

The Political Philosophy and Economy of Commercial Real Estate Investment

Prepared for

Bay Area Council / USC Lusk Center for
Real Estate Students

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Introduction

- Requirements for efficient real estate and securities capital markets.
-

"Efficient real estate and securities capital markets require strong public and private sector cooperation, disclosure of government and corporate financial conditions, and institutional and individual investor confidence in financial and political institutions"

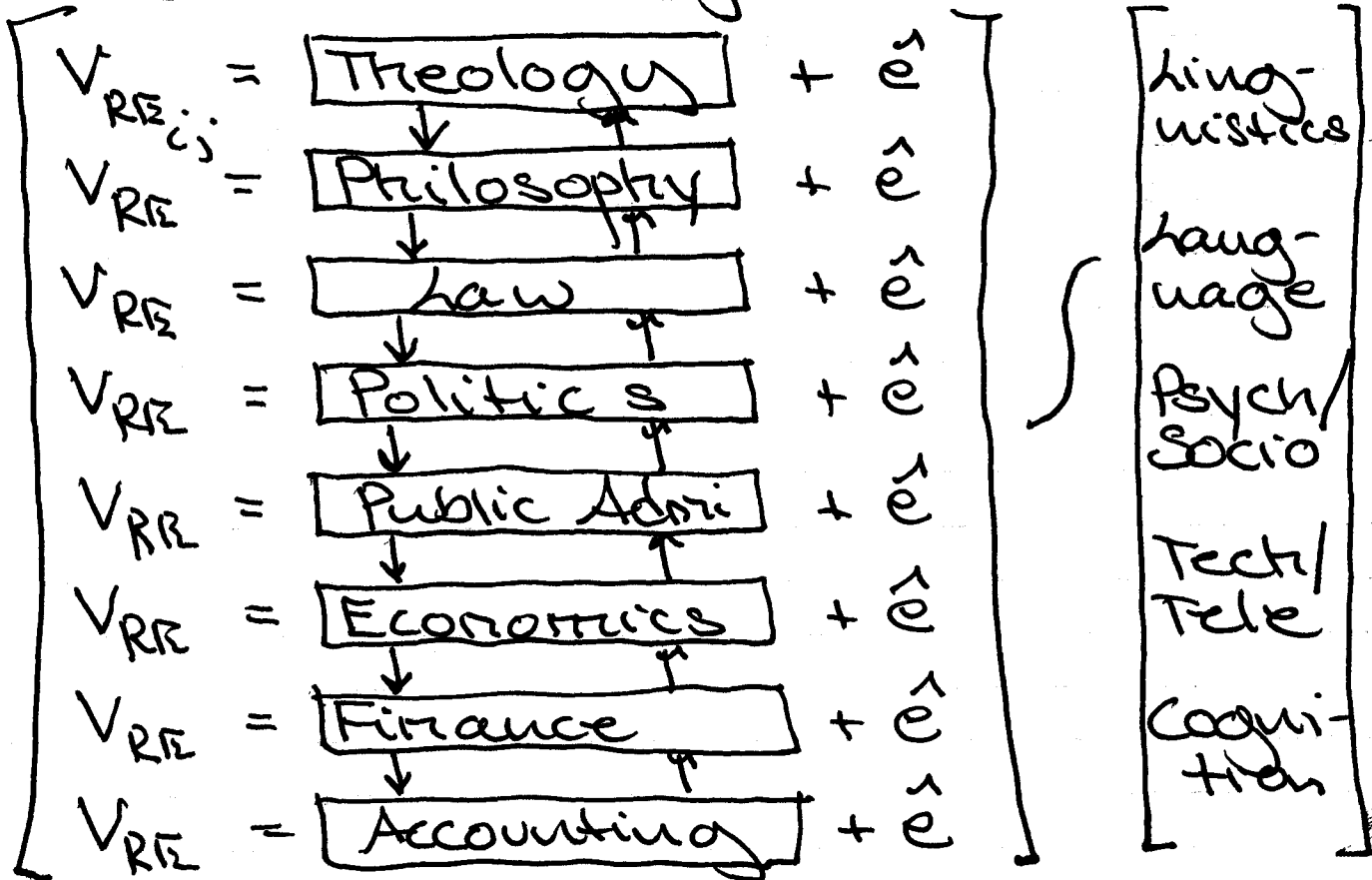
"Efficient security markets require a strong macro-economic infrastructure based on the enforcement of private property rights"

"Efficient real estate markets require a strong financial and legal system based on the enforcement of private property rights and land-use regulation."

" Efficient real estate
and security markets
require strong instit-
utional investor in-
terest, based on clearly
defined risks and rewards. "

- Table # 1 :

Nomenclature of Knowledge



- Indep. Varis.
- 50 +
- Factorial

! Solve simultaneous equation for value of real estate (stocks/bonds)

Institutional Analysis

Diagram #1:

* Hegelian Dialectic *

- George Hegel (1770-1831)
Friedrich Wilhelm

Synthesis →

- Democratic
- Capitalism
- Socialism

Conflict / Revolution

Thesis

- Church / State
- Feudalism / Aristocracy
- Communism

Antithesis

- Globalization
- Bourgeoisie
- Merchantism

Revolutions

- American
- Russian
- French

Diagram #2

* Modern Application *

Woodrow Wilsonian / Max Weber Scientific Management

Neo-Keynesian

Thesis / Synthesis

Thesis / Synthesis

20yrs • Capital Mkt
• Free Hand

50yrs • Devaluation

Anti Thesis

- Neo-liberal
- Monetarism
- Neo-Classical (Friedman)

500 years war / Revolution

WWI / II

Thesis

- Autocracy • fascist
- Authoritarian
- Dictatorship

10yrs

Anti Thesis

- Democratic / Capitalism (FDR)

Post-Modern Philosophical Thought

Pluralism / Democratic Institutional Deconstruction

Bill of Rights

Constitutional Rights

Amendments to Constitution

- Media Censorship
- Reporter Incarceration
- Evesdropping / Wiretapping
- Private Affairs / Legal Systems
- Due Process / Habeas Corpus
- Privatization Public Property / Goods
- Environmental and Food Supply Protection / Inspections
- Individual Rights (Abortion / Contraceptives)
- Separation Church and State (Intelligent Design) Church / Charities
- Political Philosophy / Political Ideology

