Corporate real estate financing methods: A statistical study of corporations' choices

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Abstract

This study examines the financing methods used by corporations to acquire real estate for their operations. It also examines the opinion of managers about the factors that they consider in choosing financing methods. The data were provided by a survey questionnaire that was sent to members of the International Association of Corporate Real Estate Executives. It was found that companies rely on internal financing (operating cash flows) and external financing such as long-term leasing, joint ventures, property mortgages and sale/leaseback arrangements. The top-ranked methods of finance include operating cash flows, property mortgages, leasing and sales/leasebacks. Use of real estate investment trusts, collateralised mortgage obligations and mortgage-backed securities were the lowest-ranked forms of financing. Managers tend to look at tax advantages of debt and availability of cash flows in deciding which financing methods to use, rather than theoretical corporate finance factors such as bankruptcy cost. There were significant differences in opinion by industry and by company size regarding the use of cash flows and the impact of debt financing on common stock prices.

Keywords: corporate real estate, asset financing, corporate financing, real estate assets

INTRODUCTION

The literature in corporate real estate contains several empirical studies examining the use and management of corporate real estate among US companies,[3] Pacific Rim corporations[4] and European firms.[5] However, until Redman and Tanner,[6]

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there had not been an inquiry into the sources of funds that corporate executives use to purchase operating real estate. Redman and Tanner investigated the sources of financing of corporate real estate and the utilisation, techniques and motivations involved in leasing real estate by manufacturing and service corporations. They found that significant sources of funds to acquire real assets for production, distribution and headquarters activities were operating cash flows rather than external sources. Leasing was a common technique to finance and acquire assets, allowing for managerial flexibility and tax-sheltering benefits and creating off-balance sheet financing.

Although recent articles by McIntosh and Whitaker[7] and Grissom[8] covered the nature of REITs and capital market access for corporate real estate executives, and Nesson[9] discussed five alternative financing methods, there has been no study of the current utilisation of financing techniques by non-real estate corporations to acquire real assets for productive use. There has been no examination of the factors that executives consider in deciding which resources to use to generate the necessary funds to purchase real assets. The purpose of this study is to shed light on the sources and the importance of different types of funds that managers tap to purchase real estate for their firms and to examine the motivation behind using those sources.

METHODOLOGY

The objectives of this study were accomplished through using a survey of the corporate real estate executive members of the International Association of Corporate Real Estate Executives (NACORE). A questionnaire was mailed to 935 members of NACORE. Fifty-six (6 per cent) of the questionnaires were returned and form the basis for the analysis. Alreck and Settle[10] state that response rates above 30 per cent are rare in mail surveys, which often range from 5 per cent to 10 per cent. The response rate in this study does conform to the findings of Alreck and Settle and should yield generally applicable results.

The survey instrument (in the Appendix to this paper) has questions organised into three subject groups: demographic questions concerning the size and industry of the respondent's company; questions relating to the financing methods used by companies; and questions regarding priority of methods used by their companies. The executives were queried about the use of REIT structures and asset-backed securities as financing vehicles for their asset purchases. The instrument also contains Likert-type questions concerning the factors that executives consider in deciding which financing tools they use to generate the necessary funds for real estate acquisitions. The questions were based on prior studies in finance that indicate the theoretical factors that influence the capital structure decisions of managers.[11]

The following section contains a discussion of the response frequencies for the questions concerning financing techniques. The discussion of the decision factors in choosing financing tools includes the distributions and the means of the responses.

RESULTS

Table 1 reports the industry and size categories for the sample. About one-third of the respondents are in the financial services industry, which includes securities brokerage firms, commercial banks, public accounting firms, land development companies and consulting firms. The category of 'other' includes companies in the

Table 1: Respondent characteristics

Category	*Percentage of responses*
A — By industry	
Financial services	32.1
Manufacturing	12.5
Retail	21.4
Technology (computer hardware; software; telecommunications)	7.2
Other	26.8
Total	100.0
B — By asset value of companies	
Small company ($1.5bn and less)	43.7
Large company (over $1.5bn)	56.3
Total	100.0

healthcare, transportation, government, engineering and aerospace industries. The retail industry includes companies in the consumer retail business and the hospitality business. In terms of company size, measured as the value of assets of the firms, most of the companies are large firms with asset values in excess of US$1.5bn.

