvre in terms of investment policy and management. While larger funds' management choices depend on the class or sub-class of assets, most small funds naturally do not have either the personnel or the skills to manage matters themselves. As the pension fund-investment chain is long and complex, using outsiders for management and advice is commonplace and it is specifically at the investment stage that the financial industry comes in. Hence there are two channels with differing operational and spatial processes for property management and investment activities.

- The first channel can be termed direct or traditional, as it applies to funds with a policy of in-house property investment management where investments are made directly. Funds thus hold the property rights to, and have operational responsibility for, their property investments.
- The second channel can be described as indirect or financialised. It attracts pension fund investments that are made through a collective property investment vehicle. As a result, management is devolved and investments are made indirectly through being pooled. This means that property rights and property management responsibilities are vested in the investment vehicle.

2. Direct and financialised investment channels

2.1. The significance of investment channels and registered pension funds with property portfolios

Eighty per cent of property investment is still made through traditional investment channels. As Table 2 shows, funds had rights over, and management responsibilities for, a building stock valued at around SFr50bn in 2002. Although the large funds (those with wealth in excess of SFr1bn), along with medium-sized funds (wealth between SFr100m and SFr1bn)[6] are fewer in number, they account for the major share of funds that are directly invested in property (Figure 1). However, there was also an increase in the use of indirect investment methods during the study period, accompanied by a sharp rise in the amounts invested (from SFr1.8bn in 1994 to SFr8.5bn in 2002).[7] Although the period 1994 to 2002 saw all types of funds making greater use of indirect forms of property investment, intuition might have suggested that the smaller funds (wealth of less than SFr100m) would have been relatively more important. Paradoxically, however, it is the large (37 in 2002 compared with 15 in 1994) and medium-sized funds (187 in 2002 compared with 120 in 1994) who have invested more in the way of indirect investments (Figure 2)[8].

[6] For the direct or traditional channel, there were 34 large funds in 1994 and 55 in 2002, while medium-sized funds totalled 214 in 1994 compared with 260 in 2002. Smaller funds numbered 961 in 1994 and 763 in 2002.

[7] In this regard, it is part of a general trend marked by a rise in the use of collective investment vehicles for other types of asset, mainly stocks and shares.

[8] For the indirect or financialised channel, smaller funds numbered 734 in 1994 and 602 in 2002.

TABLE 2: PENSION FUNDS' PROPERTY INVESTMENTS (1994-2002, SFR MILLION)

Funds (excl. collective funds)	1994	1996	1998	2000	2002
Direct Investments					
Switzerland	39,602	42,374	44,870	46,861	49,331
% of Funds Invested in Property	95.5	92.3	91.0	86.5	85.3
Indirect/Collective Investments					
Switzerland	1,866	3,520	4,443	7,311	8,469
% of Funds Invested in Property	4.5	7.7	9.0	13.5	14.7
Funds Invested in Property	**41,468**	**45,894**	**49,314**	**54,173**	**57,800**
	100	**100**	**100**	**100**	**100**

Source: SFSO

In short, taking both investment channels together, there is no question that the big funds have the greatest weight and that their significance grew between 1994 and 2002. In 2002, 55 large funds held 63% of the SFr50bn directly-invested funds (Figure 1) and 37 large funds accounted for more than half of the SFr8.5bn indirectly-invested funds (Figure 2).

FIGURE 1: PATTERNS FOR SHARES IN TOTAL DIRECT PROPERTY INVESTMENT BY PENSION FUND SIZE: 1994-2002 (SFR BILLION)

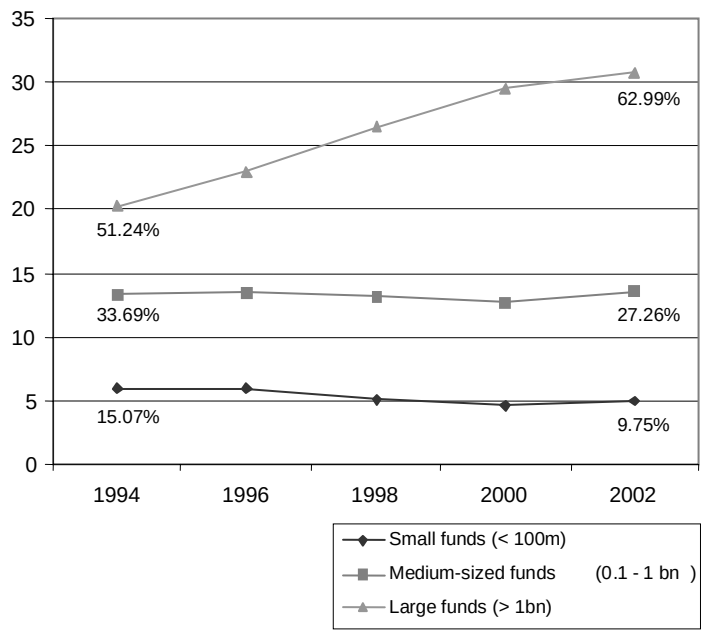
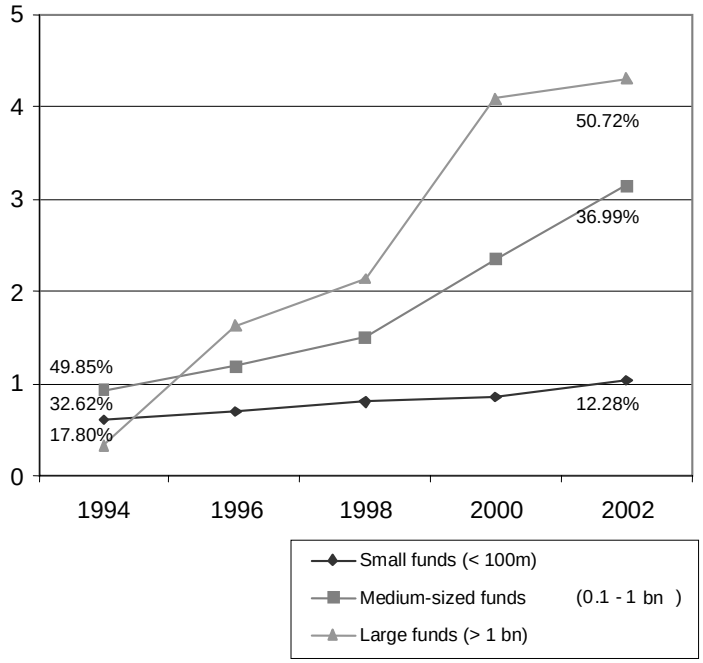


FIGURE 2: PATTERNS FOR SHARES IN TOTAL INDIRECT PROPERTY INVESTMENT BY PENSION FUND SIZE: 1994-2002 (SFR BILLION)



Source: OFS

Depending on the investment channel used, management practices, along with the operational and spatial processes that characterises pension funds' property investment, vary considerably. The traditional investment channel, where pension funds operate as investors and property managers, requires skills, staff and knowledge of property markets to ensure that the funds invested in real property are put to best use. In the second investment channel, pension funds act solely as investors, with specialist institutions taking on responsibility for all management-related work. There are three such types of institutions in Switzerland: investment foundations (mixed for property and securities investments or specialised for property investments); property investment funds; and property investment companies. In cases where the funds or specialist institutions act as property managers, the investments concern buildings which are rented for residential, mixed as well as commercial use (mainly offices and small retail outlets). Funds and institutions do not invest in houses (this is done by construction companies and private individuals) and industrial properties and/or those serving the tourist industry (hotels, restaurants etc.). Discussions with specialists in these markets indicated that the reason for this was a higher risk perception on the part of investors.