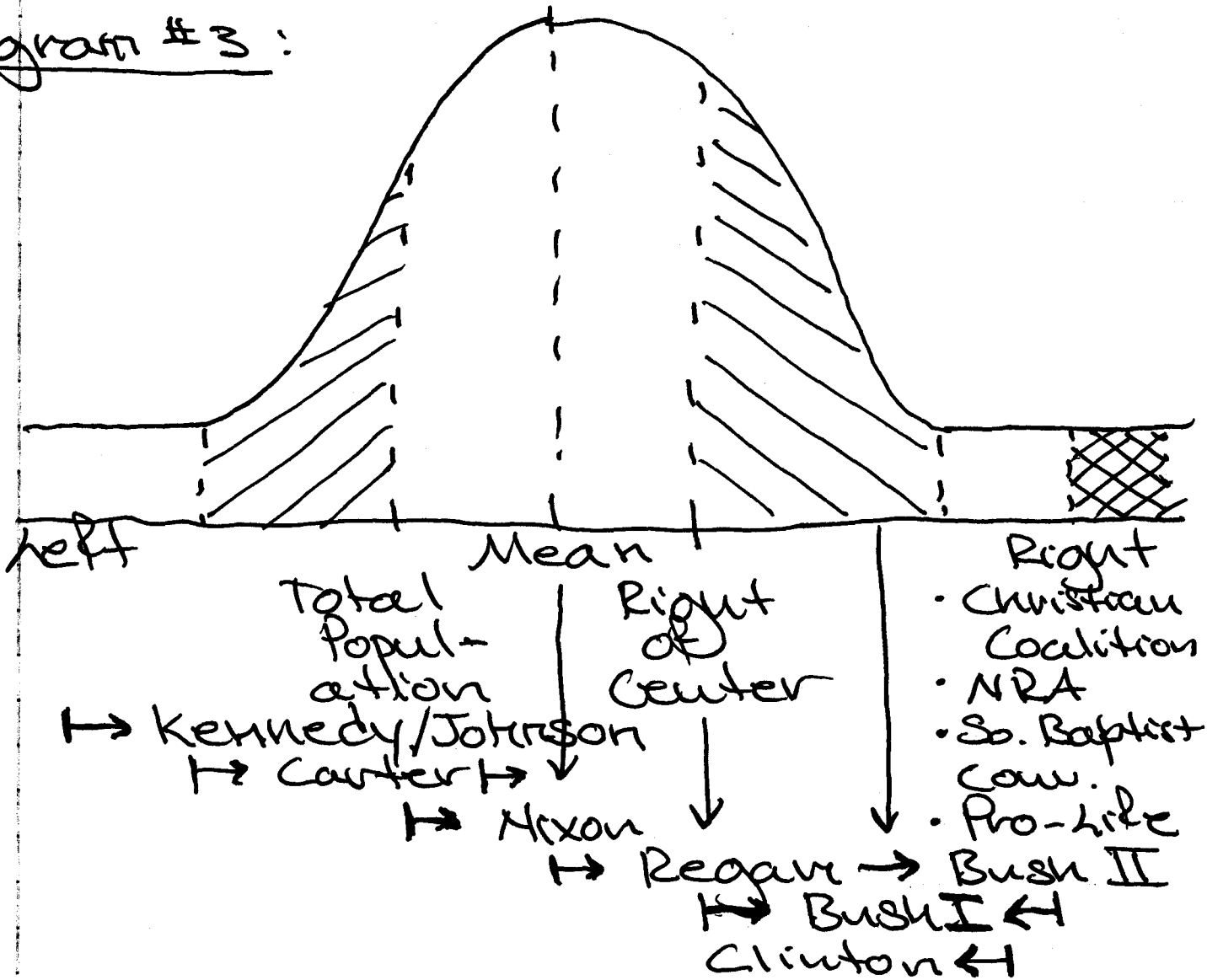
Outcomes

- Linguistic Extremes (Binary)
- Coognitive Symbols / Images
- Mythology / Culture
- Psychology / Sociology
- Actions / Behavior

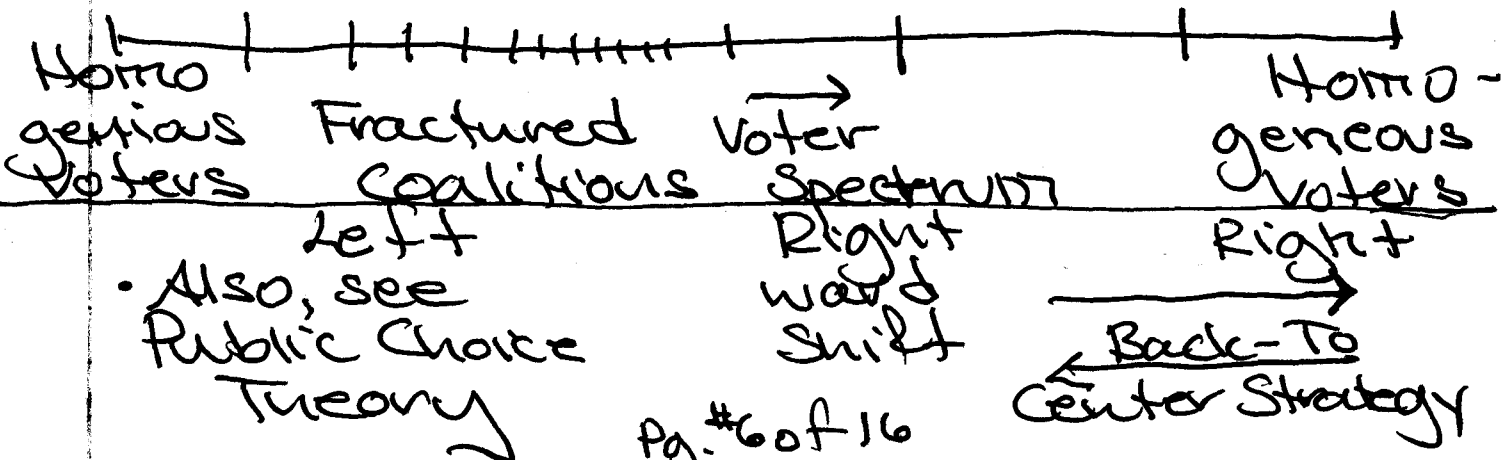
Public Choice Theory

* Mean-Voter Theorem *

Diagram #3:



