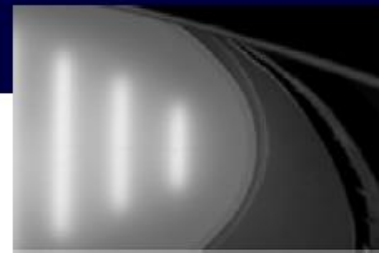


The Economics of REITs

Prof. Dr. Ramón Sotelo

Honorary Professor Real Estate Investment Vehicles

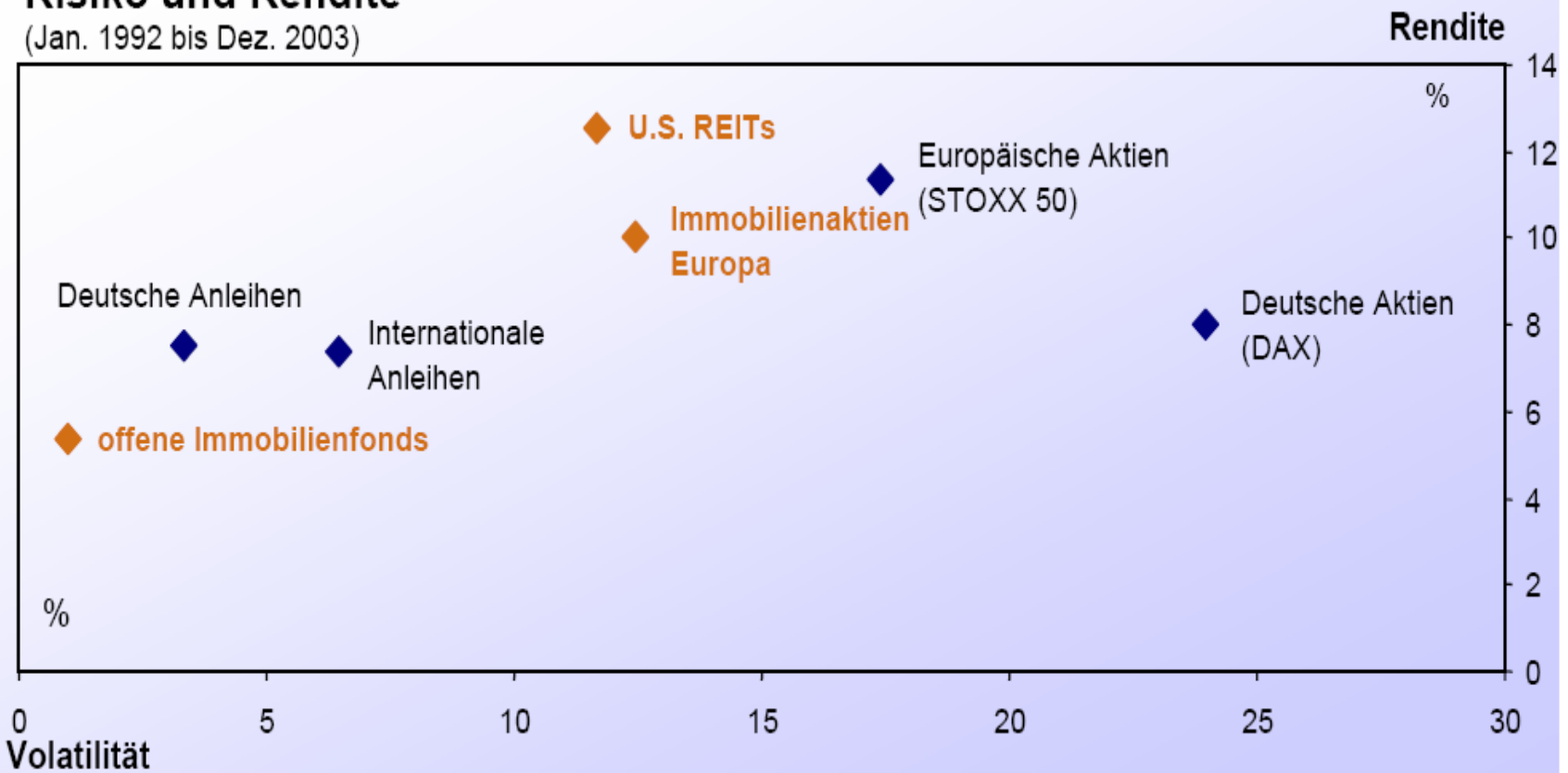
**Bauhaus-Universität
Weimar**



Why do we invest in property? Because it helps to diversify a portfolio?

