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A special issue of International Real Estate Review (IRER) on

Real Estate Debt and Finance

The International Real Estate Review (IRER) invited papers on special issues that examine "real estate debt and finance" that will cover issues relating to financial and debt-related activities and also the impact of interest rate risks on activities in both private and public real estate markets in different countries. We have accepted five excellent research papers for the special issue that examine questions from banking relationships and leverage to bankruptcy risks of REITs on the public market side of the markets. It also includes two other papers on the private real estate markets, which include the topic of collateral effects and mortgage risks on homeownership rates.

The first paper, "Banking Relationships and Financing Decisions of REITs," by Yuanchen Chang, Yi-Ting Hsieh, and Kiat Ying Seah, examines how banking relationships influence the financing decisions of real estate investment trusts (REITs). Using a comprehensive data set of loan facilities by REITs across different markets, this paper empirically tests the effect of REIT-bank relationships on credit costs and other non-price credit terms. The paper shows that REITs with past banking relationships enjoy favourable loan terms that include lower loan rates, higher loan amounts, and a less stringent collateral requirement. These favorable terms associated with the relationship banks were maintained during the global financial crisis from 2007 to 2009.

The second paper by Wouter Vangeel Vrije, Laurens Defau Johannes Kepler, and Lieven De Moor Vrije, titled "The influence of a mortgage interest deduction on European households' homeownership attainment," provides new European evidence about the relationship between the mortgage interest

deduction (MID) and homeownership. The study estimated the multilevel mixed-effects logistic regressions using Eurostat EU-SILC data in twelve countries from 2003 to 2018. The results show that a MID generally fails to advance its purpose of promoting homeownership due to price capitalization. However, the results showed (substantial) variation across household groups. The intended positive effect of a MID on homeownership probability occurs only for the highest-income households. Those who needed the most help with good-quality affordable housing were the most discouraged by this interest rate relief to become a homeowner.

The third paper, "Leverage Strategies of REITs and Real Estate Operating Companies," by Carolyn W. Chang, Kian Guan Lim, and Zhi Min Zhang, studies strategies of two related types of real estate companies – REITs and real estate operating companies (REOCs) using the data in three major Asian real estate markets - Hong Kong, Japan, and Singapore, from 2001 to 2021. REITs are bound by the rules on earning distribution, real estate holding, and leverage limits. Unlike the REIT model, which focuses mostly on investing in income-generating real estate, REOCs are exposed to a wide range of real estate development activities, from land acquisition, construction, and asset management to redevelopment and disposal. The study found that REOCs use 18.96% more debt than REITs after controlling for firms' agency risks, dividend yields, market risks, and also property sector, country, and year fixed effects. They also showed that dividend payouts have no effect on the leverage strategies, but high tax ratios increase the debt usage of REOCs relative to REITs. The study also showed that the real estate value to total firm value ratio, which is a proxy of liquidation cost, has negative effects on debt ratios for both real estate firms. REOCs with a high concentration of rental revenue stream are more vulnerable to liquidation risks and, thus, are more likely to have a lower debt ratio. REITs also have higher debt usage as rental incomes enhance cash-flow liquidity.

The collateral channel literature predicts that real estate prices increase the debt capacity of firms with more real estate assets. In the fourth paper, "Corporate Governance and Real Estate

Collateral Effect," Daxuan Zhao empirically tests the heterogeneity in collateral-investment relationships. He found that firms with strong corporate governance were more likely to increase debt capacity via the collateral channel during the real estate boom from 1993 to 2006. Entrenched managers use less debt to finance their investments when their real estate collateral values increase. The results hold after controlling for non-collateral debts and credit rating of sample firms.

In the last paper on "Bankruptcy Prediction in REITs," Tamala Amelia Manda used the vector autoregressive (VAR), logistic, and multilinear models to detect bankruptcy risks in the REIT industry. The macroeconomic variables used as part of illustrating bankruptcy are adopted from Altman (1968), with an addition of the funds from operations (FFOs). The results confirm interconnectedness among the macroeconomic variables found in Altman (1968) and its causal relationships with REIT bankruptcy risks. The profitability ratio, solvency ratio, and liquidity ratio were found to cause declining financial health and financial positions of REIT firms during tough market conditions.

We hope the five papers published in the special issues could motivate more studies into real estate finance and debt issues, especially in international markets outside the US. More studies could be conducted to examine how REIT and private real estate players will adjust their finance and debt strategies in the post-COVID period, which saw significant increases in the US Federal Reserve (FED) Effective Fund Rates after 2022.

Thank you!

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