2.2. Channel A: direct management, based on in-house skills and characterised by proximity

2.2.1. Decentralised skills

Special skills are required for direct property management and indeed for property purchases and construction. These are both technical (architectural, building standards, urban planning, law etc.) and financial (property valuation, tax etc.). In this case, one or more people inside the pension fund are concerned with managing its property estate. The use of in-house staff and skills in the areas mentioned above depends closely on the size of the fund and the importance of its property portfolio.

While real property can account, on average, for 15% of a fund's wealth, the sums remain relatively modest for the small and medium-sized funds. Property can be a fairly narrow part of their portfolios, ranging from a few properties to maybe ten or even fifteen (but rarely much more than this). Only the large funds have a critical mass which allows them to have a proper in-house investment policy covering dozens or even hundreds of buildings, thereby enabling them to use a team having all the necessary skills. Before 1985, all pension funds habitually bought or constructed buildings and acted as owners. The buildings were used as accommodation for company employees (in both the private and public sectors) or to meet a company's administrative or industrial needs. Even if the funds have gradually abandoned the purchase and construction of buildings on behalf of employees and scheme members, this heritage still continues to be felt in the properties that are owned by the funds. For some funds, notably the small and medium-sized ones, this can weigh heavily and be costly. Thanks to their size and critical mass, it has been easier for the large funds to make qualitative or geographical changes to their property portfolios. While pension funds can sometimes act as project managers in property developments,[9] they usually buy property that has already been built. Generally, unlike other institutional investors like property funds - and property investment companies[10] in particular - pension funds' investment strategies are characterised by a *buy and hold*-type behaviour. Once properties are bought or built, they remain in the funds' ownership for a long period, and a policy of property disposals is rare (Altaprima and Ernst & Young, 2004: 18).

In order for the required occupancy rate to be achieved, it is important that no mistakes are made in the choice of building and location. Thus, a major part of a property deal is the analytical stage of assessing property purchases or construction projects. This relies on specialist geographical knowledge of property markets. As urban property markets become increasingly complex, and institutional investors (banks, insurance companies and pension funds) develop and evolve, pension funds commonly draw on specialist players who have emerged within the sector. Indeed, when funds require strategic (or specific) skills in areas like portfolio operations (brokers) building development projects (engineers, architects etc.), property trusts (certified accountants, financiers) etc., they call on external, centralised expertise which is often city-based and mainly in the country's major urban centres. Three-quarters of institutions make use of outside experts as part of their property investment policy, with the biggest institutions often being the greatest users (Altaprima and Ernst & Young, 2004: 44). This should come as no surprise given that they often manage large portfolios which are often subject to change. During the process of analysing and assessing the value of a building, the various specialists base their judgements on the basic issues surrounding any property investment. These can be set out in the following stylised manner:

- The building's specifics: the buildings own characteristics such as its age, the number and area of flats/rooms, building materials used, various installations (lift, garages, various amenities) etc.
- The building's location: this includes the immediate environment of the building's location together with the local and regional environment. In the first case this refers to the locality's characteristics in terms of centrality (services and shops, leisure facilities, closeness to the city centre), socio-professional make-up, accessibility (roads, public

[9] In 2003, institutional property investment (by property funds, insurance companies, investment foundations and pension funds) mainly involved purchases, with involvement in new buildings and projects being of secondary importance. Of the SFr7.6bn invested in property in 2003, around SFr6.9bn was directly invested (65% in purchases and 35% in new development projects). The remainder (around SFr1.3bn) was invested indirectly (Altaprima and Ernst & Young, 2004: 17).

[10] The aim of these institutions is to make capital gains from property transactions.

transport) and quality of life (noise, pollution, recreational spaces etc). The second concerns the contexts of, and perspectives for, a city and region in terms of economic development (mainly for the commercial sector) and socio-demographic patterns (mainly for the residential sector).

For purely property management-related activities, namely administrative responsibilities concerned with tenant relations in matters like renting and refurbishment, management can either be internal or external. In the first case, the funds can use their own in-house management for the buildings they own in various localities and regions. In the second case, they can pass over the management of all or part of their building stock to property management companies. Such contracting out is of little or no importance since it concerns skills which are not regarded as strategic, given that that funds still remain the buildings' owners.

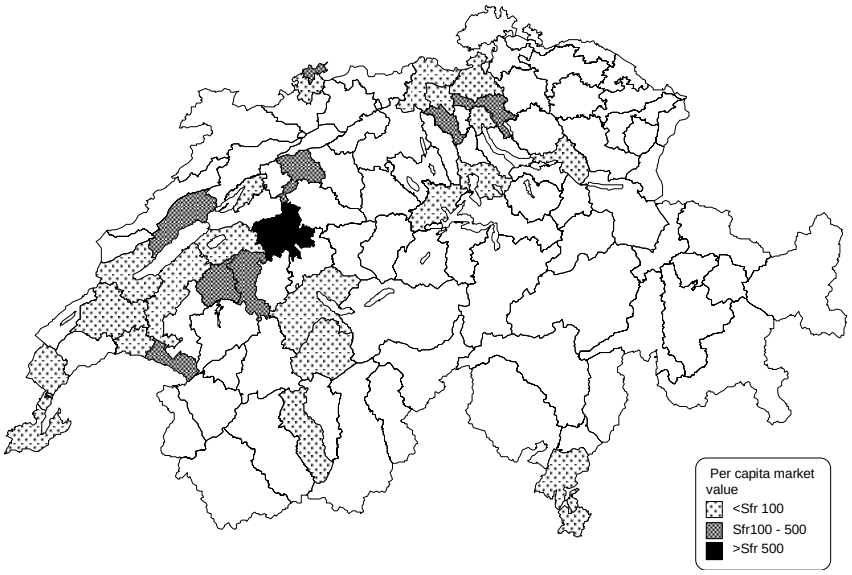
2.2.2. Investment spaces

For many funds, property is a market centred around the notion of proximity. Consequently, Swiss pension funds' investments are primarily at the regional or cantonal (sub-regional)[11] level. According to a Swissca survey (2004: 41), 60% of pension funds reported that their property investments were close to the employer. Only 13% said that their investments could be made in areas other than those where the employer was based and for independent third party users. A closer look at the spatial aspects of direct investments can be made by using recent data for five large funds, all with a property portfolio. Taken together, these funds own 822 buildings (primarily residential but with some commercial properties) with a total value of SFr5.99bn.

Three reasons can be put forward to explain why spatial proximity has been important. Historically, property investments were determined by businesses and their employees, with the general aim of funding employee accommodation. In a world where there was not yet a fully-developed finance industry, the very idea of investing in another region could hardly be justified. On the contrary, such behaviour could lead to the local economy being undermined. The property-proximity link can be seen, for example, in the activities of ASCOM, a large, Berne-based Swiss company involved in the digital communication and security systems industries. During its history it has taken over companies in the Fribourg, Neuchâtel, Solothurn and Vaud cantons, and this geographical make-up is still reflected in the properties owned by its pension fund (Map 1).