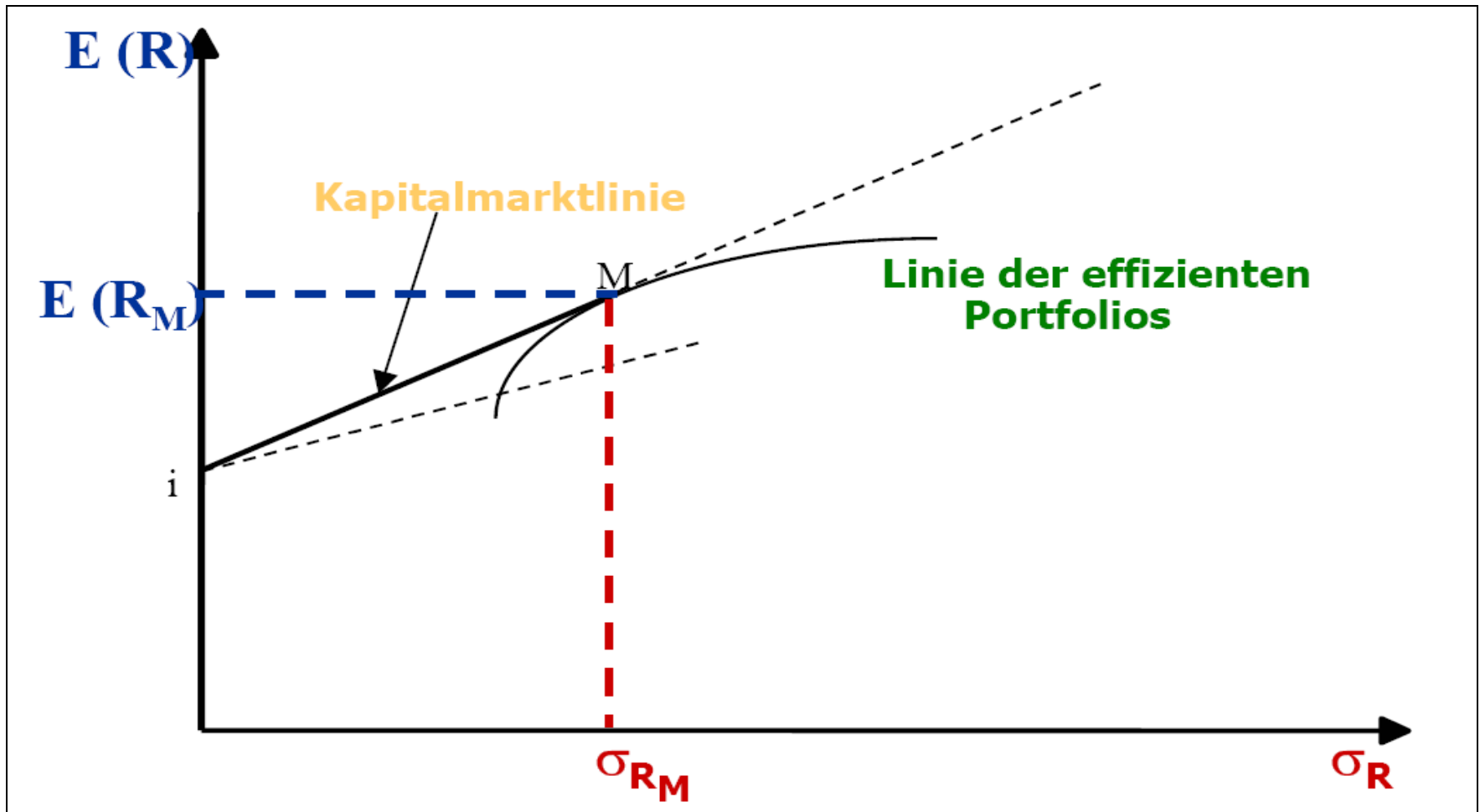
Risiko und Rendite

(Jan. 1992 bis Dez. 2003)



Traditional approach :

REITs help to elevate the investment frontier!

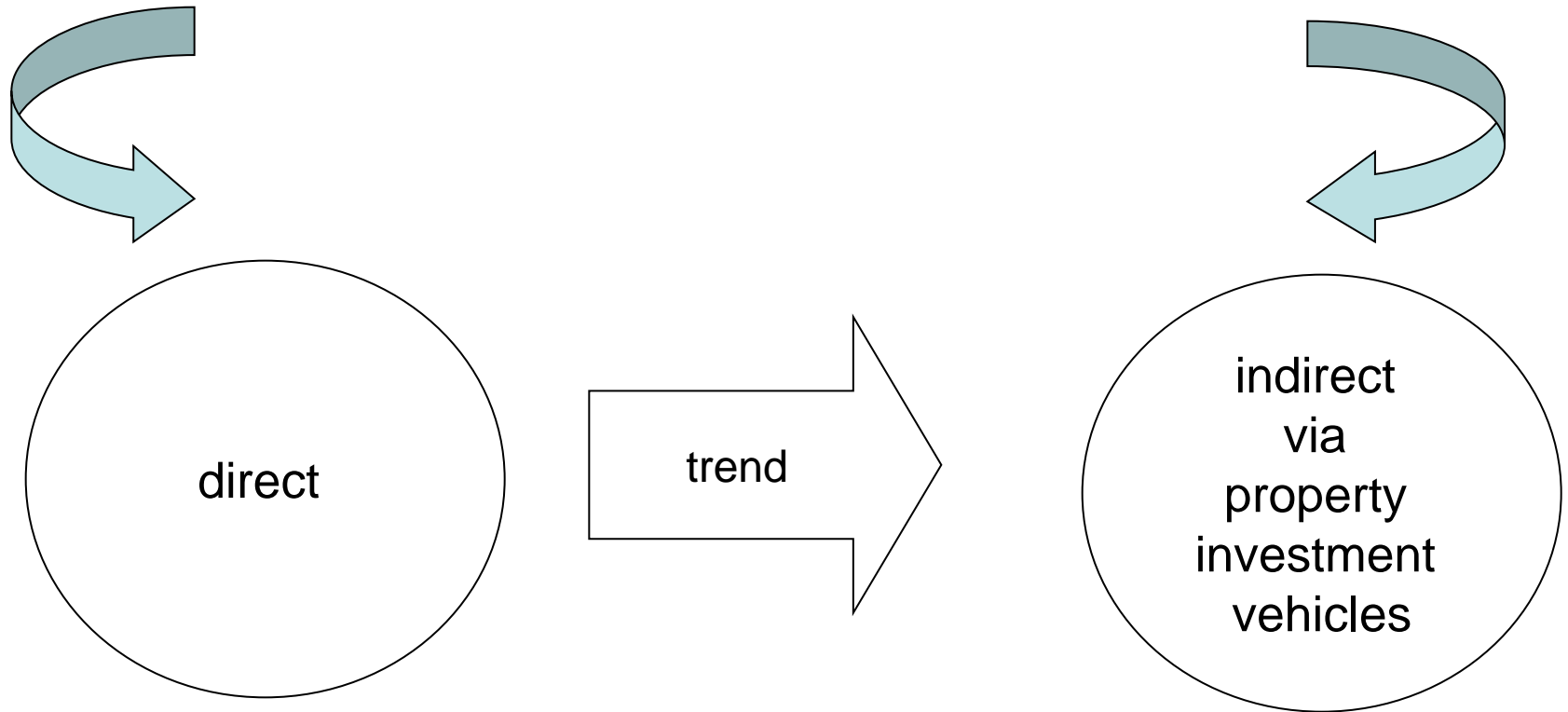


First result

1. Investors hold property besides to stocks and bonds to diversify and/or to hedge inflation risk.
2. In any case investors want to get the performance of property.
3. Financing activities connected with property like
 - development
 - Planning and construction
 - Services like property management
 - property operations

behave concerning performance and the ability of hedging inflation risk more like shares, and do not perform like properties.

