



A publication by Key Group, Ltd., a real estate company with insights on issues and opportunities in Southern Arizona

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## Joint Ventures


This article is designed to provide real estate investors with an overview of joint ventures and how they work in the industry.

► **What is a joint venture?** A joint venture is simply a partnership formed with a property owner. Typically the property owner will own a parcel of land suitable for current development, and the joint venture partner is a developer who can create additional value for the land by building something that can be leased or sold. This could include the construction of apartments, retail shopping centers, or office and industrial buildings. It could also entail development of the land into individual lots for sale.

► **Why are joint ventures formed?** The value of land "in use" is typically significantly higher than land that does not create income from sale or rental. Development is inherently a more complicated process than simply holding the land because of the wide variety of activities, which need to be coordinated to effect a successful development. The responsibilities of the developer can include the initial feasibility analysis to establish project demand. Locating and securing tenants who will satisfy lender criteria, as well as directing the design and planning phase are part of the up front activities for the developer. Finally, costing out the project, supervision of construction, and management of the finished development are typical services provided by a developer.

A great deal of risk occurs for the developer if they are forced to acquire the land prior to answering all the questions necessary regarding the land's suitability for immediate feasible development. If developers can't ask for the time necessary to answer these questions, they must generally pay a lesser price and are said to be buying for "speculative" purposes, or to "land bank" (for investment). This is done much less frequently due to the necessity of tying up significant amounts of the developer's cash.

The property owner can often get a higher price by allowing the questions regarding development feasibility to be answered, thereby lessening the developers' risk.

The "joint venture" combines the desire of the property owner to achieve the best return, and the desire of the developer to answer the questions controlling their risk. The developer may take a lesser return and have a partner if the new joint venture can use the value of the land when contributed to the new venture as the required equity. A property owner can often contribute their land to a joint venture for close to what they could sell it for, be paid from an acquisition and development loan, and still retain an ownership interest in the completed project. Any property owner contemplating a joint venture in order to maximize their current holding's return should consult real estate, legal, and accounting advice from advisors experienced with real estate matters. 

## Your Key Group Team

Your Key Group team includes the following professionals. For more information about our company, see "Inside KeyGroup" on page 3, or visit [www.keygrouppltd.com](http://www.keygrouppltd.com). We're also happy to talk to you in person. Call us at (520) 290-5656 or (800) 453-2214.

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## Investing in Tucson Commerical Real Estate

Less than 30 years ago, "Tucson" was that Southwestern community consisting of approximately 350,000 people, whose city limits were roughly defined by Golf Links and River roads to the south and north, and Wilmot and I-10 to the east and west. Today the Tucson metropolitan area includes areas from Sahuarita all the way north to the Pinal County line, and as far east as the western edges of Benson. Pima County's population now boasts approximately 933,700.

This fundamental growth has been a key in the success formula for this area's investment story. Housing, initially apartments, are needed for the continuous inflow of newcomers. In recent years with hyper-low interest rates, the newcomers are often lured into the new construction housing market. This trend has impacted the tenant turnover and associated management costs. This dramatic growth in Pima County ensures that the demand for apartments remains consistent.

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## New Ordinance May Impact Land Values

The local governments have never been reticent to ignore additional development regulations or generate more revenue by raising fees or taxes. Earlier in the year, it was Pima County that imposed a set-aside or allowance for park space for each new subdivision. In the summer, it was the city's turn, as it raised water and sewer fees, and then, more notably, created the garbage fee that imposed \$12 per month to each homeowner. It was explained that this would make the garbage division self-sustaining, which means that if there is a deficit in the future, rates will be raised to cover the deficit.

Now it is the County's turn again. Sometime in the fall, the county will be voting on an ordinance known as "Minor Lands Division". The state of Arizona currently allows a parcel to be split into five or fewer lots without a formal subdivision compliance. The new county ordinance will serve as a guide for dividing a parcel into five or fewer lots.

In the future any parcel division (with a few exceptions) will require a permit together with appropriate fees. The general requirements provisions are reasonable, requiring that each lot meet minimum zoning have

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## Investing in Tucson Commercial Real Estate

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In fact, the apartment vacancy rate in the first quarter for 2004 decreased from 10.7 percent to about 9.6 percent, perhaps indicating some resistance to the average new home cost, which has now increased to \$197,000.

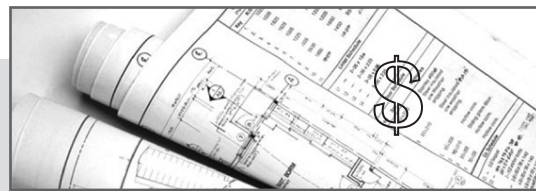
The influx of new residents creates additional daily commerce and demands for neighborhood retail shops. This is reflected in the absorption rates of retail properties. The street-side commercial vacancy rate in June 2004 was 9.9 percent, down from 10.5 percent a year ago. The shopping center vacancy rate was 9.8 percent, down from 12.2 percent last year. The greatest absorption was found in the northwest and east sides of the Tucson valley reflecting the strong growth in those areas.

Companies moving into the area require office space. During the past 12 months, there was a net positive absorption of 220,100 square feet of office space. There remains a relatively high average vacancy of 14.1 percent, for leasable space, however. When con-

sidering that over 1,000,000 square feet of office space has been built since the beginning of 2002, this represents almost 22 percent of the amount of new construction. At the end of the first quarter of 2004, there were approximately 474,000 square feet under construction, up 30 percent from the third quarter of 2003.

The Tucson/Pima County real estate market is considered small by commercial standards and has a limited appeal to the institutional investor. It is unique, however, with its diversity of investor profiles. The University of Arizona, winter visitors, and second-home ownership have brought investors from around the world to a market that would otherwise be regionally based.