Sources of financing

Table 2 presents the responses regarding the types of financing companies use to acquire real property by their firms. Redman and Tanner[3] found that 63 per cent of the executives specified operating cash flow as the source of funding, with 41 per cent specifying property-secured mortgages, 35 per cent using long-term leases, 25 per cent using sale and leasebacks and 24 per cent using joint ventures.

From Table 2 it can be seen that, even with the current sample of managers, companies generally continue to use the same source of funding. More managers (75 per cent of the respondents) specified operating cash flow, while fewer selected mortgages. Leasing was selected by 41 per cent, while sale and leaseback arrangements were chosen by 24 per cent. Limited partnerships have been used by only 5 per cent of the companies. About 20 per cent choose the miscellaneous category: the methods specified included tax-free bonds (presumably municipal bonds), short-term leasing and unsecured borrowing (possibly bank debt). Three interesting sources were mentioned. Two respondents suggested the use of 'synthetic leasing' without describing the details. Another specified that all property was leased and any construction costs above lessor allowances were capitalised and amortised over the life of the lease. Additionally, one manager cited foreign investors as a source of funding.

Because of new financing vehicles used by companies in the 1990s,[12] the authors included non-traditional sources such as real estate investment trusts, collateralised mortgage obligations (CMOs) and mortgage-backed securities. It seems that while REITs were popular

Table 2: Sources of financing for corporate real estate acquisitions

Types of financing	*Percentage of responses**
Mortgage loans — property secured	30.4
Mortgage bonds — property secured	7.1
Sale of unsecured bonds	1.8
Operating cash flow	75.0
Sale of common stock	5.4
Sale of preferred stock	1.8
Sale of commercial paper	3.6
Long-term leasing	41.1
Sale-leaseback arrangements	123.2
Joint ventures	12.5
Equity REITs	1.8
Mortgage REITs	–
Hybrid REITs	–
Sale of collateralised mortgage obligations	1.8
Sale of commercial mortgage-backed securities	3.6
Limited partnerships	5.4
Participating mortgages	–
Other	19.6

*Percentages do not sum to 100% because respondents could select more than one type of financing method.

mechanisms in the late 1980s and early 1990s, their popularity may have diminished, possibly because of the decline in popularity of REITs among investors. However, it is interesting that a small proportion of the firms have used equity REITs, CMOs and mortgage-backed bonds, with a larger proportion having used mortgage-backed bonds to secure financing. Given the complicated nature of REIT and mortgage-backed securities, it would seem that large firms with better access to investment bankers and financial markets would use these mechanisms. An additional study might be able to reveal reliance on the different methods according to company size. It might be hypothesised that the traditional financing methods of operating cash flow, mortgages, leasing and sale and leasebacks would be used by firms of all sizes, with the new sources of REITs and mortgage-backed debt having been used primarily by the larger, better-established companies with greater access to the financial markets.

Pecking order of financing

A key question asked of the managers was to rank the financing methods their companies use in priority of importance. This question follows along the line of the Pecking Order Hypothesis in finance: that corporate managements have a priority list of sources of funding that they exploit. The results are shown in Table 3 and parallel the choices shown in Table 2. The basic difference between Tables 2 and 3 is that the second exhibit shows the methods actually used by the companies, while the third reflects the preferences of real estate managers.

Table 3: Respondent rankings of financing methods

Type of financing	*Rank*
Operating cash flow	1
Secured property mortgage loans	2
Long-term leasing	3
Sale-leaseback arrangements	4
Joint ventures	5
Sale of common stock	6
Sale of mortgage bonds	7
Sale of preferred stock	8
Sale of collateralised mortgage obligations	8
Sale of commercial paper	9
Mortgage REITs	9
Sale of unsecured bonds	10
Hybrid REITs	10
Limited partnerships	11
Equity REITs	12
Sale of commercial mortgage backed debt	13
Participating mortgages	14
Other — cash and sales of industrial revenue bonds	

The top-ranked source is operating cash flow, with property mortgages as the second preferred method. Interestingly, leasing is third in priority, while having been the second most common method of financing specified. Sales of corporate securities lie in the middle of the listing, with the newer forms of CMOs and REITs towards the lower end. Overall, there may be a preference for:

(1) internal financing through cash flows generated by the company;
(2) traditional sources such as property mortgages, leasing, and joint ventures with others (possibly with contractors, as shown by Manning);[13]
(3) external financing using sales of corporate securities (common stock, bonds and preferred stock); and
(4) the non-traditional sources of REITs, CMOs and commercial property-backed bonds.