[11] Administratively, a canton is broadly comparable to a US state.

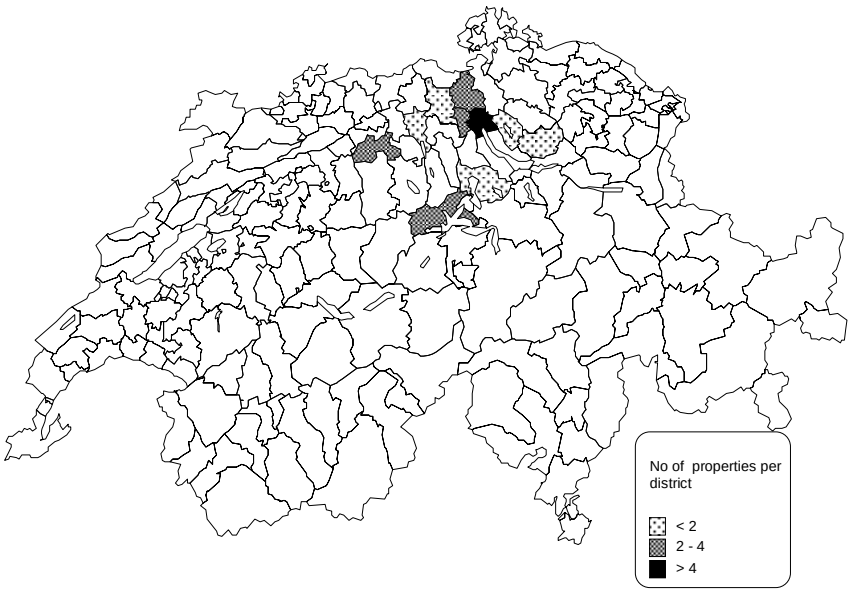
MAP 1: PROPERTIES OWNED BY THE ASCOM PENSION FUND



Source: Ascom Pension Fund 2004 Annual Report

A second explanation, which emerged from interviews with fund managers, is the importance of knowledge of local property markets. Generally speaking, Swiss property markets remain highly compartmentalised. There is a lack of clarity concerning information on prices and property characteristics, and local factors continue to be a major influence on regulations. Most property within the portfolio thus continues to be located in the region of origin of the company and its pension fund; as is the case for the pension funds for Siemens Switzerland (Map 2) and for Migros, Switzerland's leading distribution group (Map 3).

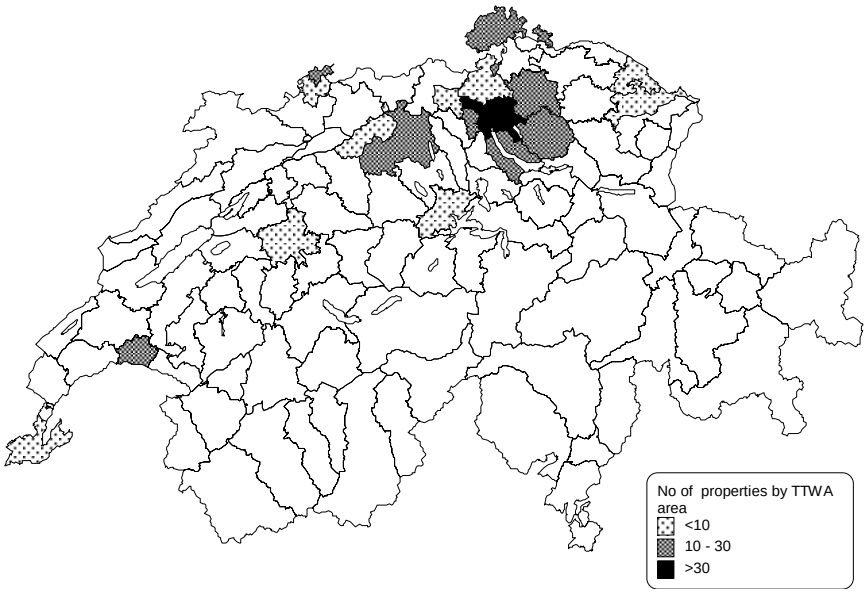
MAP 2: PROPERTIES OWNED BY SIEMENS' PENSION FUND



Source: Siemens Pension Fund Website

With regard to Migros' pension fund – whose property portfolio is a large as that of the country's biggest property fund and which owns shopping centres across the country – investments are closely linked to the areas where the group's main offices are based, namely in the Aargau, Zurich and Lausanne Travel-to-Work Areas (TTWAs).

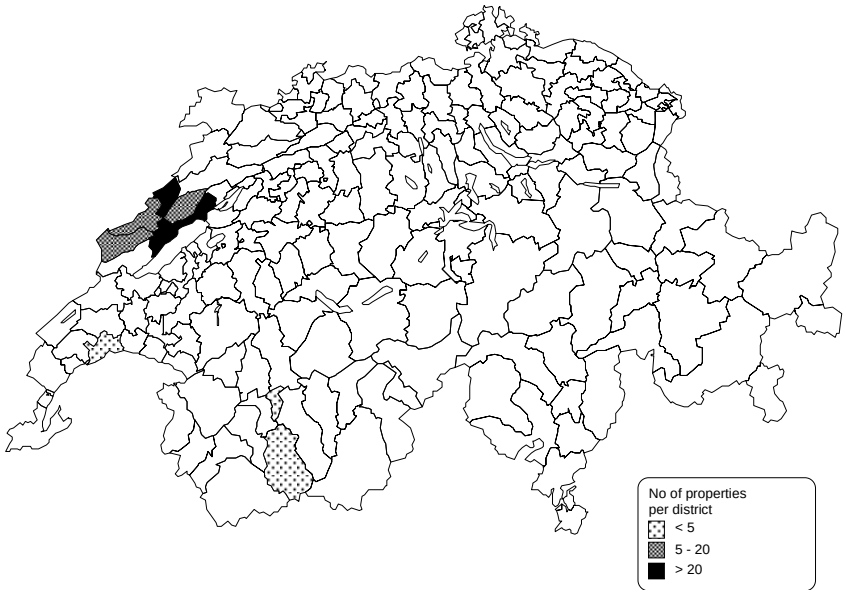
MAP 3: PROPERTIES OWNED BY MIGROS'S PENSION FUND