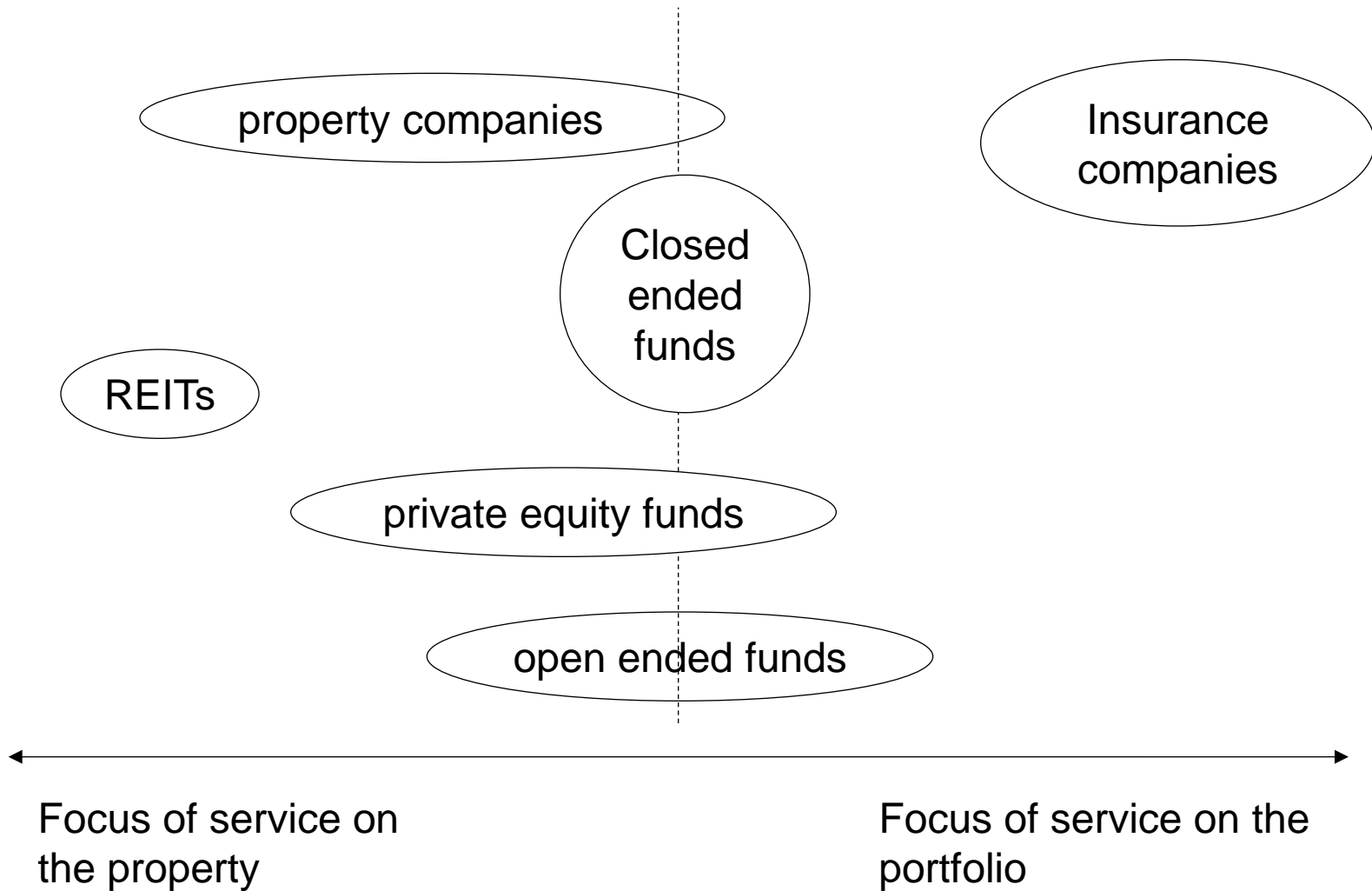
Possibilities of property investment



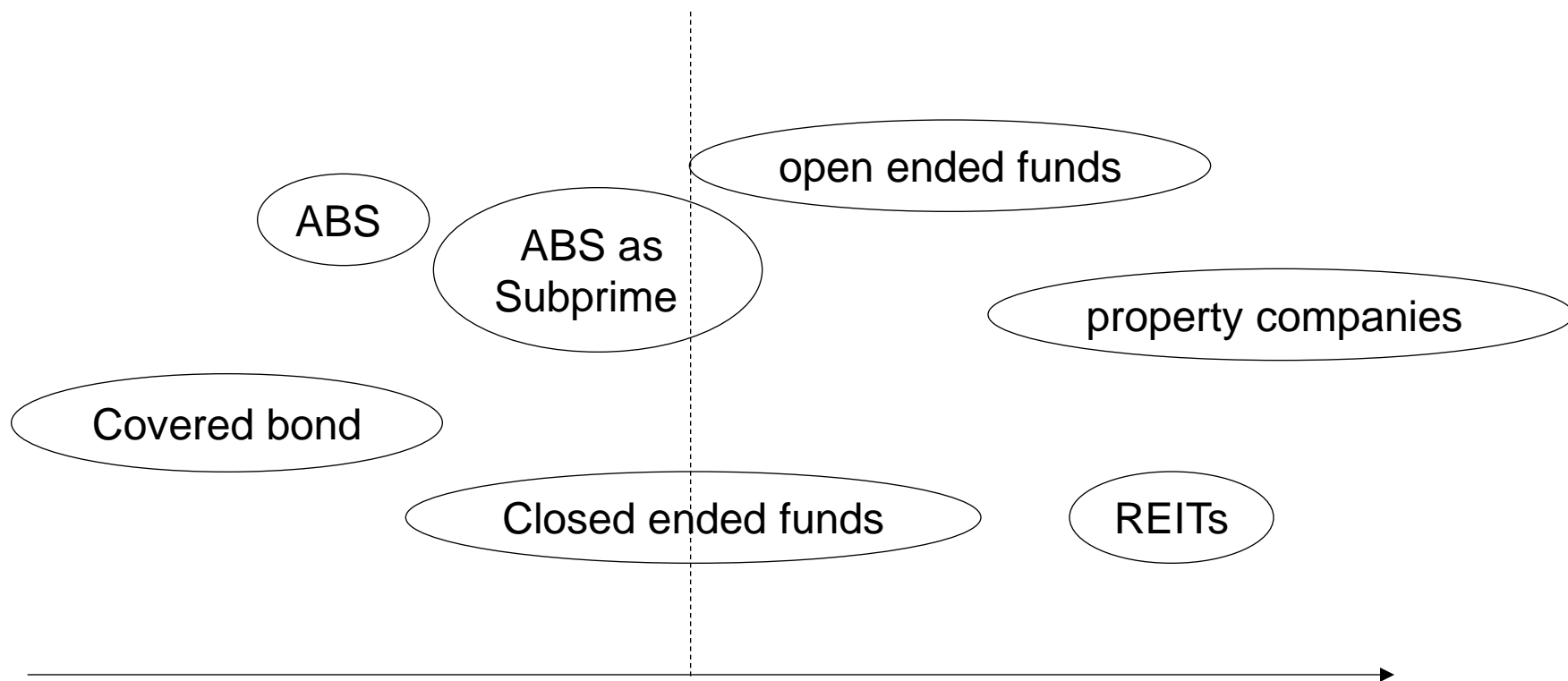
Reasons for the trend :