Obama ←



Also, see Public Choice Theory

Economic Policy and Administration

* Obama Econ. Cabinet :

- o Peter Orszag
 - White House Budget Chief
 - was Dir. Cong. Bud. Off
- o Christina Romer (UCB)
 - Chair - White House Council of Economic Advisors
- o Timothy Geithner
 - Sec. of Treas.
 - was CEO Fed. Res. Bank NY
 - Clinton Admin.
- o Lawrence Summers/Robert Rubin
 - Top White House Econ. Advisor
 - Head Nat. Econ. Council
 - was former Treas. Sec.
 - Pres. Harvard Univ.
- o Paul Volker (BI) :
 - former Fed Chair Early 1980s
 - Chair New Panel (Econ. Sec. unity)
 - Advis. Pres. on how to stabilize. fin. mkts., nav. recession

- Bill Richardson - Gov. NM
 - Commerce Dept. Sec.
 - Former U.N. Ambassador
 - Energy Sec.
 - Pres. cand.
 - Hispanic

Institutions/Ideology

<u>Keynesian</u>	<u>Friedman</u>
<ul style="list-style-type: none"> • <u>Neo-New Deal</u> • Wage/Labor • Infrastructure • Technology • Institutions • Equity/Utilitarian • Production/Mfg. • Domestic Comp. Adv.s • Full Employ. • Indiv. Rights • Industrial Policy • Budget Surpl. • Fiscal Poly. • Public Goods 	<ul style="list-style-type: none"> • <u>Market Fundamentalism</u> • Capital • Interest • Markets • Bubbles • Distribution • Finance • Services • Global Comp. Adv.s • Inflation • Prop. Rights • Mkt. Failure • Budget Def. • Mon. Poly.
* Progressive Democrats	* New Democrats

Financial Institutional Analysis + Policy Rec.

Financial Statement Analysis Balance Sheet

Assets

Liabilities + Equity

	Yr. 0x'		Yr. 0x'
Cash + Due	xxx	Trans. Depos.	x,xxx
U.S. T-Bills	xxx	Sav. Depos.	xxx
Res. Mtg. Bk. Sec.	xxx	MM Depos.	xxx
Com. Mtg. Bk. Sec.	xxx	CDs > 100k	x,xxx
Munic. Sec.	xxx	Jumbo CDs	x,xxx
Tot. Sec.s.	x,xxx	Other Liab.	xx
Fed. Fuds. Std.	xxx	Tot. Liabs	xx,xxx
Gross Res./Com Bus.	x,xxx	Stkholders Eq.	x,xxx
- Lu. Loss Res.	xx	Capital/	
Net. Bus.	x,xxx	Pre. Stk.	
Fixed Assets	xxx	Resrvs./Loss	
Tot. Assets	xx,xxx	Tot. Liab + Eq.	xx,xxx

Note: Off Balance Sheet Items (SWAPS/CDs/Per)

Income Statement

Yr. 0x'

Txbl. Int. Inc.		Pre. Lu. Losses	xxx
U.S. T-Bills	x,xxx		
Fed. Fuds. Std.	xx		
Loans	x,xxx	Non-Int. Net. Inc.	x,xxx
Tot. Int. Inc.	x,xxx		
Int. Exp.		EBT	xxx
Trans/Depo	xxx	TX	xx
Sav. Depo	xxx	Muni Int. Inc.	xxx
CDs	x,xxx	Net. Inc.	xxx
MM Depo	xxx		
Tot. Int. Exp.	x,xxx		