Source : Migros Pension Fund 2003 Annual Report

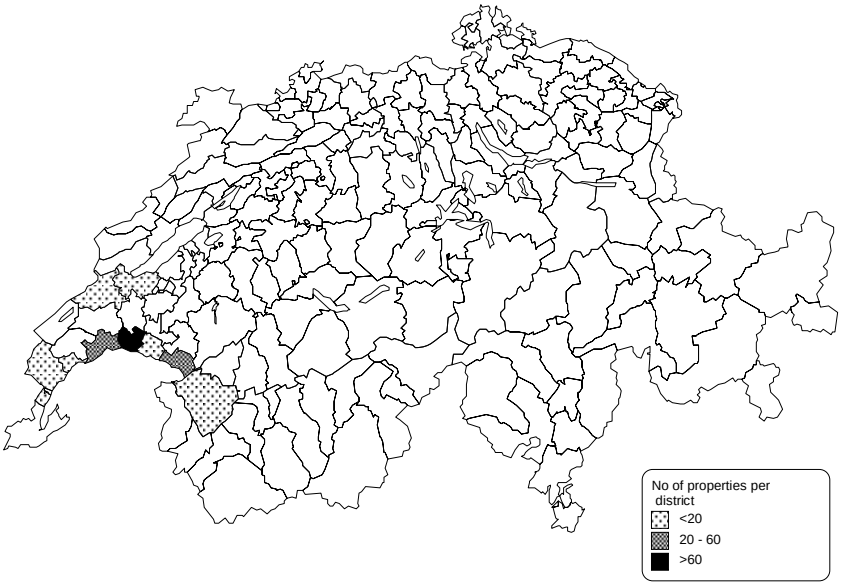
A third explanation stems from the fact that public sector pension funds are often large and that they generally directly manage their property activities. Public sectors funds, by the fact that they are in principle subject to political control and because of the active role that employees play in fund management, pursue a proximity-based strategy. While the Neuchâtel canton pension fund's investments appear to be more evenly spread among the canton's various districts, those for the Vaud canton's pension fund are heavily concentrated around the Lake Geneva area, notably along a line running from Morges to Vevey/Montreux.

MAP 4: PROPERTIES OWNED BY THE NEUCHÂTEL CANTON'S PENSION FUND



Source: Neuchâtel Canton Pension Fund 2003 Annual Report

MAP 5: PROPERTIES OWNED BY THE VAUD CANTON'S PENSION FUND



Source : Vaud Canton Pension Fund 2003 Annual Report

Underlying pension funds' direct investments is a proximity-based process whose scope varies, firstly, according the importance of the property portfolio and, secondly, according to the fund's legal status:

- Pooled or combined public sector funds: the investments of small public sector funds (in other words municipal funds) are made at local or even at council level (such as the pension funds for the cities of Neuchâtel and Basel). The investments of the biggest public sector funds (i.e. the cantons' pension funds) are made at regional/cantonal level. The degree to which investments are evenly distributed can depend on the strength or weakness of the fund's dependence on the canton (independent funds or those dependent on the canton's organisations). As for the main national-level public sector fund (namely the Publica pension fund which had a property portfolio of SFr1.27bn at the end of 2004)[12] its investment practices should follow a nationwide pattern.
- Private sector pension funds: the investments of small and medium-sized private sector funds - independent, merged or company pension funds – are mainly made at local level (municipality or districts within a canton). Investments made by the large private sector funds with significant property portfolios (mainly funds tied to companies) can be made in several regions. The geographical pattern generally results from mergers and acquisitions that have been made during the course of the company's history.

2.3. Channel B: financialised management – delegation and distance

2.3.1. Centralised skills networks

Funds can opt to pass on all their property management responsibilities and simply act as investors. Under Swiss law they can acquire shares in two types of collective institution. First,

[12] Following a public sector reorganisation in 1998, the funds for public sector enterprises such as the postal service, CFF (the Swiss rail service) and Swisscom are governed by private law.

they can decide to invest via the market through having shares in property funds[13] and property companies. Secondly, there is the possibility of investing in what are known as investment foundations, which are reserved solely for pension funds and other recognised institutions.[14] The most important investment foundations are members of an umbrella group known as the CAFP.[15] They are not listed on the stock market and pension funds often acquire an interest through contributions in kind. All these institutions have the staff and technical skills that a property investment strategy needs (engineers, architects, property experts, brokers, lawyers etc.). Because of this, their investments are direct with an internal team being responsible for property purchases, sales and construction. Apart from a few funds (notably the *La Foncière* investment fund) all the institutions involved in indirect property investment are based in Zurich. This centralisation of property management implies that adequate knowledge of regional property markets is available. These institutions thus rely on a chain of property management personnel, either as affiliates or partners,[16] who have the local knowledge needed for identifying good opportunities for selling and buying properties and for site redevelopment.

Some institutions, especially those involved in making investments abroad, often rely on indirect investment procedures. This means that collective investors are no longer property owners but have an interest in – or acquire shares in – other institutions (quoted or unquoted property funds and property companies etc.).

In the light of disappointing stock market performances over the last few years, property is once again back in fashion as an asset. Consequently, in line with what would be expected from the processes behind diversification strategies, funds have made use of all indirect investment possibilities. However, they have mainly gone for property funds and investment foundations. Although the funds can be major shareholders in stock market-quoted property companies, it has been less common for them to acquire holdings in these companies (Robeco, 2002; Lusenti, 2003).

Collective investment vehicles' property portfolio structures are based on the key principle of modern portfolio theory, namely the strategy of risk diversification. Property markets can be segmented either geographically or by sector, with each segment having its own market cycle and specific risks. Consequently, the make-up of property portfolios is generally examined from a twofold perspective: how allocations are made and the geographical spread of properties. Investors, i.e. pension funds, can thus diversify their portfolios according to what is on offer. Through the case examined here it will be seen how the risk diversification principle is put into action. The analysis covers the main players working within indirect investment channels, namely the four biggest property foundations (or property investment foundations), the three investment foundations having an internal direct property investment

[13] Property funds are generally affiliated to banks.

[14] An investment foundation's investors are limited to so-called 2nd and 3rd pillar institutions: pension funds, vested pension institutions, bodies known as *institutions supplétives* (state-regulated bodies for employers who do not meet the requirements for having a registered pension fund), security funds, investment foundations, benefit funds, finance foundations and banking foundations which come under what is known as the third pillar A – see the *Office Féderal de Assurances Sociales*/Federal Social Insurance Office (OFAS, 1999).

[15] There are nineteen major investment foundations in Switzerland which belong to the CAFP (*Conférence des Administrateurs de Fondations de Placement* or Investment Foundation Directors' Conference). Among the investment foundations are those affiliated to banks and insurance companies and those which run a direct property investment policy, plus independent foundations known as property foundations.

[16] As with pension funds, various institutions can have their own property management set-up in the areas where the properties are located for carrying out administrative and management tasks (renting, refurbishment, tenant relations etc.). Alternatively, they can rely on outside management or partners.

policy and the eight largest property funds. Data have been obtained covering their numbers, types of allocations made, the market values of properties and areas where the properties are located.[17] The channels being looked at involved 2004 Swiss-based properties valued at more than SFr 20.1bn.

2.3.2. Diversification by type of allocation

Indirect investment foundations provide products or funds offering varying degrees of specialisation. The products offered by property funds and investment foundations are almost entirely centred on residential or commercial property (including offices and small shopping centres) or take the form of mixed funds, where the split between residential and commercial properties varies. As for the portfolios of stock market-quoted property companies, these are almost exclusively centred on commercial property and still closely match the portfolios first established by those who set up the companies.[18] Only UBS's mixed funds contain industrial property among the properties on its books. On the other hand, no fund offers portfolios containing large shopping centres or buildings serving the tourist sector (hotels, restaurants, ski lifts in alpine resorts etc.). In short, for the investor, portfolio diversification according to allocation is limited to two main segments, *residential* and *commercial*.

