RE420 – Real Estate Finance and Investment

Fall 2018

Instructor: Nicholas Ordway, J.D., Ph.D.

Office Hours: Wednesday and Friday 12:00 - 1:00 pm and by appointment

Office: B-204a, College of Business Administration (This is in Suite B-201)

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Classroom meetings and times and place: Wednesday and Friday (1:30-2:45)

Catalog Description: Financial and investment techniques used to evaluate real property and real estate security investments.

Prerequisites: None

Student learning outcomes:

1. To understand the role of finance in the investment of real estate
2. To be able to understand the concept of real estate project feasibility.
3. To be able to describe primary and secondary mortgage market.
4. To differentiate various mortgage types and their financial implications.
5. To be able to describe the regulatory structure of real estate finance.
6. To understand mortgage underwriting and the loan application.
7. To be able to differentiate between solid real estate investments and “get rich quick” schemes.
8. To appreciate the importance of “ethics” in investment transactions

Additional Outcomes for Graduate Students:

9. To apply investment theory to case studies in order to distill key tactics and strategies in improving one’s analytical skills.
10. To utilize theory and analytical skills in using real-world data to determine market feasibility of a proposed real estate development.

Relation to “Institutional Learning Objectives for Undergraduate Students” (ILOs):

ILO 2a. Think critically and creatively: Elements applied in this course include – “being information literate – knowledge, procedures, processes, or products to discern bias and arrive at
reasoned conclusions”: “reasoning with numbers and other mathematical concepts (numeraacy)”.
and “developing financial literacy.”

ILO 2b. Conduct research: Elements applied in this course include - “using library and
information systems.” (Instructor’s note: particularly the Internet)

ILO 2c. Communicate and report: Elements applied in this course include – “written and oral
communication”. (Instructor’s note: short reports)

ILO 3a. Continuous learning and personal growth: Elements applied in this course include –
“ethical behaviors and judgments” and “habits of scholarly inquiry.”

Theory of the Course for graduate students: Real estate investments provide the basis for
personal long-term wealth and are an important asset class for corporate financial managers.
This class provides you with an overall framework for understanding real estate investment
theory. It uses Harvard case studies to distill key tactics and strategies in improving one’s
analytical investment skills. Students will apply theory and analytical skills to real-world data in
determining market feasibility of proposed real estate developments. The course identifies
techniques and processes that create synergistic value in real estate investments.

Textbooks:

(Hereinafter, Weidemer. Ch. _____).

David Crook. The Wall Street Journal Complete Real-Estate Investing Guidebook, Three Rivers
Press, 2006. (Hereinafter, Crook. Ch. _____).

Harvard Cases to be identified for Graduate Students based on numbers of students.

You will need a financial calculator.

Grading:

Undergraduates:

Homework Assignments (3 assignments) 21 points (plus up to 6 bonus points)

You must turn in all homework projects on date indicated in the schedule; Each project is worth
up to 7 points (not including possible bonus points): A = 7 points; B= 5 points; C=3 points. & D
= 1 point; Failing to turn in project = (- 5 points). Note: An outstanding homework assignment
can receive a bonus score of “2” additional points if student is called and shares answer with
class.

Test #1 30 points
Test #2 30 points
Final Exam 20 points

(Note: possible points are greater than 100)
Graduates:

1. Case or article presentations – 20 points
2. Test #1 - 15 points
3. Test #2 15 points
4. Feasibility Study – 35 points (5 points are based on peer reviews of your contribution to the study. On the last day of classes you need to turn in a memo to the instructor indicating the grade you deserve and the grade other members of your team earned in contributing to the study).
4. Group Project Presentation – 15 points (Will serve as Final Exam)

Grade-Score Equivalents:

A+ = 97 points +  
A  = 93 points +  
A- = 90 points +
B+ = 87 points +  
B  = 83 points +  
B- = 80 points +
C+ = 77 points +  
C  = 73 points +  
C- = 70 points +
D = 60 points
F = below 60

Class Policies:

