**Dynamics of Commercial Real Estate Asset Markets,
Return Volatility, and the Investment Horizon**

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Abstract

We compare the term structures of return volatility for UK and US direct and securitized commercial real estate using vector autoregressions. For the UK market, we find that direct real estate and property shares exhibit strong mean reversion, and unexpected returns are primarily driven by news about discount rates. In contrast, US direct real estate shows a strong mean aversion effect over short investment horizons, after which the term structure of the annualized volatility remains relatively flat. The low short-term standard deviation and the mean aversion of US direct real estate returns can be explained by the positive correlation between cash-flow and discount rate news, which can be interpreted as underreaction to cash-flow news. US REIT returns show slight or strong mean reversion in the medium and long term, depending on the data sample. UK direct real estate returns remain more predictable than property shares in the medium and long term, whereas US REIT returns appear to be equally predictable to direct real estate returns in the medium term.

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