2.3.3. Geographical diversification

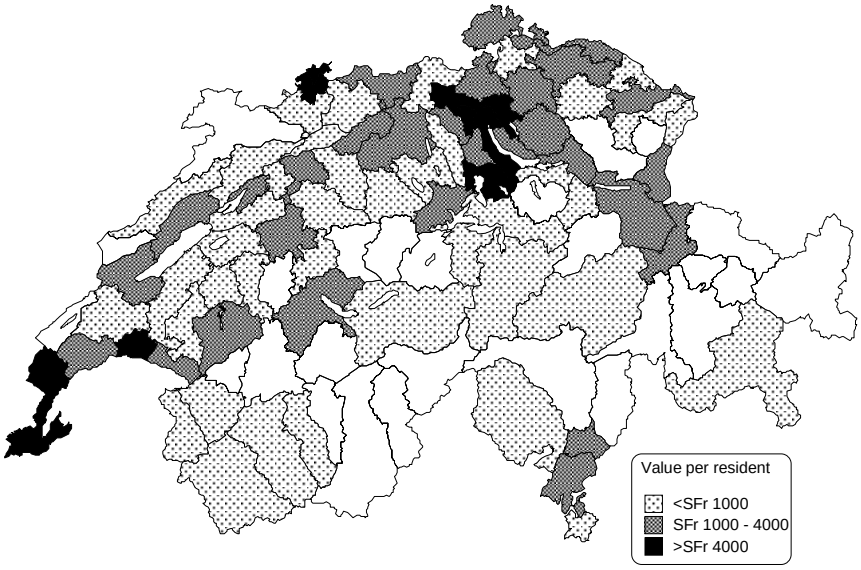
In accordance with the property-type allocations linked to investment products, the various collective investment institutions engage in risk diversification through a geographical spread of property. What characterises the geography of diversification? Is it a broad process, spread more or less evenly across the whole country, or does it favour certain areas? From a quick overview, and even when investment values are weighted by their Travel-to-Work Areas (TTWA) populations, it emerges that spatial diversification is limited solely to certain areas (Map 6).[19]

[17] Property companies have not been considered given that pension funds have made little use of these institutions.

[18] These companies arose as a result of a contracting-out process by industrial and/or commercial firms and banks and insurance companies; the aim being to get them listed on the stock market. For example, Allreal is a spin-off from Oerlikon Bührle, PSP Swiss Property a spin-off from Zurich Assurance and Swiss Prime Site a spin-off from Crédit Suisse.

[19] The map refers to all property (residential, mixed or commercial) owned via the two main indirect investment channels in which funds can hold an interest together with property owned by quoted and unquoted investment vehicles (the former being investment funds with 1250 properties worth SFr12.5bn and the latter being investment foundations with 388 properties worth SFr4.2bn) and property foundations (366 properties valued at SFr3.4bn).

MAP 6: 2004 ANALYSIS OF PROPERTY OWNED BY THE FIFTEEN BIGGEST PLAYERS USING INDIRECT INVESTMENT CHANNELS (AS OF 2003/2004)



Source: Annual Reports

Investments are spread across a large number of Swiss TTWAs, but are primarily concentrated in the country's urban areas. All major urban areas located on the Swiss plateau and in the Italian-speaking Ticino canton have market values per head between SFr1000 and SFr4000. The pattern is even more pronounced when the main metropolitan areas of Basel, Geneva, Lausanne and Zurich (Berne falling in the intermediate range) are examined. The latter areas all have values exceeding SFr4000 per resident, with the biggest concentration being in areas around Zurich. As can be seen from looking at a line running from Geneva to Vevey/Montreux, the TTWAs along Lake Geneva can also be identified as areas with significant investment concentrations. Less urbanised areas – and peripheral areas even more so - are much less well represented. In short, the following geographical structures can be identified:

- The Lake Geneva metropolitan axis
- The Swiss Plateau axis: running from Yverdon to St Gall via Berne, Basel and Zurich and then extending beyond to Coire
- The Ticino metropolitan axis running from Bellinzone to Lugano.

Hence, regardless of the degree of specialisation for investment products (in terms of the split between residential and commercial properties) collective investment vehicles have a focused geographical vision centred on urban areas, particularly the larger urban areas.

3. Pension funds' property investments in the context of the financialisation of the economy.

In 2002, the traditional investment channel was still the most common form, characterised by funds acting as both investors and having direct responsibility for all property management issues. For political or historical reasons, but especially for reasons tied in with having specialist knowledge of property assets, property purchases, sales and construction were carried out at local or regional level. In every single instance (especially when deals turn out

badly) the funds' in-house property portfolio managers make their cases before the funds' boards. This is followed by a specific examination of the special characteristics and circumstances of the properties along with their respective yields. In other words, it is a situation where dialogue is possible (Hirschman, 1986) and gives rise to a set-up where players involved at all levels within the fund can discuss matters. Furthermore, given the complex nature of property transactions (in areas like valuations, putting together financial packages, finding the required players, transaction taxes etc.), these discussions are necessarily lengthy. For the investor, specifically the fund manager, there is a *lock-in* effect.

The 1990s witnessed a growth in the financialisation of the economy, where players at the centre (Zurich) determined investment allocations. Financialised investment channels were completely different from the more traditional channels centred on the real economy. Given the changes this brought about, it can be asked how pension funds involved in property reacted to them; what were their effect on management criteria and the geographical spread of investments; and how did players' behaviour respond to these changes?

3.1. The shift to financialisation

Theory and policy are today concerned with increasing mobility and liquidity within financial markets (Corpataux et Crevoisier, 2005). Above all, financial market liberalisation policies are aimed at ensuring that capital flows freely and perfectly. Capital mobility would remain imperfect, or would not exist, if it were not able to rely on fully-developed and liquid financial markets. Most countries have implemented two types of institutional reforms in order to create the maximum degree of liquidity and capital mobility. In the first place, there are reforms which eliminate regulatory barriers hampering the free and perfect movement of capital. Secondly, there are those which strengthen capital market efficiency by promoting liquidity and transparency within markets and guaranteeing good quality, publicly-available information.

At the same time, the modern theory of finance inspired by Markowitz (1959)[20] directs players towards diversification strategies which lead them to spread their portfolios over a wider range of financial assets. The more financial markets develop and become more liquid, the greater the scope for the practical application of the theory. Increased liquidity and mobility reduces the risk created by the immobility of capital, as it gives players in the market the chance to move out of their investments at any time (Orléan, 1999; Lordon, 2000; Corpataux et Crevoisier, 2005). While the theory was primarily concerned with – and applied to – the market for shares it sought to provide a common standard for comparing different companies. From a theoretical perspective, listed companies are nothing more than entities composed of liquid assets that can be bought or sold at any time on the basis of a given set of standard and quantifiable criteria. The theory has now been extended to other areas or classes (to use the term employed in modern finance) of assets. So today, property investments have thus become a class of assets that are comparable with investments in securities, and where attempts are made to apply the investment criteria of risk and return used for securities to property.

[20] For a summary introduction of modern theories of finance and their limits see Sauvage (1999) and Rainelli-Le Montagner (2003).

