BASIC LEGAL CONCEPTS

***Real Estate*: Land** and all things "permanently" attached thereto.

Real Property: **Ownership Rights** associated with **Real Estate**.

Personal Property: **Movable** things and **Intangibles**.

Fixtures: Are **Personal Property** until they are **Attached** to a **Building**, then they become a part of the **Real Property**.

Statute of Frauds: Requires that almost every agreement relating to **Real Property** be in **Writing** in order to be **Enforceable** in a court of law (from England 1677).

***Property Rights and Estates in Real Estate*: Ownership**, **Possessory** and **Use** rights. The most complete form of ownership is a **Fee Simple Absolute** (or "Fee Simple" or "Fee"). A **Life Estate** lasts only for the life of the named person. A **Future Estate** can be a **Remainder** interest or a **Reversion** interest.

***Easement*:** A **Non-ownership**, **Non-possessory** right to **Use** or access **Land** owned or leased by someone else. They are very limited in nature.

Leasehold Estate / Lease: **Real Property** can be **Leased** by the **Landlord / Lessor** to the **Tenant / Lessee** for a particular purpose for a particular period of time. **Leases** over **One Year** must be in **Writing** to be **Enforceable** under the **Statute of Frauds**.

Title: Determines **Ownership** of the **Real Property** and is evidenced by a **Deed**.

Deed: A **Document** that grants or transfers **Title** to **Real Property** from a **Grantor** to a **Grantee**. The strongest is a **General Warranty Deed**, the weakest is a **Quitclaim Deed.** Certain **Deed Restrictions** are not enforceable under non-discrimination laws.

***Security Interests*:** A **Borrower** signs a **Mortgage** (or **Deed of Trust**) as the **Mortgagor** (or **Trustor**) in favor of a **Lender** who is the **Mortgagee** (or **Beneficiary**) pledging **Real Estate** owned by the **Borrower** to secure the repayment of a **Loan**.

Recording Act: All states have statutory rules to resolve the **Priority** of **Claims** relating to **Real Property** and to give the public **Constructive Notice** of recorded items.

Abstract of Title: Historical summary of the **Publicly Recorded Documents** that affect **Title** to **Real Property**.

Title Insurance: Method of assuring **Title** to **Real Property** used in California and all other states. Two kinds: **Owner's Policy** and **Lender's Policy** (can be **CLTA** or **ALTA**).

Mechanic's Lien: May be **Recorded** by **Unpaid Contractors**, workers and materials providers to secure payment for their work on **Real Estate** and, in California, may be **Recorded** up to 90 days after the work is completed or the materials are supplied.

NOTES AND MORTGAGES

***Promissory Note*:** Documents a **Loan** between a **Borrower** and a **Lender**. Must include the **Parties**, **Loan Amount**, **Interest Rate and Maturity Date**. Usually includes clauses relating to **Amortization**, **Assumability** or **"Due on Sale"**, **Recourse** or **Non-Recourse**, **Prepayment** or **Lockout**, **Assignment**, **Default** and **Acceleration.**

***Mortgage*:** A two-party **Security Interest** in **Real Property** to secure the repayment of a **Real Estate Loan** that is given by a **Borrower / Mortgagor** to a **Lender / Mortgagee**.

Deed of Trust: A three-party **Security Interest** in **Real Property** that is given by a **Borrower / Trustor** to an independent **Trustee** to secure the repayment of a **Real Estate Loan** for the benefit of a **Lender / Beneficiary**. Used in California and most other states where it is available, because it is preferred over a two-party **Mortgage**.

***Senior vs. Junior Mortgage*:** Determined by state statutes that determine the **Priority** of **Recording**, unless the prior recorded mortgage contains a **Subordination Clause**.

Construction Loan: A **Loan** for the **Construction** of a **Building** or **Improvements**. **Loan** draws are made against a **Maximum Loan Amount**, are secured by a **Mortgage** or **Deed of Trust** against the **Real Property**, usually with **Recourse** to the developer.

***Purchase Money Loan*:** A **Loan** made for a **Borrower** to purchase **Real Estate**.

***Default*:** Failure to perform any of the terms or conditions of the **Loan** or **Mortgage**. The most common **Mortgage Default** is the failure to pay **Interest** and **Principal** when due. **Default** can lead to **Acceleration** of the **Loan** and **Foreclosure** of the **Property**.

***Foreclosure*:** With a Deed of Trust, can be **Judicial** (in court) or **Non-Judicial** (out of court) and involves a **Lender** ultimately taking **Title** to **Real Property** or forcing a **Sale** of the **Property** to satisfy the unpaid **Mortgage** balance. All **Junior Mortgages** are extinguished when a **Senior Mortgage Lender** forecloses on a **Property**, but the **Debt** secured by those **Junior Mortgages** is generally unaffected by the foreclosure.

Deficiency Judgment: Any **Loan Balance** remaining after a **Judicial Foreclosure Sale** can become a **Personal Judgment** against the **Borrower** if the loan is **Recourse**. California law generally protects homeowners from a **Deficiency Judgment**.

Workouts and Extension Agreements: Are usually preferred by **Lenders** over **Foreclosure**, and involve **Negotiations** with the **Borrower** to extend the **Maturity Date**, to increase the **Amortization Period**, or to temporarily reduce the **Mortgage Payments**, rather than permanently lowering the **Interest Rate** or reducing the **Loan Balance**.

Short Sale: When a **Lender** allows the **Sale** of a **Property** for less than the outstanding **Loan Balance**, typically without requiring the **Borrower** to pay the shortfall.

Bankruptcy: **Chapter 7** (liquidation) and **Chapter 11** (reorganization of a business).

TIME VALUE OF MONEY

Compound Interest: **$(1+i)^n$** where "i" is the periodic **Interest Rate** and "n" is the number of periods that are **Compounded**.

Compounding: Approach to taking a **Present Value** to a **Future Value**:

Future Value (FV) = Present Value x $(1+i)^n$

Discounting: Approach to taking a **Future Value** back to **Present Value**:

Present Value (PV) = Future Value ÷ $(1+i)^n$

Annuities (PMT): **Investments** with constant future **Periodic Payments**.

Interest Rate (i), Effective Yield, Internal Rate of Return (IRR): Various measures of the **Return on Capital** or the **Cost of Capital**.

***Net Present Value (NPV)*:** The **Present Value** of all **Projected Future Cash Flows** discounted at a specified **Discount Rate**, less the cost of the **Investment**.

***Internal Rate of Return (IRR)*:** The calculated **Discount Rate** at which the **Present Value** of all **Projected Future Cash Flows** is equal to the cost of the **Investment**.