Decision factors in choosing financing methods

Following the work by Norton[14] in corporate finance, the managers were asked a series of questions concerning the financing sources. The managers were asked to state the extent to which they agreed or disagreed in the form of a five-point Likert scale, with 1 corresponding to strong agreement with the statement and 5 to strong disagreement. Selecting 3 would indicate that they were undecided (or did not have sufficient information to agree or disagree). Table 4 reports the responses and the mean responses to the questions.

The first two questions relate to the importance of cash flow as a source of financing. Corresponding to the previous discussion, operating cash flows seem to generate most of the financing to acquire real property. In question 2 in Table 4, the managers were asked if cash flow or

Table 4: Capital structure factors considered in selecting corporate real estate financing methods

		Strongly agree %	*Agree %*	*Undecided %*	*Disagree %*	*Strongly disagree %*	*Mean response*
1.	Operating cash flow provides most funding	52.9	15.7	11.8	17.6	2.0	2.00
2.	Use operating cash flow because executives do not like debt	20.4	24.5	26.5	16.3	12.2	2.76
3.	Company uses short-term debt	19.6	13.7	3.9	11.8	51.0	3.61
4.	Use cash because it is available	42.6	29.8	6.4	17.0	4.3	2.11
5.	Long-term debt is common source	22.4	14.3	10.2	8.2	44.9	3.39
6.	Main advantage of debt is tax savings	6.1	20.4	30.6	14.3	28.6	3.39
7.	We consider effects of bankruptcy	8.2	6.1	16.3	18.4	51.0	3.98
8.	Bond sales increase stock price	–	12.2	34.0	9.8	43.9	3.76
9.	Debt motivates managers	6.3	20.8	20.8	16.7	35.4	3.47
10.	Debt sends message to stockholders	16.3	–	25.6	18.6	39.5	3.73
11.	Consider interest rates	62.0	12.0	6.0	2.0	18.0	2.02
12.	Consider stock price impact of debt	25.0	22.7	15.9	6.8	29.5	2.93
13.	Debt lowers cost of capital	4.2	20.8	43.8	6.3	25.0	3.27
14.	Most important factor is cost of financing	36.0	32.0	16.0	8.0	8.0	2.20
15.	Company has a priority list of financing	22.0	20.0	12.0	20.0	26.0	3.08
16.	Common stock sends negative message	2.5	17.5	25.0	20.0	35.0	3.59
17.	We consider financial market conditions	25.0	39.6	20.8	4.2	10.4	2.35
18.	Keep balance of debt and equity	17.4	23.9	26.1	19.6	13.0	2.87
19.	Rely on investment bankers	10.2	14.3	24.5	28.6	22.4	3.39

equity financing was used because of upper management's dislike for debt. Almost one-half agreed with the statement, with a quarter undecided. A possible reason for the reliance on cash flows may lie in the risk-averse nature of some executives who may have a distaste for debt financing, which in turn may be related to the chance of bankruptcy or other factors.

In Redman and Tanner,[15] it was found that a small proportion of the companies surveyed relied on short-term debt (bank loans and commercial paper) to finance property purchases (at least on a temporary basis), contrary to what is advocated in the finance literature. The managers were asked whether their companies used short-term debt; most disagreed with the statement. The sale of commercial paper, as shown in Table 2, was chosen by only 3 per cent; however, short-term debt is still used by a small proportion of companies. It would seem that managers prefer to follow the premise in finance that financing maturities and investment lives should be matched. Responses to question 4 in Table 4 indicate a motivation for the use of cash flow is that it is readily available. As a source of financing cash has the advantage of being accessible and ready to be used, although it is not a free good.