3.2. Constructing a financialised property market: comparability and liquidity

This Swiss property market is extremely fragmented with a highly pronounced regional character. Consequently it is not particularly liquid (transaction costs remain high). Financial players are nevertheless exerting pressure to develop this market along the lines of those for securities and international property through improving liquidity, transparency and information. In traditional channels, funds' property investments are regional in nature (given the problems of investing elsewhere) and direct property management is often characterised by a financially passive approach, reflected by the infrequency of purchases and sales.[21] Indeed once bought or built, funds keep their properties for long periods and property disposal policies are extremely uncommon (Altaprima and Ernst & Young, 2004). Financial players are calling for funds to be more active and to reassess their property portfolios more often so they can be managed along the same lines as a securities portfolio. In other words, for a *buy and hold* approach to be replaced by a *buy and manage* one. The construction of a unified national market will be a source of liquidity and will mean that property deals occur more often.

Some institutional managers active within the property sector, such as Swissca (2003), are arguing for a number of reforms to increase the size of the Swiss property market and to develop its liquidity. These include new collective investment vehicles, new products, improving information and transparency, using new valuation methods based on dynamic criteria and a more active, *buy and manage* approach to portfolio management.

A whole series of measures has been taken towards achieving greater comparability of property and greater liquidity in property markets. Creating a national market effectively requires the standardisation of property accounting and valuation methods as a way of reducing the opaque nature of regional property markets, thereby enabling different properties in different regions to be compared. Contemporary financial vocabulary has been "institutionalised" in laws enacted since the 1990s which embody the three main principles of good management. Indeed, the triptych of return, risk and liquidity is part of current Swiss federal legislation governing pension funds' investment criteria (namely the LPP Act and the OPP2 Ordinance). Three concrete examples can be given of actions aimed at greater comparability and liquidity/mobility in Swiss property markets:

In the first place, investors have for several years been using property indices as a means of comparing the performance of market-listed investment vehicles.[22] Since the beginning of 2005, they have equally been able to use an index for investment foundations with a property portfolio who are CAFP members.

Secondly, a recent change to pension funds' accounting standards,[23] based on the principle of comparability of risks and returns, fits in with a financialisation framework for funds' property investments. The change means that all funds' investments have to reflect their current financial situation through valuations based on market values.

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[21] This does not mean that funds cannot be highly active within real investment channels; for example being involved in many building projects.

[22] The SWX Immofonds index covers all quoted Swiss investment funds. As for the SWX Real Estate Index, it contains property companies listed on the Swiss stock market (Crédit Suisse, 2005).

[23] In order to standardise accounting standards at national level and to make them compatible with international standards, an accounting concept inspired by practices used in the English-speaking world has been developed to cover both large and small businesses (the Swiss GAAP RPC 26). The use of new accounting standards in property has led to changes in the methods and frequency of valuations. Since January the 1st 2005, pension funds must use the new accounting standards (Meyer and Teitler, 2004).

Thirdly, the 1994 Federal Investment Funds Act (LFP in French or AFG in German) is currently being revised. It is due to be transformed into legislation covering a wider range of pooled capital investments (notably unit trust or mutual investment companies and limited partnership pooled investment companies). Amongst other things, it will favour the development of pooled investment vehicles for property, thereby enabling liquidity to be increased in various markets (Département fédéral des finances, 2004).

In this context, property investments have become a class of assets comparable to securities investments. The criteria used for property investment are identical for those for securities and are thus those that are used by financial markets. After the stock market problems at the start of the new millennium, property has become an ideal investment because it serves as a basis for pursuing diversification strategies. The research and studies that have been carried out show that the correlation between the returns on property and those on financial assets (shares and bonds) is low or even negative (for example, Bender *et al*., 2001; Hoesli, 2003). In line with what the theory recommends, property investment plays a beneficial role in mixed investment portfolios (those with several classes of assets). Consequently, it can be analysed from the viewpoint of returns and risk diversification. Indeed, it is the aim of financial markets to provide a standardised means of looking at the way property performs in various areas, both nationally and internationally. In line with the dictum of not "putting all your eggs in one basket", risk spreading is a way of coming up with more baskets by introducing a greater geographical mix to portfolios!

3.3. The shape of financialised investment channels: skills and centralised investments

When pension funds acquire shares in various investment vehicles, the aim is to pass all property management responsibilities to an outside institution and thus to act simply as investors. As has already been seen, this market has grown from a 4.5% share in 1994 to nearly 15% in 2002. In this framework, pension fund board decisions on property investment are tantamount to using comparative indices for buying and selling shares.

The indirect, financialised investment channel differs fundamentally from the traditional norm represented by the proximity-based approach. Indeed, the process by which management is devolved is both operationally and spatially standardised. Management and property investment skills are centralised, mainly in Zurich. Moreover, from 2002-2003 the use of outside management appears to have increased. Indeed, many funds have, for example, ceased managing their own portfolios by taking shares in the three property funds managed by the Zurich-based Pensimo Management.[24]

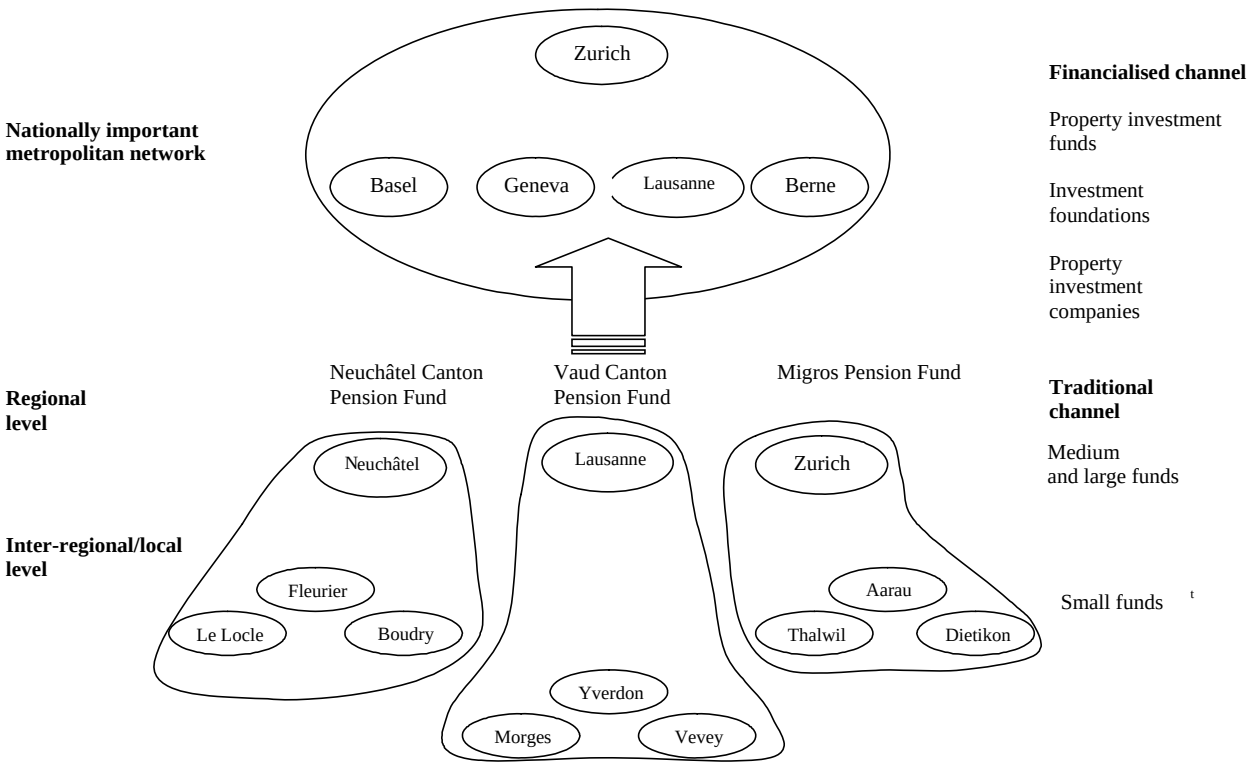
Property investments conform to a mechanistic process whereby they are standardised on the basis of risk and return criteria. Specialist institutions must ensure that returns are at least equal to the market average (as reflected by the relevant indices) and that risks are reduced through portfolio diversification (in terms of allocations between residential and commercial properties and geographically). If the fund manager is dissatisfied with the results, he or she will pull out. However, it should be noted that going down the route of financial markets leads to a push in the direction of conformity in terms of the choice of financial products on offer from collective fund managers. Indeed, in situations of crisis, for example, a fund manager will not be challenged if their poor results are in line with those of other fund managers. By

