JAMES A. GRAASKAMP COLLECTION OF TEACHING MATERIALS

V. INDUSTRY SEMINARS AND SPEECHES - SHORT TERM

I. Other Presentations In Which Either The Date And / Or Sponsoring Organization Is Missing

3. Development Topics

d. "Future Philosophy and Strategy in Buying Industrial Real Estate", circa 1985-86

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Future philosophy and strategy in buying industrial real estate — Circa 1985-86 Probably a talk to alumni

I General introduction to topic outline

A. Brief report on UW real estate program

1. Enrollment - 65-85-105

B. School searching for Dean

C. Department searching for young faculty in marketing research

D. Department thinking about 1987 curriculum (exhibit 1)

E. Alumni thinking of October seminar - Thursday evening the 18th through Saturday the 20th (Northwestern game)

F. Alumni planning corporate fundraising

G. Issue: should we report Alumni giving and promote competition among the successful

H. Challenged Fortune magazine on its MIT article; they have requested course materials.

II Misc. thoughts on the economy

A. MIT study supports operations of Kondrieteff cycle. Professor Sterman-Sloan School of Management

B. Causes of the long wave - overexpansion and decline of economy caused by lags in capital investment and long life of plant and edquipment. Overexpansion is amplified by many self-reinforcing processes, including capital self-ordering, wages and labor markets, real interest rates.

C. Symptoms of Long-Wage Peak and Early Downturn:

1. Rising unemployment
2. Declining capital expansion
3. Declining capacity utilization
4. Increqasing severity of business cycle
5. Increasing private debt burden
6. Low, then rising real interest rates.

D. A business-cycle upturn can occur during the early phase of the long-wave downturn. Especially if the downturn is gradual.

E. Economic prospects for long wave downturn and trough Present to early 1990s:

1. Low and erratic economic growth
2. High and erratic unemployment
3. High real interest rates
4. Continued defaults on debt
5. Increasing protectionism
6. Possibility of deflation
7. Emergence of leading edge sectors and regions
8. Emergence of new social forms

F. Economic prospects for next long wave expansion.
Beyond early 1990s:

1. Resumptio- of moderate growth
2. Declining unemployment
3. Declining real interest rates
4. Gradual rebuilding of debt
5. Diffusion of new innovations
6. Regulation of new institutions

G. In the short run failure to reduce deficit, uneasiness about the trade deficit and need of banks to amortize foreign losses will cause interest rates to rise slowly. for long term rates. Short term rates will stay firm since real rate of return on government's is greater than 8%.

H. 1985 is seen as a transition of moderate prosperity with a wait and see attitude about efforts to reduce the deficit and/or modify the tax law

II The Great Tax Law Debate

A. Syndicators report the sale of tax shelter investments has slowed down as investors hear talk of major tax reform. Serious analysts believe uncertainty is more significant than real economic threat to real estate.

B. Federal reserve bulliten author indicates current system with a few adjustments would work very well by increasing the zone of taxation rather than the basic philosophy change in the flat tax or the VAT tax. Major changes are likely.

C. Roulic sees taxes as a minor part of y ield.

1. Concerning the economic consequences of a 30% flat tax on real estate investment, the actual value changes may not be as severe as imagined based on research by Stephen Roulac & Company. Considering depreciation first, property can now be written off over 18 years, which is equivalent to about 5% per year, after an allocation for nondepreciable land is made. At a 50% tax bracket, the annual depreciation deduction is worth 2.5% of the purchase price (50% of 5%), whereas thr flat tax would reduce this tax shelter factor to 1.5% (30% x 5%).

2. Similarly for interest deductions, it cqn be assumed a 60% loan-to-value ratio mortgag would generate an interest deduction of approximately 7% of a property's value annually, equivalent to 3.5% tax shelter for the 50% tax bracket investor. With a flat tax, this tax shelter element would be reduced by 1.4% points (or some 40%) to 2.1 % (30% x 7%)

3. The aggregate annual difference of 2.4 percent (1.4% interest plus 1% depreciation) is equal to present value terms to approximately 7-10% over an expected five to eight year holding period for the property. But a 7-10% value reduction is readily offset by a change in the property's key components of value - current reutnr and changes in value of the capital position. Any combination of a 2.5% annual rent increase or a 70 basis points improvement in the cap rate would offset the tax shelter lo-s of the flat tax.

4. In a detailed analysis of the investment returns realized by 16 public real estate limited partnerships that have sold all their properties, and adjusting the returns for inflationarey effects, appreciation accounted for 68% of all investment retorn, cash flow 24%, and tax benefits 9%. While these ratios certainly can change over time, they do indicate that tax shelter does not loom significant as many perceive it to

be in real estate investing returns.

D. Folks at PREA thought perhaps they should lobby for tax changes which will favor investment position of tax exempt pensions by curtailing overbuilding and depressing prices to benefit cash buyers

IV. Demographic Factors Influencing Real Estate Markethold no surprises but changing segmentation

A. Old baby boom now moving into the 35-44 age group which are believed to be the most active buyer group for housing and retail.

B. Reorganization into sudo-neighborhood clusters and smaller scale shopping areas with need to identify.

C. SRI moving beyond traditional age, sex, income, education demographics to lifestyle demographics. See Atlantic Monthly October 1984.

D. If inflation flattens out to 4 - 5% deluxe rentals are cheaper than buying on a square foot per month out of pocket basis. An $80,000 townhouse costs more than $1 a square foot to own; could rent for $.80-$.90; rents will move up on residential more than commercial.

V. Neat Ideas Department

A. Jack Nickalaus - dip for the implicit assumption - redesigned the golf ball to save land on a golf course, but still plays with 72 strokes.

B. Sam Zell - Real estate strategies involve monopoly and spread - marginal revenue against average cash cost.

C. Checklist for design based on social research - John Zeisel - Building Diagnostics, Inc. 15 Kirkland Rd., Cambridge, MA 02138

D. Cady Westbey - cash flow model for cumulative sensitivity analysis on the IBM using response mathematics from nuclear engineering (include handout)