The projected area population growth, especially from the baby boomer retirement sector, indicates a stable market condition. There are some caveats to recognize. The addition of thousands of new homes and buildings has created a burgeoning assessment basis for the local taxing authorities. As a result, the ever-expanding budgets create higher taxes for the investment properties. Investors are cautioned to look carefully at leases, for example, to ensure that potentially higher taxes triggered by a property sale or purchase can be passed through to tenants. Or if not, it should be accounted for in the sales. ¶



## Impact of New Ordinance

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legal and physical access, and has reserved utility easements.

However, a bureaucratic morass will be created in the procedure provision of the ordinance. The permit process will begin with a land division application together with a sealed survey (and appropriate fees). It goes downhill from there. The next requirement is for preliminary title report providing proof of access as shown by survey.

Step 3 requires "certification from a licensed and registered engineer" providing the same proof of access as shown on the survey.

Then, for some reason, the county wants signed written acknowledgement from the property owner that no permit will be issued until general requirements are met.

The balance of the ordinance provides review of application (30 days), exception, and enforcement. Finally there is a fee schedule. Most applications will be \$150 per lot.

Each new ordinance creating new restrictions or fees for development makes the term "affordable housing" more of an oxymoron.

Minor land division is just one more ordinance that will make the creation of additional housing lots more burdensome and costly. Rest assured, it won't be the last.

As the cost of development and government regulations increase and assuring there is a ceiling to the price a homeowner can afford to pay, eventually the value of land is the component that takes the hit. (Article by William Meyer.) ¶

## Property Spotlight: Hotels & Motels

by Jesus Antonio Pujol Irastorza

The hotel industry has always been closely tied to the economy. The industry was dealt two bad hands in the form of a recession and terrorist activity; however the market has demonstrated resilience. Travel and tourism will be a major cause in job creation in the near future, as most people return to their normal travel patterns. We will soon witness the next wave of expansion for the hospitality industry. We should see major increases in average

daily rates in the next couple of months and RevPAR growth will accelerate as occupancies improve throughout the year. Investors should closely position themselves to take advantage of the next business cycle. The following sales summary of hotels and motels in the Tucson area through February 2003 to June 2004 reflect this strengthened market. These sales represent 50 percent increases in the number of sales from the prior 18-month period. ¶

Summary of Hotel/Motel Sales October 2003 to April 2004

Property Address	Property Name	Sale Date	Sales Price	\$/Unit	Down Pmt.	Units	Age
755 E Benson Hwy	Western Inn Motel	6/3/2004	\$ 1,150,000	\$ 9,583	\$ 750,000	120	27
5251 S Julian Dr	Palo Verde Inn & Suites	5/28/2004	\$ 4,217,600	\$24,379	\$ 817,600	173	20
8370 N Cracker Barrel Rd	Days Inn & Suites	5/25/2004	\$ 3,150,000	\$50,806	\$ 1,871,000	62	4
3031 S 6th Ave	Star Motel-18 Rooms	4/8/2004	\$ 375,000	\$20,833	\$ 272,000	18	58
1010 S Freeway Rd	Howard Johnson	1/21/2004	\$ 2,575,000	\$24,065	\$ 1,250,000	107	45
228 N 4th Ave	Gateway Villas B&B	1/14/2004	\$ 460,000	\$65,714	\$ 92,000	7	78
741 W Miracle Mile	Mountain View Motel	1/14/2004	\$ 315,000	\$15,000	\$ 228,120	21	54
5335 E Broadway Blvd	Embassy Suites Hotel	12/30/2003	\$ 6,500,000	\$45,774	\$ 2,700,000	142	28
350 S Freeway Rd	Pueblo Inn	11/13/2003	\$ 3,550,000	\$20,402	\$ 1,165,000	174	32
1640 N Campbell Ave	La Posada Del Valle	11/4/2003	\$ 530,000	\$75,714	\$ 53,000	7	66
201 S Williams Blvd	Courtyard Marriott Hotel	10/31/2003	\$ 8,801,811	\$53,998	\$ 8,801,811	163	7
1300 N Stone Ave	Flamingo Hotel	10/27/2003	\$ 1,625,000	\$20,312	\$ 447,500	80	34
1919 N Oracle Rd	Highland Tower Motel	10/24/2003	\$ 340,000	\$16,190	\$ 40,000	21	62
465 W Miracle Mile	Sunland Motel	10/17/2003	\$ 340,000	\$17,000	\$ 63,374	20	51
105 N Avendia Javalina	Arizona Suncatcher	10/2/2003	\$ 590,000	\$98,333	\$ 118,000	6	31
1742 N Oracle Rd	USA Extended Stay	9/2/2003	\$ 665,000	\$13,039	\$ 125,000	51	57

Sources: Hotel-Online, Comps Costar, Pricewaterhouse Coopers, Smith Travel Research.



### Inside Key Group

Key Group is a diversified full-service commercial real estate company providing a high degree of personalized investment service including brokerage, leasing management, and consulting. Now achieving more than 50 years of combined experience between the partners, we provide, with the highest professional standards, a thorough real estate market knowledge, deal negotiation skills, contracts, and inventory sources.

Jesus Antonio Pujol Irastorza recently joined Key Group as Sales Associate, involved in the brokerage of commercial investments and heads the company's hotel division. In this position, he provides hospitality consulting and advisory services, and oversees the acquisition and disposition of hotels and resorts. Pujol is a native of Nogales, where his family has been in the hotel business for more than 50 years at the Fray Marcos de Niza Hotel in Nogales, Sonora Mexico. He is a graduate of the University of Arizona, with a degree in Regional Development & Business Administration. ¶