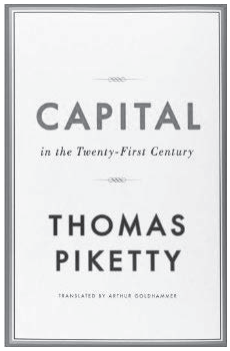
Capital in the 21st Century

by Thomas Piketty (© 2014, Harvard University Press, 696 pages)

REVIEWED BY MAHLON APGAR IV, CRE, FRICS



By the time readers have read this, *Capital in the 21st Century* will have become its publisher's most popular title ever. Author Thomas Piketty already has emerged from relative obscurity in the French Academy to become an international celebrity, and his main theme, "income inequality," is at the heart of the current political discourse in America and Europe.

Capital is heavy reading. With 577 pages of prose and 685 endnotes, readers must be seriously interested in the topic to even begin. It is, however, clearly and, at times, gracefully written, generally free of jargon, carefully targeted in its graphics, and mercifully modest in its math requirements. Though Piketty is an economist, not a historian, he has produced an economic history that may redefine him as well as economics itself. He deftly weaves social narratives and literary references into the text, enlivening the "dismal science" and increasing its accessibility for policymakers (and their commercial real estate advisors!). Analysts will appreciate his data-driven methodology and fact-based conclusions—even if they disagree with him.

Piketty's argument has clear implications for real estate professionals. He postulates that income inequality in contemporary market capitalism is structural and inevitable. His analysis shows that returns on financial capital and real property consistently exceed the returns on human capital, or productivity, by wide margins. This divergence leads to increasing concentrations of wealth, with concomitant political power that further insulates the wealthy. Capital markets, he observes, have no "self-correcting mechanism" to dilute wealth among those who can afford to save and invest; indeed, they are embedded with massive incentives that deepen the disparity.

About the Reviewer

Mahlon 'Sandy' Apgar IV, CRE, FRICS, *advises senior executives and boards of companies and governments on real estate strategy, development and operations. In consulting, public service, teaching and research, he positions real estate and infrastructure as strategic assets, combining public policy with innovative business practices and analytics.*

Apgar began his real estate career with the visionary developer, James W. Rouse. As a former partner of McKinsey & Company and the Boston Consulting Group, and founder of Apgar & Company, he has advised more than 150 corporate and government clients on over 500 projects in 13 countries.

President Clinton appointed Apgar as Assistant Secretary of the Army for Installations and Environment, with responsibility for the Army's global infrastructure and real estate portfolio. Apgar also led the design and launch of the award-winning Residential Communities Initiative.

Apgar has authored or co-authored more than 100 articles and cases, including a real estate set in the Harvard Business Review. His articles in Real Estate Issues received the Ballard Award, and he received the James Felt Award for Creative Counseling. His report on "Placemaking: Innovations in New Communities" will soon be e-published by the Royal Institution of Chartered Surveyors (RICS) and the Urban Land Institute (ULI). Apgar received a U.S. patent for a corporate portfolio evaluation system, known as the "Apgar Real Estate Score." He has taught at Harvard, Oxford, Princeton and Yale.

Apgar is vice chair of ULI's Public Development and Infrastructure Council and a ULI Foundation Governor. He was elected an "Eminent Fellow" of the Royal Institution of Chartered Surveyors. He holds a bachelor's degree in sociology from Dartmouth College and a master's degree in business administration from the Harvard Business School.

He further opines that the scale and growth of wealth in recent years is largely invisible to most people—and their leaders—until "Occupy Wall Street"-type events create periodic, though temporary, media storms. Yet, the public's fascination with celebrity billionaires and their baubles—including $50 million New York penthouses—obscures the reality that American capitalism's main

promise—"work hard, and you'll succeed"—has become virtually unattainable for many people.

Piketty is distinctive, if not unique, in highlighting real estate's role as a pillar of economic systems throughout history. He distinguishes land values from building values, while acknowledging the challenge of dissecting them, cites the inexorable shift in domestic holdings from land in agrarian economies to housing in urban economies, and prescribes the tradeoff between equity returns and leveraged returns that macroeconomists often miss. Readers may be surprised by the remarkable constancy of real estate returns from Antiquity through the Middle Ages and the Industrial Revolution to the present. They also may be intrigued by his "mystery of land values" and comparisons of returns from real estate and financial assets.

Despite more than 60 references to property and real estate, and his otherwise robust presentation, Piketty skims over two central issues facing our industry and profession. First, he does not deconstruct real estate's risk factors and assign premiums to each—assessments that often drive investors' decisions. He simply may have lacked the data, or he possibly may not fully appreciate the profound importance of real estate-specific risks. Second, he does not differentiate between value-based and fee-based returns. Thus, he fails to acknowledge the reality that most 21st century real estate business models are built on service and management fees, comparable to professional firms and certain production businesses, and are fueled by institutional and public capital; while their predecessors were founded on highly leveraged returns from property appreciation, with little personal equity at risk and only marginal fees from ancillary services. These failings do not undermine Piketty's conclusions, but they would be welcome clarifications if he ever writes a sequel.

Piketty's most controversial solution to the widening income gap is a global wealth tax, which even he admits is politically impractical, however morally justified and fiscally feasible. In this world of ever-increasing globalization, however, with 'big data' analytics and universal telecommunications diminishing the importance of geographic borders and organizational hierarchies, the simplicity of a single one to two percent flat tax eventually may override the wrangling over complicated country-by-country solutions. As readers reflect on the historic roots of Piketty's analysis, they may consider that taxation and national accounting systems developed during the French Revolution revealed theretofore obscure values of aristocrats' assets. Similarly today, governments are keenly interested in unveiling cross-border holdings of major corporations and the "one-percenters."

Piketty has illuminated the central issue in democratic capitalism: while enabling individuals to amass wealth, it has not produced a political calculus that directly benefits everyone without impeding entrepreneurial spirit, technological innovation and management prowess. Regrettably, he does not address the recent emergence of for-profit social benefit corporations, such as Patagonia and Warby Parker. These novel structures challenge the Friedman ideology that profit is the only social responsibility of business, which has dominated business management for the past 40 years. The benefit corporations appeal especially to Millennials who want to affiliate with socially responsible companies, and are proving—as have some visionary real estate developers—that private profit and public purpose are not only compatible but also synergistic. If further leveraged by wise government policies, benefit corporations could transform the behavior of 21st century capitalists, an outcome that one presumes Piketty would endorse.

The author's work accentuates the role and responsibility of real estate professionals to sharpen clients' thinking by dissecting the complex problems they face; sizing, sequencing and prioritizing analyses that improve their decision-making; isolating data and analytics that otherwise distract and may even obfuscate their decisions; and assessing societal as well as economic impacts in every project they undertake. As thought-leaders, real estate professionals often must be their clients' intellectual guides, whether or not they are so instructed. In another life, Piketty could have been a superb counselor of real estate.

Capital seems destined to become a classic with the standing of Smith's *Wealth of Nations* and Keynes' *General Theory*. The reasons have as much to do with its timing as its content. Whatever readers may think of its merits or shortcomings, they must in the end agree that Piketty and his tome are having outsized influence on policy and practice that few others can claim. Now, that's impact! ■