Risk: Is essential to evaluate in order to determine whether the expected **Investment Return** is sufficient in light of the perceived **Risk**.

n	i	PV	PMT	FV

FIXED INTEREST RATE MORTGAGE LOANS

Capital Markets: **Financial** and **Securities Markets**, including the **Mortgage Market**.

Loan Availability: **Economic Growth** prospects (global, national and local), expected **Inflation**, and other **Risks** all affect the supply and cost of **Mortgage** funds.

Lenders as Intermediaries: Most **Real Estate Lenders** sell the **Loans** they **Originate** into the **Secondary Mortgage Market** rather than holding the **Loans** to **Maturity**.

***Loan Pricing*:** The **Interest Rate**, any **Fees**, **Points** and **Costs** charged by the **Lender**, and the **Loan Terms** (including any **Prepayment Penalties**).

Real Interest Rate: The nominal or contract **Interest Rate** minus expected **Inflation**.

Risk Adjusted Return: Expected investment **Return** relative to the perceived **Risk**.

Amortization: The process of **Repaying** the **Principal Balance** of a **Loan** over time.

Balloon Payment: The **Principal Balance** of the **Loan** due on the **Maturity Date**.

Pay Rate vs. Accrual Rate: Is the actual monthly mortgage **Payment** that is made by a **Borrower** at least equal to the **Accrued Interest** amount then due on the **Loan**?

Constant Payment Mortgage: When each monthly **Payment** is the same, the **Loan** will be **Fully Amortizing**, **Partially Amortizing**, **Interest Only** or **Negative Amortizing**.

Constant Amortization Mortgage: When each **Payment** includes a fixed amount of **Principal** repayment, with the monthly **Payment** and **Interest** amounts declining.

Reverse Annuity Mortgage: The **Lender** sends fixed monthly checks to the **Borrower** who must pay the accumulated **Principal** and accrued **Interest** on the **Maturity Date**.

Loan Fees and Costs: **Origination Fees** (for loan underwriting and processing), **Appraisal** and **Credit Report**. **Loan Fees** and **Points** increase the **Lender's Yield**.

Annual Percentage Rate (APR): Provides **Disclosure** regarding the effects of **Loan Fees**, **Points** and **Costs** on **Residential Loans** (assumes the **Loan** is held to **Maturity**).

Truth-in-Lending Act: **Federal Reserve Regulation Z** requires **Lenders** to include in **APR** calculations all **Loan Fees**, **Points** and **Costs**, but not any **Prepayment Penalties**.

Prepayment Penalties: Increase the **Effective Yield** to the **Lender,** are subject to **Negotiation** and are not reflected in the **APR** of a Loan. If a **Prepayment Penalty** is paid, **the Effective Yield** to the **Lender** will be higher if the **Loan** is repaid earlier.

Effective Annual Interest Rate: **Calculation** that considers all **Loan Fees**, **Points** and **Costs** and any **Prepayment Penalties** actually paid**,** and is therefore affected by the amount of **Time** the **Loan** is held until **Repayment**.

ADJUSTABLE / FLOATING RATE MORTGAGE LOANS

Interest Rate Changes: **Indexed** to other market **Interest Rates** (plus a **Margin**).

Index: **SOFR** (Secured Overnight Financing Rate) is replacing **LIBOR** (London Interbank Offered Rate), **US Treasuries**, **COFI** (11th district Cost of Funds Index), **Prime**. The **Index** can be overnight, 6 months, 1 year, or another interest rate series.

Margin: **Lender's Profit Margin** or spread (fixed for the loan term) over the **Index**.

Composite Rate: The **Index + Margin** is the **Composite Interest Rate** on the **Loan**.

Reset Dates: When the **Interest Rate Changes** (usually every 6 months or 1 year).

Caps and Floors: **Caps** are the **Maximum** and **Floors** are the **Minimum** allowed **Periodic** and/or **Lifetime** adjustments of the **Interest Rate** or **Loan Payment** amount.

Loan Terms: Are generally the same terms as with **Fixed Rate Loans**, other than the interest rate changes, and include **Assumable** or **"Due on Sale"**, **Recourse** or **Non-Recourse**, **Prepayment** or **Lockout**, **Assignment**, **Default** and **Acceleration**.

Loan Fees and Costs: As with **Fixed Rate Loans**, **Origination Fees**, **Points** and **Costs** may be charged to the **Borrower** to increase the **Effective Yield** to the **Lender**.

Interest Only or Amortizing: As with **Fixed Rate Loans**, **ARMs** are usually **Fully Amortizing**, but can also be written as **Interest Only** or **Partially Amortizing**.

Negative Amortization: If the **Loan Payment** required is less than the amount of **Accrued Interest** then due on the **Loan** because of a **Payment Cap**, there will be **Negative Amortization**. **Interest Rate Caps** do not cause **Negative Amortization**.

Teaser Rate: Initial **Interest Rate** on the **Loan**, often far below the **Composite Rate**.

Payment Shock: When the **Interest Rate** fully adjusts to the current **Composite Rate,** the new **Loan Payment** amount is often substantially higher than the **Teaser Rate**.

Interest Rate Risk: Because **ARM Interest Rates** adjust **Periodically**, **Interest Rate Risk** is higher for the **Borrower** and lower for the **Lender**. The shorter the time interval between **Reset Dates**, the higher the **Risk** for the **Borrower** and lower for the **Lender**.

Default Risk: Because the **Interest Rate** adjusts **Periodically**, the potential for future **Rate** increases elevates the **Risk** of a **Default** by the **Borrower** leading to **Foreclosure.**

Hybrid ARMs: **3/1**, **5/1**, **7/1** or **10/1** are **Fixed Rate Loans** for the first 3, 5, 7 or 10 years, then become **Adjustable Rate Loans** with annual **Interest Rate Reset Dates**.

Conversion Option: The right of the **Borrower** to convert the **Loan** from an **ARM** to a **Fixed Rate Loan** at a specified future date, usually with a **Fee** paid to the **Lender**.

MORTGAGES: ADDITIONAL CONCEPTS

Loan-to-Value Ratio (LTV): **Mortgage Debt** divided by **Property Value** (or **Price**).

Market Value of a Loan: The **Present Value** of all expected future **Loan Payments** (i.e. all expected future payments of **Principal** and **Interest**).

Incremental Borrowing Cost: The **Marginal Cost** of the additional amount **Borrowed**, taking into consideration the **Interest Rate** and other **Loan Fees**, **Points** and **Costs**.

Home Equity Line of Credit: A **Home Equity Line of Credit** (HELOC) can be secured by a **First**, **Second** or more **Junior Mortgage** and is typically a revolving **Line of Credit**.