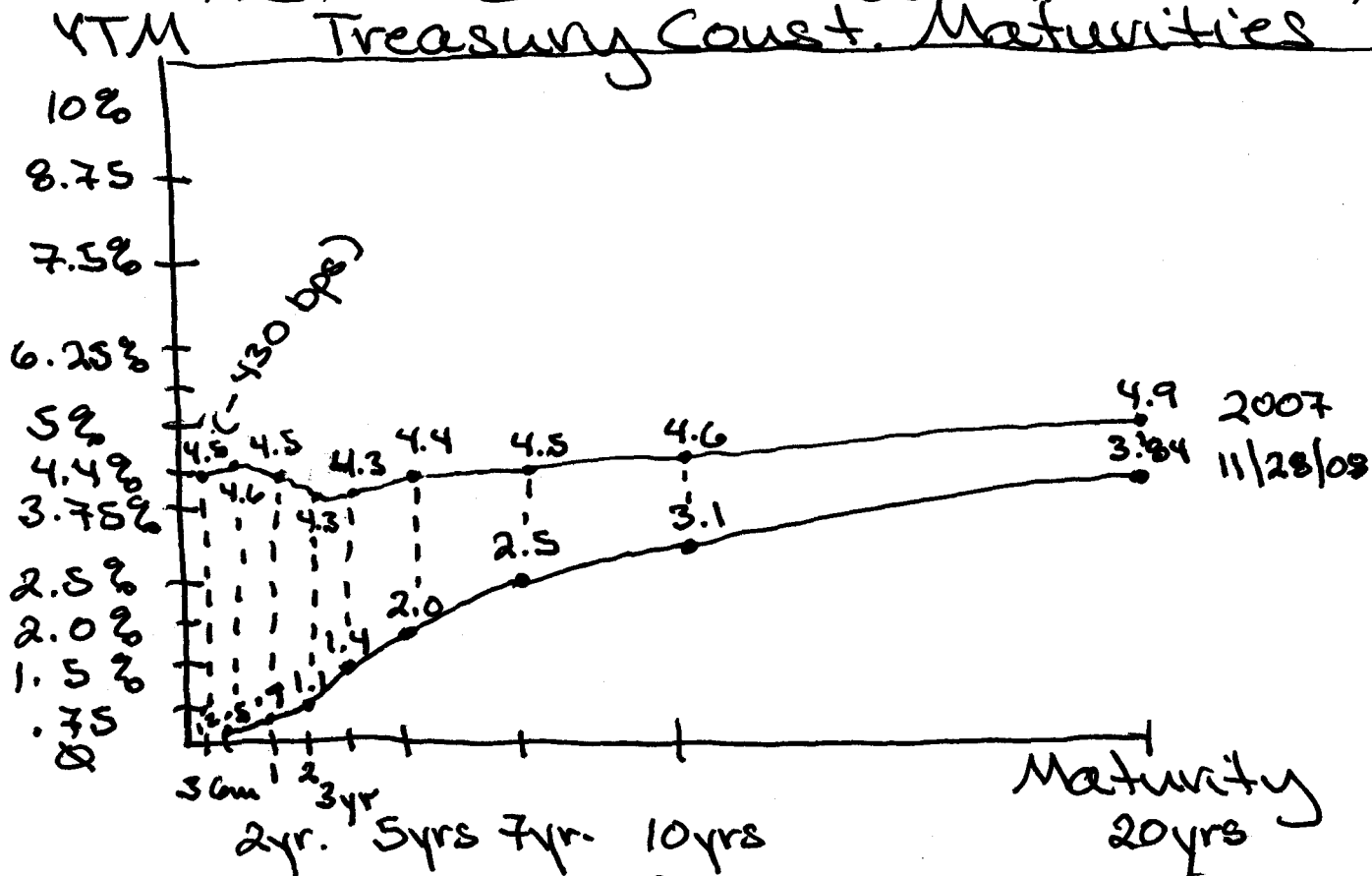
Yield Curve Analysis

"All debt and equity securities are priced off of the yield curve."

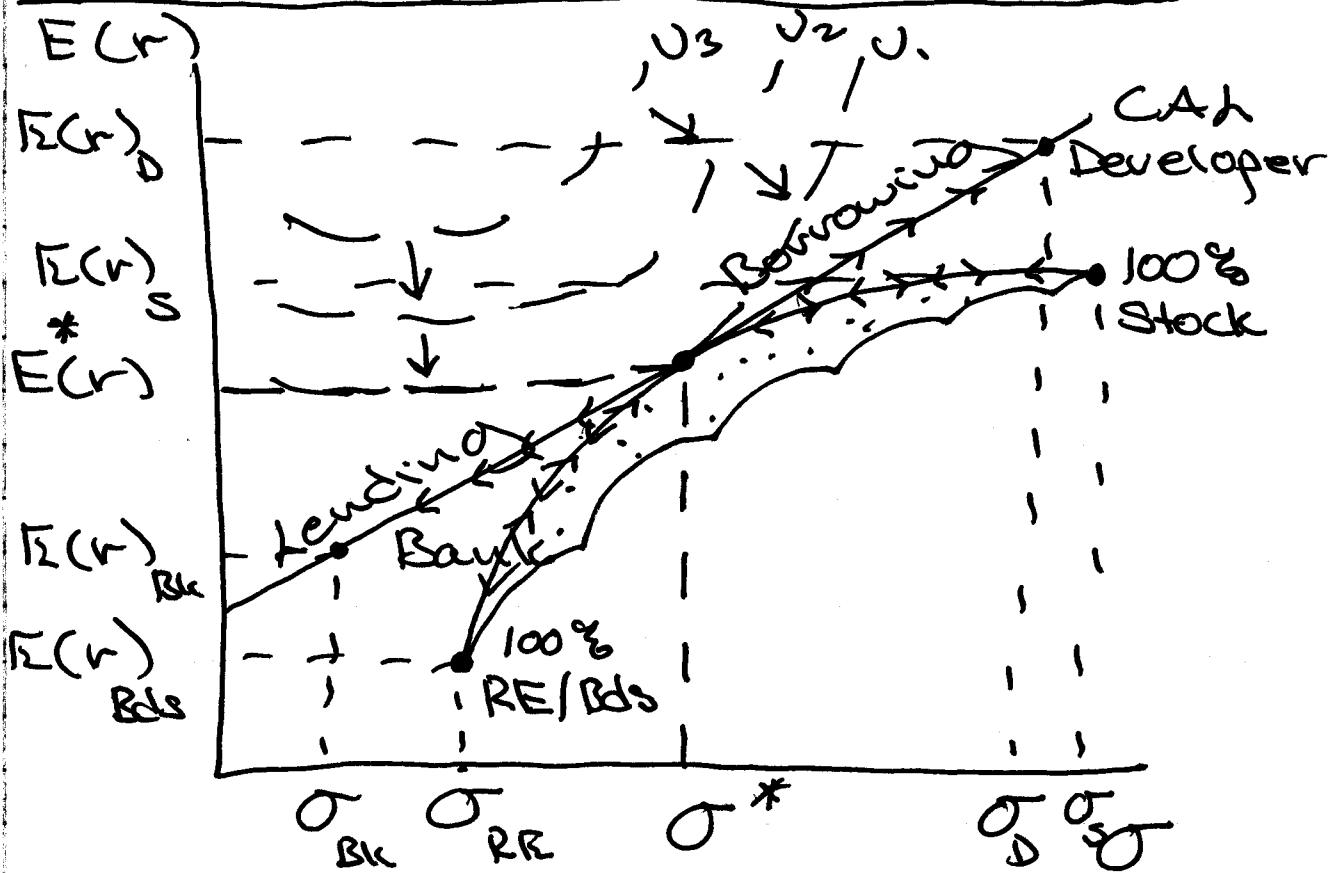
Fisher Equation

$$\downarrow \uparrow C_n = \bar{C}_{Real} + e_{Infl.}^* \uparrow \downarrow$$

Term Struct. Expectations (Pure) Mkt. (Infl.)
 • Liquidity Preference (Prem)
 • Market Segmentation (S/D)
 • Preferred Habitat (Duration)
 Treasury Const. Maturities



