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UNIVERSITI TUN HUSSEIN ONN MALAYSIA

**FINAL EXAMINATION
(ONLINE)
SEMESTER I
SESSION 2020/2021**

COURSE NAME : REAL ESTATE INVESTMENT AND APPRAISAL
COURSE CODE : BPE 34003
PROGRAMME CODE : BPD
EXAMINATION DATE : JANUARY / FEBRUARY 2021
DURATION : 3 HOURS
INSTRUCTION : ANSWER ALL QUESTIONS

THIS QUESTION PAPER CONSISTS OF THREE (3) PAGES

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Answer all questions by referring to the following case statement.

The AZB Corporation is considering opening an office in a new market area that would allow it to increase its annual sales by RM2.5 million. Cost of goods sold is estimated to be 40 percent of sales, and corporate overhead would increase by RM300,000, not including the cost of either acquiring or leasing office space. The corporation will have to invest RM2.5 million in office furniture, office equipment, and other up front costs associated with opening the new office before considering the costs of owning or leasing the office space.

A small office building could be purchased for sole use by the corporation at a total price of RM3.9 million, of which RM600,000 of the purchase price represent land value and RM3.3 million represent building value. The value of building would depreciate over 39 years. The corporation is in 30 percent tax bracket. An investor is willing to purchase the same building and lease it to the corporation for RM450,000 per year for a term of 15 years, with the corporation paying all real estate operating expenses (absolute net lease). Real estate operating expenses are estimated to be 50 percent of the lease payments. Estimates are that the property value will increase over the 15-year lease term for a sale price of RM4.9 million at the end of the 15 years. If the property is purchased, it would be financed with an interest only mortgage for RM2.73 million at an annual interest rate of 10 percent with a balloon payment due after 15 years.

- Q1**
- (a) Calculate return from opening the office building under the assumption that it is leased. (5 marks)
 - (b) Calculate return from opening the office building under the assumption that it is owned. (5 marks)
 - (c) Calculate the return on the incremental cash flow from owning versus leasing. (5 marks)
 - (d) Recommend factors that AZB Corporation need to consider before deciding whether to lease or to own. (15 marks)

Q2 Suppose that five years ago AZB Corporation had decided to own rather than lease the office building. Assume that it is now five years later, and management is considering sale-and leaseback of the property. The property can be sold today for RM4.24 million and leased back at a rate of RM450,000 per year on a 15-year lease starting today. It was purchased five years ago for RM3.9 million. Assume that the property will be worth RM5.7 million at the end of the 15-year lease.

- (a) Assess the amount of return value that the corporation would receive from the sale-leaseback of the property.

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(10 marks)

- (b) Estimate the cost of obtaining financing through a sale-leaseback method. (10 marks)
- (c) Calculate return if the corporation decides to continue to own the property. (5 marks)
- (d) Justify other alternatives that the corporation may consider before deciding whether to lease or to own. (15 marks)

Q3 AZB Corporation realizes that the benefits of leasing versus owning may be sensitive to many of the assumptions being made. Management wants to know how the return on the incremental cash flow from owning versus leasing is affected by different assumptions

- (a) Develop a cash flow statement that demonstrates the effect of zero tax bracket. (10 marks)
- (b) Develop a cash flow statement that demonstrates the effect of property value being remained constant for the whole period. (10 marks)
- (c) Develop a cash flow statement that demonstrates the effect of mortgage rate at 8 percent. (10 marks)

-END OF QUESTIONS-

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