Questions 5 to 13 in Table 4 relate to the use of debt in financing and factors that would probably be considered in using debt. The questions pertain to the hypotheses in finance that Norton examined in his survey of Fortune 500 company managers. Norton attempted to ascertain the extent to which managers followed the theoretical ideas postulated in finance to decide on the use of debt. Norton's questions related to the free cash flow hypothesis, to the concept of asymmetrical information and to the impact of debt and equity financing on stock prices. In his 1991 article, Norton[16] found that (1) taxes and market concerns were important in capital structure decisions, along with financial flexibility; (2) theoretical concerns such as agency costs, information asymmetries and information signalling were not important factors in making decisions (except for some firms), and (3) financing decisions were affected by management attitudes and expectations. Similar to Norton, this survey attempts to determine the extent to which finance theory and management attitudes apply in choosing (debt) financing in corporate real estate. The results are shown in questions 5 to 13 in Table 4.

The responses to question 5 correspond to that of the previous tables indicating that debt is a less common source of financing. Overall, the results indicate that reducing the tax burden is a consideration in choosing debt as a financing method. This is consistent with the findings of Norton and others, that tax benefits are a determinant of capital structure. Additionally, managers place importance on the cost of financing (question 14), interest rates (cost of debt, question 11) and financial market conditions (question 17). The impact of bankruptcy (that is, the importance of bankruptcy cost in choosing debt over equity) is not much of a consideration.

Most (53 per cent) of the respondents disagree that bond sales enhance their company's stock price or that the sale of stock hurts stock price, thereby affecting shareholder value, contrary to what has been found in empirical studies in finance. The managers seem to have a split opinion about the impact of debt on the cost of capital, with an almost even split between agreement that debt lowers financing costs and strong disagreement. Forty-three per cent had no opinion, which may reflect the impact of capital structure decisions and cost-of-capital computations being made in the finance departments, outside the purview of the corporate real estate manager. Being outside of the upper echelons of the company, corporate real estate executives may not have sufficient information to determine if the financing method affects their company's stock price, but from their experience they are aware of some specific considerations such as cost of financing and other factors.

Question 9 relates to the impact of the extensive use of debt in the 1980s by many US corporations, which created pressure to perform well financially so the company could repay debt used in leveraged buy-outs and acquisitions. Apparently, the corporate real estate executives do not feel the weight of debt financing. Companies in the latter 1990s have used less debt to finance acquisitions, most likely because of the rising stock market. Managers today would be under less pressure to perform because of lower debt loads. There may be other job stresses, but not, apparently, from the use of debt financing. If asked the question 10 or 15 years ago, these corporate real estate managers might have answered question 9 differently.

The responses to question 15 reflect a fairly evenly split opinion about whether firms set up a priority list. The priority listing in Table 3 may imply that managers have a preference for which methods are used to finance real estate acquisitions, while question 15 indicates that many firms do not have a (formal) ranking of financing methods. Managers who have the responsibility for making real estate decisions may have preferences for the sources of funds to finance purchases, but many of their firms do not.

Question 18 indicates an even split concerning companies having a balanced capital structure. Question 19 in Table 4 shows a possible lack of reliance on investment bankers to decide which type of financing should be used. It is possible that management may choose the financing source and rely on its investment bankers to take care of the actual details of securing the outside funding. The responses to question 19 may also reflect the common use of operating cash flow and leasing as sources that would make the expertise of investment bankers unnecessary.

Analysis of differences in responses to Likert statements

Statistical tests were performed on the responses to the questions in Table 4 to determine the statistical significance by industry classification (following the five categories in Table 1A) and by value of assets (following the two categories in Table 1B).

Analysis by industry type

Table 5 shows the results of the statistical tests of the Likert questions by industry category. Of the 19 questions asked, three were found to have statistical differences between responses by industry. Question 1, on the use of short-term debt as temporary finance, was significant at the 10 per cent level. Managers in manufacturing and other industry categories disagreed with the statement, while those in financial services mildly agreed with the statement, indicating a preference by firms in the finance industry for using short-term debt.

Question 4 — tax savings as the main benefit of using debt — was significant at the 5 per cent level, indicating significant differences between responses by types of industry. Those managers whose firms fell into the 'other' classification showed a relatively strong level of disagreement with statement 4, while respondents in manufacturing, retail, financial services and technology industries showed some level of agreement or exact neutrality with the statement.