Modern Real Estate Portfolio Theory (MREPT)



$$\therefore E(r) = c_c = r_f + \beta(r_m - r_f)$$

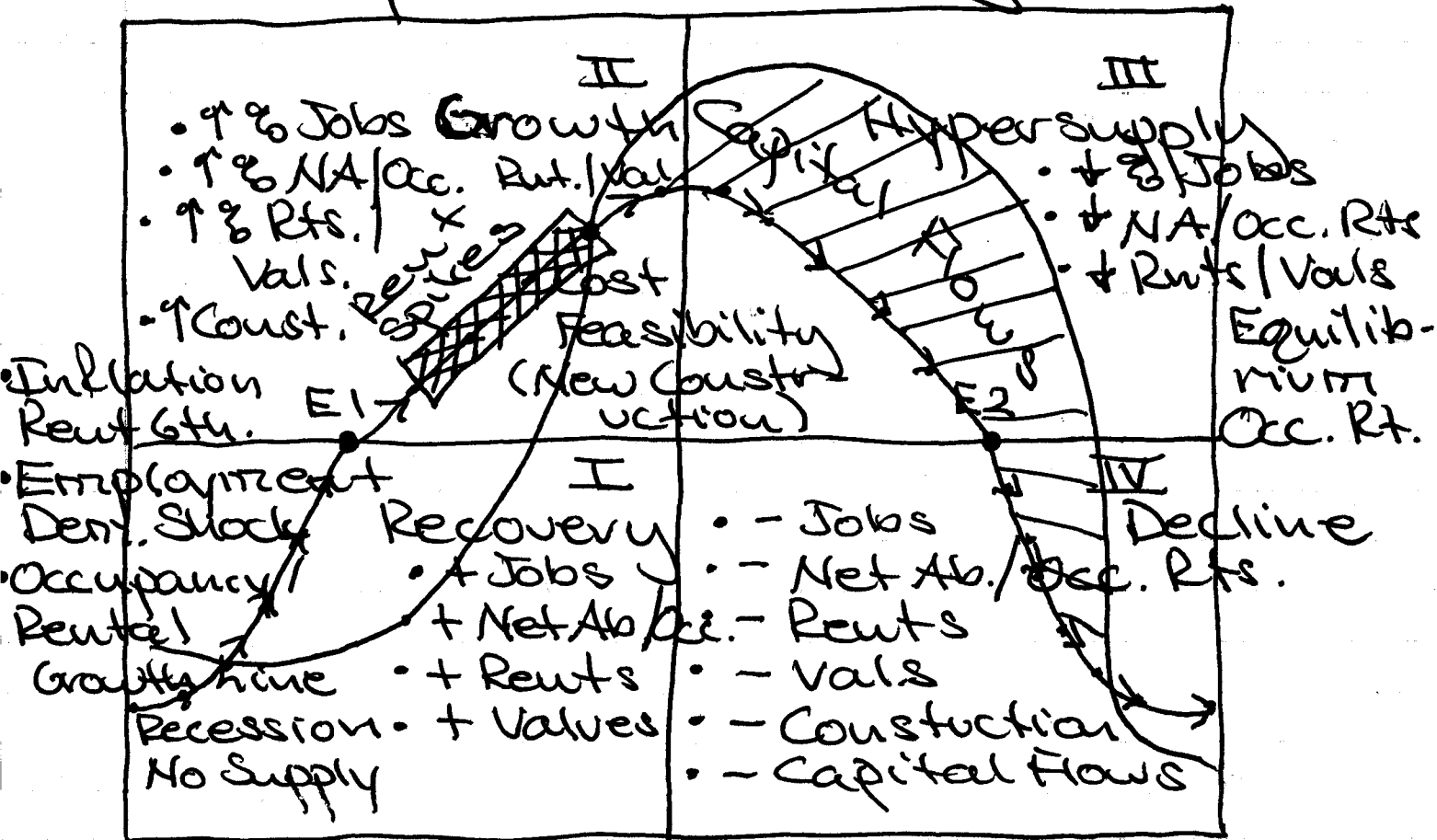
$$\therefore V_{RE} = \frac{NOI}{c_c} \quad c_{RE} = \frac{NOI}{V}$$

$$\therefore PV_{RE} = \sum \frac{NOI(1+g)^n}{(1+c_c)^n} + \frac{NOI(1+g)^{n+1}}{c_{TC}(1+c_c)^n}$$

$$\therefore C_{Risk Adj.} = \frac{Ret. Risk}{\uparrow Max Ratio} = \frac{E(r)_p}{\sigma^*} = \frac{1.5}{1.0} = 1.5$$

