FOREIGN INVESTMENT
IN THE PHOENIX REAL ESTATE MARKET

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ABSTRACT

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Our research into foreign investment in Phoenix real estate analyzes the extent of foreign participation, the entry and growth strategies of foreign investors, and their investment criteria. This study is one part of a joint study by the National Association of Realtors and the Center for Real Estate Development at the Massachusetts Institute of Technology. The purpose of the study is to: examine foreign investment activity in Phoenix, Atlanta and Honolulu, investigate strategies adopted by foreign investors with respect to vertical integration, and update similar city studies performed in 1987 on Chicago, Los Angeles and Washington.

Our findings indicate that foreigners have a large and growing presence in Phoenix real estate. Unlike other cities, however, foreign investment is almost exclusively in the form of development projects as opposed to the purchase of completed buildings. Other findings include: foreign investors have been attracted to Phoenix because of its high growth, minimal barriers to entry and perceived lack of indigenous competition; investments in Phoenix are largely part of a permanent portfolio diversification into the U.S. economy with the result that investors emphasize long term capital appreciation over current cash flow; and, despite a variety of different entry strategies, differences between foreign and local developers tend to converge over time to the point that foreign firms become indistinguishable from their local competition.

We expect foreign investment in Phoenix to grow with the dynamic economy and anticipate that the next development in this area will be the acquisition of newly completed buildings by foreign investors.

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CHAPTER 1

Introduction

Recent well-publicized acquisitions of prime U.S. property have markedly increased industry and public awareness of foreign investment in U.S. real estate. Given the record prices of the more notable of these transactions, some U.S. industry professionals are eyeing their own portfolios with a renewed interest. Other U.S. real estate professionals seem fearful of competition, while still others and some of the public are raising concerns about the "selling of America". All are interested in more information about the extent of foreign investment in U.S. real estate and its implications for domestic investment, development and/or political interests.

A joint study conducted in 1987 by the Center For Real Estate Development at the Massachusetts Institute of Technology and the National Association of Realtors systematically analyzed foreign investment strategies in the markets of Los Angeles, Chicago, and Washington. This study concluded that foreign investors have been attracted to U.S. real estate because of higher returns than those available in their home markets, U.S political and economic stability, the growth potential of the U.S. economy, and more recently, the falling value of the dollar vis-a-vis other currencies.

Recent foreign investors have concentrated on fully leased, premium quality office buildings in the Central Business Districts of major metropolitan areas. This bias may be explained by: the newcomers' desire to minimize risk by purchasing investment grade properties; the highly urban home culture of foreign investors, which are largely Western European and Japanese; and the home office's greater comfort with "name brand" product.

One conclusion of last year's research forecasts that as trophy properties in the CBDs of first tier cities become more scarce, and as foreign investors become more knowledgable about the U.S. real estate market, foreign investors will diversify into suburban properties in first-tier cities and class A office buildings in smaller, second-tier cities.

This paper is part of a followup study to last year's research that focuses on foreign real estate investments in the second tier cities of Atlanta, Honolulu and Phoenix, with our paper specifically reviewing foreign real estate investment in Phoenix. Our objectives were to identify foreign investors in Phoenix, list major foreign owned properties, evaluate the investment criteria utilized by these investors, and make conclusions about their behavior and its implications.

Chapter 2 reviews the history of foreign investment in U.S. real estate in terms of magnitude and characteristics. This chapter also examines existing literature and summarizes the findings of the CRED/NAR research conducted in 1987 to suggest why foreign firms continue to find U.S. real estate attractive. Finally, Chapter 2 discusses the impact that overbuilt conditions in many major markets has had on new foreign investment.

Chapter 3 focuses specifically on the greater Phoenix market area, which for our purposes is defined as Phoenix proper, the communities to the Northwest (Glendale, Peoria and Sun City), Northeast (Scottsdale and Paradise Valley), Southeast (Mesa, Tempe, Gilbert and Chandler) and to the Southwest (Goodyear, Avondale and Tolleson). In this chapter we examine the economic and demographic history of Phoenix and identify those factors that will likely affect future growth and investment in this region. Chapter 3 also includes an update on current market conditions for commercial, industrial and residential real estate in Greater Phoenix.

In Chapter 4, we provide a detailed list of foreign owned real estate in the Phoenix area. We also present profiles of selected foreign investors, with an emphasis on the nationality, structure, experience and future plans of each firm.

Finally, the major findings and conclusions of our study are detailed in Chapter 5 and our presented together with our projections of likely future trends for foreign investment in Phoenix real estate.

CHAPTER II

Overview of Foreign Investment in U.S. Real Estate

Who is Buying America?

Foreign investment in U.S. real estate is as old as the Republic; the Dutch purchase of Manhattan Island is just the first example of locals thinking that gullible foreigners overpaid for real estate. Despite this long history, the issue of foreigners "buying up America" has raised considerable attention in the 1980's as foreign investment in American real estate more than tripled from $6.1 billion in 1980 to $21.2 billion in 1986. While these numbers are large in absolute terms, they represent only 10% of total direct foreign investment in the U.S. and less than 2% of the total value of developed real estate in the U.S. (1)

In the last five years, attention has focused on new investment from Japanese firms, which are financially liquid as a result of large current account surpluses enjoyed by Japan with its trading partners. Backed by a strengthening yen and energized by eased restrictions on foreign capital investment, Japanese investment in U.S. real estate ballooned nearly ten-fold from $264 million in 1980 to $2.4 billion in 1986. (Exhibit 2.1)

At the same time, British and Dutch investors (traditionally the two largest investors in both the U.S. economy as a whole and in real estate in particular) increased their holdings 785% and 160% respectively. The attention paid to the Japanese by the U.S. investment community is due in large part to Japan's sudden emergence as a major player in U.S real estate and their practice of concentrating investment in selected cities and paying top dollar for "trophy" office buildings. Growing economic and political concern over the U.S.'s large trade imbalance with Japan only serves to magnify the perceived impact of Japanese investment. (2)

In fact, the new invasion of Japanese capital is only the latest wave of capital to hit American shores. Foreign capital has long been attracted to the United States due to the sheer size of its economy, its political and economic stablility, and its relatively open free market system. For example, following the oil shock of 1979, recycled petrodollars financed the OPEC countries' 191% increase in investment in U.S. real estate from $300 million in 1980 to $872 million in 1986. (3)

As of 1986, four countries accounted for nearly

EXHIBIT 2.1

Foreign Direct Investment in U.S. Real Estate ($millions)
By Country

	1980	1981	1982	1983	1984	1985	1986
Canada	1,158	1,770	1,882	2,106	2,844	2,750	3,182
Belgium	4	9	11	10	10	9	9
France	24	24	24	28	66	41	55
W. Germany	493	651	780	815	966	1,100	1,138
Netherlands	999	1,507	1,742	2,189	2,471	2,212	2,601
United Kingdom	569	1,220	2,051	3,140	4,135	4,764	5,037
Japan	264	302	394	457	744	1,536	2,480
OPEC	300	373	551	610	707	726	872
All Other	2,309	3,033	3,962	4,591	5,818	6,264	5,857
TOTAL	6,120	8,889	11,397	13,946	17,761	19,402	21,231

EXHIBIT 2.2

Foreign Direct Investment in U.S. Real Estate
By Country As A Percent Of Total

	1980	1981	1982	1983	1984	1985	1986
Canada	18.9%	19.9%	16.5%	15.1%	16.0%	14.2%	15.0%
Belgium	0.1%	0.1%	0.1%	0.1%	0.1%	0.0%	0.0%
France	0.4%	0.3%	0.2%	0.2%	0.4%	0.2%	0.3%
W. Germany	8.1%	7.3%	6.8%	5.8%	5.4%	5.7%	5.4%
Netherlands	16.3%	17.0%	15.3%	15.7%	13.9%	11.4%	12.3%
United Kingdom	9.3%	13.7%	18.0%	22.5%	23.3%	24.6%	23.7%
Japan	4.3%	3.4%	3.5%	3.3%	4.2%	7.9%	11.7%
OPEC	4.9%	4.2%	4.8%	4.4%	4.0%	3.7%	4.1%
All Other	37.7%	34.1%	34.8%	32.9%	32.8%	32.3%	27.6%
TOTAL	100%	100%	100%	100%	100%	100%	100%

Sources: Real Estate Review, "Foreign Direct Investment in U.S. Real Estate." Summer 1987 page 69; and Survey of Current Business, June 1987 page 45.

two-thirds of the foreign direct investment in U.S. real estate (Exhibit 2.2). These were the United Kingdom (24%), Canada (15%), the Netherlands (12%), and Japan (12%).(4)

Why They Buy

A number of theories have emerged to explain the steadily growing appetite that foreigners have exhibited for U.S. real estate. A recent factor has been the decline of the U.S. dollar with respect to most other major trading currencies. Beginning in 1984, the dollar has steadily retreated from all-time highs against the yen, the pound and the DM. As the dollar declines in value, it becomes relatively cheaper for foreigners to acquire assets denominated in dollars. While the evidence is not conclusive, it appears that a weak dollar is a buy signal to foreign investors, but conversely, a strong dollar is not a primary inducement to foreign investors to sell real estate assets to recognize windfall foreign exchange gains.

In addition, the U.S. remains a capital haven with political stability, economic growth, good labor relations and limited government intervention. Combined with the "hard" nature of real estate assets, which tend to hedge against inflation, these factors have made American real estate attractive to foreigners seeking a store of value.

The U.S. real estate market remains the largest national marketplace in the world's largest economy. As such, it provides investors with unparalleled opportunities to diversify risk by investing in a wide variety of real estate products, investment vehicles, and geographic regions.

In addition, the current yield available for prime U.S. commercial real estate is estimated at 8.5%, while comparable returns in Europe and Japan are 3%-5% and 1%-2%, respectively. Although current yields are distorted by varying levels of national inflation, investors generally receive higher returns from U.S. real estate investments than in other real estate markets because of tax rates, financing arrangements, ease of market entry, and frequent product turnover.

What Drives Foreign Investors' Willingness to Pay

The willingness in recent years of foreign firms, particularly Japanese, to pay hefty premiums for signature office properties located in stable regional markets gives rise to two questions:

1. Why do foreigners value these properties more than do Americans?
2. Have foreigners been paying prices higher than necessary to purchase these properties?

Given that the U.S. real estate market functions as an auction with assets therefore sold to the highest bidder, it is clear that some foreigners value U.S. real estate assets more highly than do domestic investors. Because foreign investors (especially newcomers) are often initially less knowledgeable of local market conditions and therefore prefer to limit risk by investing in fully leased office buildings in a few major cities, the presence of these large capital sources in cities like New York and Los Angeles has had a profound impact on prices paid for first class office buildings in these markets. Domestic investors appear to percieve risk-adjusted returns to be more favorable in other sectors of the real estate market.