Buydown Loans: When a **Seller** pays a **Fee** to a third-party **Lender** to buy down the **Interest Rate** on a **Purchase Money Loan** to induce the **Buyer / Borrower** to acquire the **Real Property**. The amount paid to buy down the **Interest Rate** will be much less than the **Present Value** of the reduced **Loan Payments** from the lower **Interest Rate.**

Below Market Seller Financing: When the pricing of **Seller Financing** (**Interest Rate** and **Loan Fees**, **Points** and **Costs**) is less than the **Market** pricing of available **Financing**, often to improve the **Sale Price** of a **Property** by a motivated **Seller**.

Wraparound Loans: Might be used by a **Seller** in a slow housing market and when the **Buyer** has poor credit to help sell a **Property.** The **First Mortgage** must stay in place, so it does not work if there is a **"Due on Sale"** clause in the **Loan Agreement**.

	n	i	PV	PMT	FV
A	360	0.5000%	$1,000,000.00	***-$5,995.51***	$0.00
B	360	0.5000%	**$500,000.00**	***-$2,997.75***	$0.00
C	360	**1.0000%**	$500,000.00	***-$5,143.06***	$0.00
D	360	**0.4583%**	$500,000.00	***-$2,838.95***	$0.00
E	360	**0.5000%**	***$473,512.22***	-$2,838.95	$0.00
F	**96**	0.4583%	$500,000.00	-$2,838.95	***-$434,189.63***
G	96	***0.5001%***	**$485,000.00**	-$2,838.95	-$434,189.63
H	360	**0.4167%**	$500,000.00	***-$2,684.11***	$0.00
I	360	**0.5000%**	***$447,686.73***	-$2,684.11	$0.00
J	**41**	0.4167%	$500,000.00	-$2,684.11	***-$473,199.86***
K	41	***0.4998%***	**$485,000.00**	-$2,684.11	-$473,199.86

BLUE = Input Change, *BOLD ITALICS = Output Change*

INCOME PRODUCING PROPERTIES - LEASES

Commercial Properties: **Office**, **Retail**, **Apartment**, **Industrial**, **Hotel**, **Mixed-Use**, …

Supply and Demand Analysis: Important for the **Valuation** of **Properties** and the projection of future **Rent** and **Occupancy** levels. **Global**, **National**, **Regional**, and **Local** factors affect the **Value** of **Properties** and **Rent Levels** for **Commercial** space.

Location: The most important factor in **Real Estate** because it is **Location** specific.

Occupancy / Vacancy: **Occupancy = 100% - Vacancy**. Driven by many factors, including **Supply and Demand**, **Location**, **Quality** (age, design, construction, etc).

Lease Terms: The **Parties** (**Landlord** / **Tenant** or **Lessor** / **Lessee**), **Premises**, **Term**, **Base Rent**, **CPI increases** or **Percentage Rent**, **Security Deposit** and/or **Guarantors**, **Allowable Uses**, **Insurance**, **Repairs** and **Maintenance**, **Damage** or **Destruction**, **Property Taxes** and other **Expenses**, **Assignment** and **Subletting**, **Defaults** and **Remedies**, **Subordination, Attornment** and **Non-Disturbance**, **Signage**, **Right of First Refusal** or **Expansion Option** on **Adjacent Space**, **Notices**, **Governing Law**.

Rental Income: **Flat Base Rent**, **Step-up Rent**, **CPI** or **Indexed Rent** with **Caps** or **Floors**, **Percentage Rent** with **Overage Rent** above a sales amount **Breakpoint**.

Concessions: **Free Rent**, reduced **Rent**, **Tenant Improvement** allowance (**TI**).

Property Expenses: **Gross Leases** (**Tenant** pays no **Expenses**), **Modified Gross Leases** (e.g., electricity), **Triple Net Leases** (**Tenant** pays all **Operating Expenses** including **Property Taxes**, **Insurance**, **Repairs** and **Maintenance**, and **Utilities**).

Expense Stop: **Property Expenses** per **Rentable Square Foot** up to the **Expense Stop** will be paid by the **Landlord** with **Expenses** over that amount paid by the **Tenant**.

Rentable vs. Usable Square Feet: **Rentable Square Footage** is **Usable Square Footage** plus the **Tenant's** pro rata share of **Building Common Areas** (including the public areas, shared hallways, shared restrooms, public stairwells, elevators lobbies).

Load Factor: **Rentable Area** divided by **Usable Area** (a lower ratio is more efficient).

Parking: Specific **Parking Spaces** can be assigned to a **Tenant** or per thousand square feet of rented space. **Parking Charges** can be added to the **Rent** or included.

Office Leases: **Anchor Tenants**, **Signage**, **Parking**, **Expansion Option**, **Purchase Option** or **Right of First Refusal**, **Overloading**, **Gross** or **Net** or **Expense Stops.**

Retail Leases: **Anchor Tenants**, **Signage**, **Parking**, **Co-Tenancy** clause, **Exclusivity**, **Radius** clause, **Termination** or **Kick-Out** rights, **Operating Times**, and **CAM** charges.

VALUATION OF INCOME PROPERTIES / APPRAISAL

Market Value: The **Price** at which a willing **Buyer** and a willing **Seller**, each without undue pressure, would **Buy** and **Sell** a particular **Property**, as of a particular **Date**.

Appraised Value: An estimate or **Opinion** of **Property Value**, for a particular **Purpose** as of a particular **Date**, by a particular **Appraiser**. The three primary **Appraisal Methods** are: **Sales Comparison**, **Capitalization of Income**, and **Replacement Cost**. Each of the three **Appraisal Methods** should, in theory, produce a similar **Valuation**.

Sales Comparison (or Comparable Sales): Compares recent **Sales** of highly **Comparable Properties** that are similar in **Location**, **Size**, **Age**, **Construction Quality**, and other factors. This is generally the only method used for **Residential Properties**, and one of the three methods used to appraise **Commercial Properties.**

Capitalization of Income: **Gross Rent Multiplier**, **Capitalization** of **Net Operating Income**, and **Discounted Present Value (DCF)** of projected future annual **NOI**.

Gross Rent Multiplier: **Annual Rental Income × Gross Rent Multiplier = Price** (or **Value**). The **Gross Rent Multiplier** must be derived from the **GRMs** on **Sales** of **Comparable Properties**. This simple method is often used for valuing **Apartments**.