1. You have a limited license to tape record lectures for your own personal use.
2. Generally any open time/date is available for appointments. Probably the best way to make appointments is by e-mail.
3. You are encouraged to use e-mail to ask questions. However, e-mail is not acceptable for turning in assignments. Grades will NOT be provided by e-mail or telephone. However this information is always available to you if you personally come to my office.
4. I tend not to answer my phone calls until a sufficient number of messages have group up (Time management). If you make a phone call – make sure you leave a message.
5. You are encouraged to meet with the professor outside of class if you need additional help understanding the concepts. Let me know by e-mail if you plan to come in so that the outer door can be opened (if necessary).
6. All assignments must be typed.
7. Unexcused late paper will suffer a penalty. Any excuses must be documented.
8. There are many handouts in class. If you are not present when these handout are given, you will need to make an appointment with the instructor to obtain the handout.
9. Try not to come to class late – Often the instructor provides valuable test tips during the first five minutes of class. These tips are not provided again during the test reviews which also start at the beginning of a class period.

10. If you are more than fifteen minutes late for a test, you may be required to take a make-up test at a later time or date. (This applies primarily for the Final Exam which is a multiple-choice test).

11. Academic Honesty: Because UHM is an academic community with high professional standards, its teaching, research, and service purposes are seriously disrupted and subverted by academic dishonesty. Such dishonesty includes cheating and plagiarism as defined below. Ignorance of these definitions will not provide an excuse for acts of academic dishonesty.

A. Cheating includes but is not limited to giving or receiving unauthorized assistance during an examination; obtaining unauthorized information about an examination before it is given; submitting another’s work as one’s own; using prohibited sources of information during an examination; fabricating or falsifying data in experiments and other research; altering the record of any grade; altering answers after an examination has been submitted; falsifying any official University record; or misrepresenting facts in order to obtain exemptions from course requirements.

B. Plagiarism includes but is not limited to submitting, in fulfillment of an academic requirement, any work that has been copied in whole or in part from another individual’s work without attributing that borrowed portion to the individual; neglecting to identify as a quotation another’s idea and particular phrasing that was not assimilated into the student’s language and style or paraphrasing a passage so that the reader is misled as to the source; or submitting the same written or oral or artistic material in more than one course without obtaining authorization from the instructor involved.

12. Service to Students with Disabilities: If you are a students with a physical and/or mental disability, you are encouraged to contact the Kokua Program (956-7511) on the ground floor of the new Student Services Center.

SCHEDULE

Caveat: Minor changes may be made in the schedule as the semester progresses. Graduate student case presentations will be scheduled if needed.

**Session 1 (W - Aug. 22) -** Introduction. course objectives: So You Want to be a Millionaire. Crook, Ch. – “Introduction”.

**Session 2 (F - Aug. 24) -** Real estate investment decision stages – (attached to syllabus). Presentation: “Time Value of Money – Foundation for Real Estate Investment Analysis.”

**Sessions 3 (W- Aug. 29) -** Stage One – Organization (real estate investment decision stages).

Session 5 (W- Set. 5) - The players – class handout; “Getting in on the Ground Floor”, Crook Ch. 2.

Homework #1: Homework Assignment One: Prepare a report on the nature of Hawaiʻi’s real estate economy. Be sure to use the Internet for some of your information); (Note: You can do this project individually or create groups of up to 4 people. Group will turn in one report with all names of participants). Note: All other assignments are individual efforts. Assignment due Sept. 26.

Session 6 (F-Sept. 7) -Stage Three - Screen Alternatives AND Stage four – Select Probable Choice (real estate investment decision stages).

Session 7(W- Sept. 12) – Real Estate Feasibility Analysis – class handout.

Session 8 (F – Sept. 14) – Feasibility analysis continued

Session 9 (W – Sept. 19) – Walt Disney Case

Session 10 (F – Sept. 21) – Walt Disney Case continued.


Session 13 (W – Oct 3) - Real Estate on Wall Street. Crook. Ch. 9; discussion of Assignment #1.

Session 14 (F- Oct. 5) – TEST #1.

Homework #2: Take any commercial market at any location in Hawaii and identify those supply and demand factors that make it possible for real estate projects in that market to succeed. Be sure to define the geographic nature of the market (trade area). Assignment due Oct. 24


Homework #3: Make a list of “due diligence” considerations that are applicable to your subject property, particularly those that are applicable to Hawaii properties. Explain why these considerations may be important. Due ________

Assignment #2 is due.