The fact that certain foreign investors have been criticized for paying too much for the properties they want to buy is also due to the nature and method of the bidding system. The closed-bid system tends to disadvantage the bidder when the asset being sold is highly desirable and the purchasing power and willingness to pay of competing bidders is not known. Because the Japanese had highly specified investment criteria, they seemed to initially prefer running the risk of over-bidding for a property over losing the ownership opportunity. Given the amount of time and money likely spent analyzing this new market, the Japanese wanted to *guarantee* their market entry and made aggressive but nevertheless acceptable bids from the standpoint of their required return criteria. Since these transactions have in hindsight enlightened the Japanese regarding domestic investors' willingness to pay, future transactions may be more finely tuned. However, the presence of multiple foreign investors with similar return criteria and cost factors in the same market will likely produce continued high prices (by domestic standards) for premium grade real estate properties. So while the Japanese have left money on the table in a number of major transactions, sometimes significant amounts, it is noteworthy that they were able to justify these prices at the time.

Foreign investors are often confronted with limited investment choices at home, and returns on these opportunities are lower than those that can be found in the U.S. In recent years, Japanese investors have been highly liquid and have been freed from significant government restrictions on overseas investment. This fact, together with a booming U.S. real estate market, appears to have influenced these buyers to pay top dollar for premium properties, believing that properties of this quality might not be available in the market again for a considerable time.

Much has also been said concerning the longer time horizon of the investment decisions of foreign investors. Because of tax benefits from converting current income into long term gain, the long term benefit of financial leverage, and the ability to hedge against inflation, much of an investment's appreciation in value occurs over the long term. Investors willing and able to wait (due to favorable liquidity positions) are likely to value these long term benefits more highly than an investor with a short term time horizon or a requirement for immediate cash returns.

Foreign investors, benefitting from corporate cultures that look beyond a few quarters, have generally sought long term value in their real estate purchases and as such have been active buyers in the market. Clearly, because much of a real estate investment's value is created over the long term, investors who discount the future less than other investors are going to pay higher prices.

Another factor affecting the foreign investor's investment decision is the expanding anti-growth political sentiment that is occuring in most of the strong real estate markets in the U.S. The obvious effect, if this sentiment translates into effective anti-growth legislation, will be to limit the supply of new commercial real estate. Given an expectation for economic growth and demand for new space, prices would rise as competition for existing and limited new supply intensifies.

We have discussed the effect that the low value of the dollar versus the yen, for example, has on the willingness to pay of the Japanese. It appears that the Japanese might not only be thinking that real estate looks cheap at these exchange rates, but also that the dollar's current level is abnormally low, and the opportunity for exchange gains is good as the dollar recovers to more normal levels. While the foreign investor might be induced to invest in dollar denominated assets for foreign exchange profit opportunities, we believe that this circumstance is a factor in the buy decision, but of secondary importance in decisions concerning asset management or disposition.

Today and Tommorrow

While foreign investment in U.S. real estate is as old as the Republic, it is likely to have the longevity of the Republic as well. Direct investment in U.S. real estate by foreigners was estimated to be $21 billion at year-end 1986. Clearly, this is a continuation of a trend toward more investment in the U.S. and we expect that the future will bring even more foreign ownership of real estate assets in the U.S. Continuing innovations in global capital markets, in addition to continuing favorable political and economic conditions in the U.S., should instigate existing and new investors to continue investing in U.S. real estate.

Innovations in foreign capital formation, continuing trade surpluses, and limited investment opportunities at home should continue the need for forign investors to find external investment opportunities. For example, new vehicles for capital formation now being structured in Japan are tapping large capital pools previously restricted to domestic investment. Several recent offerings have been completed in Japan that combined Wall Street financial expertise with Japanese capital for the purpose of buying U.S. real estate. Partnerships are being formed to cater to the individual Japanese investor, who to this point has had few investment alternatives. Given Japan's high savings rate, this represents a potentially significant untapped capital source.

Investment restrictions on many foreign capital sources are being relaxed. Limitations on the level of asset commitment to foreign assets as a percentage of total assets are being eased and new entities are being allowed to invest overseas. The financing capacity and superior credit ratings of many major foreign banks are likely to spur additional investment and expand the kinds of positions taken in property investments. Convertible and participating loan structures should increase the number and size of joint ventures occuring between foreign capital sources and American developers.

Continued and expanding foreign capital availability for U.S. investment and the scarcity of signature investment grade properties, together with growing familiarity on the part of foreign investors with the U.S. real estate market should serve to broaden the investment band satisfactory to these investors. This is likely to result in considerable levels of investment in secondary cities as well as in secondary locations within major cities.

Having identified the scope and motivation for foreign investment in U.S. real estate, we turn in the next chapter to a review of the background and nature of the Phoenix economy and real estate market.

Chapter III

The Phoenix Real Estate Market

Early Development

Phoenix, a metropolitan area of approximately 1,940 square miles located in South Central Arizona, is the capitol of Arizona and the fastest growing city in the Southwest. Phoenix is second only to Los Angeles in population growth during the 1980's and had a 1987 population of about 2 million. Since 1867, when miners from a small camp at Wickenburgh fifty miles to the north first settled in Phoenix, the city developed, protected and promoted its considerable resources to become the leading commercial and tourist center in the Southwest. The once remote location and desert conditions initially obscured the potential of the area for commerce and agricultural development. However, available land, rich soil, a long growing season, and favorable weather drew determined settlers seeking to build new lives for themselves.

Phoenix is the rebirth of a Hohokum Indian settlement. The Hohokum Tribe mastered an early water distribution and storage system to irrigate large land areas for agricultural use. The new settlers rebuilt and expanded this canal system to exploit the significant agricultural potential of this area. As far back as 1903, the City of Phoenix had established regulatory policies over water management, in recognition of the potentially adverse impact that growth and development might have on this precious resource. Development at that time occurred around water access areas, and the amount and location of growth largely depended on the extension of water canals. By 1885, over 200 miles of canals were in place supporting the raising of livestock and citrus and grain crops.

Railroads and the Roosevelt Dam

Later development depended on the City's ability to improve transportation access for tourists seeking to enjoy the dry, temperate climate and to open up trading export routes for its agricultural economy. In 1887, a branch of the Southern Pacific was completed that connected Phoenix to this southern transcontinental railroad line. Eventually, later lines were added and Phoenix was connected to major cities in the North. Regional transportation and transcontinental distribution routes became the key to continued growth and prosperity for Phoenix.

Water management continued to be a principal factor in the continued growth of the metropolitan Phoenix area. The

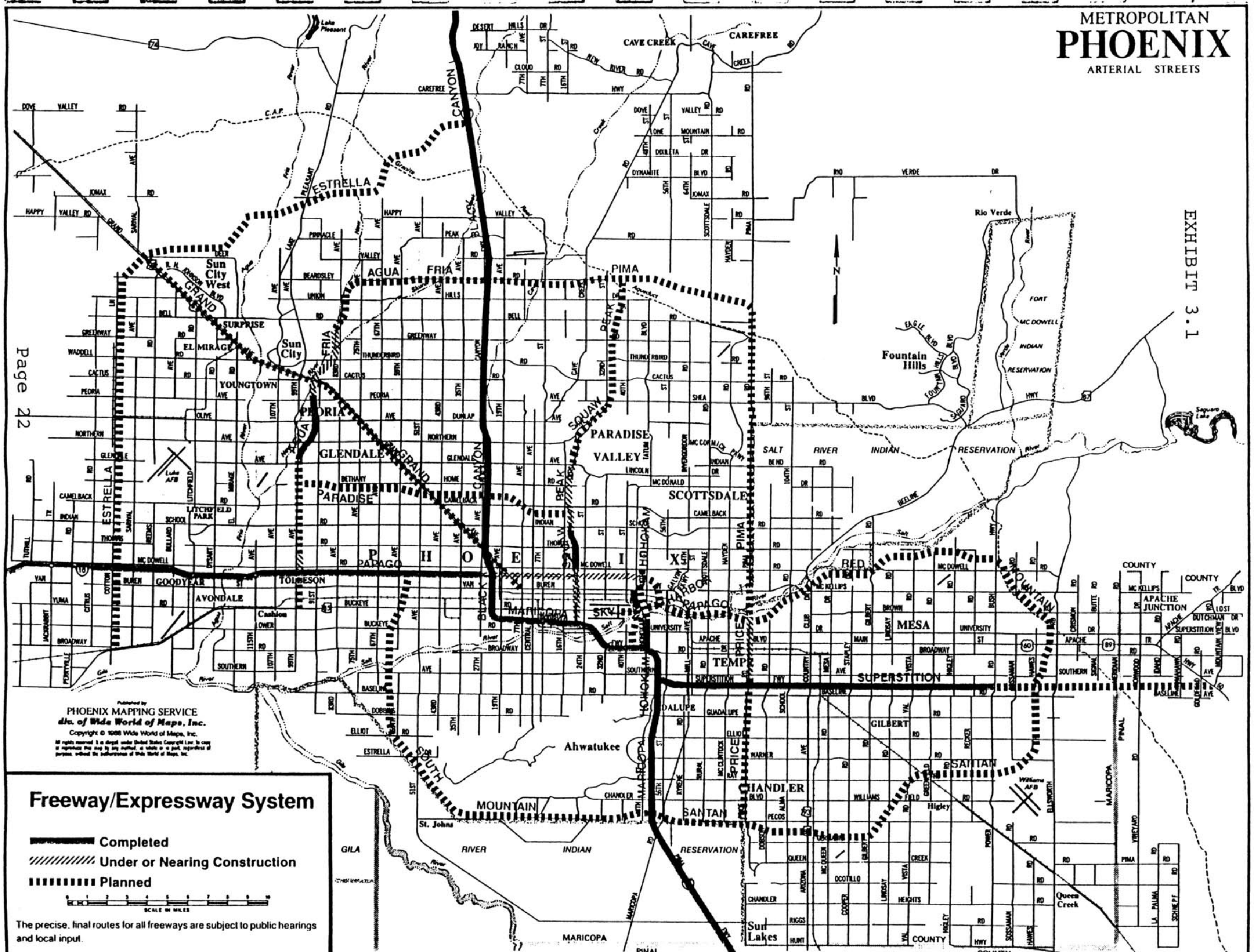
Roosevelt Dam, which was partially sponsored and funded by the City of Phoenix, was completed in 1911 and provided a secure water source for Phoenix to realize its full agricultural potential.

Freeways

With the introduction of the automobile in the 1920's and the beginnings of the trucking industry, new development occurred in areas that could be served by automobile and truck rather than by rail or wagon. The effect was dramatic. The next wave of prosperity in the area was largely dependent on the area's development of sufficient road and access systems to generate additional growth. Phoenix today is essentially an automobile town and its freeway system is an integral part of life in the City. A number of significant freeway improvement projects are underway.

Phoenix has developed from an agricultural community into a diversified economy dependent for its economic base on manufacturing, construction, tourism and agriculture as well as a large stable of service businesses. The area benefitted greatly from the government spending in the war effort during the 1940's as well as the stationing of large numbers of military personnel (primarily Army Air Corps) in the region. Around that time, several manufacturing facilities re-located

EXHIBIT 3.1



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Fountain Hills
Rio Verde
SALT RIVER INDIAN RESERVATION
FORT MC DOWELL INDIAN RESERVATION
MESA
APACHE JUNCTION
TEMPE
GUADALUPE
GILBERT
CHANDLER
Higley
Williams AFB
Ahwatukee
GILA RIVER INDIAN RESERVATION
Sun Lakes
Queen Creek
MARICOPA
PINAL
COUNTY

to the Phoenix area due to the availability of land and labor resources. Motorola was the first significant company to open a manufacturing facility in the Phoenix area.