Capitalization of NOI: **Cap Rate = NOI ÷ Price**, so **NOI ÷ Cap Rate = Price** (or **Value**), and **Cap Rate** x **Price = NOI**. The **Capitalization Rate** (aka **Cap Rate**) is derived from recent **Sales** of **Comparable Properties** and is affected by **Market** conditions. Falling **Interest Rates** will tend to lower **Cap Rates**, while rising **Interest Rates** will increase **Cap Rates**. An increase in **Demand** relative to **Supply** in the local **Market** will lower **Cap Rates**, while an increase in **Supply** relative to **Demand** will raise **Cap Rates**.

Discounted Present Value (DCF): A 10-year cash flow model is typically created. The **Discount Rate** used (or required **Internal Rate of Return**) is based on the Buyer's assessment of the **Risk** of achieving the projected future **NOI** and projected future **Sale Price** relative to current alternative **Investments** and **Capital Market** benchmarks.

Replacement Cost: The sum of **Land Value** + **Depreciated Replacement Cost** of the **Improvements**. **Depreciation** of the **Building** can come from **Physical Depreciation, Functional Obsolescence,** and **External Obsolescence**. The **Land Value** is derived from a **Comparable Sales** analysis of similar **Land** parcels. The **Replacement Cost** approach is more reliable when the **Improvements** are relatively new.

Land Value: A "**Highest and Best Use"** analysis to determine the **Value** of a particular **Land** site, whether the **Land** is **Vacant** or **Improved**. A particular **Land** parcel might actually be worth more if the existing **Improvements** are demolished and removed.

INVESTMENT ANALYSIS AND TAXATION OF INCOME PROPERTIES

Investment Benefits: **Cash Flow** (after **Taxes**), **Price Appreciation**, **Diversification**.

Real Estate Cycle: The **Real Estate** industry is **Cyclical**, with periods of **Growth** and periods of **Decline** in **Rents, Occupancy** and **Property Values**. The industry is very large and highly competitive, with many owners and limited concentration of ownership.

Investment Strategies: **Risk/Return** focus (**Core, Value-Added,** or **Opportunistic**), **Property Type** (e.g. **Office, Retail, Apartments, Hotels**), and/or **Geographical** focus.

Market Analysis: **Supply/Demand** analysis for **Property Type** and **Local Market,** and local **Absorption** projections to forecast future **Occupancy Rates** and **Rent Levels**.

Leverage: The use of **Debt** to acquire or own **Property**.

Loan to Value Ratio (LTV): **Mortgage Balance** divided by **Property Value** (or **Price**).

Debt Service Coverage Ratio (DSCR): Annual **NOI** divided by **Mortgage Payments**. A higher **DSCR** shows a greater ability for the **Borrower** to make **Mortgage Payments**.

Net Operating Income (NOI): **Rent** and other **Property Income** minus **Operating Expenses**. **NOI** is often **Capitalized** to determine the **Market Value** of a **Property**.

Before Tax Cash Flow: **NOI** minus **Debt Service** and **Capital Expenditures** (Cap Ex).

After Tax Cash Flow: **Before Tax Cash Flow** minus **Taxes**. The **Government** is your partner in every **Investment** through its power to **Tax** the annual **Income** and **Capital Gains** from **Sale**. **Federal**, **State**, **Local** and all other **Taxes** must be considered.

Taxable Income: **Net Operating Income** minus **Interest** and **Tax Depreciation**.

Tax Depreciation: The amount of the **Purchase Price** allocated to the **Improvements**, exclusive of the **Land**, is the **Depreciable Cost Basis** of the **Property**. The **Depreciable Cost Basis** can be **Amortized** as **Tax Depreciation** over **27.5 years** for **Residential Income Properties** and **39 years** for **Non-Residential Income Properties**.

Mortgage Interest Deduction: The **Interest** portion of the monthly **P&I Payments** is fully **Tax Deductible** for **Investment Properties**. Limited for primary and secondary **Homes** to the annual **Interest** on a total of up to **$750,000** of **Mortgage Debt**.

Unleveraged Returns vs. Leveraged Returns: The **IRR**, **ROE,** and **Equity Multiple** due to **Mortgage Financing**. The **Leveraged** returns should generally be higher than the **Unleveraged** returns to account for the additional **Risk** from the use of **Leverage**.

FINANCIAL LEVERAGE / FINANCING ALTERNATIVES

Financial Leverage: Allows an **Investor** to use less **Equity** to acquire an **Investment**, potentially achieve a higher **Leveraged Return** on **Equity**, and benefit from the **Tax Deductibility** of **Mortgage Interest**. **Investors** who desire a higher **Leveraged Return** on **Equity** might borrow at a higher **LTV** ratio, but as the **LTV** increases, **Risk** increases.

Positive and Negative Leverage: **Positive Leverage** is when the **Return** on **Equity** is higher with **Debt** than without, and **Negative Leverage** is when the **Return** on **Equity** is lower with **Debt** than without. With **Positive Leverage**, the higher the **LTV** ratio, the higher will be the **Leveraged Return** on **Equity**. With **Negative Leverage**, the higher the **LTV** ratio, the lower will be the **Leveraged Return** on **Equity**.

Loan Underwriting: The **Loan to Value Ratio (LTV)** and **Debt Service Coverage Ratio** (**DSCR**) are two of the key elements of a **Loan Underwriting**. Although the maximum **LTV** ratio and minimum **DSCR** levels vary with **Mortgage Market** conditions, **Lenders** are always more secure with a lower **LTV** ratio and a higher **DSCR**.

Prepayment Penalties, Yield Maintenance, Loan Lockouts: **Mortgage Loan** terms that make it costly or impossible for a **Borrower** to **Payoff** or **Refinance** a **Loan** before the contract **Maturity Date**.

Interest-Only Loan: **Borrower** pays only **Interest** on the **Loan**, with no **Principal Amortization**, and a **Balloon Payment** due at **Maturity**. Also called a "**Bullet Loan"**.

Negative Amortizing Loan: When the **Payment Rate** on a **Loan** is less than the **Accrual Rate** (i.e. **Interest** amount then due), there will be **Negative Amortization** and the **Loan Balance** will increase. Might be used when **Interest Rates** are very high.

Participating Loan: The **Lender** receives additional **Interest**, based on a formula, typically related to **Gross Income**, **NOI**, or **Cash Flow**, that is called a **Participation** or "**Equity Kicker**" but the **Lender** does not have any **Ownership Interest** in the **Property**.

Convertible Mortgage: When the **Lender** has the right to **Convert** part or all of the **Loan Principal** to an **Ownership Interest** in the **Property** at a specified time.

Mezzanine Loan: A **Loan** that is often **Secured** by the **Owner's Equity** in a **Property**, rather than by a **Mortgage** on the **Property** itself. Usually requires an **Inter-Creditor Agreement** between the **Mezzanine Lender** and the **First Mortgage Lender**.

