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**Abstract**

The paper examines the performance of commercial and Residential Real Estate Investments in Ikeja, Lagos Nigeria. It conducts a comparative analysis of the performance of residential and commercial property investments within the period of year 2004 and 2013; focusing on average return, income growth and capital appreciation. The results showed that commercial property investments performed better than residential property investments with a mean annual return of 15.2% as against 11.7%. In terms of income and capital growth, the performance of commercial property investments was also higher during the period of measurement. The study concluded that while both residential and commercial property investments performed well with positive mean returns, commercial property outperformed residential property investments.

**Keywords:** Property Investment, Performance Analysis, and Investment Decision in Nigeria.

1. **INTRODUCTION**

An investment essentially involves an initial outlay to recoup a future income stream or future capital repayment. According to Isaac (1996) an investment is an asset which produces income during or at the end of the life of the asset. There are three main areas of traditional investment opportunity (excluding gold, commodities and work of art) namely: fixed interest securities, company stocks and shares, real property. The stock exchange which is centralized provides a market for listed shares and certain fixed securities while the property market is fragmented and

dispersed. Before undertaking an investment, an investor, analyzes what is required of the investment and according to Isaac (1998), the approach to the analysis is best done as a check list of questions and answers, which ranges from security and regularity of capital and also liquidity, security and regularity of income, opportunities for growth in value, etc. The prospective investor uses these qualities of a good investment as a bench mark for determining the suitability of alternative or possible investment opportunities. Some investments outperform others in this comparison. The study of performance of real estate investment, whether residential or commercial, is very important at this time when emphasis is on investment performance analysis in many parts of the world. This is even more important in Nigeria where only few studies have been carried out on the level of performance achieved by property investment. Moreover the impact of the ongoing changes in the global and local economy on the performance of real estate investment is serving to highlight the need for its careful consideration in the investment decision making process. Since 1990s, the demand for commercial properties has risen astronomically in most urban centers in the country. This is as a result of the economic recession which compelled the unemployed and public servants to explore trading activities in addition to their normal jobs. The investors’ reaction to this development has been to increase the number of commercial properties at the expense of residential property developments. Therefore in many towns and cities of Nigeria, open spaces, offices, shops etc within the vicinity of public institutions have been irrationally developed to accommodate commercial activities. The situation is further compounded with the perceived notion among Nigerian property investors that commercial property performs better than residential property investment. According to Ajayi and Fabiyi (1984) the investors can no longer base their decision on intuitive grasp of the market which considered inadequate for success in property ventures. Also it is crucial to show the past performance of similar or comparable investments to enable the investor make strategic management decisions. Isaac (1998) opines that strategic property decisions would determine the proportion of the total portfolio to be devoted to property, the allocation of funds to the different types of property.

**1.1 RESEARCH QUESTIONS**

1. What is the performance of commercial and residential properties in the study area in recent time?
2. What is the performance of commercial and residential properties in ikeja in terms of income growth within the period of study?
3. What is the relationship if any, between the three indices (Rental Value (RV), Capital Value (CV) and return over the period under study?
4. What is the performance of commercial and residential properties in terms of risk adjusted return?

**1.2 AIM AND OBJECTIVES**

The aim of this paper is to examine the performance of residential and commercial property investments in the study area. This will provide for better investment decision and risk management for real estate investors in Lagos and comparable locations in Nigeria.

**OBJECTIVES**

1. To evaluate the performance of commercial and residential properties within ikeja.
2. To determine if there has been growth in rental and capital values of residential and commercial properties in the study area during the period.
3. To compare the return on commercial properties to residential properties in the study area.
4. To examine the performance in terms of risk adjusted return

**2.0 LITERATURE REVIEW**

Various studies that are relevance to the Analysis of the performance of commercial and residential real estate investment have been conducted. They include Wendt and Wong (1965), Brueggman et al (1984), Zerbst and Cambon (1984). These studies compared the performance of real estate with the performance of non-real estate investments such as stocks and bonds. The major conclusion from the studies is that real estate performed better than other forms of investment and also act as an overall risk reducer when included in a portfolio**.**