Significant freeway expansion and improvements underway and planned for the area are certain to improve access and expand the range of development in outlying districts. Ninemajor freeways are planned to link interior locations in Greater Phoenix (see Exhibit 3.1). In addition, the completion of the Sky Harbor International Airport has had a positive effect in making Phoenix a major regional commercial and tourist center.

The Phoenix metropolitan area is expected to grow rapidly over the next two decades as more companies locate or start-up in the region and as an aging national population seeks to relocate to more favorable climates. Public policy measures in freeway development and water use and storage should provide controls over development and create an ability to meet expected demand in the area.

Demographics

The population of Phoenix is forecast to grow dramatically over the next two decades. Mountain West Research forecasts that the population of the Phoenix Metropolitan area will increase 77% over the next fifteen years and will jump from being the 22nd largest metropolitan area to the 12th largest metropolitan area in the U.S.

The population is not particularly diverse with relatively low numbers of minority residents. Approximately 1/4 of the population is in the senior citizen age range, with very high geographic concentrations as retirement communities have tended to be developed in certain sections of the metropolitan area. Since 1970, retired households have increased almost 200% in number while the total population has grown at about half that rate. About 85% of the senior citizen population owns a single family home, condominium or townhouse.

The median educational level of Phoenix-area heads of household is 12.3 years with a median age of 29.9 years. 43% of college graduates have attended graduate school and there are eleven colleges, including Arizona State University, located in the Phoenix area.

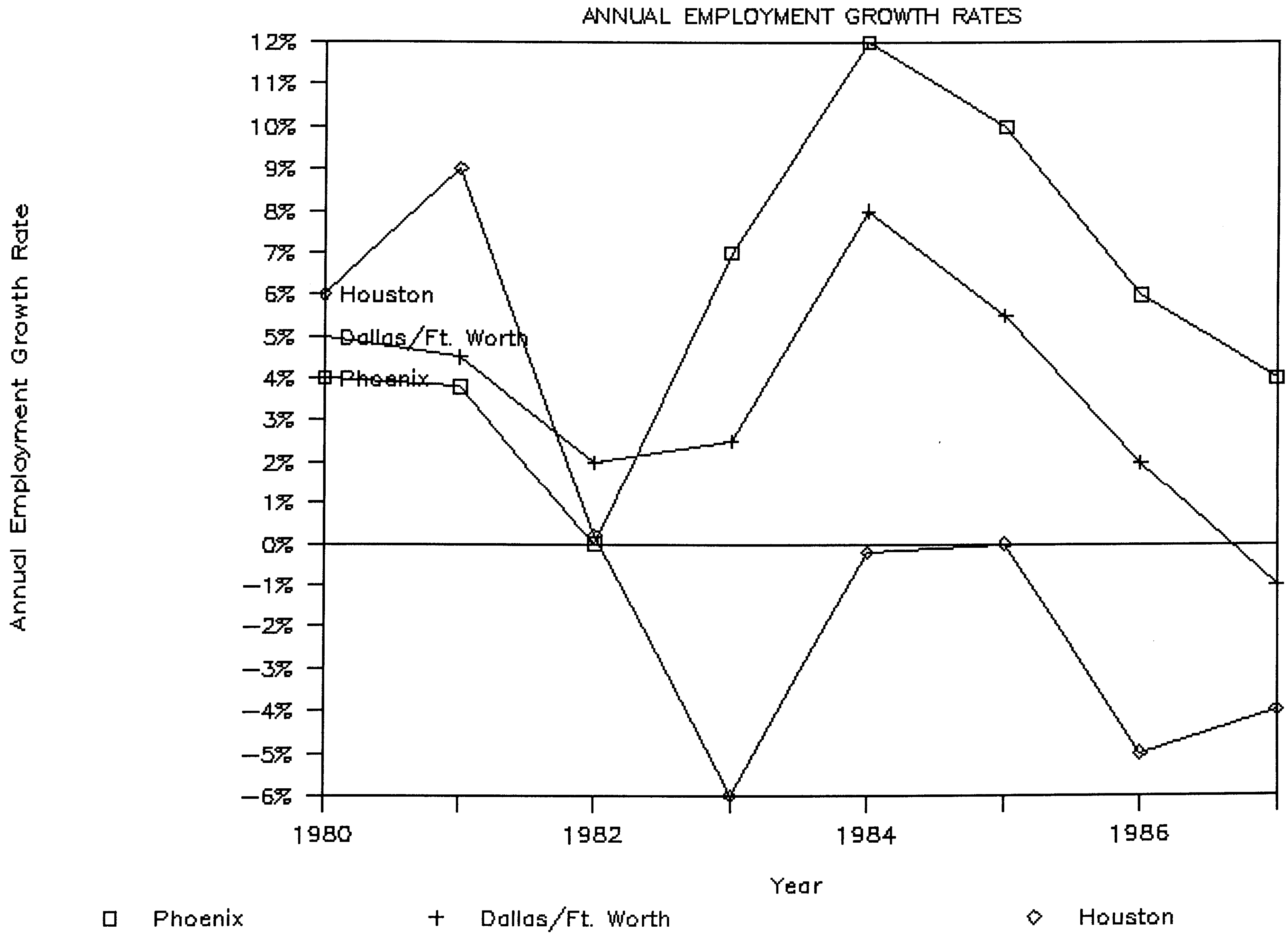
__Employment__

The Phoenix economy has grown rapidly over the past five years fueled by in-migration, a strong services sector and a strong base in high technology manufacturing. After a brief downturn during the 1982 recession, the Phoenix economy recovered strongly from 1983 to 1987 as evidenced by employment increases of 11% in 1984 and 9% in 1985. Employment growth has continued strong through 1987, though at reduced rates of about 5% annually in 1986 and 1987. The downturn in employment growth is attributed to steep declines in construction activity and lower growth in defense related industries. Because of continued strong in-migration, population growth and growth in the services sector of the economy, Wharton Econometric Forecasting Associates projects that Phoenix will have an average annual growth in employment of 3.6% through 1996. This is the highest growth rate of any large U.S. city. (1)

Phoenix vs. other Sunbelt Cities

Phoenix's recent strong growth and near term prospects are in contrast to other Sunbelt cities such as Houston and Dallas/Fort Worth. Houston's economy was heavily oil-dependent and outpaced the rest of the country when oil prices were high, but collapsed along with oil prices in 1982. Net losses in employment have been shown annually beginning in 1982 except for a brief and weak recovery in 1983. Houston's economy is still in a no growth pattern. (2)

EXHIBIT 3.2


ANNUAL EMPLOYMENT GROWTH RATES
12%
11%
10%
9%
8%
7%
6%
5%
4%
3%
2%
1%
0%
−1%
−2%
−3%
−4%
−5%
−6%
Annual Employment Growth Rate
Houston
Dallas/Ft. Worth
Phoenix
1980
1982
1984
1986
Year
Phoenix
Dallas/Ft. Worth
Houston

Dallas/Fort Worth has a more diversified economy than Houston with major strengths in services, manufacturing and distribution not directly related to the energy industry. Nevertheless slumps in the construction, real estate and finance sectors led to losses in employment beginning in 1986. (3)

Exhibit 3.2 shows comparative employment growth rates for Phoenix, Houston and Dallas/Fort Worth.

CURRENT REAL ESTATE MARKET SITUATION

Fueled by strong population and employment growth, new construction in the Phoenix area reached record levels in the early and mid-1980's. While Phoenix has continued to grow, economic growth was outpaced by new construction. At present the Phoenix market, as detailed below, is typified by a slowdown in new construction and continued absorption of existing space in order to reduce current high vacancy levels.

Office Market

The Phoenix office market has grown dramatically since 1970 when the market had a total of 3.2 million square feet. By 1987, the market had grown nearly ten-fold to 31.2 million square feet (4). New construction from 1981 through 1987 responded to surging population and employment growth. While absorption of new space was robust, it could in no way keep up with the massive additions to supply and vacancy rates rose to a high of 31% in 1986 (Exhibit 3.2). New construction slowed in 1987 and the average vacancy rate for the office market was down to 25% although it was as high as 32% in some submarkets (5). In response to overbuilding and high vacancy rates, construction has been sharply reduced with 2.6 million square feet of space being completed in 1987 as opposed to 5.6 million and 4.3 million square feet in the two previous years. Completions in 1988 and 1989 are expected to approach 2 million square feet (6). The following section describes the various principal geographic submarkets comprising the Phoenix office market.

Central Corridor includes the central business district and accounts for about 45% of of the metropolitan office base. *Camelback Corridor* is the second largest submarket with 5.5 million square feet of space or 18% of the market total. This area is considered a highly desirable business location and developments are generally high quality with prestige name tenants. The lack of developable land is causing a slowdown in new developments and encouraging a trend away from garden office buildings to higher density office towers.
Northwest Phoenix has recently emerged as an attractive market with 4.2 million square feet of office space and a year

EXHIBIT 3.2
Summary of Phoenix Office Market Data

	1982	1983	1984	1985	1986	1987
Office Employment	177,700	212,200	241,000	259,100	283,737	309,566
Office Inventory (1)	9,349,057	15,542,921	18,724,157	25,332,842	28,603,932	31,207,350
Annual Construction (1)	1,541,614	1,529,084	3,181,236	4,420,500	5,606,022	2,603,418
Annual Absorption (1)	959,795	1,485,096	2,060,696	2,808,782	2,967,490	3,200,000
Vacancy Rates	14.3%	20.6%	23.4%	26.0%	30.1%	25.7%

(1) As measured in square feet

Sources: Mountain West Research, Inc.; and Grubb & Ellis, Inc.

end 1987 vacancy rate of 21.3%, the lowest of any submarket. *The Airport Area* is also a new market which appeals to tenants because of its excellent transportation access and large population base. Recent developments, such as the Gateway Center, have tried to compete with Camelback Corridor properties by providing similar design quality and amenities at a more competitive price. The Airport Area has approximately 2.6 million square feet of office space.
Scottsdale has 4.5 million square feet of office space. High vacancy rates since 1985 have caused new construction to fall off dramatically in the last year.
The East Valley is emerging as a location for regional headquarters. It has a base of 3.9 million square feet of space and vacancies at year end were 32.8%. New construction has fallen off and land sales have been unusually light for the past year. (7)

The Industrial Market

While vacancy rates remain high, the industrial market is at present the one stable commercial market in terms of occupancy and rental rates as absorption continues to be strong and new construction proceeds at significantly lower levels than previous years. Approximately 2.5 million square feet of industrial space was added in 1987 as opposed to about 10 million square feet in 1986. At the same time, absorption outpaced new supply at a level of 3.1 million square feet. Industrial vacancies in 1987 averaged 15% and were concentrated on speculative higher finish R & D facilities. Rents at year end 1987 were from $.20 to $.30 per square foot of warehouse/ distribution space; $.60 to $1.00 per square foot for business park space and up to $1.40 per square foot for highly finished R & D space. (8)

The Retail Market

In 1987 there was a slowdown in shopping center developments reversing a growth trend which began in 1984. The retail base grew to 51 million square feet in 1987 as 43 centers totalling 3.8 million square feet were completed. In 1986, 55 centers totaling 4.3 million square feet were completed.