Preferred Equity: An **Investment** in the **Ownership Interest** of a **Property,** that is not a **Mortgage**, with a **Preferred Return** that takes **Priority** over other **Equity Investors**.

Sale-Leaseback: An alternate means of **Monetizing** a **Property** where the **Seller** retains **Use** of the **Property** for the duration of the **Lease Term**. With a **Repurchase Option** in the **Lease**, the **Seller** may reacquire **Ownership** of the **Property** in the future.

RISK ANALYSIS

Risk: The higher the **Variability** of **Expected Returns**, the greater the **Risk** of an **Investment**. The lower the **Variability** of **Expected Returns**, the lower the **Risk**.

Risk Averse: **Investors** are generally **Risk Averse**, which means they require a higher **Expected Return** (probability weighted mean return) as compensation for incurring more **Risk** (i.e., higher **Variability** / **Volatility** / **Uncertainty** of **Expected Returns**).

Risk vs. Return: This is the key **Investment** consideration. When comparing potential **Investments**, their **Internal Rate of Return** (**IRR**) or projected **Net Present Value** (**NPV**) must be viewed in light of the **Risks** associated with each potential **Investment**.

Investment Risks: **Economic Risk** (global, national, and local), **Business Risk**, **Financial Risk**, **Interest Rate Risk**, **Liquidity Risk**, **Inflation Risk**, **Management Risk**, **Environmental Risk**, **Legislative Risk**, **Pandemic Risk**, etc.

Due Diligence: The **Process** of identifying the various **Risks** and potential **Returns** of an **Investment** by evaluating all the relevant and available **Information** to assess and determine whether the potential **Returns** are sufficient for you in light of those **Risks**. **Due Diligence** on a **Property** would include a review and analysis of a **Market Study**, the **Rent Roll**, major **Leases**, **Physical Inspection**, **Design** and **Engineering**, **Title** and **Survey**, **Zoning and Code Compliance, Taxes**, **Insurance**, **Litigation**, etc.

Sensitivity Analysis: **Modifying** key **Assumptions** about future **Investment Performance** (e.g., **Rent Levels**, **CPI**, **Vacancy Rates**, exit **Cap Rate**, **Sale Timing**), often done two at a time, to see their impact on the **IRR** and **Equity Multiple**. The **Assumptions** can be changed to model various scenarios in light of the potential **Risks**. The **Sensitivity Analysis** will show how sensitive the **Expected Return** (e.g., **IRR, NPV** or **Equity Multiple**) is to changes in your **Assumptions**.

Partitioning the IRR: Determining the portion of the **Investment Return** that comes from the annual **Cash Flow** and the portion that comes from the **Sale**/**Residual Value**.

DISPOSITION / RENOVATION OF INCOME PROPERTIES

Exit Strategies: To realize the increased **Equity** value created from an appreciated **Property**, an owner may **Sell**, **Exchange,** or **Refinance** the **Property**.

Hold/Sell Analysis: Analyze the **Marginal Rate of Return** from **Holding** the **Property** for an additional period of **Time** as compared to **Selling** the **Property** currently.

Property Sale: **Sell** for **Cash** and **Pay Off** all outstanding **Debt** and pay all federal, state, and local **Taxes** on any **Capital Gain**. See **IRS Form 1040 and Schedule D**.

Installment Sale: **Sell** on an **Installment Sale** basis receiving the **Sale Price** over **Time** and paying a proportional amount of the **Capital Gain Tax** with each **Installment** received. The amount of **Installment Sale Income** to be reported each year upon which **Tax** must be paid is a function of the **Ratio** between the "**Gross Profit"** on the **Sale** (i.e. **Sale Price** minus **Adjusted Tax Basis**) divided by the **"Contract Price"** as defined in **IRS Form 6252**. An **Installment Sale** is a form of **Seller Financing**.

Section 1031 Exchange: **Trade** the **Property** for **"Like Kind" Property** in a **U.S. Internal Revenue Code Section 1031** exchange transaction to **Defer** the **Taxes** on any **Capital Gain** but with the **Exchange Property** receiving a **Substituted Tax Basis**. **Section 1031** requires that the **Exchange Property** be **Identified** within **45 days** of the **Prior Sale** closing date, and the **Exchange Property** must be **Acquired** within **180 days** of the **Prior Sale** closing date. **"Unlike" Property** acquired in a **Section 1031** transaction is called **"Boot"** and is subject to **Capital Gain Taxes** on the **Sale**. **"Boot"** includes **Cash**, **Personal Property**, and any **"Unlike" Real Property** received in the transaction. See **IRS Form 8824**.

Refinancing: Replacing an existing **Loan** with a new **Loan**. If you **Refinance** with a larger **Loan** you will not pay any **Tax** on the additional **Loan Proceeds** received in connection with the **Refinancing**. If **Interest Rates** have fallen, it might be possible to **Refinance** with a larger **Loan** while reducing the annual **Borrowing Cost**, but **Points**, **Appraisal Fees** and other **Loan Costs** must be considered.

Renovation: As an alternative to a **Sale**, a **1031 Exchange,** or a **Refinancing**, the **Property** may be held and **Renovated** to increase **Rents**, increase **Occupancy**, and/or reduce **Operating Costs**, all of which should increase the **Net Operating Income** and thereby increase the **Property Value**. But in addition to the estimated **Renovation Costs**, the **Time**, **Effort** and **Opportunity Costs** related to the **Renovation** must also be carefully considered.

Sale-Leaseback: An alternate means of **Monetizing** a **Property** where the **Seller** retains **Use** of the **Property** for the duration of the **Lease Term**. With a **Repurchase Option** in the **Lease**, the **Seller** may reacquire **Ownership** of the **Property** in the future.

FINANCING CORPORATE REAL ESTATE

Lease vs. Own Analysis: Decision factors include: **Space** needed (relative to the size of the **Property)**; **Time** needed (**Short Term** or **Long Term**); **Risk** from **Property Ownership**; **Control** and **Management** of the **Property**; **Maintenance** and **Special Purpose Buildings**; **Tax** considerations from **Depreciation**; impact on the **Financial Statements** (**Balance Sheet** and **Income Statement**); access to and **Cost of Capital**.

Residual Value: A **Property's** projected future **Residual Value** (aka "**Exit Value"**) may not be an important part of a company's **Purchase Decision**. Instead of acquiring a **Property** that it needs to run its business, a company could negotiate a **Lease** with an **"Equity Kicker"** or a **Purchase Option** that might provide future value.

