



RE STRATEGIC SOLUTIONS, LLC

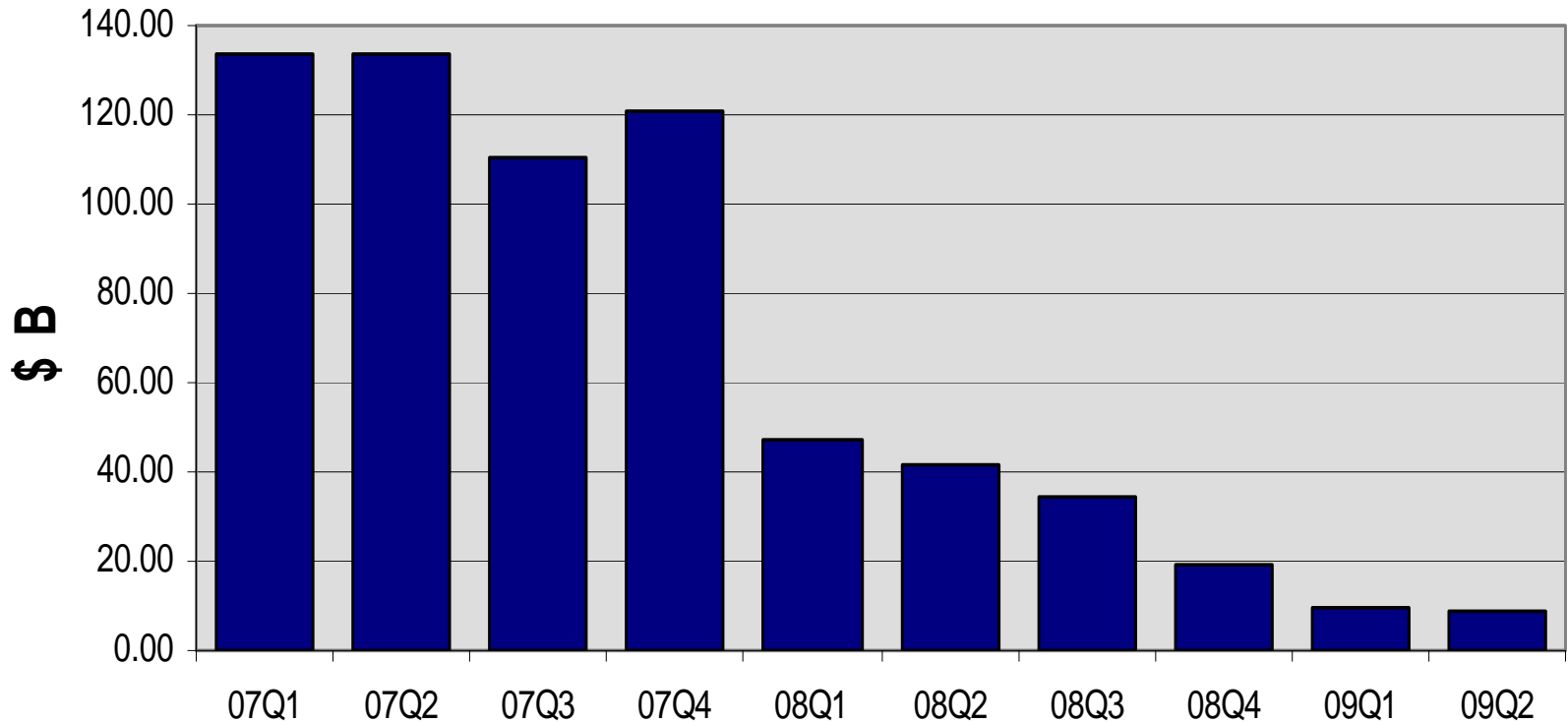
Deriving Valuation Metrics From the REIT Market

**Appraisal Institute Fall Conference
November 19, 2009**

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Sales volume of CRE down 90%

Quarterly Volume (transactions > \$5M)



NO SALES – NO PROBLEM

- **Cap Rate**
 - **Price/SF or Price/Unit**
 - **Effective Gross Income Multiplier**
- Can be derived from REIT stock prices**

Traditional Ro

- Comparable Sales
- Band of investment
- $R_o = Y_o - \triangle a$
- Surveys
- $R_o = DCR \times M \times R_m$

Rely on transactions or mortgage info

Premise of New Model

- Institutional investors indifferent btw buying private or public real estate, i.e. their current actions in either market should reflect fair value
- Real estate fundamentals (rent, rent growth, vacancy, expenses etc.) affect public and private real estate similarly
- Public real estate pricing moves in same direction as (although often leads) private real estate

$$Ro = Io / Vo$$

- **Io (net operating income) can be measured from info in a REIT's quarterly SEC filings and website reports**
- **Io can be annualized going forward based on analyst's and company's guidance of Io growth over N4Qs**

$$V_o = V_m + V_e$$

- V_m = liabilities and non-convertible preferred stock
- V_e = stock market price X number of shares outstanding

Therefore,

$$R_o = I_o / (V_m + V_e)$$

Only variable is stock price!

Skills an appraiser needs to have

- **Analyze an income statement**
 - GAAP net income vs. real estate NOI
 - Straight lining of rent
- **Analyze a balance sheet**
 - Non-convertible subordinated debentures???

Limitations of the model

- REITs more liquid/volatile than private real estate

Yes, but

- REIT investors accept more liquidity in exchange for more volatility
- Private investors accept less liquidity in exchange for less volatility.
- Volatility differences can be mitigated by using ave. stock price L30D

Limitations of the model

- REIT assets may not mirror subject property

Yes, but choose “comp” REITs with

- similar geographic “tilt”
- similar physical and economic characteristics, as reflected by ave. rent per unit or per SF

CA “tilted” REITs (by reported % of NOI or base rent)

■ Office

- Douglas Emmett (95%)
- Kilroy Realty Corp (97%)
- Maguire Properties (100%)

■ Industrial

- Mission West Properties (100%)

■ Retail

- Regency Centers (30%)

■ Apartments

- BRE Properties (80%)
- Essex Property Trust (80%)
- Equity Residential Trust (30%)

Need for Add't Research

- **Back-testing data to determine the historical correlation between R_o in the private market versus R_o extracted from the public market.**

Conclusion

- Evidence of current market activity, as demonstrated daily in the public markets, can represent alternative market information for appraisers
- See *Appraisal Journal*, Fall 2009, “Deriving Capitalization Rates and other Valuation Metrics from the REIT Market”.