Overdevelopment has resulted in increasing vacancies especially for unanchored strip developments where vacancies range from 25% to 30%. Vacancies in neighborhood centers are about 10% and about 3% in regional malls.

Rental rates for retail space vary widely in the market depending on location, extent of competition, size of tenant and type of center. Rents have been relatively constant over the last three years, but concessions in new properties with high vacancies are reportedly as much as 40% of the asking rent. (9)

Hotels

Nearly 3,500 rooms were added to the Phoenix metropolitan area's base of approximately 21,000 rooms in 1987. Most of the area's markets saw new additions to supply, with the greatest concentration in the north along the Black Canyon Freeway. These additions combined with recent record levels of construction are expected to bring occupancy levels to their lowest point in four years. Despite record demand for room nights, 1987 occupancy was only 58% according to a Pannell Kerr Forster estimate. Because of the higher quality of the newly completed projects, room rates continued to grow and reached $70 in 1987.

Except for two new resort projects under construction in Scottsdale, new construction has slowed since 1987 and occupancy levels are expected to benefit from the reduced level of construction and continued growth in the market area. (10)

In this chapter we have reviewed the Phoenix economy and various components of the real estate sector. In the next chapter, we profile specific strategies employed by a cross section of foreign firms active in the Phoenix market.

CHAPTER IV

Profiles of Strategies Employed by Foreign Firms

The first significant foreign investment in the Phoenix area was initiated in 1971 when Jerry Nelson's Pinnacle Peak Land Company joint ventured the development of 320 acres of land north of Scottsdale with two Japanese firms. Other than foreign investment in some Arizona mining operations, the Pinnacle Peak project represented the first capital investment in the Phoenix economy by foreign investors.

Foreign investment in U.S. real estate has normally followed direct investment in other assets such as manufacturing facilities in a particular market. Real estate has been an initial entry investment for foreigners in the Phoenix market. This fact reflects the fundamentals of the Phoenix economy, in which construction has been the single largest industry for most of the last two decades, population growth has been strong and steady, and a free market, growth-oriented culture has welcomed new development and the imported capital necessary to support it.

During the 1970's, Phoenix emerged as one of the stars of the Sunbelt and foreign investment, primarily in real estate, continued. Foreign investors sought the returns, growth potential and freedom from regulation offered by the U.S. economy in general and Phoenix in particular. Often, a move into Phoenix real estate by foreign firms has followed the accumulation of large dollar holdings resulting from a surge in export earnings. Initially seeking profitable investment opportunities, many foreigners remaining in the Phoenix market have become progressively more active.

Exhibit 4-1 details Phoenix real estate assets currently owned by foreign investors. The overwhelming majority of these properties represents projects that were developed by foreign investors either alone or jointly with American partners. To the extent that these investor/developers have developed and sold other projects, the list understates the role of foreign firms in the Phoenix real estate market. The list of foreign investments detailed in Exhibit 4-1 is also incomplete to the extent that it does not include property owned by anonymous foreign investors.

As illustrated in this list, foreign activity has been concentrated on the development of office space, hotels, and to a lesser extent, retail space. While large in absolute numbers, known foreign ownership of real estate assets in these sub-markets is relatively small. Total office space in the Phoenix market is estimated at 31.2 million square feet. Of this only 7% or 2.2 million square feet is owned by foreign based entities. Likewise, of the 21,000 hotel rooms in the Phoenix market, only 1,967 or 9% involve foreign ownership.

Investors from Canada, Japan, Norway, Belgium and the United Kingdom have been the most active in the Phoenix market. Because their involvement has been in development and not acquisition, quantifying the amount of "investment" (as opposed to current value) has not been possible. The remainder of this chapter profiles the real estate activities of groups with their original bases in Canada, Japan, Norway and Belgium and the operating strategies adopted by these groups.

THE CANADIANS Looking for a place in the sun

Canadian investment in Phoenix real estate began in the early 1970's. To a large extent, the Canadians that came to Phoenix were from the Western oil-producing region of the country. Direct air links have been available between Phoenix and the Western cities of Winnipeg, Vancouver and Calgary for some time. Since many Canadians from the west had vacationed in Phoenix, the market was familiar to potential investors.

The oil crises of the early 1970's led to an energy boom in western Canada which left a number of firms and individuals with substantial investable dollar funds. The Canadian economy is significantly smaller than that of the United States, taxes are higher and government regulation is more pervasive. Faced with the somewhat anti-business policies of then-Prime Minister Trudeau's Liberal Party, many Canadians looked south for investment opportunities. Phoenix was attractive to many because of the good air transportation links, strong economic fundamentals and a pro-business growth orientation.

According to local sources, by the 1982 downturn in the Phoenix real estate market, most Canadian investors had either sold their holdings, taken their profits and gone home or gotten into trouble and turned the properties back to the banks. This timing would have coincided with the rise of the U.S. dollar against the Canadian dollar. This in turn would have maximized the local currency gain on any investment liquidated by Canadians and made it more expensive to support struggling U.S. investments with cash infusions from Canada.

Snowbird Properties (1)

Snowbird made a long term commitment to the Phoenix market, weathered the downturn and eventually expanded its operations. Snowbird entered the U.S. market 15 years ago and is now a major developer in the Southwest, virtually indistinguishable as foreigners. Snowbird is the successor company to Predecesor Properties, which in turn was a subsidiary of a Winnipeg real estate development and management firm. In the mid 1970's, Predecessor began to acquire and manage apartment buildings in the western United States. Through these activities, Predecessor became familiar with the U.S. real estate industry, local market conditions, and local developers.

Predecessor decided to invest in the United States because of limited opportunities for growth in their home market of East Yukon, the stronger economy, and a more favorable governmental environment in the U.S. In 1977, Predecessor systematically reviewed a number of U.S. cities as potential sites for development activities. The study focused on demographic trends including net migration, income and employment growth. Based on this study, Predecessor identified Dallas, Denver, Phoenix, Tampa, Atlanta and San Diego as attractive markets.

Dallas and Denver were Predecessor's two best markets in the late 1970's, but the company switched emphasis to Phoenix in the wake of the oil bust.

Also in 1984 the administration of Predecessor's U.S. interests was transferred to Phoenix. While Predecessor and Snowbird share common ownership, they are independent "sister" companies. Snowbird and its subsidiaries have evolved essentially into an American development company financed with Canadian capital. Snowbird is perceived in Phoenix as a "local" company. Snowbird doubtlessly reinforces its local identity by its practice of using local banks, design professionals, contractors and law firms for its deals.

Projects Completed

Since 1984, Snowbird Properties has developed over 1 million square feet of office and industrial space in the Phoenix market. Snowbird has diversified its projects among office, residential and industrial. In making such a major commitment, Snowbird capitalized on the strong economic and demographic trends in Phoenix, the lack of significant national competition in several market segments, the fine climate and quality of life, low land prices, and the chance "to be a big fish in a small pond within a relatively short period of time".

Snowbird is essentially a merchant builder and therefore looks to sell the projects that it builds. Typically, developments are sold following the second lease cycle when short term rents and NOI (and thus the sales price) reach short term peaks. Land held by Snowbird for future development may also be for sale at the right price.

Foreign Exchange Exposure

Snowbird's Canadian investors were particularly interested in putting capital to work outside of Canada. Snowbird does not concern itself with "cross-border" issues such as income taxes or exchange rate fluctuations. Each individual investor is expected to manage its own positions with respect to tax liabilities and currency exposures. Snowbird itself plans and manages its operations strictly for dollar results. Since "there has been essentially no interest in taking funds back to Canada", earnings have generally been reinvested locally and the fluctuating value of the dollar has not unduly concerned or influenced Snowbird's investors.

Diversification

In addition to development, Snowbird is also active in property management through its three local subsidiaries. Property management contracts are held on buildings owned by Snowbird, about half of the buildings developed and later sold by Snowbird, and on a few buildings developed and owned by third parties. Snowbird currently manages buildings totalling about 1 million square feet. Although management is a break even undertaking for Snowbird, it is considered important since it allows Snowbird to control the value of its assets and effectively manage relationships with tenants who will provide the demand for Snowbird's new buildings.

Snowbird has also initiated a general contracting operation. Dissatisfied with the level of work on tenant improvements for a large office project, Snowbird took over the contract themselves and drew heavily on construction experience at its sister company in Canada. While Snowbird would not act at this time as general contractor on a complex high-rise project, it has taken the construction contract for some smaller industrial development and small third party deals. General contracting is not a major business thrust for Snowbird, but it does provide the company with an expanded range of services and the ability to keep in touch with the local construction market.

The Future

Snowbird sees "several painful years ahead" for U.S. real estate. While Phoenix will not be spared the consequences of overbuilding, a strong and expanding economy will allow Phoenix to grow out of its problems faster than other Sunbelt cities such as Houston or Denver. Snowbird's decision to purchase five downtown parcels for future development and its acquisition of 400,000 square feet of industrial space for resale indicates its strong long-term commitment to the Phoenix market.

THE JAPANESE - Looking for a few good partners

In cities such as New York, Los Angeles and Washington, Japanese investment in real estate has typically been through the acquisition of developed properties. These acquisitions have concentrated on fully leased first class office buildings in prime downtown locations. Japanese investment in Phoenix real estate, by contrast, has been in the form of joint ventures with local firms to develop new projects. The Japanese investors that have received so much attention recently for paying record prices for "trophy" office buildings will not find that type of product in Phoenix. Existing buildings generally are not of the size or quality of trophy buildings in the downtowns of New York and Los Angeles. Also, low Phoenix land prices and the absence of barriers to entry make it difficult to establish monopoly positions for a single property.

Since investment opportunites in existing buildings did not meet their criteria, Japanese firms interested in investing in Phoenix became involved in developments that both responded to market demands and satisfied their interests in quality. As a result, joint ventures involving Japanese partners have developed resort hotels (Phoenix is a leading destination resort and tourism is the third largest industry), residential subdivisions (to meet the housing requirements of the nation's fastest growing city) and suburban office buildings with unique locational advantages (thereby creating a monopoly position rather purchasing it).

So far, Japanese investment in Phoenix has come in the form of joint ventures with prominent local developers. Two groups of Japanese have been the most active and best illustrate this entry strategy: Nichimen Trading and Toya Real Estate in their long-standing partnership with Pinnacle Peak Land Co., and Shimizu Construction and Mitsui in their partnerships with Westcor (and, more recently, The Symington Co.).

Japan Realty Investors (2)

Northwest Land Company started a partnership with Japanese investors in the early 1970"s to develop 320 acres of land into a new residential community. That partnership lasted until 1988 and was responsible for developing several thousand acres consisting of more than a dozen different subdivisions.