Corporate Real Estate Financing: The **Acquisition** of **Property** for **Company** use can be **Financed** with either **Mortgage Debt** or unsecured **Corporate Borrowing**. **Mortgage Debt** will generally be preferred if it is cheaper than the company's unsecured **Borrowing Cost**.

"Capital" Lease: Formerly, if a **Lease Term** exceeded 75% of an **Asset's** remaining economic life, or if the **Present Value** of future **Lease Payments** was the majority of the **Property's FMV** at **Lease Commencement** (90%+), or if **Property Ownership** was likely to be **Transferred** to the **Lessee** upon **Lease Expiration** (e.g. a **Purchase Option** substantially below **FMV**), then the **Lease** was treated as a "**Capital**" **Lease** and reported as if that part of the **Asset** was **Owned** by the **Lessee**.

"Finance" vs. "Operating" Lease: Under the recent ASC 842 of the FASB, the **Present Value** of all **Lease Payments** for **Leases** over one year must be **Capitalized** and reported on the **Balance Sheet** as a **Right-of-Use Asset** and a **Lease Liability**, and annual **Lease Payments** will be reported as an **Expense** on the company's **Income Statement**. If the **Lease Term** is one year or less, **Lease Payments** will only be reported on the company's **Income Statement** and not on the **Balance Sheet**.

Sale-Leaseback: A company might **Sell** a **Property** it owns and simultaneously **Lease** it back on a **Long-Term** basis to obtain **Cash** while retaining **Use** of the **Property**. The company might negotiate a **Repurchase Option** into the **Lease** to give it the possibility to re-acquire that **Property** in the future. **Selling** a **Property** and **Leasing** it back in a **Sale-Leaseback** transaction, with the **Lease** written so that it will be reported as an **Operating Lease,** is a form of **Off Balance Sheet Financing** for the company.

"Hidden" Corporate Real Estate Value: Companies are required to report **Property Values** at the **Lower** of **Depreciated Cost** or **Market Value**. This can lead a publicly traded company to become an **Acquisition Target** when the **Market Value** of its **Properties** substantially **Exceeds** the reported depreciated **Book Value**.

FINANCING PROJECT DEVELOPMENT

Project Development: **Acquiring** a **Land Site**; **Financing** and **Construction** of a **Building** (**Office**, **Apartments**, **Shopping Center**, **Warehouse**, **Hotel**, **Self Storage**, etc.); **Leasing** and **Managing** the **Property**; then **Selling**, **Exchanging** or **Refinancing**.

Mixed-Use Development: A **Combination** of **Real Estate** uses in a single **Project**.

Development Decision Factors: Global, national and local **Economic Forecast**; **Supply** and **Demand** for space (i.e. **Tenant** demand); **Competition** from other **Current** and **Planned Developments**; **Capital Markets** (i.e. **Financing Cost** and availability).

Project Feasibility: A **Feasibility Study** should be done to forecast **Tenant Demand**, **Rent Levels**, **Construction Costs**, **Project Timing**, **Exit Strategies** and future **Sales Price**, and evaluate the **Risks**. **Location** is always a key factor in the analysis.

Construction Financing: Covers the **Hard Costs** and **Soft Costs** of **Construction**. **Construction Loans** are disbursed in **Draws** after **Costs** are incurred, are typically **Recourse** to the **Developer**, are usually **Short Term** (maturing after **Construction** is expected to be completed), and **Floating Rate** with **Construction Interest Capitalized** into the outstanding **Loan Balance**. **Construction Lenders** want a **Permanent Lender** ("**Take-Out**" **Lender**) in place to pay off and replace the **Construction Loan** when **Construction** is completed and various **Leasing** targets have been achieved. A **Stand-By Lender** is a **Permanent Lender** who doesn't intend to actually fund their loan.

Project Development Issues: **Building**: **Footprint**, **Envelope**, **Façade**, **Stacking Plan**; **Traffic Mitigation Plan**; **Property Taxes; Permitting**: **Zoning Codes**, **Building Codes**.

Permitting: The process of obtaining local **Government Approvals** (e.g. city planning, city council) to **Permit** the proposed **Development**. The **Project** must comply with local **Zoning Codes** and **Building Codes** (or obtain a **Variance**) for a **Building Permit** to be issued. The **Permitting** process involves **Negotiation** with city planners and their staff.

Zoning Codes: **Allowable Uses**; **Maximum Floor Area Ratio** (**FAR**); **Height Restrictions**; **Minimum Lot Size**; **Minimum Parking Ratios**, **Building Setbacks**, etc. **Zoning Codes** specify what may be **Permitted** to be built as of right (e.g. **R1**, **R2**, **R3**, **R4, R-5, C-1**, **C-2**, **C-3**, **M-1**, **M-2**, **M-3**, **A-1**, **A-2**, …) and may include incentive zoning, inclusionary zoning, and/or cumulative zoning.

Building Codes: Specify the **Materials** and approved **Methods** for **Construction**. City staff must approve the **Architectural** and **Engineering Designs** and **Specifications** for the **Project**, including the **Site Plan**, **Elevations** and **Project Renderings**. **Code Compliance** is enforced by city inspectors during **Construction** before a **Certificate of Occupancy** ("**C of O**") will be issued by the local authority after **Project Completion** in compliance with all **Building Codes** and **Zoning Codes**.

FINANCING LAND DEVELOPMENT

Land Development: A highly **Fragmented**, **Competitive** and **Local** business.

Land Acquisition: **Option Agreements** are often used to give **Time** to the **Land Developer** to pursue the **Entitlement Process**. Periodic **Option Payments** can be made over an extended time frame (monthly, quarterly, annually), and if the **Developer** ultimately exercises the **Option** the **Option Price** for the **Land** will be paid at the closing of the **Land Acquisition**.

Zoning and Land Use: City or county **Land Use Plans** specify the allowed uses for each **Land** parcel (e.g. **Residential**, **Commercial**, **Industrial**, **Agricultural, Special Purpose, …**) with subcategories for allowed density of use (e.g. **R-1**, **R-2**, **R-3**, **R-4**, **R-5**, **C-1**, **C-2**, **C-3**, **M-1**, **M-2**, **M-3**, **A-1**, **A-2**, …). The local **Land Use Plan** is usually updated every 5-10 years, and the local **Zoning Code** can be revised, in whole or in part, whenever necessary.

Entitlement Process: The process by which the **Land Developer** applies to the local authorities to convert **Unentitled Land** to **Land** that is **Entitled** to be **Subdivided** and **Developed** for a particular purpose and size (**Office**, **Apartments**, **Shopping Center**, **Warehouse**, **Hotel**, etc.) **Developing** a project that is inconsistent with the local **Zoning Code** and **Land Use Plan** requires a **Variance** from the local **Planning Authorities**.