[24] For Pensimo's Turidomus Foundation (large shares) the pension funds of Nestlé, Swissair, and the Swiss postal service (La Poste) can be given as examples. For the Pensimo Foundation (medium shares) the pension funds for the Lucerne canton and the city of Zurich can be mentioned, while the pension funds of Grisons and Zoug cantons can be cited in the case of Imoka Foundation (small shares).

contrast, unsatisfactory short- and medium-term results, compared with other managers' markedly better results, can cost a manager their job. Consequently, when it comes to making investment decisions, a fund manager finds it difficult to go against the prevailing "consensus".

From an investment perspective, the analysis has clearly shown that, in Switzerland, there is primarily a focus on areas recognised as centres of activity and that they follow an urban-based hierarchy (Figure 3). Outside of these areas, investment is almost non-existent. By analogy with the stock market, we can talk of "blue chip" and "small/midcap" areas which are plugged into the investment network and "unquoted" areas similar to SMEs in areas characterised by industry and tourism (which these days experience problems in obtaining finance). It may be wondered why investments are made in these centres of activity when there is no evidence available on the comparative inter-regional profitability of property investments of a given duration. Investment "pockets" seem to depend on financial players' actions and whims, which appear to play a central role in the way areas are selected. It is a process in which urban areas seem very well placed, making it easy to justify and market financial products.

FIGURE 3: SPATIAL PATTERN OF SWISS PENSION FUNDS' PROPERTY INVESTMENTS (1994-2005)



Source : Own outline

3.4 Limits to transferring a share-based model to property

3.4.1. The various meanings of risk in finance and in the real world

While fully-developed and liquid markets are a *sine qua non* for the proper functioning of financial markets, finance has its own unique concepts of *risk* and *return* (Table 3). In the real economy, return is characterised by the accumulation and control of capital over time, in other words in line with economic cycles, whether they are short (e.g. production cycles) or long (product or technological cycles). Accumulation takes place at different levels (company, regional, sectoral or national) in line with the organisation of production, consumption and real transactions. In the financial economy, return is not calculated on the basis of real cycles over time (where time is required for a firm to reorganise its production processes and for innovation to take place), but on the basis of comparative returns which are continually assessed in relation to the returns on other financial market investments. The assessment and valuation process is thus continuous and disconnected from production-related time (Orléan, 1999). In a nutshell, short term dips and the threat of pulling out are substituted for the productivity which comes from a commitment made over time. *Accumulation over time is replaced by mobility across space*; the social link of a stakeholder giving way to shareholder value. Involvement in a property or industrial project having its own specific risks and circumstances is replaced by an act involving the purchase of standardised financial assets in the form of securities. However, while the introduction of greater uniformity in accounting standards is welcome, several doubts can be raised over the way direct and indirect investments are compared. To what extent do the indices for quoted and unquoted investment vehicles reflect real property values? In other words, are "real" prices based on the capitalised yield values (rents) in line with prices on financial markets? While property valuations can be made in an identical manner, given that pension funds and pooled investment vehicles tend to use the same appraisal techniques (e.g. discounted cash flow or DCF),[25] there is little chance of the market values of quoted investment vehicles' property portfolios coinciding with real values. Up to 2000, when sentiment was in favour of securities markets, the property market was under-valued and building stock values (the market values on real property markets) were lower than stock market values (i.e. at a discount). Today, the reverse is true, building stock values are higher than stock market (i.e. at a premium). Does the same apply to unquoted investment vehicles in the sense that the index for investment foundations belonging to the CAFP corresponds to the DCF value of all the properties they own?

In the real economy, an entrepreneur's risk-taking is hard to rationalise in terms of a mathematical formula. The entrepreneur takes a view on a future which is not perfectly known or knowable. Such uncertainty, which Keynes termed "fundamental", covers a future which is unknown, or is at least one where a mathematical probability cannot be assigned to the event, and where it is impossible to list the future states of the world. In conventional economic theory and the theory of finance, the notion of risk has a different and specific meaning. Indeed, since Knight, the term "risk" has been applied to situations where there is only imperfect knowledge of outcomes, but where all possible outcomes are known *a priori*; in other words it is possible to give a mathematical probability of the likelihood of each outcome occurring – all states of nature are known from the outset.[26] Markowitz's uncertain

[25] According to the DCF method, the monetary value calculation incorporates factors such as refurbishment costs which will be attributed over several years or future rent increases. In this method, the determining factor is the net return from future cash flows discounted at a risk-adjusted rate (Swisscanto, 2005: 14).

[26] For an overview of the debates see Moureau N. and Rivaud-Danset D. (2004).

universe corresponds to a risk than can be assessed in terms of a probability and is, above all, a risk that can be reduced by following the appropriate diversification strategy.

For those who subscribe to an efficient financial markets hypothesis, these latter approaches are said to be capable of working out, or correctly forecasting, the discounted future income flows in a universe where probabilities can be calculated. The risk/return pairing corresponds to a solution which can be found as an exercise in financial engineering. However, in the real world, it is extremely difficult to make a firm forecast of the return and risk attached to purchasing a property or an industrial project.

TABLE 3: COMPARISON OF PROPERTY INVESTMENT CRITERIA BETWEEN DIRECT AND FINANCIALISED INVESTMENT CHANNELS

	Real Economy (Direct Channel)		**Financialised Economy**	
	Basis of calculation	**Spatial and temporal factors**	**Basis of calculation**	**Spatial and temporal factors**
Return (Yield)	Expected future project returns of project	Time horizon for real project, accumulation; place where project is located	Comparison with market indices (over- or under-performance).	Instantaneous and comparable profitability in a globalised, financialised channel
Risk	Industrial or technological risk or one linked to market for goods and services	Linked to where project takes place	Can be given a probability and be reduced through diversification among asset classes and between countries where trends are uncorrelated	Creating an area mix with uncorrelated patterns and trends and which is financialised
Liquidity	High transaction costs. Difficult to assess prices of transaction prices	Requirement for physical proximity, long process	Continuously defined/worked out price, low and known transaction costs.	Instant mobility over long distance by centralised and IT-intensive financial markets.

Source: Own framework

3.4.2. Limits to constructing comparability and liquidity

Can the indirect investment channel really transcend compartmentalised property markets so that investors can make investments independent of specific local circumstances, thus making property investment management liquid?