Structure

In 1975 the two parties decided to develop the land owned by the joint venture. It took Northwest only two days to negotiate the joint venture agreement with his Japanese partners. Northwest maintained operating control and his partners provided all of the cash. To address the Japanese' concerns for security, Northwest agreed to all financial and reporting requirements requested by its partners. Moreover, Northwest did not charge the partnership any fees, commissions or expenses for the development projects. The partnership was structured so that any funds taken out of the partnership would be shared evenly by Northwest and the Japanese.

In order to facilitate the resolution of future disputes, Northwest wanted to control 51% of the joint venture. This was the one "deal breaker" for his Japanese partners who insisted that the joint venture be structured as a 50/50 partnership. The Japanese insisted that any disagreements that did arise could be worked out by negotiation, and Northwest agreed to a 50/50 structure. According to Northwest, there never were any major disagreements since each side worked to respect the requirements of the other party.

For example, Northwest always found his partners responsive to his proposals concerning taxes, capital gains and the timing of profits, issues that were important to him but not his partners.

By not asking that the joint venture pay him fees or commissions, Northwest believes that he gained instant credibility with his partners. He agreed to share the risks with his partners and showed his commitment to "making money together". Northwest's partners stated that Northwest was the first American partner that did not want to make its profit from a joint venture at the front end of the deal.

Personal Relationships

Northwest understood the importance of personal relationships with the executives at the two large companies which were its partners. Northwest always attempted to respect customs and protocols. When the Japanese visited in the U.S., for example, Northwest would entertain at home and serve traditional Japanese food.

Northwest was careful not to cause the executives responsible for the joint venture to be embarrassed with their superiors. Northwest always made certain that the appropriate executives were up to date on all potential problems and allowed the individuals executives to inform their boards as they thought best. In addition, Northwest supplied its partners with conservative projections. In all cases, his results met or exceeded the projections.

An Exit From the Market

Despite earning an average 50% p.a. return on investment, JRI is withdrawing from the U.S. real estate market. This decision followed three ill-fated investments that JRI made in deals (not involving Northwest). The first such deal was a joint venture that built high-rise luxury condominiums in the Southeast. Problems, including poor marketing, caused the deal to go bad and the U.S. partner walked.

The Japanese investors also lost a significant amount on investments in Houston real estate when that market crashed. Finally, they suffered large losses in a Western land deal where the land was purchased with the expectation that rezoning approvals could be obtained. When a zoning variance could not be obtained, the project could not be pursued and the Japanese were left with land worth significantly less than what they paid for it.

Shimizu Construction and Mitsui

A joint venture between Phoenix developer Westcor and

Japanese investors was also arranged through high level contacts. In Westcor's case the partnership resulted from a high level introduction to Shimizu and Mitsui arranged by William Turner, a local businessman and former Ambassador to the Organiztion for Economic Cooperation and Development. Turner was well known to Shimizu's senior managagement and his opinions were highly valued by the board.

The Westcor Deals (3)

Shimizu is the third largest construction company in the world. While they had been involved in real estate ventures in Australia and the United Kingdom, the Westcor partnership marked their entrance into U.S. real estate. The key factor for Shimizu in entering the Phoenix market was locating a high quality partner that was "reliable and believable". Shimizu was also attracted to Phoenix because it is a young city with a strong high-technology industrial base, a pro-business atmosphere and plenty of available land.

Shimizu and Mitsui's first joint venture with Westcor was to develop a 310,000 square foot office building. This building is located in Paradise Village Office Park, an upscale office park developed by Westcor. As such the park had an established quality location which was a key consideration for the Japanese investors. In this deal, Shimizu and Mitsui were financial partners supplying a disproportionate share of the equity capital for a combined 50% equity position. Westcor, as the development partner was responsible for managing the project.

Shimizu and Mitsui again combined to form a joint venture with Westcor to develop Westcourt in the Butttes, a $35 million resort hotel in Tempe. This was also structured with Shimizu and Mitsui as 50% financial partners and Westcor as the development partner.

Shimizu and Westcor recently formed a third partnership to purchase the Anasazi Golf Course which is adjacent to the Paradise Village Office Park. The purchase included the 160 acre golf course and 30 additional acres which are zoned commercial and are being land banked for future development.

A fourth, and more speculative, partnership has been formed by Shimizu and Westcor. This joint venture has paid $150,000 for an option on undeveloped land in California. The land is zoned for agricultural use and a rezoning to commercial must be obtained before the partnership will exercise its options. If the partnership cannot arrange for rezoning, they will forfeit the option payment.

Advantages

By any standard, Westcor and Shimizu have a successful development relationship. This success is largely the result of the values that the two firms share. Westcor is willing to put its own money into projects and share the cash risks with its financial partners. At the same time, Shimizu is willing to share development risks in exchange for its ownership in the project. Shimizu's willingness to "walk through all of the risks" of a project with the developer enhances the value of their participation in a project.

In Westcor's view, Shimizu is an ideal development partner. Shimizu takes a long term view and is willing to spend extra money to ensure quality and to build a project having unique locational and physical competitive advantages. Shimizu matches its investments to the economics of the deal by, for example, budgeting for long leaseups in new office buildings and not requiring an immediate cash-on-cash return. Because Shimizu is willing to share development risks and defer seeing a return on their investment until the project is stabilized, Shimizu earns significantly better returns on investment than any of Westcor's other financial partners.

The Symington Deal (4)

In addition to its partnerships with Westcor, Shimizu has entered into a joint venture with the Symington Companies for the phased development of Camelback Esplanade which is located at one of the choice remaining corners in the Camelback Corridor. The first phase of the project is under construction and involves a 240,350 square foot office tower and a 301 room hotel that will be operated as a Ritz-Carlton. Shimizu agreement to provide equity financing for this project allowed construction to proceed after a year long delay when earlier financing arrangements fell through.

Diversification and the Future (5)

In addition to acting as financial partner, Shimizu has expanded its development role and will be responsible for monitoring and verifying progress draws under the construction loans. Gradually expanding its role in development by drawing on its organizational experience in construction is a strategy that Shimizu expects to pursue. The logical result of this trend would be for Shimizu eventually to pursue its own development and construction projects.

THE SCANDANAVIANS - The Vikings Rediscover America

Similar to the entry of Canadians and Japanese investors into the Phoenix real estate market, the arrival of the first significant Scandinavian investors coincided with the accumulation of large dollar surpluses. In the case of the Scandinavians, the source of the dollar earnings was the export of North Sea oil and gas. Valhalla Development is an example of a foreign real estate company combining its experience and capital resources with local expertise to penetrate the U.S. market.

Valhalla Development, Inc. (6)

Valhalla was formed by Thor Construction, one of Scandinavia's largest construction and development firms. With a net worth of about $400 million, approximately 65% of the Group's home country operations are in real estate. The balance is in non-real estate manufacturing operations acquired as part of a diversification strategy.

Thor Construction saw strong growth in its operations from 1965 on. By the late 1970's however, the Group's principals had concluded that opportunities for further growth, even through continued diversification, were limited by the home country's small economy. Also, Scandinavia's socialist politics were perceived to detract from the long term attractiveness of the economy. As a result, Thor Construction decided that the best opportunities for future growth would be through geographic diversification in the industry they knew best - real estate investment and development.

The Decision on Phoenix

Thor Construction was initially attracted to the Southwest region of the United States because, at the time, that region was growing faster than any other part of the United States. Of the possible markets in the Sunbelt, Thor Construction decided to make its initial investment in Phoenix. Phoenix was chosen because the Group believed that it had the strongest and most broad-based economy of the major cities in the Sunbelt and because there were fewer quality development firms against which to compete. The combination of strong growth potential and limited first-class competition offered the potential to be a "big fish in a small pond". This was in essence a niche market strategy.

The management of Valhalla consists exclusively of American professionals recruited by the company because of their development expertise and familiarity with the local market. Generally speaking, the local management proposes new projects to the Board which makes the "go - no go" decision. The Board is not generally involved in Valhalla's day to day operations.

Projects

Valhalla hit the ground running after its formation and quickly intitiated three deals. Since 1981, the Company has been involved in nine separate transactions. These projects include a large multi-building office park, a hotel, a residential development and five purchases of pre-development land.(7)

Diversification

Valhalla's primary diversification has been geographic with the development of a 140,000 square feet office building in Houston (1983). While this project has been successful, Sunbelt is not interested in new deals in Houston until the economy there improves.

Valhalla has established a property management company. The property management company only holds contracts on buildings owned by Valhalla. Valhalla does not see substantial profit potential in property management, but considers it essential to maintain the value of its assets and to protect tenant relationships.

Early "passive" stock investments in non-real estate related companies both in the U.S. and abroad were not particularly successful and were largely divested in 1985 in order to allow the company to focus on real estate activities.

Differences and Advantages

The primary difference between Valhalla and many U.S. real estate developers is the long-term entry strategy adopted by Thor Construction. Valhalla's owners have a twenty year time horizon and capitalized Valhalla at levels sufficient to support this strategy. Since Valhalla's owners emphasize value per share as opposed to current cashflow per share, the company is free to invest in land deals and other ventures where the potential payoff is large, but likely years down the road. With a strong capital base (estimated net worth of $40 million) Valhalla has the financial flexibility to finance these long term investments.

A major advantage to American managers in dealing with the Scandinavians was access to international banking relationships of Thor Construction. The credibility provided by this association was especially important in the Company's early start-up years. While Valhalla has maintained these original relationships, its track record has attracted a wide variety of financing sources. With access to local banks, money center banks, pension funds and insurance companies, Valhall's financing differs from that of large domestic developers only in that it may be more flexible. (It is interesting to note that Valhalla has negotiated potential joint ventures with Japanese insurance companies but never reached final agreement since their "long lead times" negated the benefit of competitive terms.)

A less tangible benefit for Valhalla in its association with Thor Construction is "the mystique of foreign ownership". In many instances, Valhalla has instant credibility in negotiations because of the perception that "their capital must be endless". (7)

Stategy For The Future

Over the seven years, Sunbelt has established a good track record for development in Phoenix, and, to a lesser extent, in Houston. Valhalla still likes the long term prospects in Phoenix and with a substantial inventory of land has made a strong commitment to the market. Valhalla will concentrate on the ongoing development of its office projects and will bring undeveloped land into production as the market strengthens. While they "are always interested in new proposals" the focus for the next few years will be on Phoenix.

THE BELGIANS - Preparing for Armageddon

A number of firms investing in Phoenix real estate are run by expatriates who act to a degree as investment managers for wealthy individuals and institutions which wish to invest in U.S. real estate but do not have the expertise or contacts to do so directly. One such firm is Overseas Investment Company (OIC), which is financed largely by Belgian capital.

Overseas Investment Company (8)

OIC is run by Jacques Brun, a Belgian by birth who came to the U.S. in the mid-1970's. Brun's family operates one of the largest real estate consulting firms in Belgium and is well established in that market.

The Move to the United States

Brun came to the U.S. with a pool of capital initially attracted through family connections to be invested in U.S. real estate. According to Brun, investments in the U.S. were motivated 75% because of the economic slowdown in Europe that afforded few attractive investment opportunities and 25% by the fear of creeping socialism and the perceived "Finlandization" of Europe.