- higher fungibility
- clear responsibility for results
- advantage of comparative advantages

Investment vehicles in the spectrum of services



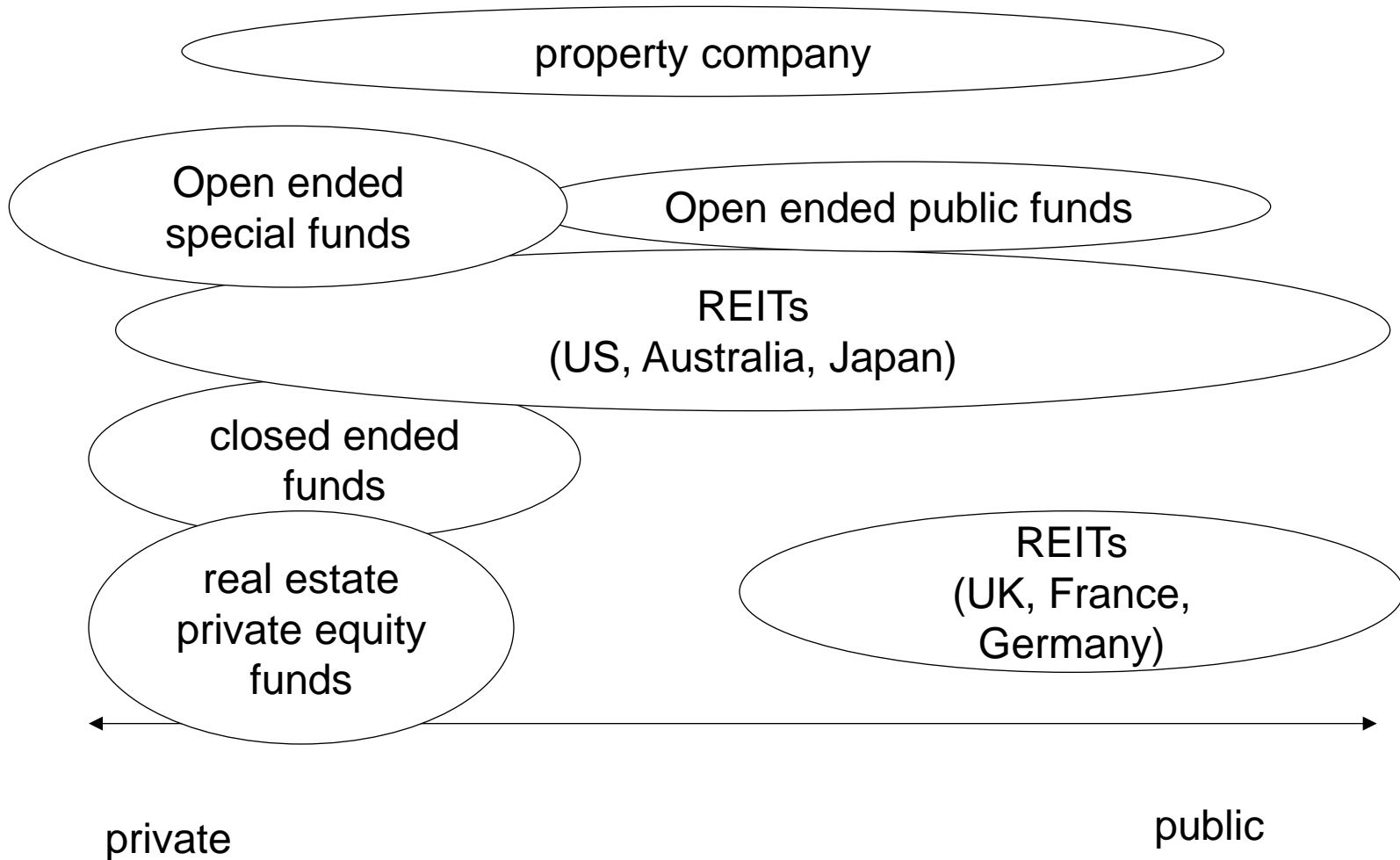
Property investment vehicles between equity and debt



Vehicles with debt character

Vehicles with more equity character

Property investment vehicles: public or private?



Second result

1. Investors hold property investment vehicles to become engaged in property risk.
2. Different property investment vehicles have a different focus on services, different fungibilities depending partly on the existence of secondary markets.

Remaining questions?

What is the ideal investment vehicle?

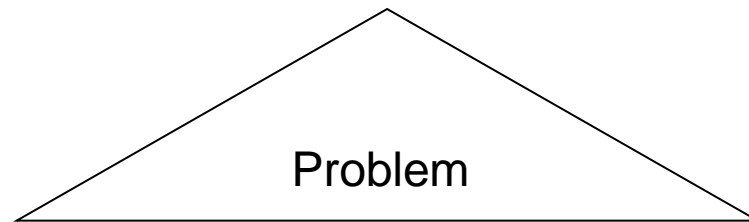
What is the category to measure the suitability of an property investment vehicle?

Is there a competitive situation between different property vehicles?

How can different property investment vehicles work together?

