KENYATTA UNIVERSITY

UNIVERSITY EXAMINATIONS 2017/2018

DIGITAL SCHOOL OF VIRTUAL AND OPEN LEARNING

SECOND SEMESTER EXAMINATION FOR THE DEGREE OF BACHELOR OF COMMERCE

BAC 414: REAL ESTATE FINANCE

DATE: Friday 22nd June 2018 **TIME: 8.00a.m -10.00a.m**

INSTRUCTIONS:

- **Answer All questions**
- **Show All the necessary workings**

QUESTION ONE

a) Explain the meaning of the following terms as used in real estate property transactions.

i) Title assurance [1 marks]

ii) Abstract of title [2 marks]

iii) Easements [1 mark]

iv) Encumbrances [2 marks]

b) Outline five common law requirements for adverse procession. [5 marks]

c) Clearly distinguish the following terms as used in the classification of real estate based on property rights;

i) Estate at sufferance and Estate at will [2 marks]

ii) Estate for years and Estate from year to year [2 marks]

iii) Reversion and remainder [2 marks]

iv) Freehold and leasehold [2 marks]

QUESTION TWO

a) Identify any Five factors that influence the supply of the space market as considered by investors and appraisers when undertaking a market analysis. [5 marks]

b) Jamii commercial complex has three floors of rentable space with a single tenant on each floor The first floor has 15,000 square feet of rentable space and is currently renting for Kshs. 18 per square foot. Three years remain on the lease. The lease has an expense stop at Kshs 5 per square foot. The second floor has 20,000 square feet of rentable space and is leasing for Kshs 20 per square foot and has four years remaming on the lease. This lease has an expense stop at Kshs. 5.50 per square foot. The third floor has 15,000 square feet of leasable space and a lease just signed for the next five years at a rental rate of kshs 22 per square foot, which is the current market rate. The expense stop is at Kshs 6 per square foot, which is what expenses per square foot are estimated to be during the next year (including management expenses). Management expenses are expected to be 5 per cent of effective gross income and are not included in the expense stop. Each lease also has a CPI adjustment that provides for the base rent to increase at a third of the increase in the CPI. The CPI is projected to increase 9% per year. Estimated operating expenses for the next year include the following :

Property taxes-Kshs.100,000

Insurance - Kshs20,000

Utilities-Kshs90,000

Janitoria-Kshs40,000

Mintenance-Kshs50,00

Property taxes and insurance expenses are projected to increase 3 per cent per year, Utilities by 2% per year and maintenance by 4% per year. The market rental rate at which leases are expected to be renewed is also projected to increase 3% per year . When a lease is renewed, it will have an expense stop equal to operating expenses per square foot during the first year of the lease. To account for any time that may be necessary to find new tenants after the first leases expire, vacancy is estimated to be 10 percents of EGI for the last two years (years 4 and 5).

Required:

Compute the net operating income (NOI) for the next five years. [5 marks]

QUESTION THREE

a) Assume that a fully amortizing mortgage loan for Kshs. 20 M is made for 20 years at 12 percent interest with consensus of lenders at the time the loan is made is that a 12 % rate of interest is sufficiently high to compensate them for all forms of risk bearing expected to occur over the time that the lean is expected to be outstanding. However, warranting at 4% interest rate instead of 12% . Determine the magnitude of the loss to the lender over the 20 year-period.

[5 marks]

b) A 25-year fixed rate mortgage is extended to a borrower by CBT Bank Ltd for Kshs 20,000,000 at annual interest of 12 per cent with constant monthly payments. Compute the constant monthly mortgage assuming:

i) Full amortization [2 marks]

ii) Partial ammonization with a balloon payment of Kshs 7,000,000 at the end of the mortgage period. [2 marks]

iii) Negative amortization leading to a mortgage balance of Khs.25 m as at the end of the mortgage period. [2 marks]

c) Highlight any Five attributes upon which syndicates" investment objectives generally vary around. [5 marks]

QUESTION FOUR

i) Briefly explain the following investment strategies that an investor may adopt in the real estate industry.Contrarian investing [2 marks]

ii) Arbitrate investing [2 marks]

iii) Value strategy [2 marks]

a) Elaborate how each of the following factors would affect an Own versus lease decision:

i) Space requirements 2 marks]

ii) Maintenance [3 marks]

iii) Access to capital markets [2 marks]

iv) Off balance sheet financing [2 marks]