Some other studies examined the linkages between direct real estate and indirect real estate investmentperformance. Among them are Giliberto (1990), Newell, Matysiak and Venmore-Rowland (1997), McAllister (2000), Newell, Chau and Wong (2004), Newell, Chau, Wong and McKinnell (2005), Hoesli and Lizieri (2007), Newell and Hsu (2007) and Newel et al (2009) who considered the performance of direct real estate along that of indirect real estate investment represented by listed companies and REITs returns in the UK and USA respectively. The outcome of the studies suggested that direct real estate produce lower returns and lower risk, and that indirect property investment behaves partly as stocks and partly as real property investment. This has also been confirmed with recent literatures on performance of real estate with particular references to case studies of Nigerian property market as discussed below.

Some studies also examined the performance of residential alongside retail property, among them are Miles and MicCue (1982), Webb and Sirmans (1982), and NCREIF (1984). In the a study conducted in US, Miles and MicCue (1982) examined the rates of return on different types of properties held by sixteen Real Estate Investment Trusts (REITs) over the period of 1972 – 1978. The study which employed regression equation estimate found that residential property performed better than retail during the period of study. Although, the study was a good attempt at analyzing the comparative performance of different property types, it failed to examine the risks associated with each of the property sectors. Another US study by Webb and Sirmans (1982) bridged the gap left by Miles and MicCue (1982) by analyzing the return and risk on different types of real estate property over the period of 1966 – 1976. The study employed real estate data from the American Council of Life Insurance and estimated the investment yields of specific property types for fifteen companies. The results of the study showed that retail property performed better than residential property in terms of return. However, the empirical result indicated that retail property was riskier than residential property. National Council of Real Estate Fiduciaries (1984) employed the index of income producing properties generated by the Frank Russel Company to determine the return on different types of real estate property. The outcome of the study which considers the performance within 1978 - 1983 showed that residential property outperformed retail property in term of return. The result also indicated that residential property was riskier than retail property. Lorenz and Truck (2008) in a European study investigated the risk and return performance in European markets. The authors who conducted a comparative study of different property types across France, Germany, Ireland, Netherlands and UK found that retail property performed better than residential property in France and Germany while the residential property outperformed retail in Netherlands. The data for residential property was not available for Ireland and UK. Many of the studies relating to real estate performance carried out in many parts of the world were done under social, economic and political situations different from Nigerian situation.

In the Nigerian context, some works have been done by scholars on the performance of real estate. For example, Olaleye (2000); examined portfolio management and performance of property portfolio in Lagos. The study showed that while portfolio in Ikeja performed better in terms of their mean return when compared with the free risk rate for the same period, portfolio in Yaba performed below the investor’s targeted rate. Apart from the fact that this study did not focus on residential or commercial property, other some shortcomings do exist in the study.

First, the study’s emphasis was basically on the performance of management and not on investment. The second constraint is premised on the size of the sample. The small sample size has the potential of distorting results by allowing the peculiar characteristics of the properties and their market to have significant effect. Bello (2003); evaluated the relative performance of residential property and securities in Lagos in terms of mean returns, risk adjusted return, income growth and capital growth. He concluded that investment in ordinary share performed above that of residential property in absolute term and risk adjusted return. The study also showed that

the risk associated with residential property is lower than that of ordinary shares. However, the study did not consider the performance of commercial property. Comparing the performance of commercial property alongside residential property investment which this study hope to achieve, will give a broader picture of investment performance. Oyewole (2006) study direct and indirect property investments in Lagos examined the comparative performance of direct property of eight listed property companies, and UACN property development company shares within the

period of 1999 to 2004. The author employed relative importance index, coefficient of variation measure and sharp ratio to estimate mean return, risk adjusted return, income appreciation and capital appreciation. The study showed that while indirect property performed better in terms of rate of return in absolute term and capital growth, the direct property performed better in terms of risk adjusted return. The shortcoming of this study is also premised on its failure to specifically focus on residential and retail property.

Oyewole and Adewusi (2009) examines the relative performance of real estate and financial assets as security for mortgage lending in Nigeria with a view to ascertain whether or not the drift towards financial assets is justified. Using a sample of Forty six transactions involving landed and financial assets and test of difference between two population means, the study reveals that although, the banks still prefer financial asset, however, both real estate and financial assets provided cover for the secured loans but real estate has a superior performance on the long run. In addition, Real estate exhibited higher growth than financial asset over the loan period.