Statement 9, that company management feels that debt financing sends a positive signal to stockholders, was significant at the 1 per cent level. The respondents in the various industries dif-

Table 5: Comparisons of average responses to Likert statements by industry type

Likert statements	*Mean responses†*						
	Fin††	*Man††*	*Ret††*	*Tech††*	*Oth††*	*F-stat*	*p-value*
1. Our company has often used short-term debt as temporary financing to construct or buy property.	2.62	4.14	3.38	3.5	4.14	2.093	0.097★★-★
2. Most of the funding for property acquisitions comes from operating cash flows.	1.83	2.57	2.0	2.0	1.91	0.428	0.787
3. Long-term debt is a common source of funding for our property acquisitions.	3.5	4.0	2.38	3.5	3.5	0.996	0.42
4. The main advantage of using debt is the tax savings from the interest deduction.	3.0	2.86	2.75	2.5	4.1	3.556	0.013★★
5. Our company has a priority list of financing sources that it uses to decide which source to use.	2.92	3.71	2.25	3.5	3.24	1.009	0.413
6. When we decide to borrow funds to acquire properties, we take into consideration the possibility of bankruptcy and job losses.	3.83	4.83	3.88	4.0	3.86	0.729	0.577
7. When our company has sold bonds, the price of our common stock has increased.	3.45	4.0	3.86	3.0	4.21	1.015	0.413
8. Using debt motivates our managers to invest company funds carefully.	3.0	4.14	3.38	2.5	3.84	1.481	0.225
9. Our management feels that using debt to fund property acquisitions sends a positive signal to our stockholders that our company is doing well.	3.8	4.17	2.71	2.5	4.28	4.138	0.007★
10. Using common stock to finance property acquisitions sends a negative signal to our investors.	3.3	3.67	3.14	3.5	4.2	1.349	0.271
11. When we borrow or sell debt to finance property purchases we take into consideration interest rates.	1.64	2.43	1.5	1.0	2.36	0.991	0.422
12. In deciding which type of financing to use, our management considers the impact of debt financing on our stock price.	2.89	3.0	2.0	1.5	3.42	1.532	0.212
13. The most important factor considered in choosing the financing source is the cost of the financing.	2.0	2.43	2.13	2.5	2.23	0.157	0.959

Table 5 (continued)

Likert statements	Mean responses†						
	Fin††	*Man††*	*Ret††*	*Tech††*	*Oth††*	*F-stat*	*p-value*
14. We use operating cash flow or equity financing because our senior executives do not like debt.	2.42	2.71	3.13	3.5	2.75	0.51	0.729
15. Using debt lowers my company's overall cost of financing.	3.0	2.86	2.86	3.0	3.71	1.386	0.255
16. An important consideration in choosing the type of financing we use to acquire property is the condition of the financial markets.	2.09	2.43	2.63	2.5	2.35	0.228	0.921
17. My company uses operating cash flows to fund purchases because it is readily available.	1.64	2.0	2.5	3.0	2.15	0.841	0.507
18. My company tries to maintain a balance between debt and equity when choosing which source to use to fund property purchases.	2.9	3.0	2.63	3.0	2.89	0.09	0.985
19. In deciding which financing method to use, my management relies on the advice of our investment bankers.	3.0	3.86	3.25	3.0	3.52	0.603	0.662

Key
*Significant at the 0.01 level **Significant at the 0.05 level ***Significant at the 0.10 level
†1 = Strongly agree; 2 = Agree; 3 = Undecided; 4 = Disagree; 5 = Strongly disagree
††Fin = financial services, banking accounting, consulting or land development
††Man = manufacturing or petroleum refining
††Ret = retail, hotel-motel or hospitality
††Tech = computer software, Internet development or telecommunications
††Oth = other

fered substantially in their responses to the statement. Retail firms agreed with the statement, while managers in financial services, manufacturing and 'other' categories showed a relatively high level of disagreement. Technology firms slightly agreed with the statement.

All industry types had about the same level of agreement or neutrality with the statement that their companies had a priority list of financing sources to make real estate acquisitions. However, all five categories of firms showed the same level of disagreement with the statement that bankruptcy and job losses are considered in debt-financing decisions, which could be viewed as a somewhat optimistic outlook with respect to borrowing for property purchase. This positive outlook was also evidenced by the fact that all industries, regardless of category, generally agreed that when they sold bonds, the price of their common stock increased. They also tended to disagree that debt financing motivated their managers to be more careful when investing company funds.