Land Financing: Difficult to obtain, **Low LTVs**, generally **Recourse** to the **Borrower** and with **Tight Conditions** from the **Lender** to assure **Repayment**.

Release Schedule: The **Time** frame within which the **Lender** expects the individual **Land Parcels** in a **Land Development Project** to be **Sold** according to **Release Prices** agreed to in the **Land Loan** documents so that the **Loan** will be **Repaid**.

Release Prices: The pre-agreed **Minimum Prices** at which the **Developer** can **Sell** individual **Land Parcels** and obtain the **Lender's Release** from its blanket **Mortgage Lien** for the **Land** parcels **Sold**.

Onsite Improvements: Land grading, internal paving, private streets, lighting, landscaping, etc.

Offsite Improvements: Public roads, street lighting, traffic lights, sewer line extensions, parks and schools, etc.

STRUCTURING REAL ESTATE INVESTMENTS

Organizational Forms: To **Minimize Taxes**, **Limit Liability**, and define **Management** roles and responsibilities in **Investments**. **Partnerships**, **Limited Liability Companies** (**LLCs**), and **Real Estate Investment Trusts** (**REITs**) are the primary **Legal Entities** used for structuring the **Acquisition** and **Ownership** of **Real Estate Investments**.

Pass-Through Entities: **Pass-Through Entities** do not pay **Taxes** directly but instead pass on their **Taxable Income** or **Loss** to the **Partners**, **Members**, or **Shareholders** in those **Entities** who must report their allocable share of the **Taxable Income** or **Loss**.

Partnerships: Can be either a **General Partnership** or a **Limited Partnership**. All **Partnerships** are **Pass-Through Entities** for **Tax** purposes and have a **Finite Life**. **Title** to **Property** owned by the **Partnership** will be in the name of the **Partnership**. In a **General Partnership**, each **General Partner (GP)** has **Decision-Making Authority** and **Unlimited Liability**. A **Limited Partnership** must have at least one **General Partner**, who will have **Decision-Making Authority** and **Unlimited Liability**, and any number of **Limited Partners (LPs)**, with no **Decision-Making Authority** and whose **Liability** is generally **Limited** to the amount of their **Investment**. **Partnership Interests** are **Personal Property** and so are not eligible for a **Section 1031 Exchange**. A **Partnership Agreement** governs the rights and responsibilities of the **Partners**.

Limited Liability Company (LLC): In 1988, the IRS approved the **Limited Liability Company** structure. In 1994, California became the 46th state to enact an **LLC** law. **LLC Investors** are called **Members**, and all **Members** have **Limited Liability**. In California, only one **Member** is needed to form an **LLC,** and **LLCs** have **Unlimited Life**. **LLCs** are managed by a **Managing Member** or a third party, can elect **Pass-Through** status for **Tax** purposes, and are governed by an **Operating Agreement**.

Limited Liability Partnership (LLP): In California, only professional organizations can be **LLPs** (law firms, etc.), so an **LLP** cannot be used for **Real Estate Investments**.

Corporations: **Legal Entities** owned by **Shareholders** (individuals or other legal entities), managed by a **Board of Directors** in accordance with their **Articles of Incorporation** and **Bylaws,** and have **Unlimited Life**. **Dual Taxation** (**Corporate** and **Shareholder** levels) makes **"C" Corporations** unattractive for **Property Investments**. **"S" Corporations** have **Shareholder** restrictions but can elect **Pass-Through** status.

Joint Venture: In the U.S., not a **Legal Entity** but rather an **Agreement** between at least two parties to pursue a specific investment objective. **Joint Ventures** will typically involve a **Partnership**, **Limited Liability Company**, **Corporation** or other **Legal Entity**.

Syndication: Not a **Legal Entity** but a means of **Financing Investments** by selling **Partnership Interests** or **LLC Interests** in a proposed or existing **Project**.

Capital Account: **Accounting** of an **Investor's Share** in the **Net Worth** of an **Entity**.

THE SECONDARY MORTGAGE MARKET

Fannie Mae and Freddie Mac: The **Federal National Mortgage Association** ("**Fannie Mae**" – created in 1938, privatized in 1968) and the **Federal Home Loan Mortgage Corporation** ("**Freddie Mac**" – created by the Emergency Home Finance Act of 1970) are the largest buyers of **Home Loans** in the United States. Together, they buy almost half of all residential home loans. **Fannie Mae** and **Freddie Mac** are huge, NYSE listed companies with $7 trillion of mortgage loans and securities. During the global financial crisis of 2007-2008, **Fannie Mae** and **Freddie Mac** nearly went bankrupt and were placed under the conservatorship of the **Federal Housing Finance Agency** ("**FHFA**" – Housing and Economic Recovery Act of 2008).

Ginnie Mae: **Government National Mortgage Association** ("**Ginnie Mae**" – HUD Act of 1968) is a wholly owned U.S. government corporation within the **Department of Housing and Urban Development (HUD)**. **Ginnie Mae** guarantees **Mortgage Backed Securities**.

Conforming Loans: **Mortgage Loans** that **Conform** to **Fannie Mae** and **Freddie Mac Underwriting Guidelines** for **Loan Size** (for 2023: $726,200 and $1,089,300 in high cost counties), **Creditworthiness** (**FICO** score), **DSCR**, **LTV**, and other criteria.

Non-Conforming Loans: **Mortgage Loans** that **Do Not Conform** to all the **Underwriting Guidelines** of **Fannie Mae** and **Freddie Mac** at a particular time.

Subprime Loans: **Mortgage Loans** that fall below the **Underwriting Guidelines** for **Creditworthiness** (**FICO** score), **DSCR**, and/or **LTV**. Not related to **Loan Size**.

Seasoned Mortgages: **Mortgage Loans** that have been paying monthly **Principal** and **Interest** on time. The longer the payments stay current, the more "**Seasoned**" the **Mortgage**.

Residential Mortgage Backed Securities ("RMBS") and Commercial Mortgage Backed Securities ("CMBS"): Created when pools of **Residential** or **Commercial Mortgage Loans** are **Tranched** into **Securities** for sale to other **Investors** in the **Capital Markets**. The primary **Risks** associated with these **Securities** are **Default Risk** and **Prepayment Risk**.

Default Risk: When the **Default Rate** on the pool of **Mortgage Loans** underlying the **Mortgage Backed Securities** is higher than was projected at the time of the MBS offering.