Olaleye, Adegoke and Oyewole (2010) examined the characteristics of direct property and listed Property Company in comparison with other securities in the Nigerian Stock Exchange over the period of 2001 through 2007. The study evaluated the capital return and diversification potential of the investment media through the use of mean return, standard deviation, correlation and Sharp market index model. The results showed that while various investment options in real estate and stock market offered attractive returns, real estate investment outperformed stocks and offered diversification benefits for investors of a mixed assets portfolio. Other indigenous studies such as Amidu et al (2008), Olaleye and Ajayi (2009), Adegoke (2009) and Bello (2012), either consider the performance of property investment in general, indirect property investment or residential property investment and stocks. None of these available indigenous studies has examined the difference between the performances of residential and commercial real estate investments considered in this study.

**3.0 THE PROPERTY MARKET**

Keogh (1994) provides a model of the property investment market and this shows that property investment is part of a market, which includes a user market, an investment market and a development market. While Fraser (1996) also suggests a schematic model of the property investment market which concentrates on the interrelationship of the market in three principal sectors: the letting, user or occupational sector, the investment sector, and the development sector. Fraser's model has a single ring with three arcs for the principal market sectors. It provinces a context of international, national and local economies to the setting of the market and suggests that occupational demand drives the letting market, investment demand drives the investment market and development costs the development sector; these three sectors in turn establish the property stock. While Isaac (1998) opines that the other division of the investment market is to look at the types of property involved. Thus the main sectors or traditional classes in the investment market are: Retail and retail warehousing, offices and business space, industrial and warehousing, agricultural land and woodland, leisure and healthcare, residential.

* 1. **Residential Property:**

Lawal (1997) sees housing or residential properties in 3 dimensions viz-private, institutional and public. Non government agencies and individuals initiate private housing development for investment or occupation. Institutional housing is meant to serve the collateral interests of institutions (e.g. the military, university) whose goals are the provisions of facilities without reference to profit. Public housing is government supported housing programmes created by a wide variety of legislative, administrative, administrative and financial mechanisms as a means of providing decent, safe and sanitary housing at affordable cost. (Lawal 1997). Bourne (1980) sees the residential property market as a mechanism for allocating housing. He cites two principal mechanisms for allocation:- the traditional private 'market' which allocates households to housing on a competitive basis in terms of the values people attach to housing and their ability to pay; and the other being the public sector allocation in which governments, housing officials or some other community group, distribute housing according to individual and collective needs and the objective of the agencies involved. Lawal (1997) further creates two subdivisions of private sector housing type viz:

(a) Single dwelling residential buildings which are (detached) individual houses and bungalows; including semi-detached and row houses called 'town houses'. In these types, consumers or enjoy the conventional detached single family house benefits (e.g. private entrance, multi-story separation of living and work spaces, backyard patio etc). According to Lawal (1997) the single dwelling residence is a prime example of real estate purchase or development for use rather than investment. However in recent times a very high percentage of such dwellings are being let, thus becoming an avenue for investment.

(b) Multi dwelling residential buildings. There are maisonettes flats and rooming tenement buildings, which are mainly developed for investment.

**3.2 COMMERCIAL PROPERTY:**

Commercial property is an important asset class for major institutional investors especially in developed economies where they have robust and matured property markets that offer a good number of options of stocks to buy into. The important of this is made more prominent by the quantum of transactions that commercial assets command which is put at $19 trillion investable globally (EPRA,2009). Although the ownership of commercial property (I.e. office building, shopping centre, industrial properties and hotels) does not offer any tax shelter like residential property, it can offer greater security to the investor (Saft,2004).

**4.0 THE STUDY AREA**

Ikeja is a suburb of the city of Lagos and the capital of Lagos state. It is also one of the Nigeria’s 774 Local Government Areas (LGAs). Ikeja Lagos Nigeria is one of the most popular places within the state. Legend has it that, Ikeja was founded by an Awori (A Yoruba tribe in south west Nigeria) hunter with first name Akeja, after whom the area is named. Some notable communities in Ikeja include Maryland, Anifowoshe, Ipodo, Ogba, Agidingbi, Opebi, Allen Avenue, Alausa (State Government Secretariat is located here), Oregun, Idi-Iroko, Akiode and Ojodu.