Background: Does finance matter? The Problem of MM

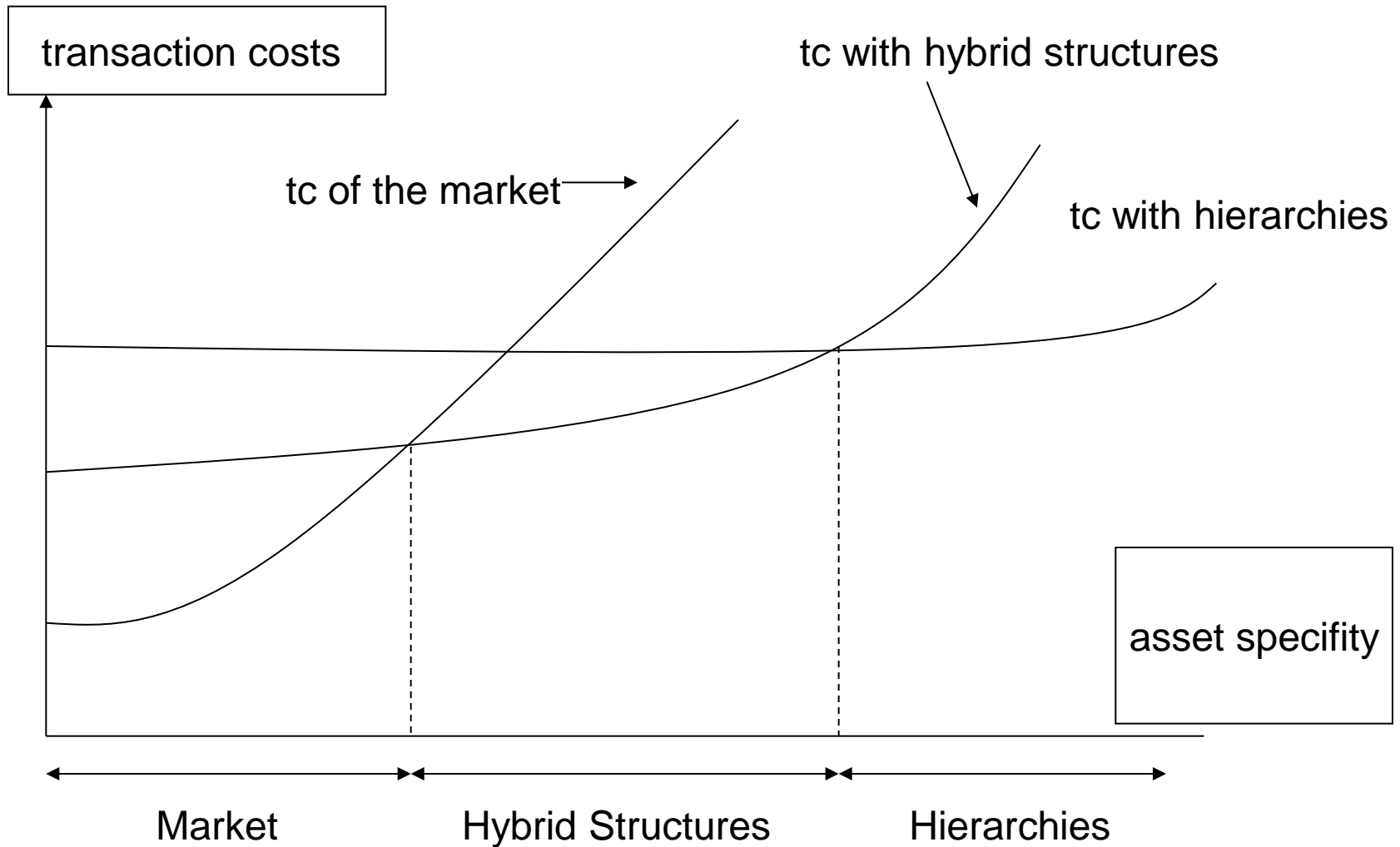
- To understand the way property investment vehicles work, we must interpret them as financial institutions.



- Within finance theory our thought are driven by the theorem of irrelevance of capital structure from Modigliani/Miller (MM-Theorem).
- According to MM The question of capital structure is not relevant.
- Concerning property investment vehicles, it should not be relevant to finance via an open ended funds, a property company, a closed ended fund or a REIT-Structure. Within MM the choice and the construction of property investment Vehicles is than not an economic issue.

Costs of different form of Transactions

Coase 1937: The Nature of the Firm

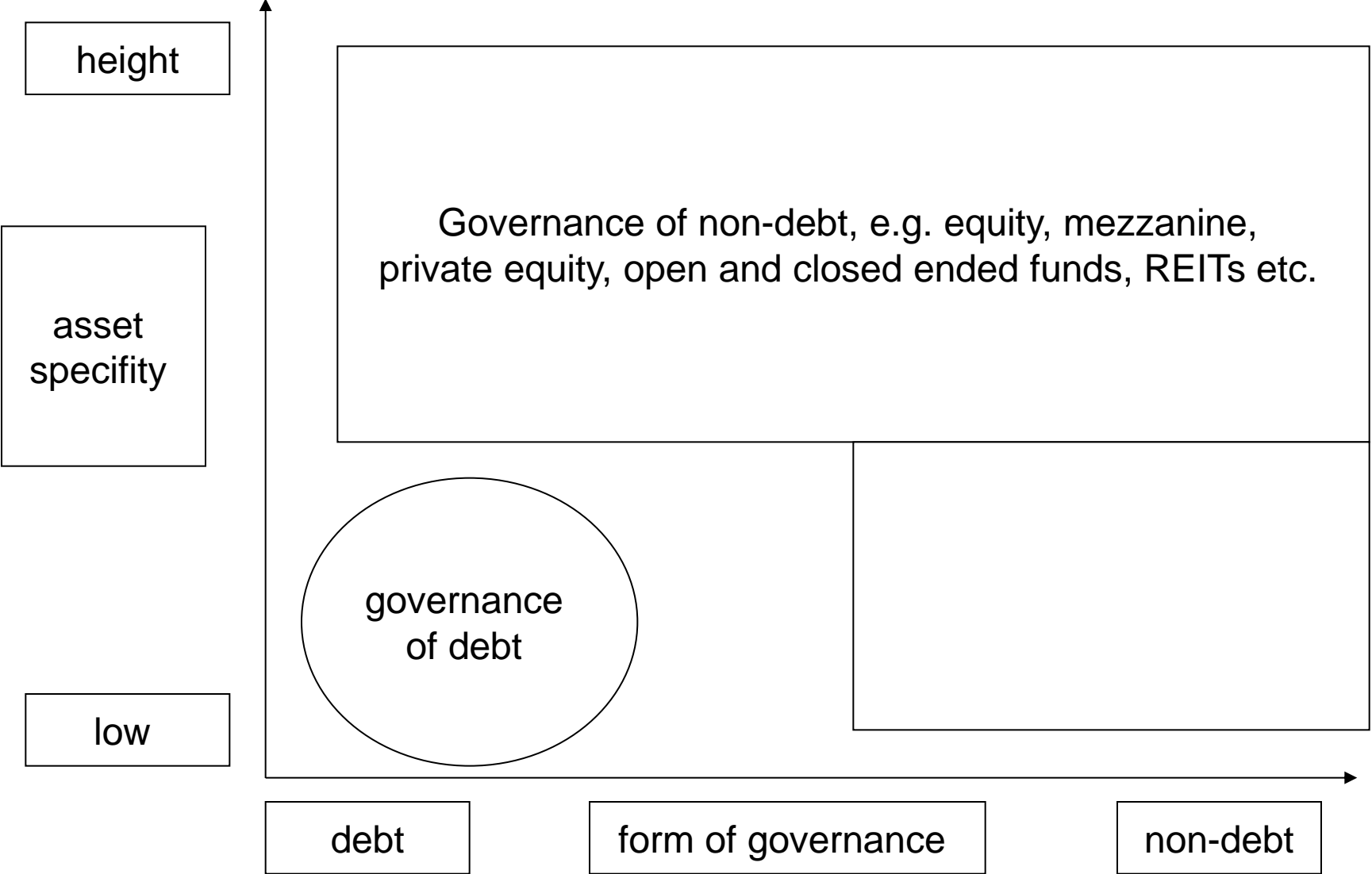


Capital Structure according to Oliver Williamson (1988)

Non specific assets are to be financed with debt, specific assets are to be financed with equity.