As such, the United States was seen as a safe haven for foreign capital. Real estate investments served both as a hedge for capital and as a haven to which Europeans could flee if Europe became too inhospitable to capital.

Brun was originally involved in deals in California, but moved to Phoenix largely because of the perception that it would be an easier market for a small player to establish itself.

Projects

Brun's investors are largely families and individuals who invest via U.S. corporate vehicles. Because the investors have no need for tax benefits, Brun could not match the prices offered for completed buildings by tax-driven investors. As a result, Brun was pushed into developing properties by the economics of the situation prior to tax reform. Brun originally joint-ventured with local developers, but as he gained more experiencene he began to develop his own projects.

OIC now supervises an investment portfolio of about $200 million, manages over 500,000 square feet of property and has developed more than 300,000 square feet of office, retail and industrial space.

Foreign Exchange Risk

Brun runs the Company strictly for dollar results. His investors have been interested in the long term preservation of wealth and have not been concerned with the short term fluctuations in the value of the dollar. Since placing capital in a safe haven was a primary motivation in these investments, earnings have been largely reinvested in the U.S. as opposed to repatriated to Belgium.

Strategy for the Future

Brun is involved with projects throughout the Southeast and is willing to continue his geographic diversification. While his original Belgian investors are still around, he is doing an increasing amount of new business with American investors. The Belgian economy is booming largely due to the expansion ofthe European Economic Community aand NATO offices in Brussels. This, together with a swing to the right in European politics, is making the prospects for investments in Belgium more attractive. As a result Belgians are less interested in investing money offshore and, in certain instances, are beginning to repatriate funds from this county to finance investments in Belgium.

In addition to diversifying its investor base and geographic range, OIC has also become a full service real estate firm providing asset and property management, financial controls, construction, brokerage and land development services.

In the next chapter, we summarize and analyze the criteria of foreign firms investing in the Phoenix market with an emphasis on the similarities, or otherwise, beween local and foreign firms and the evolution of investment criteria over time for individual firms.

EXHIBIT 4.1

PHOENIX REAL ESTATE WHOLLY OR PARTIALLY OWNED BY FOREIGN INTERESTS

	NAME & ADDRESS	TYPE	SIZE	OWNERS	NATION-ALITY	PCT. OWNED
1.	Gateway Center PHOENIX	Office	455,000 sf	a. Sunbelt Holdings b. U.S. Pension Funds	Norway U.S.	50% 50%
1a.	Doubletree Hotel	Suite Hotel	242 rms	a. Sunbelt Holdings b. U.S. Pension Funds	Norway U.S.	50% 50%
	Gateway center is a 35 acre multi-use development that will eventually total 1.2 million sf.					
2.	Residential Land SCOTTSDALE	Land	194 acres	a. Sunbelt Holdings b. Evans & Whithycombe	Norway U.S.	
3.	Predevelped Land CHANDLER	Land	248 acres	a. Sunbelt Holdings	Norway	100%
4.	Predeveloped Land Lindsay & Germann Sts. GILBERT	Land	155 acres	a. Sunbelt Holdings	Norway	100%
5.	Predeveloped Land 44th & Van Buren PHOENIX	Land	26 acres	a. Sunbelt Holdings	Norway	66.6%
	Site is adjacent to Gateway Center and plans call for the eventual development of 1 million sf muti-use space					
6.	Predeveloped Land PHOENIX	Land	19.5 acres	a. Sunbelt Holdings	Norway	100%
7.	Predeveloped Land Price & Pecos PHOENIX	Land	320 acres	a. Sunbelt Holdings	Norway	100%
8.	2035 N. Central Avenue PHOENIX	Office	30,000 sf	a. Wolfgang Porsche	Germany	100%
9.	Westcourt in the Buttes TEMPE	Resort hotel	325 rms	a. Westcor Co. b. Shimizu Construction c. Mitui America	U.S. Japan Japan	50% 25% 25%
10.	Paradise Village Mall PARADISE VALLEY	Reg. Mall		a. Westcor Co. b. Electricity Bd. Pension Fd	U.S. U.K.	
11.	Paradise Village OP III 11811 N. Tatum Blvd. PHOENIX	Office	310,000 sf	a. Westcor Co. b. Shimizu Construction c. Mitui America	U.S. Japan Japan	50% 25% 25%

EXHIBIT 4.1 (cont'd)

PHOENIX REAL ESTATE WHOLLY OR PARTIALLY OWNED BY FOREIGN INTERESTS

NAME & ADDRESS		TYPE	SIZE	OWNERS	NATION-ALITY	PCT. OWNED
12.	Anasazi Golf Course North Tatum Blvd. PHOENIX	Land	190 acres	a. Westcor. Co b. Shimizu Sonstruction	U.S. Japan	50% 50%
	Parcel acquired in 1988 primarily to land bank 30 acres zoned commercial.					
13.	Camelback Esplanade 24th and Camelback PHOENIX	Office	240,000	a. Symington Co. b. Shimizu Construction	U.S. Japan	50% 50%
13a.	Ritz Carlton Hotel Hotel	Hotel	300 rms	a. Symington Co. b. Shimizu Construction	U.S. Japan	50% 50%
	Above buildings under construction as Phase I of 5 phase project on 20 acre site.					
14.	The Crossings MESA	MPC	1,023 acres	a. American Continental Corp. b. Taiyo Investments	U.S. Japan	50% 50%
15.	Pinnacle Peak Village SCOTTSDALE	MPC	5,600 acres	a. Pinnacle Peak Land Co. b. Nichimen Trading Co. c. Toyo Land	U.S. Japan Japan	50% 25% 25%
	Recently completed master planned community consisting of 27 subdivisions.					
16.	Scottsdale Princess SCOTTSDALE	Hotel	600 rms	a. Spector Development b. Jones Development c. Princess Properties d. Japan Development Co.	U.S. U.S. U.K. Japan	25% 25% 25% 25%
17.	Park Central Mall Central Avenue PHOENIX	Reg. Mall/ Office	1.3 mil. sf	a. Lehndorff, Inc.	Germany	100%
18.	United Bank Center Central Ave. & Osborne PHOENIX	Office	26 storeys	a. Bell Canada Development	Canada	100%
18a.	United Bank Center Central Ave & Osborne PHOENIX	Office	24 storeys	a. Bell Canada Development	Canada	100%
19.	Undeveloped Land I-10 and Sunvalley Pkwy PHOENIX	MPC	35,700 acre	a. Burns International b. Rosenhaugh Plc c. Montleigh Plc	U.S. U.K. U.K.	50% 50% 50%

EXHIBIT 4.1 (cont'd)

PHOENIX REAL ESTATE WHOLLY OR PARTIALLY OWNED BY FOREIGN INTERESTS

	NAME & ADDRESS	TYPE	SIZE	OWNERS	NATION-ALITY	PCT. OWNED
20.	Gainey Ranch SCOTTSDALE *Master Planned Community developed and sold by subsidiary of Hudson's Bay Co.*	MPC	562 acres	a. Markland	Canada	100%
21.	Scottsdale Ranch SCOTTSDALE *Master Planned Community developed and sold by subsidiary of Hudson's Bay Co.*	MPC		a. Markland	Canada	100%
22.	McCormick Ranch SCOTTSDALE *Master Planned Community developed and sold by subsidiary of Hudson's Bay Co.*	MPC		a. Markland	Canada	100%
23.	Mercado del Lago McCormick Ranch SCOTTSDALE	Office/ Retail	50,000 sf	a. National Portfolio, Inc.	Belgium	100%
24.	Mercado at Scottsdale Ranch SCOTTSDALE	Neighborhd. Center	150,000 sf	a.National Portfolio, Inc.	Belgium	100%
25.	Aztech Court TEMPE	Office/ Warehouse	70,000 sf	a. National Portfolio, Inc.	Belgium	100%
26.	Various TEMPE	Retail	45,000 sf	a. National Portfolio, Inc.	Belgium	100%
27.	The Amberly 83rd to 91st Sts btwn McDowell & Thomas PHOENIX	MPC		a. English and Continental	U.K.	50%
28.	Glendale Galleria GLENDALE *Under Construction*	Retail	200,000 sf	a. English and Continental	U.K.	50%
29.	Sherwood Mesa MESA	Retail	80,000 sf	a. English and Continental	U.K.	50%
30.	Arizona Biltmore SCOTTSDALE	Hotel		a. Rostland Corp.	Canada	100%
31.	Paradise Corporate Park TATUM	Office		a. Marwest Group Ltd.	Canada	100%

EXHIBIT 4.1 (cont'd)

PHOENIX REAL ESTATE WHOLLY OR PARTIALLY OWNED BY FOREIGN INTERESTS

	NAME & ADDRESS	TYPE	SIZE	OWNERS	NATION-ALITY	PCT. OWNED
32.	Scottsdale Corporate Center SCOTTSDALE	Office		a. N.H. Clausen Holdings	Canada	100%
33.	Fiesta Mall 1445 W. Southern Ave MESA	Retail		a. Grosvenor Holdings Plc	U.K.	100%
34.	Chaparral Plaza PHOENIX	Retail	70,000 sf	a. Snowbird Properties	Canada	100%
35.	Crystal Point 12th & Osborne PHOENIX	Condo.	128 units	a. A. Akman & Son Ltd b. Snowbird Properties	Canada Canada	
36.	Northwest Industrial Center PHOENIX	Industrial/ R&D	78,000 sf	a. Snowbird Properties	Canada	100%
37.	43rd Avenue Distribution Ct PHOENIX	Industrial/ R&D	39,000 sf	a. Snowbird Properties	Canada	100%
38.	River Drive Plaza I PHOENIX	Industrial/ R&D	32,000 sf	a. Snowbird Properties	Canada	100%
39.	River Drive Plaza II PHOENIX	Industrial/ R&D	49,000 sf	a. Snowbird Properties	Canada	100%
40.	Fairmont Commerce Center PHOENIX	Industrial/ R&D	89,000 sf	a. Snowbird Properties	Canada	100%
41.	Rosegarden Center PHOENIX	Industrial/ R&D	72,000 sf	a. Snowbird Properties	Canada	100%
42.	Roosevelt Tech Center PHOENIX	Industrial/ R&D	60,000 sf	a. Snowbird Properties	Canada	100%
43.	2929 Tech Center PHOENIX	Industrial/ R&D	60,000 sf	a. Snowbird Properties	Canada	100%
44.	Palo Verde Industrial Park PHOENIX	Industrial/ R&D	183,000 sf	a. Snowbird Properties	Canada	100%
45.	Thomas Center PHOENIX	Industrial/ R&D	40,000 sf	a. Snowbird Properties	Canada	100%

EXHIBIT 4.1 (cont'd)