Ikeja was a well planned, clean and quiet residential environment with shopping malls, pharmacies and government reservation area. The situation is different today, new buildings mostly commercial buildings are springing up there. Ikeja is easily the best place on Lagos mainland to situate a business because of its strategic location and market structure. Ikeja has a very strong commercial base. It now boasts of a large shopping mall “Ikeja City Mall” which is the biggest mall in the Lagos mainland. A large number of businesses mostly retail and service based businesses operate in the area.

**5.0 RESEARCH METHODOLOGY**

The methodology employed for this study is data collection. It also describes the two main sources of data used. These are; primary and secondary sources of data. The secondary sources of data comprises mainly of relevant data gotten from published books and journals. The primary data was obtained through the administration of questionnaires. The targeted population for the study are the Registered Estate Surveyors and Valuers practicing in Ikeja. The list of the practicing Estate Surveyors and Valuers was taken from the 2014 Directory of The Nigerian Institution of Estate Surveyors and Valuers. In the Directory, there are 70 registered Estate Surveyors and Valuers practicing in Ikeja. Questionnaires were distributed on the seventy (70) Estate Surveyors and Valuers out of which 56 were retrieved which is good for analysis. The questionnaires were designed to extract information on the annual rent paid for 3 bedroom flat and office spaces in the four neighborhood for the past ten years. The data collected was analyzed using descriptive statistics .The research was carried out in some selected parts of Ikeja. These are neighborhoods like Opebi, Allen Avenue, Obafemi Awolowo Way, and Anifowoshe.

HPRt = HPRt=[CVt-CVt-1]+NIt

CVt-1

Where

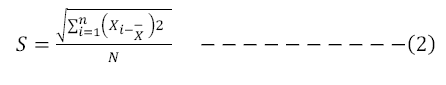
HPRt = holding period return in period t

CVt= Capital value at the end of period t

CVt-1 = Capital Value at the beginning of period of t-1

NIt = Net income received during period t

To measure the risk or volatility of the investment, standard deviation was used. It is a summary of how much the value deviate from their steady state which is:



Where X is the mean value and N is the number of observation. The coefficient of variation was calculated as follows:

Coefficient of variation (COV) = S

V

**5.0 FINDINGS**

**5.1 Performance in Terms of Average Returns**

The holding periods return profile of investors calculated from rental and capital value collected is shown in table1. The results as indicated in the table show that mean annual total return of the commercial property ranges from 8.2% and 20.3%, a range of 12.1%. That of residential property range from 5.6% and 18.5%, a range of 12.9% within the same period. On the whole, residential properties are shown to have experienced a mean annual return of 11.7% as against 15.2% for commercial properties. The implication of the results is that commercial property investment performed better than residential property investments in terms of return.

**Table 1: Return on residential and retail property investments (2004 – 2013)**

|  |  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- | --- |
| Year | COMMERCIAL PROPERTIES | | | RESIDENTIAL PROPERTIES | | | |  |
| Total  return in % | Income  return in % | Capital return in % | Total return in % | Income return in % | | Capital return in % |
| 2004 | 8.5 | 4.6 | 3.9 | 5.6 | 2.5 | 3.1 | |
| 2005 | 13 | 4.6 | 8.4 | 6 | 2.5 | 3.5 | |
| 2006 | 14.2 | 5.3 | 8.9 | 6.9 | 2.8 | 4.1 | |
| 2007 | 14.3 | 5.4 | 8.9 | 8.7 | 3.2 | 5.5 | |
| 2008 | 21.3 | 4.5 | 16.8 | 13.2 | 4.1 | 9.1 | |
| 2009 | 8.2 | 5.5 | 2.7 | 13.2 | 4.1 | 9.1 | |
| 2010 | 14.8 | 6.6 | 8.2 | 13.8 | 5.5 | 8.3 | |
| 2011 | 17.7 | 7.7 | 10 | 15.2 | 6.1 | 9.1 | |
| 2012 | 19.4 | 8.8 | 10.6 | 16 | 6.5 | 9.5 | |
| 2013 | 20.3 | 9.5 | 10.8 | 18.5 | 8.5 | 10 | |
| Mean | 15.2 | 6.3 | 8.9 | 11.7 | 4.53 | 7.1 | |