Assets	Liabilities
specific assets	equity
Non-specific assets	debt

Williamson on Property Investment Vehicles

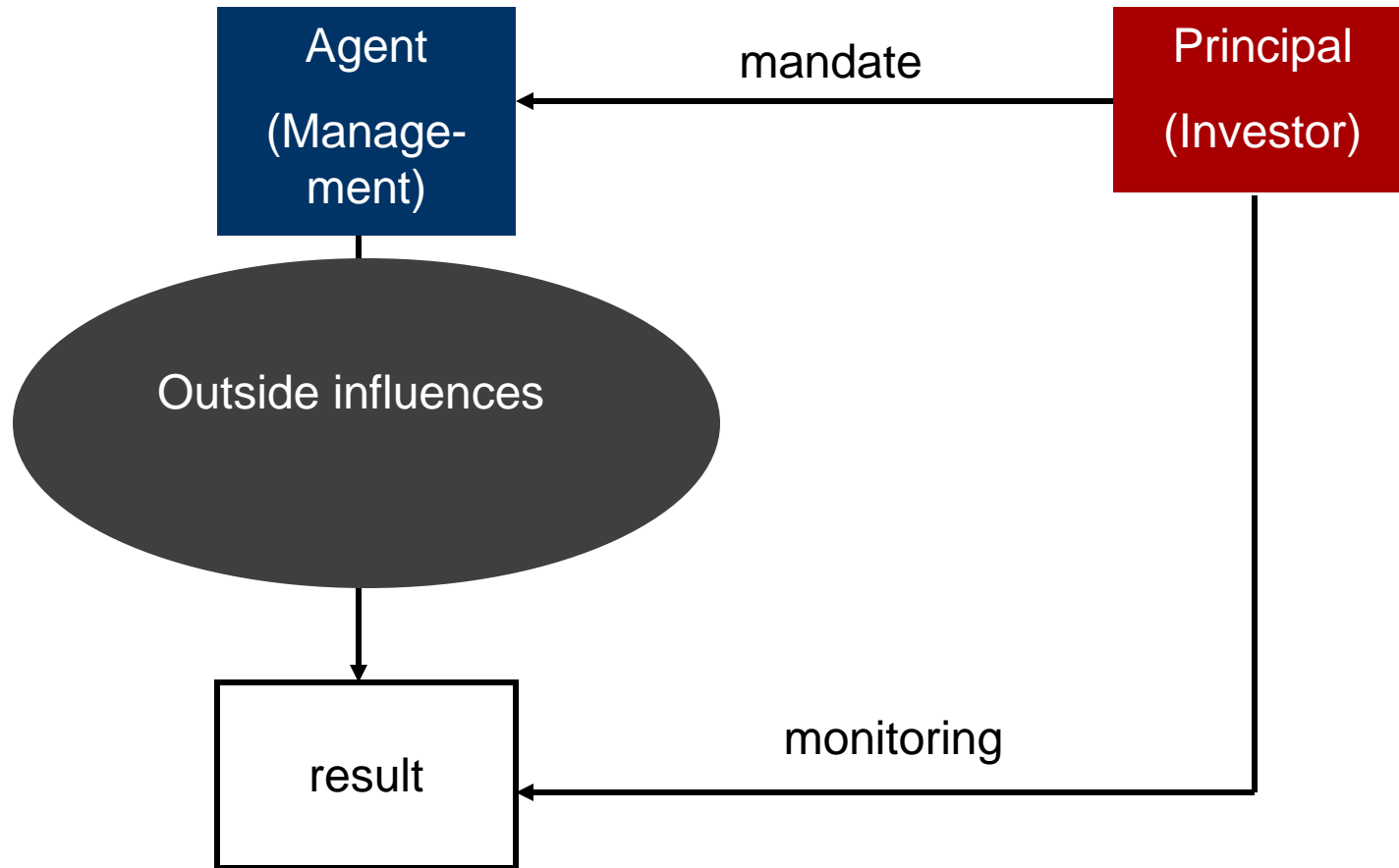


Developing theory of finance beyond Williamson

assets	liabilities
specific assets	non-debt
non-specific assets	debt

1. Non-specific assets are to be financed with debt, specific assets cannot be financed with debt.
2. We introduce a second category: The room of manoeuvre of the agents against the principals. This room of manoeuvre can be called the specificity of the liability.