PHOENIX REAL ESTATE WHOLLY OR PARTIALLY OWNED BY FOREIGN INTERESTS

NAME & ADDRESS		TYPE	SIZE	OWNERS	NATION-ALITY	PCT. OWNED
46.	Broadway Center PHOENIX	Industrial/ R&D	101,000 sf	a. Snowbird Properties	Canada	100%
47.	Hardy and Fairmont PHOENIX	Industrial/ R&D	25,000 sf	a. Snowbird Properties	Canada	100%
48.	Gateway Court PHOENIX	Office	45,000 sf	a. Snowbird Properties	Canada	100%
49.	Westwood Court PHOENIX	Office	92,000 sf	a. Snowbird Properties	Canada	100%
50.	Glendale Financial Center GLENDALE	Office	45,000 sf	a. Snowbird Properties	Canada	100%
51.	The Park 44th and Camelback PHOENIX	Office		a. Snowbird Properties b. MSS Associates	Canada U.S.	50% 50%
52.	Predeveloped Land Central and Encanto PHOENIX	Land	4.3 acres	a. Snowbird Properties b. Unnamed financial institution c. Local investors	Canada Canada U.S.	
53.	Predeveloped Land Central and Osborne PHOENIX	Land	5 acres	a. Snowbird Properties	Canada	100%
54.	Predeveloped Land Arizona Ave. and Germann Rd. PHOENIX	Land	43 acres	a. Snowbird Properties	Canada	100%
55.	Predeveloped Land Osborn and 12th PHOENIX	Land	9 acres	a. Snowbird Properties	Canada	100%
56.	Predeveloped Land Southern and 40th PHOENIX	Land	4 acres	a. Snowbird Properties	Canada	100%
57.	Predeveloped Land Chandler and Pecos PHOENIX	Land	45 acres	a. Snowbird Properties	Canada	100%

EXHIBIT 4.1 (cont'd)

PHOENIX REAL ESTATE WHOLLY OR PARTIALLY OWNED BY FOREIGN INTERESTS

NAME & ADDRESS	TYPE	SIZE	OWNERS	NATION-ALITY	PCT. OWNED
58. Airpark Office Plaza Scottsdale	Office		a. China International Trust b. Ambanc	PRC U.S.	
59. Predeveloped land Goldfield Ranch	Land	142.6 acres	a. China International Trust b. Ambanc	PRC U.S.	

CHAPTER V

Summary and Conclusions

New Money vs. Old Money

Foreign investors do not make U.S. real estate decisions using ouija boards, nor do they generally consult the heavens any more than do domestic investors. But critics contend that some foreign investors, notably the Japanese, pluck numbers from the sky before they make bids on U.S. real estate. In our view, the foreign investors that we interviewed are rational in their approach to U.S. real estate investment, in some cases more rational than U.S. investors. The biggest difference between some foreign investors and domestic investors appears simply to be knowledge of the local market. New foreign investors tend to use a combination of the following strategies to enter new markets: joint ventures, investment in limited property types of the highest quality; and acquisition of low risk properties with evolution toward higher risk transactions. Established foreign investors familiar with a local market tend to behave like domestic investors, showing a wide variety of risk tolerance and return requirements. The availability and cost of capital influence the investment strategy of an established foreign investor, as it would any investor. But capital characteristics do not seem to affect investment decisions in a way that sets established foreign investors apart from their domestic counterparts.

For example, Canadian investors we interviewed in Phoenix were virtually indistinguishable from their domestic counterparts in how they evaluate and execute investment plans. Many had been in Phoenix for fifteen years, and despite the fact that their capital supplies were still largely Canadian, they tend to behave just like American investors. There do not appear to be prejudicial inclinations, constraints, or unusual terms attached to the source capital. Just as some established investors prefer to buy AAA office space and others prefer to speculate in land, differences exist in the investment policies of established foreign investors in Phoenix. However, none of these differences seem to result solely from the national origin of source capital.

New entrants to a particular market tend to follow certain patterns. The Japanese, although active in Pinnacle Peak as early as 1971, represent the new wave of capital entering Phoenix. As we've read about in newspapers and seen in other studies, the Japanese generally seek premiun locations, top quality projects and relatively low risks in terms of the development stage. They have traditionally leaned toward fully leased office buildings rather than pre-development or construction phase projects. They look for competitive advantage and have been willing to pay for it.

But these specific strategies appear to have as much to do with the local market and the range of available investment opportunities as they do with the inclinations of these investors. Phoenix's availability of land and its economic make-up have long attracted foreign capital seeking quality and safety, but these same factors channel capital to opportunites other than signature office properties. While Phoenix has much to offer, it does not have fully leased premium grade office buildings on Central Park.

Foreign Investors Adapt To Local Markets

A significant finding of our study is that while new foreign capital still seeks security and high quality, these sources have not tried to apply specific investment strategies used in other U.S. markets to the unique Phoenix market. In fact, some of the prominent foreign investors in Phoenix are not even in other U.S. markets. Foreign investors are not looking in Phoenix for fully leased signature office property, but rather for market opportunities and competitive advantage.

A common strategy is to ally with an established development firm in the area. In this way, foreign investors gain an immediate foothold and begin to build an understanding of the market through the track records and visions of their partners. Because the Phoenix market does not offer the kind of institutional grade product typically sought by foreign investors in first tier cities, the new foreign capital in Phoenix is investing instead in relationships with local firms with strong track records. The specific investments made by new foreigners in the Phoenx market are strongly driven by the recommendations of these local partners. The Japanese, for example, are now investing in development deals in Phoenix, which while carrying a greater degree of associated risks than AAA acquisitions, are generally some of the best available projects in the city.

They have not thrown out their concerns over safety, but rather are seeking security by teaming with some of the best people on projects in the most opportunistic investment spectrum in Phoenix. In addition, the local developers have been generally willing to put real equity into the joint ventures. The foreign investor's security is competitive advantage and the characteristics of the capital they supply make them attractive joint venture partners for local developers.

Capital Pieces in the Product Puzzle

Square pegs do not fit in round holes. True competitive advantage is achieved when not only the real estate product produced is superior, but when the attendant project financing supports and enhances the creation of superior product. For example, a major development project in Phoenix was financed using Japanese capital within the structure of a joint venture. The project was financed 50% equity and 50% debt carrying a below-market rate coupon. The equity ownership was split 50% / 50% between the foreign and domestic partners; the cash funding of the equity was split somewhere on the order of 90% / 10% (unconfirmed), with the foreign parnter providing the larger share. The contribution by the U.S. developer of cash to the project in addition to expertise was a significant factor to the foreign investor, since so often U.S. partners are unable or unwilling to take cash risks. In addition, the project was built to hold which was conducive to top quality construction and compatible with both partners' investment objectives.

This financing structure resulted in lower than conventionally financed carry costs during the development and lease-up stages. Because of the foreign partner's willingness to supply equity funds, which were not dividend bearing, and because of a below market rate coupon on the debt financing, the cash requirements for the project were considerably lower than in conventionally financed projects. In addition, the terms of the debt provided a five year grace period before principal repayment on the debt, thereby allowing a significantly longer lease-up period and greater investment in hard costs than conventionally financed projects. Since a smaller level of capital budget funds were allocated to carry costs, a proportionally higher level of funds were available to buy revenue-producing project amenities as well as highest quality construction.

Conventionally financed projects having higher carry costs are more likely to be pressured to cut capital costs, avoid design experimentation, offer fewer amenities, and cut back on construction quality. Also these projects are more likely to be under pressure to lower rent levels in a slow market due to limited financial flexibility and shorter allowances for lease-up periods. In addition, the conventionally financed project is less likely to withstand lower rent levels due to higher carry costs and therefore operate at a competitive disadvantage to properties financed as described above. Thus the equity investor in the conventionally financed project is likely to bring a lower quality project to the market, at higher financial risk.

Capital financing geared to long term value creation seems to produce higher quality and more competitively positioned product. The breathing room and capital investment incentives provided by this financing structure in turn creates value that justifies this structure. In fact, the U.S. firm we interviewed concerning this joint venture indicated that, in the long run, this capital was more expensive than conventional financing. However, the domestic partner's return was also higher than average. Much of the foreign investors return was created by the benefits of the financing structure, which in turn promoted the creation of a superior product. The foreign capital was more expensive than other sources because its equity share was a piece of a larger than average pie. The local partner was by no means complaining.

Expected Returns and Benefits

Return expectations of foreign investors do not appear to differ significantly from domestic investors, especially in the case of established long term investors. In the case of more recent entrants to the U.S. real estate investment marketplace, the structure of these returns offer certain advantages to U.S. developers. For example, as mentioned above, recent Japanese investors in Phoenix have been willing to provide capital on a joint venture basis with U.S.

development partners bearing little or no coupon requirement.

These investors' willingness to seek returns from value appreciation in the property through equity ownership is more pronounced than is that of U.S. pension funds or life insurance companies. While convertible permanent financing is available from domestic sources, construction financing in that instance must usually be done on a conventional basis, with higher attendant carry costs and shorter lease-up period allowances. So, while overall return expectations are similar to or greater than those of domestic investors, the structures of many foreign transactions reflect a commitment to a long term U.S. real estate position, with less emphasis on current returns.

Foreign exchange considerations do not appear to play an important role in the structure of investments by foreign capital suppliers or in their sensitivity to current returns. For the most part, U.S. dollar investments are expected to remain dollar investments over the long term. The foreign managers we spoke with were responsible for the performance of the U.S. investment portfolio measured in terms of U.S. dollar returns. They had no responsibility for currency hedging or conversion values. However, it is likely that their dollar capital is allocated on a long term basis as part of a global currency diversification strategy managed by the corporate head office. Certainly, the low value of the dollar against many major currencies in the recent past has made U.S. investment more attractive. We do not believe, however, that it now has a large impact on the financial structure of transactions nor that it will play a key role in overall disposition strategies.

Structure and Role

When foreign investors initially enter the U.S. real estate market, it is often in partnership with major U.S. development firms. After these investors have come to understand the market, they usually begin developing projects on their own. We found several examples of Canadian, British, Belgian and Norwegian firms following this strategy.

The joint venture arrangements established by foreign investors and U.S. development companies typically begin as limited partnerships, with the foreigner taking a limited partnership equity interest and acting as the financial partner. Over time, this arrangement usually grows so that the foreign partner takes on more management responsibility, eventually becoming a general partner. Of course, this position also carries additional liability, which justifies a greater voice in the management of the partnership and provides incentive for the American partner.

Product and Location

Foreign investors in the Phoenix market are involved in virtually all product types, although there appears to be some concentration in offices and resorts (which includes hotels and amenities such as golf courses) and residential subdivisions.

Since Phoenix is not configured around a dominant central business center, but instead is comprised of a number of smaller business centers, recent foreign investors have become involved in major developments conceived as destination points, where the value of the location is created by the development. In addition, since there remains a fair amount of buildable land in Phoenix, the potential for competition from new construction always exists. Therefore, investors have sought to become involved with signature properties that create locational acceptance. Much of this activity has been associated with resort development.

Pinnacle Peak is an example of a planned community development that has been joint ventured with foreign capital sources. Pinnacle Peak was considered an outlying district at the time of its initial development in the early 1970's. The success of that project has been in the product appeal and sense of place that the developer has been able to create. Clearly, participation by foreigners in development projects in outlying areas was primarily based on the potential for the site as envisioned by the local development partner.

A number of land banking deals involving foreign capital have been done in the past and many are currently in hold patterns in the Phoenix marketplace. Various foreign investors participating in these deals include British, Canadian and Norwegian firms, as well as others. There appear to be a number of new land transactions which we could not confirm that include investments from Taiwan and Hong Kong.