Note: Units Return for Unit Risk. $\rho_{0*} = 1.0$
 $\rho_{0*} = 0.5$

Commercial Real Estate Cycle Theory

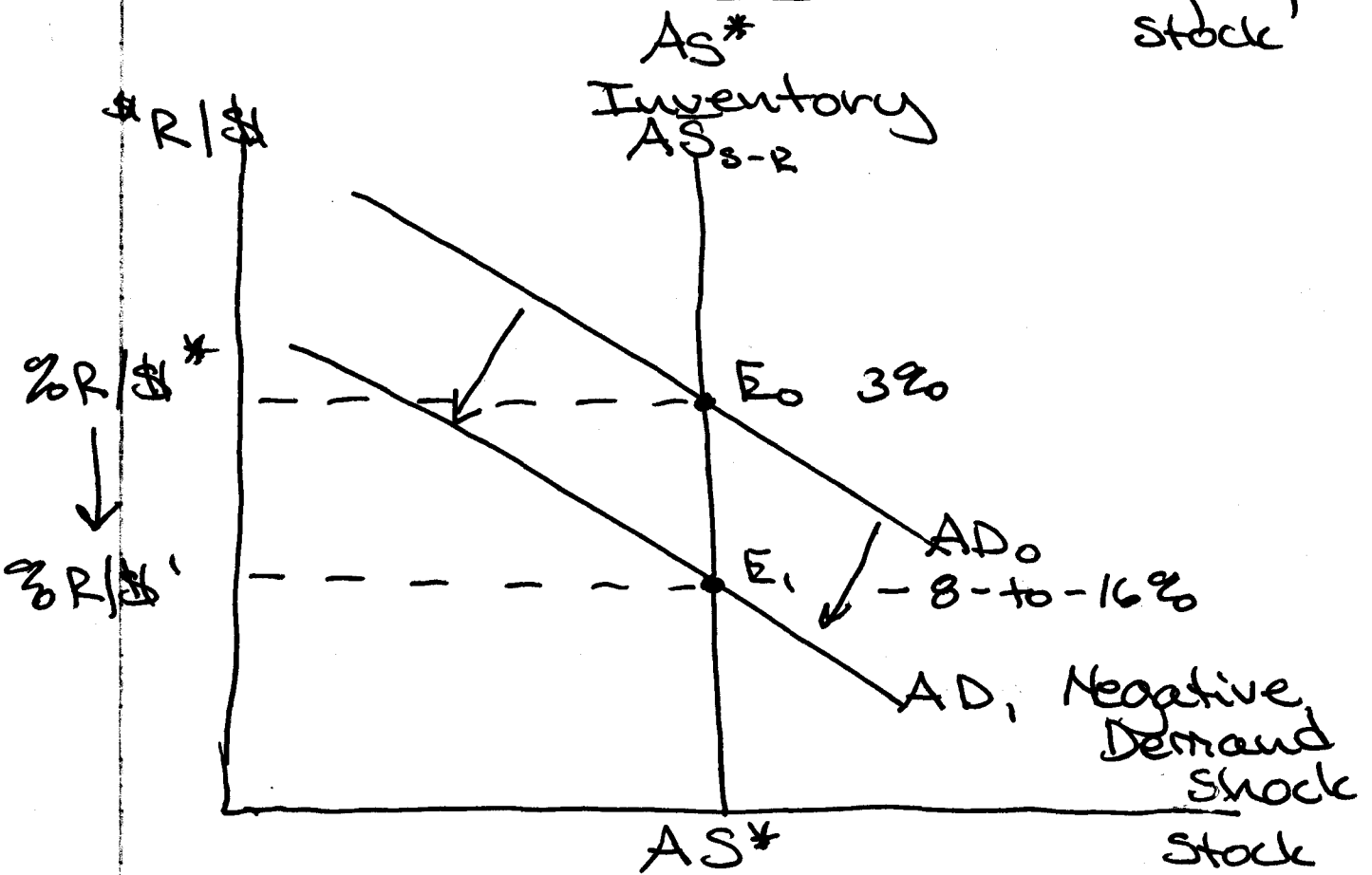
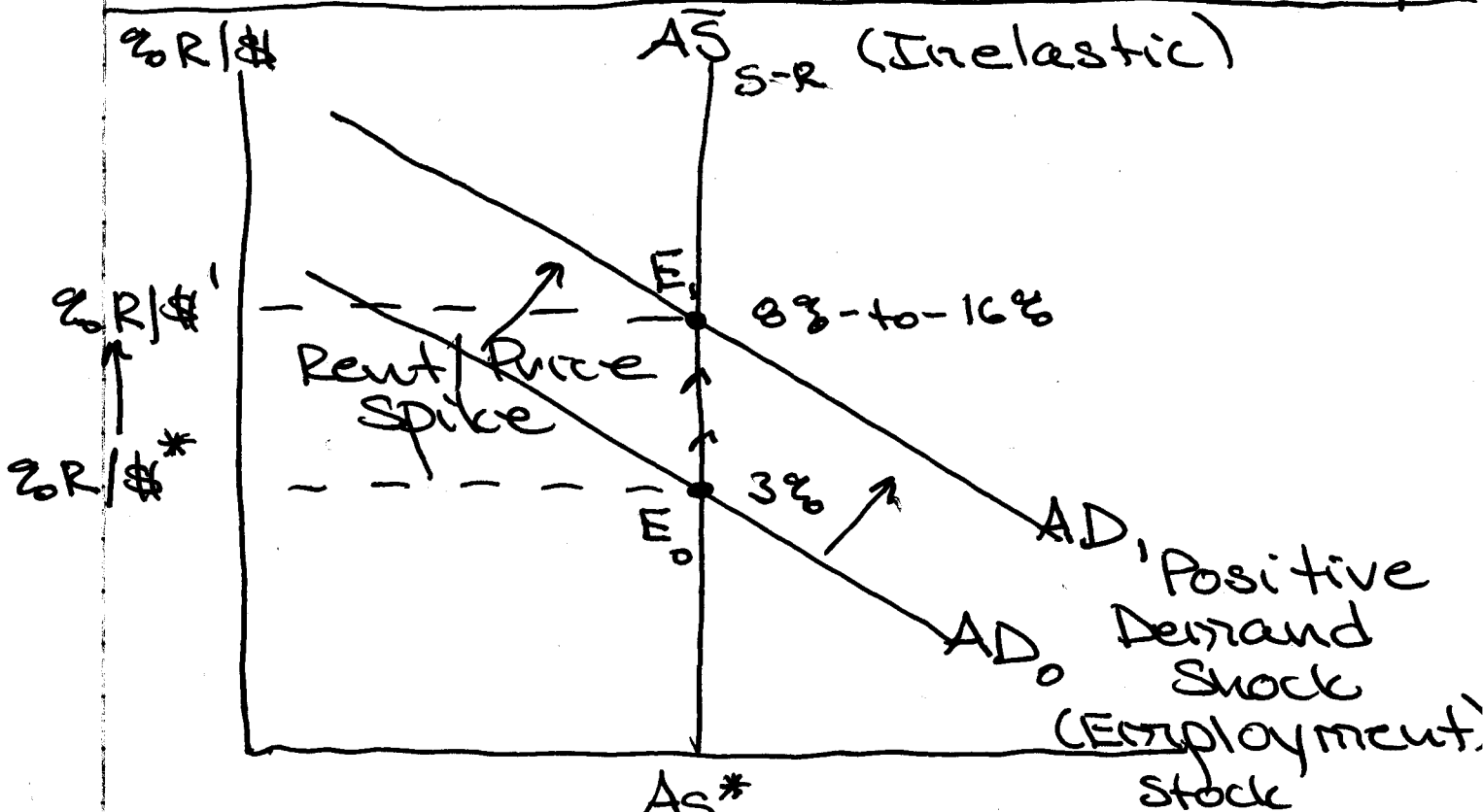