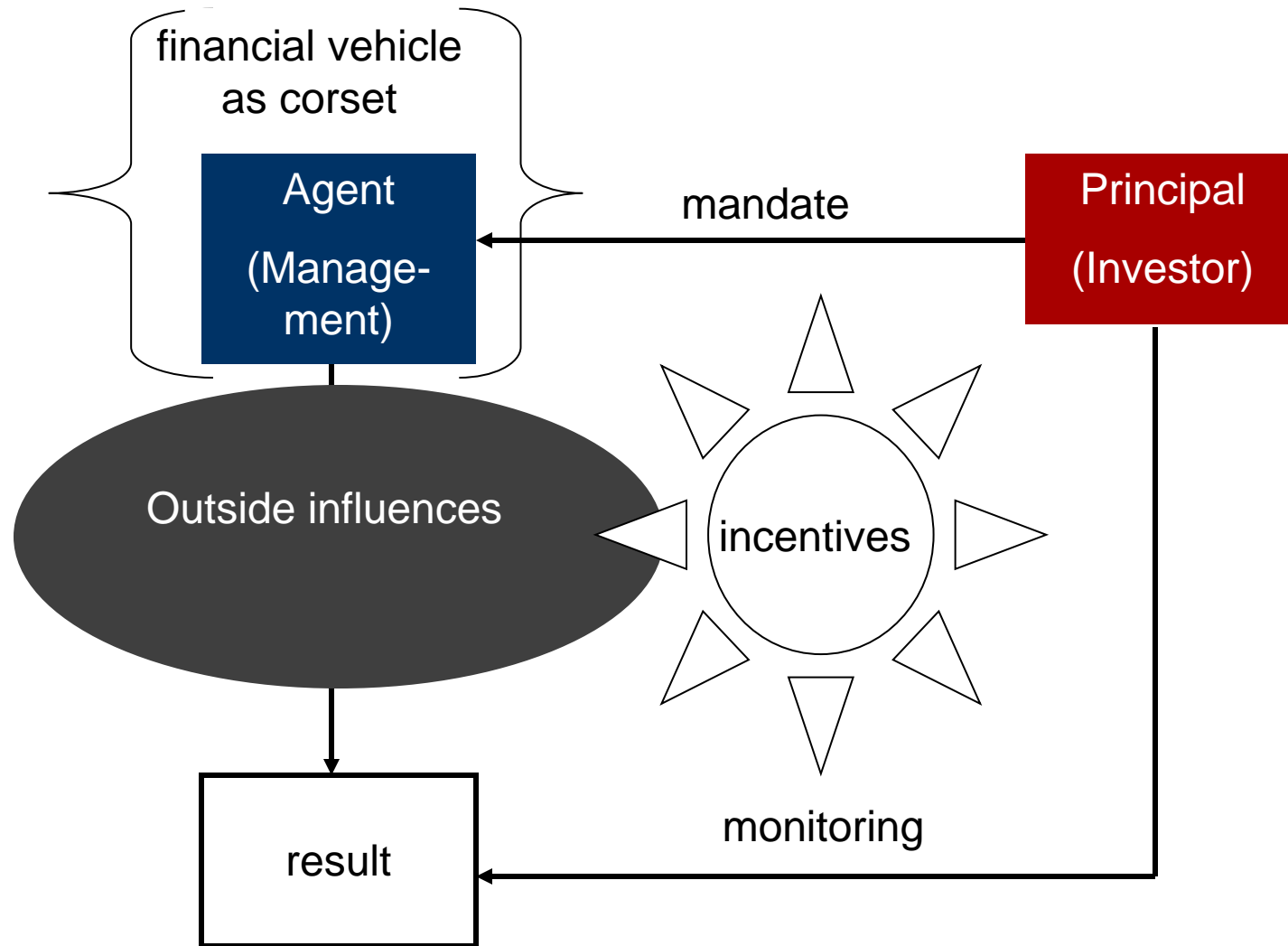
Investment vehicles as a P-A-problem



P-A-topics

1. incentives of the agents to harmonize interests of principals and agents
 - e.g. option-program for the management
2. reduction of the room of manoeuvre for risk reduction
 - e.g. approval of certain deals

Investment vehicles as a P-A-problem



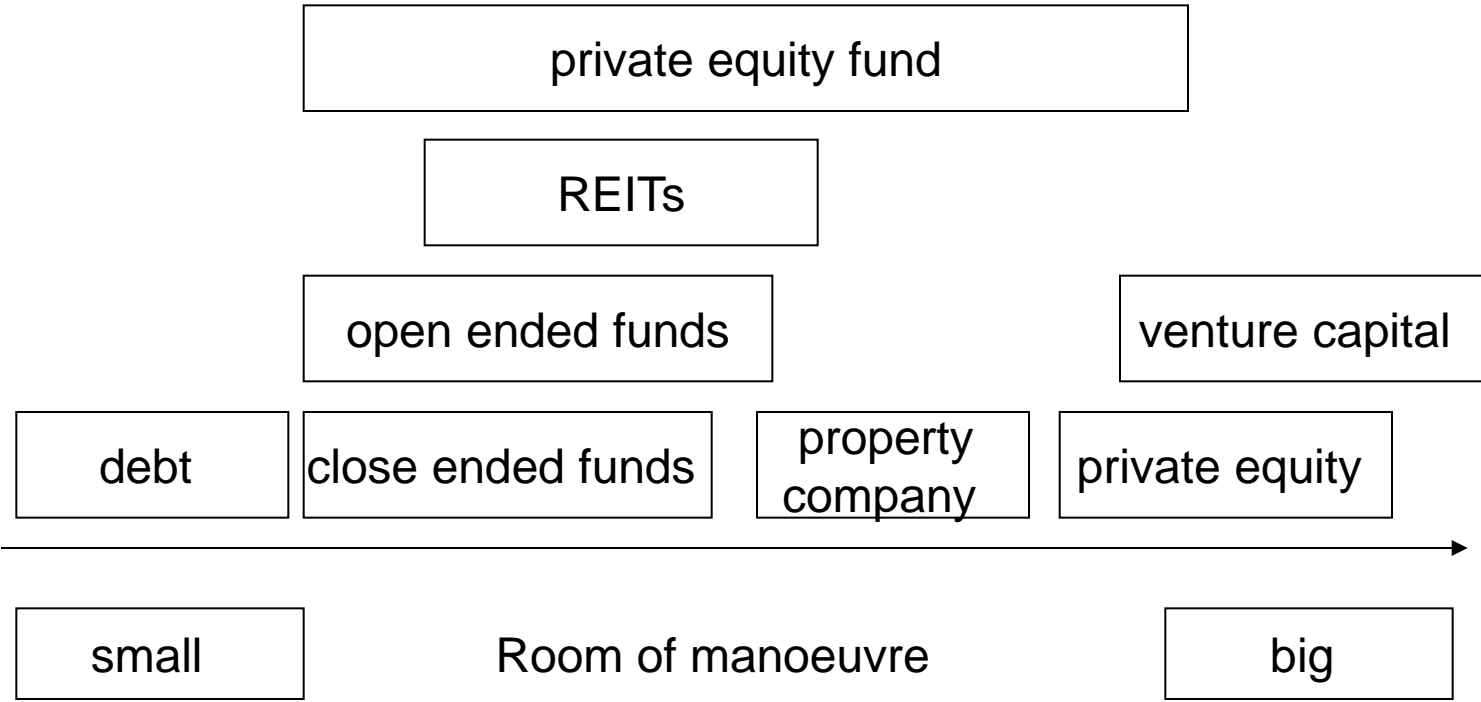
Concept of the room of manoeuvre (latitute)

The room of manoeuvre (latitute) describes the spectrum of possibilities of action the principal gives to the agent to comply the duty connected with the business the agent runs for the principal.