Analysis by company size

Table 6 contains the mean responses by asset value of firm, *t*-statistic and probability value. Seven statements were found to have statistically significant differences in responses. Statement 1 was significant at the 1 per cent level, with both groups of respondents agreeing that they had often used short-term debt as temporary financing; but the managers of large firms showed a substantially stronger agreement with this statement. Both categories of respondents showed about the same level of agreement with the statement that most of their funding to buy real estate came from operating cash flows, although there was no statistically significant difference in the responses.

Statement 3 — long-term debt is a common source of funding — was statistically significant at the 5 per cent level. Respondents in small companies agreed that they used long-term debt frequently, while those in large companies disagreed with this statement. However, managers from both categories showed about the same level of disagreement with the statement that the main advantage of using debt financing is tax savings, although the mean responses were not statistically significant.

Statement 6, that bankruptcy costs and job losses are considered in decisions to use debt, was significant at the 5 per cent level, with managers from large firms more strongly disagreeing with the statement than those from small firms. The responses to statements 8 and 9 (that debt is a motivator to managers and that the use of debt sends a positive signal to stockholders, respectively) were significant at the 10 per cent level. For each statement there was stronger disagreement by the respondents from large firms.

Statement 15 — debt lowers the firm's cost of financing — was significant at the 5 per cent level. Respondents in small firms tended to agree with the statement, while those in large firms tended to agree more strongly.

Statement 17 — management uses operating cash flow to fund real estate purchases because of its availability — was significant at the 10 per cent level. There was a difference in agreement with this statement, with managers in large companies agreeing with this statement more strongly than small company managers.

Although the responses to the other questions were not found to be statistically significant, further inferences can be made from these responses. While the managers from small companies showed slight agreement with the statement that their firms have a priority list of financing sources, those from larger firms showed slight disagreement.

Respondents from large and small firms agreed that interest rates were considered when debt financing was used; managers from small firms showed a substantially stronger level of agreement than those from large firms. Managers from small firms slightly agreed with the statement that their executives considered the impact of debt financing on stock prices, and those from larger firms slightly disagreed with the statement.

Respondents in both size groups agreed that the most important factor considered when choosing a financing source is the cost involved. With respect to whether or not their senior executives do not like debt and prefer the use of operating cash flows or equity, small-company managers were neutral and large-company respondents showed a slight level of agreement. Additionally, managers of both types of firms felt that the condition of the financial markets should be an important consideration when choosing the type of financing to acquire real property. They also agreed that their firms try to maintain a balance between debt and equity

Table 6: Comparisons of average responses to Likert statements by size ($$) of total assets

Likert statements	*Mean responses†*			
	Assets of $1.5bn or less	*Assets greater than $1.5bn*	*t-stat*	p-*value*
1. Our company has often used short-term debt as temporary financing to construct or buy property.	2.86	2.25	−3.188	0.003*
2. Most of the funding for property acquisitions comes from operating cash flows.	2.29	1.761	1.486	0.144
3. Long-term debt is a common source of funding for our property acquisitions.	2.75	3.89	−2.433	0.019**
4. The main advantage of using debt is the tax savings from the interest deduction.	3.29	3.52	−0.627	0.534
5. Our company has a priority list of financing sources that it uses to decide which source to use.	2.71	3.39	−1.544	0.129
6. When we decide to borrow funds to acquire properties, we take into consideration the possibility of bankruptcy and job losses.	3.52	4.37	−2.333	0.024**
7. When our company has sold bonds, the price of our common stock has increased.	3.75	3.96	−0.563	0.577
8. Using debt motivates our managers to invest company funds carefully	3.2	3.85	−1.693	0.097***
9. Our management feels that using debt to fund property acquisitions sends a positive signal to our stockholders that our company is doing well.	3.44	4.12	−1.977	0.055***
10. Using common stock to finance property acquisitions sends a negative signal to our investors.	3.4	3.83	−1.08	0.287
11. When we borrow or sell debt to finance property purchases we take into consideration interest rates.	1.52	2.43	−2.067	0.044**
12. In deciding which type of financing to use, our management considers the impact of debt financing on our stock price.	2.89	3.04	−0.306	0.761
13. The most important factor considered in choosing the financing source is the cost of the financing.	2.19	2.21	−0.065	0.949

Table 6 (continued)