Prepayment Risk: When the **Prepayment Rate** on the pool of **Mortgage Loans** underlying the **Mortgage Backed Securities** is higher than was projected at the time of the MBS offering.

Collateralized Mortgage Obligations ("CMOs"): **Debt Securities** that are issued using a pool of **Mortgage Loans** as **Collateral**, where the **Issuer** retains **Ownership** of the **Loans**.

Collateralized Debt Obligations ("CDOs"): Any **Debt** can be **Collateral** for the **Securities**.

Principal Only Tranches ("POs"), Interest Only Tranches ("IOs"), Floaters and Inverse Floaters: Some of the unique **Securities** that can be created to appeal to different **Investors**.

REAL ESTATE INVESTMENT TRUSTS (REITS)

REIT Structure: The **REIT** structure was created by the US Congress in 1960 to allow small **Investors** to participate in the **Property Markets** without paying a **Corporate Tax**. **REITs** provide **Liquidity, Dividends**, **Diversification**, and **Professional Management**. If all **REIT Rules** are met, a **REIT** will not pay **Tax** at the **Entity** level, **REIT Dividends** will be **Taxed** to the **REIT's Shareholders**, but **REIT losses** will not be passed through to the **Shareholders**.

Types of REITs: Most **REITs** are **Equity REITs** that primarily own **Properties**, and the rest are **Mortgage REITs** that primarily own **Mortgage Debt** and **MBS**. Most **Equity REITs** focus on a single **Property** type (**Office**, **Retail**, **Apartments**, **Industrial**, **Hotels**, **Self-Storage**, etc.). **Mortgage REITs** focus on either **Residential Mortgages** or **Commercial Mortgages**.

REIT Qualifications: **REITs** must be managed by a **Board of Directors**; must have at least **100 Shareholders**; not more than 50% of a **REIT's** shares can be held by five or fewer **Shareholders** ("**5/50" Rule**); **Shares** must be **Fully Transferrable**; can be **Public** or **Private**.

Distribution Requirements: At least **90%** of a **REIT's Taxable Income** must be distributed as **Dividends** to the **REIT's Shareholders**, otherwise the **REIT** will pay **Corporate Tax**.

Asset Requirements: At least **75%** of a **REIT's Assets** must be related to **Real Estate**, government securities or cash, and not more than **20%** of a **REIT's Assets** can be in **Taxable REIT Subsidiaries** (TRSs were authorized by the **1999 REIT Modernization Act**).

Income Requirements: At least **95%** of a **REITs Gross Income** must be from **Real Estate Rents**, **Profits** from **Asset Sales**, **Mortgage Interest** income and **REIT Dividends** received.

Net Asset Value (NAV): **Net Asset Value** is an accounting measure of a **REIT's Net Worth**, which may or may not accurately reflect its current **Market Value** if the **REIT's Assets** have increased or decreased in value relative to their **Depreciated Cost**. If a **REIT's Stock Price** reflects its **NAV** more than its true **Market Value**, the **REIT** may be a takeover candidate.

Funds from Operations (FFO): **REIT Income** is measured as "**Funds from Operations**", which is **Earnings per Share** (**EPS**) adjusted by adding back **Depreciation** and excluding any **Profits** or **Losses** from **Asset Sales**, and is a measure of its **Dividend** paying ability.

UPREITs: **Umbrella Partnership REITs** issue **Operating Partnership Units** (**OP Units**) that are **Convertible** into **REIT Shares** and allow a **REIT** to buy **Appreciated Properties** with **OP Units** instead of cash so **Sellers** of the **Properties** can achieve a **Section 1031** tax deferred exchange. When **OP Units** are converted into **REIT Shares**, **Capital Gain Taxes** will be due.

REIT Growth Drivers: **REITs** can 1) Increase the **Net Operating Income** from their existing **Properties** by increasing **Rents** and **Occupancy Levels**; 2) **Acquire** additional **Properties**; 3) **Renovate** or **Expand** existing **Properties** or **Develop** new **Properties** on excess **Land**; 4) Provide **Property Services** through **Taxable REIT Subsidiaries** (**Leasing** or **Property Management**); 5) **Financial Engineering** (**Property Debt** or **REIT Corporate Leverage**).

REAL ESTATE INVESTMENT PERFORMANCE AND PORTFOLIO CONSIDERATIONS

Risk vs. Return: **Investments** with more **Risk** (i.e., more **Volatility** of **Returns**) should provide a higher **Expected** (i.e., mean) **Return**. **β** (beta) is a measure of the **Volatility** of **Returns** for an **Investment** relative to a benchmark, and **α** (alpha) is a measure of the **Actual Return** of an **Investment** relative to the benchmark given the level of **Investment Risk**.

Property Performance Information: Unlike stocks and bonds, **Real Estate Performance** information is much less available. The **National Council of Real Estate Investment Fiduciaries** (**NCREIF**) produces quarterly returns for five **Property Types** (**Office**, **Retail**, **Apartments**, **Industrial** and **Hotels**), but values are based on **Appraisals** giving imperfect **Market Value** information, and the **NCREIF Index** is an **Unleveraged Index**. **REIT Stock Price** performance information is a proxy for certain types of **Real Estate Performance**, but **REIT Stock Prices** are also affected by non-real estate related stock market movements.

Business Risk: Specific to the **Property Type**, **Location** and **Market Conditions**.

Default Risk: **Properties** are usually **Leveraged**. Higher **LTVs** cause higher **Default Risk**.

Liquidity Risk: **Selling** a **Property** takes time. **Real Estate** is an **Illiquid Investment**.

Diversification: A way to lower the **Volatility** of a **Portfolio's Expected Returns**.

Correlation Coefficient: Measures the relative movement of one set of numbers as compared with another, ranging from **+1** (**Perfectly Positively Correlated**), to **0** (**No Correlation** at all), to **-1** (**Perfectly Negatively Correlated**).

Inflation Hedge: **Real Estate** is considered a good **Inflation Hedge** as it is **Positively Correlated** with **Inflation** (when **Inflation** increases, **Property Values** also tend to increase).

Portfolio Diversification: Buying **Properties** in different **Geographic Regions** and of different **Property Types** will generally provide greater **Portfolio Diversification**.

Global Diversification: The increasing number and variety of **Investment Opportunities** around the world provide **Diversification** benefits from low or negative **Correlations** with investments in the United States (or your home country) that might reduce **Portfolio Risk**, but **Foreign Investments** may have additional **Risks** that must be managed.

Foreign Investment Risks: 1) **Information Risk**; 2) **Legal**, **Tax** and **Property Rights Risk**; 3) **Currency and Interest Rate Risk**; 4) **Political Risk**; 5) **Culture/Communication Risk**.