Session 21 (W- Oct. 31) – Trump New York case studies

Session 22 (F – Nov. 2) – Continued: Comment on Stage Ten. Review for Test # 2.

Session 23 (W - Nov. 7) – Test #2.

Session 24 (F - Nov. 9) – Other Financing Practices. Weidemer, Chapter 13. Comments by instructor on Stages 8, 9 and 10; “Front Door, Back Door” approach to project pricing- class handout. Assignment #3 is due.

Session 25 – (W – Nov. 14) Discussion of Assignment #3:

(Wednesday Nov. 21) – No formal class. Classroom will remain open for groups to meet and finalize their projects and presentations.

(Friday Nov. 23) – Non-Instruction day because of Thanksgiving break

Session 27  W - (Nov. 28)  – Feasibility Report Due and Presentations.

Session 28 (F – Nov. 30) - Presentations, continued. Discussion about what was learned in this course; case presentations, etc.

Session 29  (W - Dec. 5) – Review for Final exam for undergraduates. Return of Feasibility Reports and any final presentations for graduates.

Monday December 10 – Final exam for undergraduates. 2:15 – 4:15 pm.
REAL ESTATE INVESTMENT DECISION STAGES

Stage One - ORGANIZATION:
- Investment Philosophy
- Business Objectives
- Entity Selection
- Internal Team
- External Human Support Group

Stage Two - INVESTMENT ENVIRONMENT
- General Economic Conditions
- Cycle Considerations
- Market Opportunities and Constraints
- Government and Political Issues
- Infrastructure Support
- Physical Environmental Conditions

Stage Three - SCREEN ALTERNATIVES
- Evaluation Criteria
- Establish Priorities and Tradeoffs
- Consider Sustainability Issues
- Target Markets
- Target Investor Partners
- Search Procedure

Stage Four - SELECT PROBABLE CHOICE
- Determine Type of Development
- Establish Pricing Range
- Find Sites Meeting Criteria
- Select Negotiation Strategy
- Do Preliminary Feasibility Analysis
- Analyze Financing Alternatives
- Negotiate Basic Contract Terms

Check for Consistency With Stage 3
Stage Five – DUE DILIGENCE
- Physical Inspection
- Phase I Environmental Assessment
- Examine All Leases and Contracts
- Analyze Public Sector Risks
- Validate Market Assumptions
- Identify Insurable Risks
- Determine Uncertainty Areas
- Anticipate Probable Litigation Risks
- Identify Value-Added Opportunities
- Apply Discounted Cash Flow Models
- & Ratios

Stage Six – STRUCTURE THE TRANSACTION
- Negotiate or Renegotiate Final Terms
- Negotiate Government Concessions
- Finalize Financing & Lender Covenants/Conditions
- Structure to Maximize Tax Benefits
- Risk Assessment and Acquire Appropriate Insurance
- Negotiate Asset Management Contract

Stage Seven – CLOSING AND ACQUISITION
- Finalize All Contracts
- Hire Property/Asset Management Team
- Closing and Punch List
- Resolve Conflicts
- Grand Opening/Brand Positioning
- Reinforcing Tenant Relations
Stage Eight – OPERATIONS
• Stabilize Operations
• Vesting of Public Entitlements
• Identify and Correct Physical Defects
• Value Engineering
• Periodic Asset Reviews
• Monitor Market and Competition

Stage Nine – MODIFICATIONS
• Physical Changes (Renovation)
• Market Repositioning
• Tenant Mix Adjustments
• Refinancing
• Seek New Government Concessions

Stage Ten – END GAME CONSIDERATIONS
• Portfolio Balancing
• Major Capital Modifications
• Disposition (Sale-Leaseback, Exchanges, etc.)
• Buying Out Partners or Other Internal Restructuring
• Reinvestment in New Project
• Creative Bankruptcy

Review Stage 2
Go Back to Stage 3
Real Estate Activity Framework
Figure 3
Model to Estimate Maximum Project Price
Figure 4
Stage Three: After Tax Analysis
FIGURE 2: THE REAL ESTATE BUSINESS MODEL

Emerging Business Models

Market (customers/competitors)

- Land
- Improvements
- Leases/Management Contracts
- User Enterprises
- Redevelopment Options
- Exit Options

Risks

Linkages

Strategic Values

Synergy Principles

Alternate Combination Scenarios