Likert statements	Mean responses†			
	Assets of $1.5bn or less	*Assets greater than $1.5bn*	*t-stat*	*p-value*
14. We use operating cash flow or equity financing because our senior executives do not like debt.	3.0	2.52	1.281	0.207
15. Using debt lowers my company's overall cost of financing.	2.85	3.59	−2.197	0.033**
16. An important consideration in choosing the type of financing we use to acquire property is the condition of the financial markets.	2.14	2.54	−1.105	0.275
17. My company uses operating cash flows to fund purchases because it is readily available.	2.43	1.78	1.877	0.067***
18. My company tries to maintain a balance between debt and equity when choosing which source to use to fund property purchases.	2.95	2.8	0.379	0.707
19. In deciding which financing method to use, my management relies on the advice of our investment bankers.	3.19	3.56	−0.977	0.334

Key
*Significant at the 0.01 level **Significant at the 0.05 level ***Significant at the 0.10 level
1 = Strongly agree; 2 = Agree; 3 = Undecided; 4 = Disagree; 5 = Strongly disagree

financing. Lastly, managers said that they basically do not rely on the advice of investment bankers when deciding which financing method, debt or equity, to use to fund the acquisition of real estate for their companies.

SUMMARY AND CONCLUSIONS

This paper examined the financing sources, the ranking of financing sources and factors that may influence the selection of funding methods by a sample of US corporations. Corporate real estate members of NACORE were surveyed with the responses reported.

Comparing the results of this survey to that of Redman and Tanner,[17] companies continue to rely on internal financing (in the form of operating cash flows) and 'traditional' types of external financing such as long-term leasing, joint ventures, property mortgages and sale and leaseback arrangements. The newer sources, such as real estate investment trusts (REITs), collateralised mortgage obligations (CMOs) and mortgage-backed securities (MBSs), have been used by a small proportion of the respondents.

The managers were asked to rank the financing methods and the results were consistent with the methods used.

Operating cash flow ranked as the top method, property mortgages were second, leasing was third and sale and leasebacks were fourth. Traditional external financing methods of security sales had a lower priority to cash flow, mortgages and the like. Use of REITs, CMOs and MBSs was at the bottom of the list.

The managers were asked 19 questions regarding the factors that their companies consider in selecting financing methods for company real estate acquisitions, with the questions reflecting the work of Norton[18] and others in finance. Analysis of the responses by industry revealed that managers in manufacturing and technology feel that the advantage of using debt financing is the tax advantage of deducting interest as a business expense. Real estate managers in the retail industry feel that using debt sends a positive signal to stockholders, similar to the overall findings of Norton. Analysis by company size revealed that managers agree that their firms have used short-term debt as temporary funding to acquire real estate, with managers of large companies more strongly agreeing. There was a general agreement that operating cash flow is commonly used because it is available. Similar to the findings of Norton, the managers in this survey disagreed that debt is a motivator to better real estate property decisions and that bankruptcy cost is a consideration in using debt to finance the purchase of real estate.

Overall, the managers look to financing costs, the interest costs of debt, financial market conditions and tax savings as factors to consider in corporate real estate financing. Theoretical concerns of academic finance related to information asymmetries, agency costs and bankruptcy are probably of less concern, although a few firms may look at these factors as they decide which financing methods to use. These findings corroborate those found in the survey studies in corporate finance, which are that managers look to practical considerations rather than theoretical concerns in making asset-financing decisions. A few companies may have a priority listing of which financing methods they use, while relying on advice from investment bankers may be of less importance to companies, possibly because of the emphasis on internal financing sources to purchase real property.

APPENDIX

Corporate real estate financing survey

(1) Which of the following industries does your company fit into?

- Manufacturing
- Retail
- Financial Services — Securities Brokerage, Insurance, etc.
- Commercial Banking
- Public Accounting
- Land Development
- Management and Financial Consulting
- Petroleum Refining and Distribution
- Hotel/Motel Hospitality
- Computer Software/Internet Development
- Telecommunications
- Other

(2) What is the approximate size of your company, in market value of assets?
- Under $250m
- $250m–$1.5bn
- $1.5–$10bn
- Over $10bn

(3) When your company acquires real estate that is used in its operations (such as office buildings, warehouses, plants, research facilities) what sources does your firm use to generate the funds needed for acquisition or construction? (Check all that apply.)
- Mortgage loans secured by the acquired property
- Cash flow from operations
- Mortgage bonds secured by the acquired property
- Sale of common stock
- Sale of unsecured bonds
- Sale of preferred stock
- Sale of commercial paper
- Long-term leasing
- Sale-leaseback arrangements
- Joint ventures
- Equity real estate investment trusts
- Mortgage real estate investment trusts
- Hybrid real estate investment trusts
- Sale of collateralised mortgage obligations
- Sale of commercial mortgage-backed securities
- Limited partnerships
- Participating mortgages
- Other, please specify.