Phoenix Growth Attracts Foreign Investment

Phoenix offers near unique opportunities to enter a high growth, pro-development real estate market at a point in its cycle when overbuilding has created attractive entry values for the long term investor. The local economy has been steadily and rapidly growing and is continuing to diversify into a well-balanced economic area offering strong demographics for manufacturing and service employment, as well as low land and labor costs. A low cost of living and relatively low business costs have been contributing factors to this trend. Phoenix's fundamentally sound, expanding economy combined with a quickly expanding population base are attractive to foreign investors seeking long term appreciation potential in U.S. assets. Combined with the fact that Arizona's economy is heavily export dependent, these factors create a need for additional outside capital investment and foster a receptivity to foreign capital sources.

Ease of Market Entry

Foreign investors choose varying approaches to entering the Phoenix market. Each strategy depends on obtaining local market knowledge. In some cases, the foreign investor has hired the local talent needed to provide input to the decision makers, and in other cases, the foreign investors have joint ventured with knowledgeable developers in the Phoenix market. In still other cases, a U.S. company has been purchased to allow immediate entry to the market. In the cases of some Canadian firms we interviewed, these investors gained market knowledge gradually over a period of years while visiting the market as vacationers.

While some investors came to know the area by vacationing in Phoenix, others invested in Phoenix after extensive market analysis, and still others were attracted to the area through the recommendations and goodwill of relationships they had established with Americans located in the region. Business and governemnt leaders in Phoenix increasingly recognize the necessity of imported capital to sustain and support the population growth now occurring and anticipated in the future. The development climate for foreign capital investment in Phoenix is favorable and strengthening.

Destination Point or Secondary Market?

Phoenix is a destination point for many foreign investors active in this market. Rather than finding foreign investment in Phoenix to be spill-over from foreign investment activity in other U.S. markets, we discovered little activity resulting from decisions to expand geographically or vertically in the development process. Generally speaking, foreign investors have entered Phoenix as a niche market in the U.S. where their particular resources (be they capital, construction experience or marketing expertise) can be used to best advantage in a growing economy with a relatively few competitors.

Shimizu is an example of a major Japanese investor whose first U.S. real estate invetsment activity took place in Phoenix. This is attributable to the relationship this company had with William C. Turner, an international business consultant and former ambassador to the OECD. Mr. Turner is largely responsible for Shimizu's decision to invest in Phoenix. This emphasizes the high regard the Japanese have for relationships and the opinions of those they know well and trust.

Value Through Development

Considering the nature of the real estate market in Phoenix, it is not surprising that foreign investors are taking an active role in development opportunities. It is interesting though that these investors are taking investment positions quite different from those about which so much has been written in the past few years, at least with respect to the Japanese.

Some investors believe that lack of significant land supply constraints in Phoenix will produce a downward pressure on rent levels, which in turn will diminish the upside potential of holding Phoenix real estate in the medium term. These investors believe that merchant build development operations create optimum value and upside potential in the development process. These investors therefore have chosen to engage exclusively in this area. Unlike real estate markets having severe land supply constraints in which high demand and product scarcity tend to produce long term value through increasing cash flow, some investors believe the return potential for exisiting property does not compare favorably, on a risk adjusted basis, to returns on development projects in the Phoenix area.

Local Market Knowledge is Favored Currency

Another key factor in the decisions of many foreign investors to become active in the Phoenix market appears to be relative ease of entry. As mentioned elsewhere in this study, the lack of land constraints as well as a favorable regulatory climate make Phoenix a desirable place to begin operations. The presence of a few rather than a plethora of high quality developers was also a consideration since existing developers could provide local market knowledge through joint venture arrangements, while the relative small number of major developers left ample room for market entry once independent deals were pursued.

In addition, foreign investors' ability to enter into arrangements with local development companies and the city's acceptance of foreign capital as necessary for continued growth has made entry relatively easy. Entry can be accomplished in a number of ways we have seen demonstrated in this market. For example, some foreign investors hire local professionals, others buy companies outright, and still others initially joint venture projects until they have acquired adequate market knowledge to make independent investment decisions. This is not to imply that joint ventures among foreign investors and U.S. developers will become obsolete, but rather that the value added by the U.S. developer to the joint venture is likely to diminish as the foreign investor acquires deeper market knowledge. This may influence the frequency of these agreements and the structure of those that do occur.

Foreign Investors of all Shapes and Sizes

Active foreign investors in the Phoenix area comprise a broad range of investor types. They range from large pension funds to relatively small firms offering syndications to wealthy foreign investors. Most activity has been focused on office and resort development.

With the Japanese investment community, the investors active in the development market of Phoenix tend to be construction and trading companies, while the Japanese investors engaging in first tier markets and prime acquisition property tend to be trust banks and insurance companies.

Most Foreigners are Positioning for Independent Action

The market and growth strategy favored by foreign investors after entering the Phoenix real estate market appears to be founded on the desire for eventual independent action. The alliances they make and the projects they consider appear to be made and evaluated in the context of acheiving the ability to undertake projects on their own and to create business opportunities for other business components of their operations.

Established Foreigners Act No Differently Than Locals

It is clear from our interviews of both domestic development companies and foreign investors that once a foreign investor has been active in a market for a comfortable period of time, their investment activities become virtually indistinguishable from those of their domestic counterparts. Domestic developers often remarked to our inquiries that they had not noticed the nationality of many prominent Canadian investors for some time because these investors had penetrated the market deeply and behaved essentially similar to other competitors in the marktetplace. Other nationalities, while perhaps more readily remembered by domestic developers as foreign due to language differences, also did not behave differently from domestic investors in terms of the development and investment activities they undertook.

Foreign Exchange Does Not Drive Decisions

While currency valuation does play a role in the initial evaluation of an American investment, it does not appear that currency exchange considerations are important to the ongoing management of the asset or that it affects management decisions regarding the asset's development or disposition. We do not believe that a resurgence of the U.S. dollar against other major currencies, as occurred in 1981 and 1982, will cause these investors to dispose of assets to gain windfall exchange profits. The foreign managers we spoke with were evaluated on the basis of their returns in U.S. dollars. Investment decisions regarding allocation of assets in terms of currency and asset risk are generally made, in the case of a major international firm, at the head office.

Patient Capital

Our research confirms that foreign investors in Phoenix real estate are, as has been stated in the past, patient investors. However, the prime reason for this long term view is not so much "cultural/corporate differences", but a dollar and cents decision permanently to diversify assets into the U.S. in general and Phoenix real estate in particular. Motivated by long term concerns emphasizing capital growth over current returns, foreign investors in the growing Phoenix market are well positioned to realize substantial capital gains on development projects with only minimal current cash flow potential. This is not to say that foreign investors will accept lower returns on their investments than will locals, but that they will take the returns in the form of value appreciation over the long run as opposed to short run cash flow.

This focus on the creation of long term value over short term earnings is reflected in the strategy of investors to manage their Phoenix operations for dollar results and to ignore short term exchange fluctuations.

Foreign Investment and Local Real Estate Professionals

To date, little of the foreign investment in Phoenix real estate has involved the acquisition of existing buildings. As a result, traditional brokerage services targeted towards this segment of the market have not been necessary. To the extent that a) foreign investment has established a firm foothold in Phoenix and b) new construction will soon introduce a number of investment grade properties to the downtown scene, foreign investors may soon be acquiring buildings in addition to developing them. Local real estate professionals may wish to access the overseas market to identify potential purchasers of these soon to be completed properties. Foreign firms established in Phoenix having contacts both in Phoenix and abroad may be the most effective source for introductions to potential foreign purchasers.

Our research also points out the importance to foreign investors of establishing long term relationships with local players and having a network of "contacts". This is most evident with Japanese firms, who were introduced to their local partners through intermediaries trusted by both sides and who have gone on to establish long standing relationships. Local real estate professionals interested in arranging foreign investments on their own or in third party deals must be willing to invest a substantial amount of time to establish a basis of trust and understanding with prospective investors. Without a foundation or track record of some kind, negotiations will be marked by a frustrating cycle of inconclusive meetings designed more as "get to know you" sessions than as deal cutting meetings.

Foreign Investment in Phoenix is Likely to Grow

Continued population and economic growth in Phoenix together with global market forces propelling foreign investment activity are likely to continue to attract additional investment in Phoenix real estate from abroad. William Turner aptly summed up in a recent address to members of the Phoenix real estate community that:

> "A significant increase in future foreign real estate investment in Arizona will continue to be a result of the push/pull phenomenon. The push of global market forces where exceptionally strong currencies and successful economies will continue to seek a happy home for available excess funds in politically safe and economically dynamic markets, and the pull of the exceptionally attractive investment environment, relatively low land prices, the prospect of longer term growth markets, strong absorption rates, and experienced partners, all of which Arizona can offer."

FOOTNOTES

Chapter II

1. U.S. Department of Commerce, Bureau of Economic Analysis. Survey of Current Business. Volume 67 Number 6. Washington, D.C., June 1987.

2. Ibid.

3. Ibid.

4. Ibid.

Chapter III

1. Sack, Paul. The Southwest Dallas/Ft. Worth, Houston, Phoenix Office, Industrial Reatil and Apartment Markets. Institute For Fiduciary Education, 1988. Page 2.

2. Ibid. Page 3

3. Ibid. Page 2

4. Mountain West Research. "Phoenix Metropolitan Area." Urban LAnd Institute - Market PRofiles 1987. Washington, D.C., 1987. Page 124 ff.

5. Ibid. Page 116.

6. Sack, Paul. The Southwest Dallas/Ft. Worth, Houston, Phoenix Office, Industrial Reatil and Apartment Markets. Institute For Fiduciary Education, 1988. Page 6.

7. Coldwell Banker Commercial Real Estate Services. Arizona: The Commercial Real Estate Market. Phoenix, AZ, 1988. Page 2 ff.

8. Mountain West Research. "Phoenix Metropolitan Area." Urban Land Institute - Market Profiles 1987. Washington, D.C., 1987. Page 126 ff.

9. Ibid. Page 123.

10. Ibid. Page 124.

Chapter IV

1. "Snowbird Properties, Inc.", Phoenix, AZ. Private interview with senior company official, June 1988. Snowbird is a pseudonym for a Phoenix company not wishing to be idenified in this thesis.

2. Northwest Land Co. Private Interview with senior company official, June 1988. Northwest is a pseudonym for a Phoenix company not wishing to be idenified in this thesis.

3. The Westcor Co. Private Interview with senior company official, June 1988.

4. Shimizu Construction Co., Inc. Private Interview with senior company official, June 1988.

5. Ibid.

6. Valhalla Development. Telephone interview with senior company official, July 1988. Valhalla Development is a pseudonym for a Phoenix company not wishing to be idenified in this thesis.

7. Valhalla Development. Telephone interview with senior company official, July 1988. Valhalla Development is a pseudonym for a Phoenix company not wishing to be idenified in this thesis.

8. Overseas Investment Co. Private Interview with senior company official, June 1988. Overseas Investment is a pseudonym for a Phoenix company not wishing to be idenified in this thesis.

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