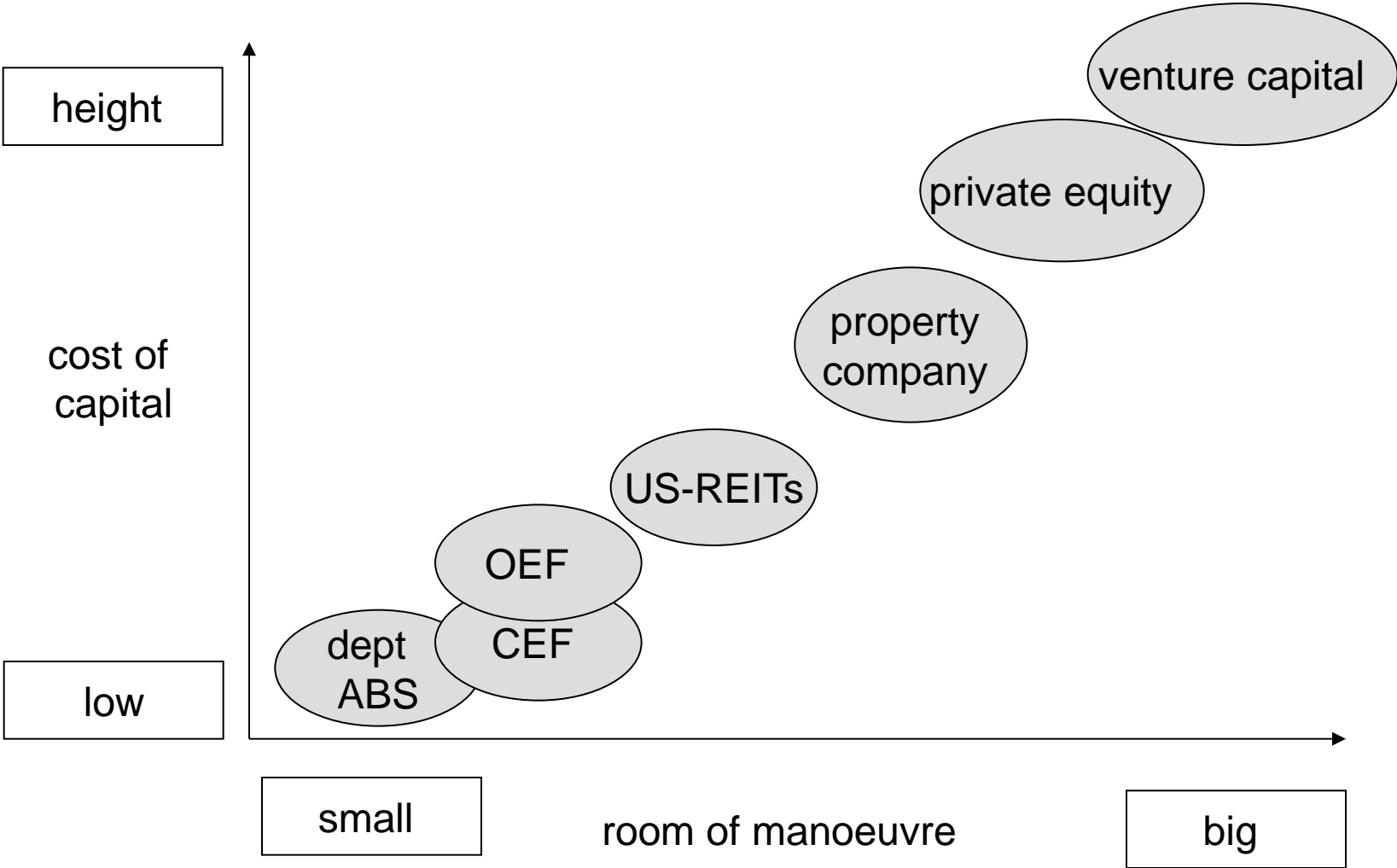
Developing theory of finance beyond Williamson

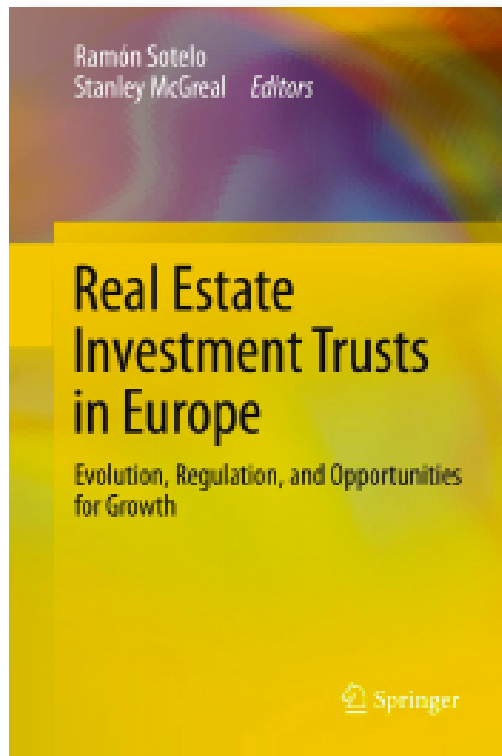
- The higher the room of manoeuvre, the higher the risk for the agent and in consequence the higher the cost of capital
- The financial institution is optimum, if the room of manoeuvre is exactly what the agent needs for the business.
- When different types of business are run, each one should be financed by its own or change the type of finance each time.

Room of manoeuvre of property investment vehicles



Room of manoeuvre and the cost of capital





2013, XV, 236 p. 80 illus., 63 illus. in color.

 Printed book

Handbook

R. Sotelo, S. McGreal, University of Ulster, Belfast, United Kingdom (Eds.)

Real Estate Investment Trusts in Europe

Evolution, Regulation, and Opportunities for Growth

- ▶ Presents a pan-European perspective on origins of REIT, regulatory differences
- ▶ Country-wise analyses of different REIT regimes
- ▶ Economic analysis on REITs and view on specific REIT-structures in Europe
- ▶ Includes the perspective of EPRA and NAREIT
- ▶ Introduction to European REITs based on lessons learned in mature markets around the world

Shortly before the beginning of the global financial crisis of 2008 REITs were introduced in several European countries based on their success in mature markets like the US, Australia and some Asian countries. While the history of REITs in Europe has been relatively brief, REITs are well on the way to become an industry standard as a real estate investment financial vehicle not only in Europe but throughout the developed world. This book provides both academics and decision makers an introduction to the economics of REITs beyond tax transparency, an overview of the mature REITs markets, and a closer reflection of the development of different REIT-structures in Europe including the history, regulation and markets of each country.

Real Estate Investment Trusts in Europe – Evolution, Regulation, and Opportunities for Growth

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Thank you for your attention!

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