- Plot along line:
 - Property Sector / Type
 - Geography
 - US / Global
 - Region / State
 - MSA / USA
 - County / City
 - Submarket
 - Neighborhood
 - Census Tract / Block

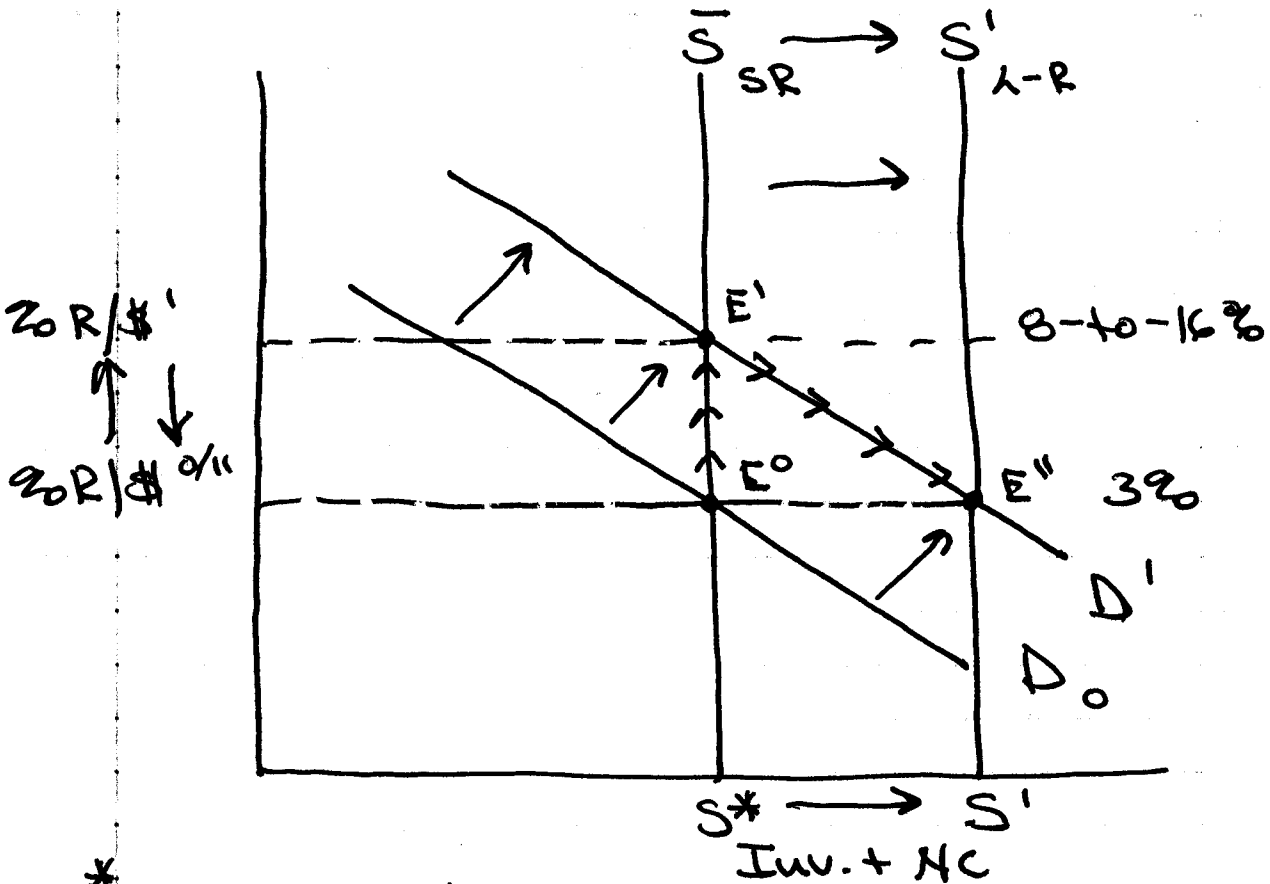
Note: Market can move through cycle to next phase, or back along line to prior phase; could stay stagnant for years.