**Source: Field Survey, 2015.**

**5.2 Performance on the Basis of Risk Adjusted Returns**

In order to examine the performance in terms of risk adjusted return, the co – efficient of variation method was employed. The results are as shown in the table below:

**Table 2: Risk Adjusted Return of Commercial and Residential Property Investment in Ikeja**

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
| Property Types | Mean | Variance | Standard Deviation | Coefficient of Variation |
| Commercial | 15.2 | 18.8 | 4.3 | 0.28 |
| Residential | 11.7 | 19.23 | 4.4 | 0.38 |

**Source: Field survey, 2015**

The results in table 2 revealed that the co – efficient of variation are found to be 0.28 for commercial property and 0.38 for residential property investment. This has placed residential property investment as more risky than commercial property investment.

**5.2 Performance in terms of income and capital growth**

The performance of real estate investment in terms of income growth within the period of study is summarized in the table 2 below: The results reveal that with 2004 as the base years, the rental income index of residential property rose from 208 in 2004 to 350 in 2013. During the same period, the rental income index for commercial property rose from 210 to 380. The implication of this is that the rate of growth of commercial property income is higher than that of residential property between 2004 and 2013.

**Table 2: Average index for rental income of property investment**

|  |  |  |
| --- | --- | --- |
| YEAR | RESIDENTIAL | COMMERCIAL |
| 2004 | 208 | 210 |
| 2005 | 210 | 220 |
| 2006 | 210 | 230 |
| 2007 | 250 | 280 |
| 2008 | 270 | 300 |
| 2009 | 300 | 350 |
| 2010 | 320 | 355 |
| 2011 | 320 | 355 |
| 2012 | 325 | 360 |
| 2013 | 350 | 380 |

**Source: Field Survey, 2015**.

The table 3 revealed that residential property capital value index in 2004 is 250 as against 270 for commercial property capital value index. In the year 2013, these rose to 390 and 490 for residential and commercial property respectively. The result just as in case of income growth shows that the rate of capital growth in commercial property investment is higher than that of residential property investment.

**Table 3:Average Index for capital income of property investment.**

|  |  |  |
| --- | --- | --- |
| Year | Residential | Commercial |
| 2004 | 250 | 270 |
| 2005 | 270 | 280 |
| 2006 | 270 | 310 |
| 2007 | 280 | 350 |
| 2008 | 310 | 350 |
| 2009 | 330 | 400 |
| 2010 | 350 | 420 |
| 2011 | 380 | 450 |
| 2012 | 380 | 470 |
| 2013 | 390 | 490 |

Source: Field Survey, 2015.

**6. Discussion and Findings**

The results presented in this paper provide initial analysis of the performance of commercial and residential property investments in ikeja, Lagos state. The results bring out some interesting features on performance over the period of measurement. The higher return, income growth and rate of capital appreciation generated by commercial property investments indicate that commercial property performed better in ikeja property market. The higher co-efficient of

variation attracted by residential property indicates that investment in residential property is more risky than investment in commercial property.

**6.1 Summary and Conclusion**

This study has examined the performance of residential and commercial property investments in ikeja between 2004 and 2013.The research has shown that in ikeja commercial property investment performed better than residential property during the period of measurement. The results clearly identified commercial property as a more attractive form of investment option. In terms of means annual return and income growth and capital appreciation, commercial property performed better. In terms of risk, the results revealed that both residential and commercial property investment are somewhat risky in the study area. However, the residential property with the co-efficient of variation of 0.38 is more risky than commercial property with co-efficient of variation of 0.28. Both residential and commercial property investment performed well with positive mean returns throughout the period, commercial property out-performed residential property not only in terms of return. However, the danger if the trend is not checked is that the supply of commercial property may soon overtake the demand, leading to the problem of void, while the resultant scarcity of the residential properties may lead to acute housing shortage and associated problem.

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