Editor's Note

BY PETER C. BURLEY, CRE

"To build may have to be the slow and laborious task of years. To destroy can be the … act of a single day."
—Sir Winston Churchill

People build things. It's what we do. Skyscrapers, supermarkets, strip malls, movie theaters, stadiums, highways, bridges. Homes, streets, neighborhoods. Fences, gardens, barns, and sheds. We build to serve a purpose—or multiple purposes. We build to improve our lives and our society. We build things to last beyond our own short existence. We build to leave a legacy.

I have been thinking a lot about how we build things, how long it takes to build them, and how long things last. In particular, as I prepare to move this household and this office to Washington, I have been thinking about what was left by those who lived here before me and about what I will leave to those who come after.

My house was built in 1910. It is a solid structure, set on a foundation of hand-formed concrete that was mixed on-site with water and sand from the creek nearby. It was built for family life, with four bedrooms upstairs, and a parlor, kitchen, and pantry downstairs. Originally, it had no indoor plumbing or electrical wiring or heat (other than a large fireplace and a wood-burning stove in the kitchen). Years later, bathrooms were added, as were electrical wires and light fixtures. Many years after that, a garage was added to house several cars. The driveway was paved in the 1980s.

Residents here have added and subtracted to accommodate various changes in situation and lifestyle. Some of the remodeling that has taken place here still leaves us wondering: "what on earth were they thinking?" For the most part, though, the changes over the years have been for the better. I am not sure if I would have bought the place if the kitchen, for instance, had not been updated to include a gas range or dishwasher. And, I certainly don't think we would have moved out here if our bath time had required a walk down to Cook Creek once every other week.

The Legacy of a Solid Structure *Photo courtesy of Tallant Burley*

A hundred years ago, when the house was first built, the original residents here also constructed a small stable where the horses likely spent the night and where various equine supplies were kept. It was well built, like the house, with hand-crafted concrete and heavy timber studs and rafters. But, over the years, particularly after the new garage was built, it fell into neglect, slowly falling into disrepair. In the fall of 2008, a fierce canyon wind pushed a very large willow tree onto the structure, bringing whatever remained of its useful life to an end. The tree and the outbuilding lie, just as they fell, at this very moment. We have not addressed the situation (for which I feel some personal guilt) as neither the old shed nor the the tree have been priorities in our life in the country—we keep no horses, we require no tack, and eventually the tree will provide a cord or two of firewood.

Back behind the house is another old outbuilding that was originally built, we believe, as a chicken coop. The family that built the chicken coop likely shuffled "out back" every day to gather eggs for breakfast or a hen for dinner. Later, there is evidence that the chicken coop was converted into a smokehouse, where a steer or hog was prepared as winter meat. The building is also in a state of slow decline, having fallen into disuse over these past many decades. We don't keep chickens (few people do these days), and we don't smoke our own livestock.

The things we build—and the things we change in the things we build—reflect purpose, our sense of what is important in our lives.

Stuff happens. Sometimes that stuff changes our lives or, at least, changes our perceptions of what is important. Sometimes, structures are threatened. Sometimes, structures collapse or are crushed by very big events, or trees, and circumstance. That the tree fell on an old stable that we don't use enabled me to build and to improve other, more important structures on this property. If the tree had fallen on the house, I would have hurriedly repaired the damage in order to keep the house—and our lifestyle—intact.

That ill wind, the one that brought down the old willow and flattened the stable, blew in about the same time that the financial markets and our economy were nearly brought down by a devastating windstorm of their own. A number of the financial and economic structures that we, as a society, had built over the years (some more sturdy than others) were heavily damaged. This time, the storm damaged the very house in which we live and do business, and it became imperative that we repair the damage, and shore up the foundation and the structural supports, in order to keep the house intact. Other structures were severely threatened. And, the questions we have asked ourselves since the storm have rightly focused on what we should rebuild, where we might remodel, what we should simply let lie as perhaps no longer useful.

This edition of *Real Estate Issues* focuses on where some of the damage was done and what is being done—as well as what yet needs to be done—to restore our financial and economic house and to keep it intact.

Historically, real estate has been one of the stronger and more reliable components in restoring and rebuilding after damaging economic storms. This time around, that has not been the case, as **Tony Downs, CRE**, suggests in his Insider's Perspective, **"The Outlook for Recovery in U.S. Real Estate Markets."** In fact, Downs points out that real estate has been largely responsible for most of the damage we have experienced in the recent downturn. We set our expectations too high, in believing that real estate values would simply continue to rise, leading us to forget that "what goes up, must come down." In fact, the damage that was done was done largely as a result of a poorly constructed foundation, as it were—we crafted much of our financial and economic structure on those expectations, weakening the structure itself.

But, what kind of damage has been suffered, and what kind of structural repair might be undertaken to gird against subsequent economic windstorms? In a special *Real Estate Issues* **Leadership Roundtable**, Downs engages three experts, **CREs Marc Thompson** and **K.C. Conway**, and CNLBank President **Sandy Hostetter**, in a conversation that runs through some of the issues that have emerged in the financial sector during and after the recent crisis. They offer a look at the structures and regulations that have been put in place as well as a glance at some of the implications for the banking industry and for real estate going forward. We may need some new approaches this time around. As Conway suggests, "…we need to begin to think about how different this situation is and what kind of policies need to be different rather than finding the same old tools of the old recession."