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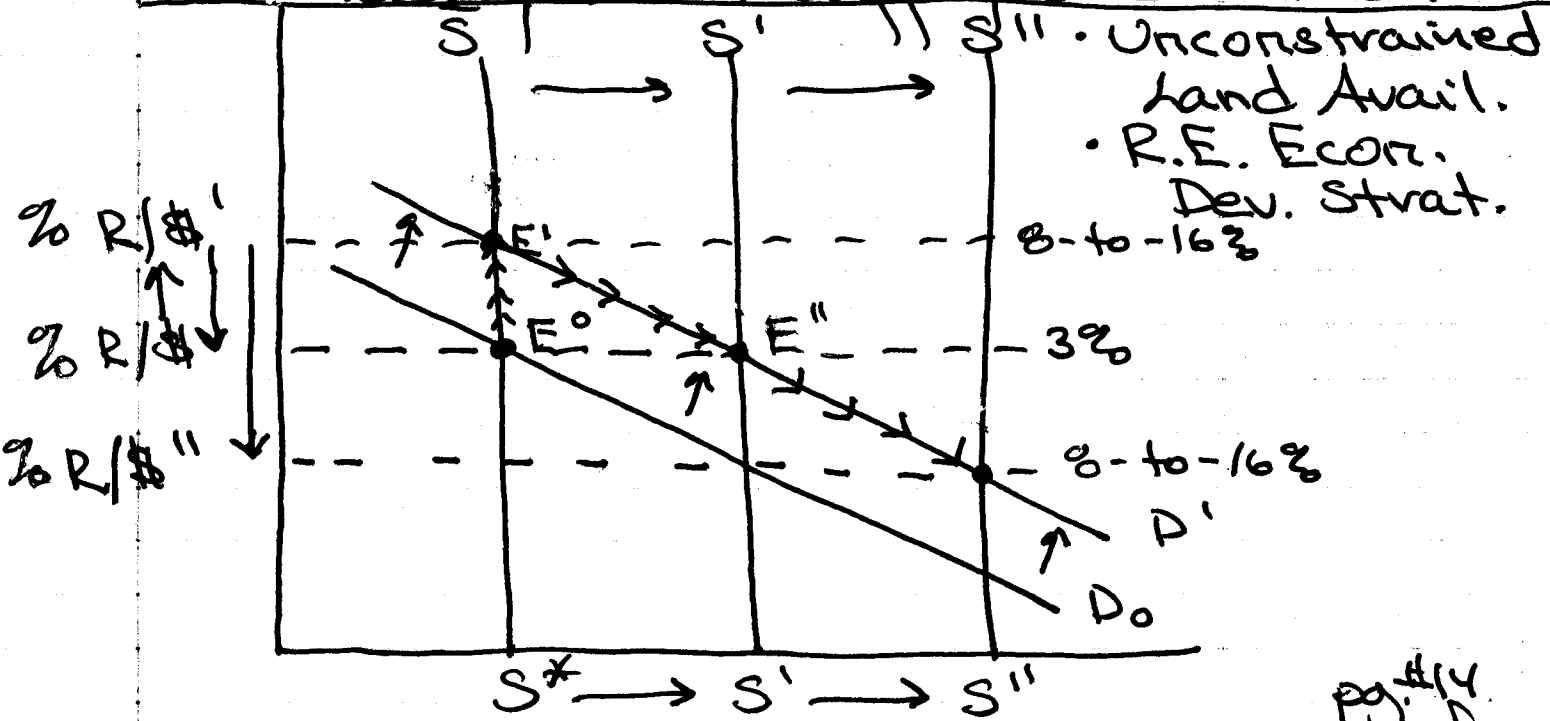
Commercial Real Estate Micro Econ. Any.



Long-Run Supply Response

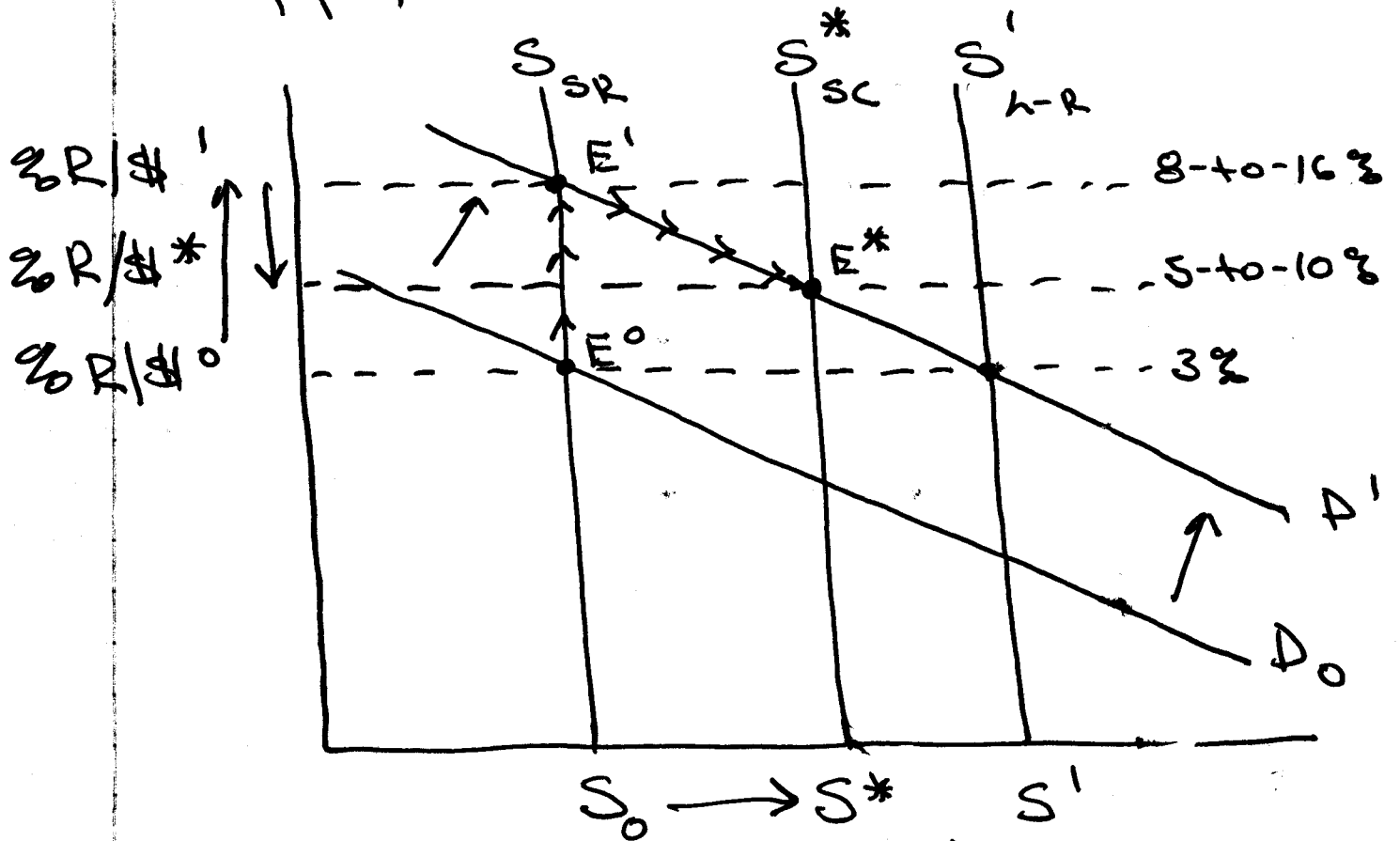


* Commodity-Mkt Supply Overstoot



* Supply Un-Constrained Market

Supply Constrained Market



Negative Employ. Demand Stock - Commodity - Mkt Supply Overshoot