A. Restriction of liquidity in real property markets

Buying, selling or constructing property is by no means straightforward. Choosing a building requires specific technical and financial skills. Regardless of whether these activities are conducted in-house by the pension fund or passed over to a collective institution, it is important that the right choice is made so that the building can be fully let and can provide the

required return. While the price at the time of a sale depends on economic conditions (supply and demand), the buildings themselves are heterogeneous on account of various characteristics associated with their nature and location. It is difficult to compare a property located in Geneva with one in Glaris, or even between properties in the same town or city; or indeed ones in the same locality. The property market has strong regional and local characteristics which give it a fragmented nature. It is, furthermore, a market based on mutual agreement, where research and feasibility study costs, along with transaction costs, are very high.

Within a framework where collective investment institutions act as both investors and proprietors, the anticipated return on a building arises from the rental income it generates. This means that the purchase and construction of property is seen within a long-term perspective, even though, by their nature, some property investment vehicles (property companies or property funds) engage in property speculation within the commercial sector. Consequently, the various levels of property deals have to conform to current standards (building, development and planning, legislation in area like lease rights etc.). If standards in areas like taxation (transfer tax) are added to the picture, the result is that only very limited liquidity within the market is possible and that real returns cannot be moulded at will. Given the real difficulties surrounding property deals, collective institutions equally behave in the same *buy and hold* manner as pension funds acting as investors and managers (and for which they have been criticised). The financialisation of real property thus turns out to be not as easy to achieve as was anticipated. Furthermore, as discussed below, property-related financial markets are still under-developed in Switzerland.

B. Restrictions on financial markets' liquidity

Funds have two options. First, they can choose to invest through financial markets, which because of their liquidity, are supposed to enable an active management strategy to be pursued (the *buy and manage* approach). Alternatively, they can take up their allotted shares in investment foundations. In the first instance, it remains the case that the Swiss market is still restricted.[27] In the second case, the main advantage of unquoted investment vehicles, namely their ability to avoid the irrationalities of the market (Crédit Suisse, 2003: 40), is cancelled out by their lack of liquidity. Indeed, entry and exit can be even more problematic given that there is no secondary market.[28] In this case the investor faces a whole set of drawbacks; those arising from financial markets and those linked to real property markets.

C. Restrictions linked to the territorial representation of financial players

The other advantage of the indirect channel, namely better risk management through portfolio diversification, as a way of getting round the lack of geographical diversification of pension funds' direct investments does not also stand up to empirical scrutiny (Figure 3). It was seen that certain areas and certain types of allocation were favoured when investments passed

[27] The stock market value of property securities only represented less than 1.5% of shares in the Swiss Performance Index (SFr1257bn at the end of 2000). The same proportion only accounts for around 1% of the total Swiss property market (Bender *et al*., 2001)

[28] Firstly, the investor can sell their holdings by finding a buyer. It goes without saying that conditions of sale and the directly-negotiated market price depends on economic conditions. Secondly, shares held by the investor can be bought back by the investment foundation. This purchase is made at book value and the process is fairly long as it depends on giving several months' notice before the end of the current year. The delay can be even longer if the amounts being bought back are significant. Furthermore, there is a sales commission for the transaction (Crédit Suisse, 2003).

through financialised channels. Thus, whether one is banking on long-term returns through rents or short-term returns through realising capital gains, the picture painted by collective-type investment instruments is a territorially-targeted one which is focused on the country's main urban areas. However, according to portfolio diversification theory, shouldn't there then be greater diversity in terms of areas and allocations? Investments made in peripheral regions or sectors like tourism can be wholly justified and be in line with the theory because non-systematic risk can be offset by the systematic risk linked to the entire portfolio. The investments of various collective investment vehicles are based on financial market criteria. So is it only the case that the country's urban areas, particularly the metropolitan areas of Basel, Berne, Geneva, Lausanne and Zurich, are the only ones able to meet the conditions of the criteria and to offer advantageous returns at a low risk? There is nothing to say that this is the case.

In short, it can be said that institutions within the indirect investment channel are acting in the same way as directly-investing pension funds. The only notable exception being that the relevant areas considered for investment are the country's main urban areas, or the ones close to financial players (as opposed to areas that are close to the pension funds).

4. Conclusion: the financialisation of the property sector

At a theoretical level, the argument put forward was concerned with the relations between the financialisation of the economy and spatial organisation and development. Financialisation enables projects, players and spaces to be compared, but it makes the relationship between the holders of capital and the real investor distant and opaque. Financialisation centralises the management of the economy in a number of financial centres and favours the concentration of investment in major cities. Finally, it standardises management criteria and places them in a hierarchy. As a result, certain real economy criteria, such as the technical specificity of investments, their location and, more generally, their characteristics, are no longer considered as being relevant. The result is a *homogenisation* of the economic development process, which militates against innovation and decentralisation (Crevoisier, 1999); both of which are, by definition, underpinned by a notion of differentiation. Indeed, the finance industry develops through favouring the integration of space (the abolition of borders), standardising the way projects and areas are analysed and, lastly, through different areas (national and international) having identical legislation. By finance, we mean the institutions that allow investments to be disconnected from investors by making the two remote from each other in a way that means that the investor's choice is solely determined by risk and return in the financial sense of the terms. Finance is the whole set of conventions which makes it possible for financial capital (as opposed to real capital) to be mobile (or "liquid", as financiers would say) in the short-term and over long distances. The finance industry is to capital what the transport industry is to people and goods: it unifies markets, makes products comparable and, as a result, increases competition while enabling economies of scale and the centralisation or concentration of economic power to take place (Corpataux and Crevoisier, 2001).

The case study of the Swiss pension fund property sector shows that financialisation is not a phenomenon which affects the entire sector uniformly. It occurs at various rates and in different spaces. It also primarily attracts certain players (the smallest funds and more recently the biggest funds which are close to the financial community), it invests in particular types of property (large residential and potentially commercial properties) which are situated in the country's three or four biggest urban centres.

But there are also limits on how far financialisation can go because of the particularities of the Swiss property sector and the institutions working within it. In the property sector, high transaction costs (which cannot be put down to the tax system!) mean that owners are forced to keep their properties over a long period and to take a long-term view in estimating real returns. In a sector where rents only move slowly, and where costs are primarily financial, it is difficult to achieve rapid increases in income or cost reductions as a response to the wishes of financial markets. It is equally difficult to overcome the opaque nature of local markets, where players hold on to information and where highly specific local laws and regulations continue to remain.

Since 1985, when the second pillar of Switzerland's so-called three-pillar retirement provision system was established, the amount at the disposal of pension funds has grown significantly. Property investment has followed suit, but to a lesser degree. Today, property investment has become attractive again because of the fall in share values at the start of 2000. Not only are the returns on property no longer considered as being poor, but property is increasingly being associated with the virtues of diversification (again along the lines of portfolio theory) as there tends to be a low correlation between property investments and other classes of assets.

With regard to this last point, the watchword is caution. Indeed, we have seen the extent to which investments are highly concentrated geographically. In this sense, it may be feared that pension funds are intensifying a property bubble, in the same way as they contributed to the rise in the stock market in the 1990s by investing considerable amounts in shares... and the property sector that would be affected by such a bubble is one with an extremely narrow range.

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