Real Estate Finance in a Canadian Context
BUSI 221 Review Lecture

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• Comments on Project 2
• Format of exam
• General exam tips
• Key topics and multiple choice questions
• Mortgage Finance Review Questions
• Questions?
Project 2 Comments

• Part 1: calculation questions: show your work, BEGIN key, rounding of payment
• Part 2: most did Case Study—well done
221 Final Examination

REAL ESTATE DIVISION

- 3 hours, 100 marks
- 2 sections: multiple choice and written/calculation
- Multiple choice: 25 marks
- Essay/written: 75 marks
- Essay/written portion: calculation and written answers
- Mtg finance calculations: appx 50% of exam
- Law: 5%-10% of exam
General Exam Tips

• Watch your time, especially multiple choice questions
• Do questions in any order
• Show your work for calculation questions
• Point form is ok for written answers
• Try every question, especially multiple choice
• Terms: i.e., financial leverage, financial market, wheel of economy, money market, capital market
• Why use debt?
• History of Cdn mortgages
• Sub-prime market
• Bank of Canada
• Interest rates
• Mtg market and characteristics of mtg loans as investments
Multiple choice question 1

As a result of the economic collapse during the 1930s Great Depression, lenders switched from:

(1) Fully amortized loans to partially amortized loans
(2) Interest only loans to partially amortized loans
(3) Interest only loans to fully amortized loans
(4) Fully amortized loans to interest only loans
Ch. 2: Mtg Finance and Market Participants

- Identify and describe key players: chartered banks, credit unions, trusts and insurance companies

- Mtg brokers and mtg fraud
Which financial institution was a dominant participant (in terms of mtg loan approvals) in the mtg market during the 1980s?

(1) chartered banks
(2) credit unions
(3) trust companies
(4) life insurance companies
The two main types of mortgage fraud are:

(1) value fraud and brokerage fraud  
(2) counterfeit fraud and brokerage fraud  
(3) identity fraud and value fraud  
(4) none of the above
History of Housing Policy in Canada

- Dominion Housing Act
- National Housing Act
- CMHC
  - Mortgage Loan Insurance
  - Mortgage Rate Insurance
Ch. 4 and 5: Law Review

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- Real property law
- Contract law
- Mortgage law
- Mortgage fraud
- Implementation and enforcement of mtgs
Ch. 6: Mtg Math Review

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- Interest rates, payment, OSB
- Accrued interest
- Annuities: definitions and calculations
- Mortgage constant
- P/I split: one payment and over time
- Final Payments
- NPV, IRR, Profitability Index (PI)
Calculate the annual mortgage constant for a loan with monthly payments over a 25-year amortization period at an interest rate of 5% per annum, compounded monthly.

(1) 0.0585
(2) 0.0702
(3) 0.0933
(4) impossible to determine with information provided
5 I/YR
12 shift P/YR
1 PV
300 N
0 FV
PMT = -5.84590042E-3
X 12 = -7.0150805E-2

0.070150805, rounded to 0.0702
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Ch. 7: Residential Borrower Qualification

• Information Collection: application, credit analysis, appraisal

• Lending Policy
  • Income: GDS and TDS Ratios
  • Security: LTV
The loan amount a borrower qualifies for can be increased by:

(1) decreasing the amortization period.
(2) decreasing the loan-to-value ratio.
(3) decreasing the total debt service ratio.
(4) increasing the gross debt service ratio.
• Compare commercial vs residential underwriting

• Cash flow analysis (find NOI)

• Lending constraints
  • Income: safety margin, DCR
  • Security: LTV
A lease where the tenant is required to pay a specified percentage of gross or net sales made upon the premises is known as a:

(1) net lease
(2) gross lease
(3) percentage lease
(4) triple net lease
Which of the following mortgages best protects lenders from a loss in purchasing power?

(1) price level adjusted mortgage
(2) straight line principal reduction
(3) shared appreciation mortgage
(4) interest only mortgage
Ch. 9: Mtg Loan
Repayment Plans

- Straight line principal reduction
- Variable rate mortgage
- Graduated payment mortgage
- Sinking fund assisted mortgage
- Reverse mortgage
- Participation mortgage (SAM and income)
- Price level adjusted mortgage
The book value of a mortgage represents:

(1) an estimate of the amount that might be received if an existing mortgage is sold in an arm’s-length transaction under current conditions

(2) the amount of principal outstanding at a particular point in time

(3) the price an investor will pay for an existing mortgage

(4) the cost of funds advanced
Ch. 10: Loan Mgmt and Refinancing Options

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- Partial and full prepayment
- Arrears and default
- Refinancing:
  - Why refinance?
  - Options: new 1st, 2nd mtg and blended rate
- Loan pricing:
  - book value, market value, investment value, cost of funds advanced, yield to lender
The four major categories which track the stages of activity in the land development process are:

1. Business costs, project initiation, development management, and final marketing
2. Market monitoring, land acquisition, construction financing, and sales
3. Exploratory costs, planning costs, development management, and property management
4. Fixed overhead costs, feasibility studies, management decision, and leasing
• Overview of land development: costs/process
• Development financing options:
  • reserves, line of credit, construction financing
• Construction financing:
  • Underwriting and qualification, structuring and funding the loan
• Alternatives to construction financing:
  • joint ventures, participation loans, long-term loan with progress advances
Ch. 12: Leasehold Finance

- Types of leases
- Occupation leases
- Ground leases
- Sale-leaseback
- Appraisal of leasehold interest
- Valuation methods
A parcel of land currently valued at $2,500,000 can be obtained on a 80 year ground lease at an annual rent of $200,000. The land is currently vacant and a developer plans to construct a building on the site. Upon completion, the property will rent for $450,000 per annum (net). A market discount rate of $j_1=6\%$ is used to value the profit rent. What is the appraised market value of the leasehold estate?

(1) $3,301,800
(2) $4,992,900
(3) $3,765,500
(4) $4,127,300
Profit Rent = $450,000 - $200,000
Profit Rent = $250,000

6 I/YR
1 shift P/YR
250000 PMT
80 N
0 FV
PV -4,127,282.69257
12 mortgage finance review questions on website
Covers concepts in chapters 6-10
Detailed solutions provided with calculator steps
Good luck on the final examination!