(4) Please rank the financing methods you use to generate the funds to acquire real estate for your company as to which are important. Use 1 for the most important, 2 for the method of second importance, etc.

	Rank
Mortgage loans secured by the acquired property	________
Cash flow from operations	________
Mortgage bonds secured by the acquired property	________
Sale of common stock	________
Sale of unsecured bonds	________
Sale of preferred stock	________
Sale of commercial paper	________
Long-term leasing	________
Sale-leaseback arrangements	________
Joint ventures	________
Equity real estate investment trusts	________
Mortgage real estate investment trusts	________
Hybrid real estate investment trusts	________
Sale of collateralised mortgage obligations	________
Sale of commercial mortgage-backed securities	________

Limited partnerships ________
Participating mortgages ________
Other

Corporations, in order to more provide financing and to structure their corporate real estate operations more cost effectively, have moved to securitise their real estate by creating real estate investment trusts (REITs) and transferring these assets to the REITs. Changes in the REIT laws since 1992 have facilitated this trend. The following questions relate to your firm's participation in this trend.

(5) Has your company formed a real estate investment trust to transfer the ownership of the firm's real estate within the past 7 years?
________ Yes ________ No, skip to question 8

(6) Has your company, anytime since 1992, taken advantage of the Umbrella Partnership (UPREIT) law to create a REIT to own the firm's real estate?
________ Yes ________ No

(7) If your firm has created a REIT to finance its acquisition or to hold ownership of the company's real estate, has your company sold the REIT shares:
In the public financial market?
As a private placement to an institutional investor (such as a pension fund)?
Both?

(8) The following questions were designed to find out what factors your company considers when deciding which type of financing method or methods are to be used to generate the funds needed to acquire real estate for company operations. For each question circle the number of the response that most closely describes your opinion. The responses range from strongly agree (1), agree (2), undecided (3), disagree (4) and strongly disagree (5).

(a)	Our company has often used short-term debt as temporary financing to construct or buy property.	1	2	3	4	5
(b)	Most of the funding for property acquisitions comes from operating cash flows.	1	2	3	4	5
(c)	Long-term debt is a common source of funding for our property acquisitions.	1	2	3	4	5
(d)	The main advantage of using debt is the tax savings from the interest deduction.	1	2	3	4	5
(e)	Our company has a priority list of financing sources that it uses to decide which source to use.	1	2	3	4	5
(f)	When we decide to borrow funds to acquire properties, we take into consideration the possibility of bankruptcy and job losses.	1	2	3	4	5

(g)	When our company has sold bonds, the price of our common stock has increased.	1	2	3	4	5
(h)	Using debt motivates our managers to invest company funds carefully.	1	2	3	4	5
(i)	Our management feels that using debt to fund property acquisitions sends a positive signal to our stockholders that our company is doing well.	1	2	3	4	5
(j)	Using common stock to finance property acquisitions sends a negative signal to our investors.	1	2	3	4	5
(k)	When we borrow or sell debt to finance property purchases we take into consideration interest rates.	1	2	3	4	5
(l)	In deciding which type of financing to use, our management considers the impact of debt financing on our stock price.	1	2	3	4	5
(m)	The most important factor considered in choosing the financing source is the cost of the financing.	1	2	3	4	5
(n)	We use operating cash flow or equity financing because our senior executives do not like debt.	1	2	3	4	5
(o)	Using debt lowers my company's overall cost of financing.	1	2	3	4	5
(p)	An important consideration in choosing the type of financing we use to acquire property are the conditions in the financial markets.	1	2	3	4	5
(q)	My company uses operating cash flows to fund purchases because it is readily available.	1	2	3	4	5
(r)	My company tries to maintain a balance between debt and equity when choosing which source to use to fund property purchases.	1	2	3	4	5
(s)	In deciding which financing method to use, my management relies on the advice of our investment bankers.	1	2	3	4	5

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