A Theory of Commercial Real Estate Development, REIT Investments and Taxes[1]

Marta Faias

Universidade Nova de Lisboa

Jaime Luque

Department of Real Estate and Urban Land Economics

University of Wisconsin - Madison

Abstract: We consider a two-stage general equilibrium model of commercial real estate (CRE) development in a multi jurisdictions economy with segmented markets. Local CRE assets produce consumption goods that are sold to households in the jurisdiction. The developer's capital structure, CRE cash flows, as well as the equity, debt and commodity prices are all endogenous. Strategic jurisdiction authorities choose property taxes to attract global REIT investors. An equilibrium exists and demand differentiability holds even when CRE assets are co-linear among jurisdictions. We provide examples of our model, and discuss the role of taxes, including the Tax Incremental Financing (TIF), in attracting CRE investments and promoting development.

JEL Classification : D52, D53, G12, G14, G15. G18.

Keywords: commercial real estate (CRE) development; global investors; local households; urban planning; multiple jurisdictions; co-linear CRE assets; equilibrium; demand differentiability; taxes; TIF.

---

[1] We would like to thank for comments and suggestions Bernard Cornet, Carlos Herves-Beloso, Peter Ritz, Juan Pablo Torres-Martinez, and Yiannis Vailakis, and the participants at the conferences of SAET (2013), EGWE (2013), PET (2013), and the V Workshop on Equilibrium Analysis (2014), and seminars at the U. Indiana, Purdue U., and U. Wisconsin-Madison. Email addresses: mcm@fct.unl.pt (M. Faias) and jluque@wisc.edu (J. Luque). Corresponding author: Jaime Luque; University of Wisconsin-Madison; 5259 Grainger Hall, 975 University Avenue; Madison, WI 53706, USA; Phone: (+1) 608-265-5322.