New tools. **William "Bill" Pittenger** points out in **"A Brief Look at the Dodd-Frank Act"** that: "The financial crisis that began in 2008 was largely a product of outdated regulation and supervision" along with innovations in technology and credit markets that were "advancing faster than regulatory and risk management controls." Pittenger reviews the Dodd-Frank Act, which creates new agencies and oversight for various financial institutions, with an eye on the Act's possible unintended consequences and some of the difficulties in implementing many of its provisions. Not addressing the future of the GSEs in the Act, he points out, leaves a very big hole. Additionally, Pittenger says, "… the Act's many provisions and those that will follow with creation of numerous regulations will increase regulatory and legal risk and the cost of doing business for virtually all financial service institutions."

Dodd-Frank may be, as Pittenger says, "the most sweeping piece of financial legislation enacted in the U.S. since The Great Depression." In addition to the new structures and regulations put in place by that legislation, Congress has also passed, and the President has signed into law, the Patient Protection and Affordable Care Act, followed closely (March 30, 2010) by the Health Care and Education Reconciliation Act. A look at the tax implications of health care reforms for small businesses and real estate investors is provided in **"The Income Tax Effects of Health Care Reform on Small Businesses and Real Estate Investors,"** by **J. Russell Hardin, Ph.D**. Hardin offers tips and advice for businesses trying to navigate their way through the new law. He concludes that "…a law as complicated as this Act commands a great deal of study by investors and small business owners who desire to maximize returns and minimize the tax burden."

Government assets, including real estate, are the subject of an article, **"Government Property Assets in the Wake of the Dual Crisis in Public Finance and Real Estate: An Opportunity to Do Better Going Forward?"** by **Olga Kaganova, CRE**, of the Urban Institute. Kaganova reminds us that "… government property assets constitute a very substantial share of public wealth in most countries… these assets often make up the lion's share of public wealth." Good data on "on the size and composition of government property and business holdings is still lacking," however. In fact, even in the United States, she points out that nearly half of the states do not have even basic property or asset data. This can have important financial implications, she tells us, since creditworthiness ratings of governments issued by credit agencies usually do not depend on assets owned by the government." That can "prevent implementation of rational financial solutions." And, government assets can be part of the solution to current fiscal crises at many levels. Given how large and complex property portfolios can be, Kaganova suggests that governments enlist the expertise available through such organizations as The Counselors and RICS to make the best use of those assets in the future.

In their article, **"Timing the Market: You Don't Have to be Perfect," Randy Anderson**, **CRE**, and **Joshua Harris** ask the question: "Is there an optimal strategy to time purchases and dispositions based on changes in the real estate or macroeconomic cycle?" Through a simulation of macroeconomic cycles and real estate cycles, as represented in the NCREIF Index, Anderson and Harris develop a perspective of real estate asset performance during and after recessions and a view of active market timing. Buying at or near a market low, for instance, clearly benefits an investor by producing returns higher than a simple buy-hold strategy. There is also benefit in exiting an investment before a downturn hits. They conclude: "…do not fear recessions and downturns, but do plan on worst-case scenarios and be prepared."

In addition to the recent changes brought by the Dodd-Frank bill and Healthcare Reform, the Small Business Jobs Act of 2010, which was signed by President Obama in September 2010, provides additional tax relief for small businesses and promises additional support in the economic recovery. **Mark L. Levine**, **CRE**, and **Libbi Levine Segev** outline some of the provisions and discuss some of the legal ramifications of the Act in **"Small Business Jobs Act of 2010: Impact on the Real Estate Market."**

Finally, *Real Estate Issues*' Associate Editor **Mary Bujold**, **CRE**, reviews *Emerging Market Real Estate Investment: Investing in China, Brazil and India*, by **David Lynn**, **CRE,** and **Tim Wang, Ph.D**. With China, Brazil and India comprising a combined GDP of roughly $12.4 trillion, and with each country moving rapidly up the economic scale, these countries represent significant opportunity for real estate investment. But, investment in these, or any emerging market, can prove a daunting task. The book's authors outline a systematic framework for evaluating emerging markets and measure the desirability of investing in those markets based on locational factors, the competitive environment and growth factors.

There has been a lot of repair and rebuilding in our financial and economic house since the last violent storm. Hopefully, the work that has been done will prove sturdy enough to withstand the next storm. Just like my old house, of course, as the times and challenges change, we may be required to rebuild yet again, or to remodel or, in some cases, to simply let lie. But, with the experience and insights we have gained, particularly with the expertise represented in this edition of *Real Estate Issues*, we will be better prepared to do so.

I would like to extend my heartfelt thanks to all of our contributors, especially to Tony Downs for assembling the Roundtable discussion and to K.C. Conway, Marc Thompson and Sandy Hostetter for agreeing to take time out to participate. Also, a special thanks to Carol Scherf, our managing editor, for her continued efforts in producing, once again, another fine edition of *Real Estate Issues*.

PETER C. BURLEY, CRE
EDITOR IN CHIEF