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Jian Ye Li:

Assessing and Managing Risks in International Real Estate Development

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This Cornell University Real Estate Case was prepared to stimulate analysis and discussion in undergraduate and graduate real estate courses. While the case is drawn from a range of actual experiences, it is not intended to illustrate correct or incorrect applications.

Jian Ye Li:

Assessing and Managing

Risks in International Real Estate Development

ABSTRACT

This case focuses on a USD $108.6 million mixed-use development project in Shanghai, China from the perspective of a U.S.-based private equity firm. The firm has been presented with an opportunity to co-invest in the project alongside a state-owned Chinese development entity and an international development firm active in the Asia-Pacific region. The case is centered around risk identification and analysis and provides students with an opportunity to explore all of the major risks that are encountered by developers and investors in both domestic and international real estate development projects. The protagonist of the case is Guy Fulton, a young real estate professional who has been tasked with weighing the various risks against the return projections for the project and who must devise a strategy with regard to proposed joint venture arrangements with the other project participants. In doing so, Guy must navigate a complex assortment of development issues and determine how his firm can proceed with the project while still satisfying the investment objectives and risk tolerances of the fund and its limited partners.

This case study incorporates the following real-estate themes and issues:

Risk Analysis

International Real Estate Development

Historic Preservation

Investment Analysis

Mixed-Use Projects

Jian Ye Li: Assessing and Managing Risks in International Real Estate Development

By: David Schaefer and Syed A. Hyat

The Jian Ye Li project represented an attractive opportunity for us. The location, the historical element, the uniqueness and the returns were all compelling. However, significant risks were present as well. Partnering with a state-owned entity, gaining entitlements, re-locating existing residents, and meeting the preservation standards of the municipality, all gave us pause. Above all, we would have to ask ourselves whether we would leave the built environment better than we found it, while meeting the return requirements of our investors.

David Schaefer, Former Head of Citi Property Investors, Asia Pacific

Guy Fulton leaned back in his chair and let out a measured sigh. Since completing his MBA at New York University in 1999, Guy had been steadily perfecting his Mandarin while building his career in a number of Asian real estate markets. He had recently risen to Vice-President and Chief Representative of Citi Property Investors (CPI) in China. Now, sitting in his Shanghai office, Guy pondered an intriguing project. Associates at Portman Holdings, LLC (Portman), a highly regarded international developer based in Atlanta, Georgia had approached him to form a joint venture with Hengfu Property Company (Hengfu), a local state-owned entity, to redevelop the Jian Ye Li site in the French Concession neighborhood of Shanghai. Portman envisioned a modern, mixed-use project with luxury townhouses, hotel-style serviced apartments, and high-end retail, all within historically preserved 'Shikumen'-style facades. Portman had a track record of successfully executing premier international projects but little was known about Hengfu, other than the fact that it held title to the land and would be responsible for relocating the existing residents.

It was December 23rd, 2005 and the CPI Investment Committee (Committee), headed by David Schaefer, had provided the go-ahead for Guy and his team to proceed with due diligence. They had less than three weeks to perform their financial analysis, prepare an investment memorandum, and make a formal recommendation to the Committee. If the Committee decided to move forward as an equity partner on the project, Portman would submit the final bid on behalf of the consortium on January 17th, 2006. Even though the Christmas and New Year's holidays were approaching, Guy knew that there wasn't a minute to waste. CPI's analysts had already modeled the projected returns, but even prior to seeing the numbers Guy had a gut feeling that they would be solid, and perhaps even spectacular. The real question was whether the returns would justify the significant risks involved.

Risky Business

CPI was approached by Portman to participate in a project that would have a total estimated budget of USD $108.6 million. Portman was proposing that CPI make an equity investment that would be split between a short-term joint venture (STJV) and a long-term

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joint venture (LTJV). The STJV would develop and sell 50 luxury townhouses and the LTJV would develop and lease 4,666 square meters of retail space and 40 serviced apartments (see **Exhibit 1 – Project Concept**). This bifurcated joint venture structure would achieve the dual aim of allowing CPI to exit the venture early, while ensuring that there was a long-term hold aspect to the project that would allow Hengfu to retain their investment and operational control of the retail and serviced apartment position. CPI would contribute USD $33.7 million in equity and an additional USD $25.3 million would be provided by Portman and Hengfu. A construction loan of USD $49.6 million (approximately 45% LTV) would complete the financing of the project. The interest rate for the construction loan had not been finalized, but would be in the range of 6% to 7%. CPI would hold a 56% beneficial interest in each of the joint venture vehicles, while Portman would hold 14% and Hengfu would hold 30%. However, CPI had some optionality in that it could decide to participate in only one of the two joint ventures if it wished to do so. Given the projected returns, both joint ventures were considered to be attractive but the LTJV carried with it significant risks that CPI would have to carefully consider.

CPI's exit from the STJV would occur when the company was dissolved upon the sale of all of the 50 townhouses. It was initially estimated that both developments would take 19 months to complete, and thus completion was expected to occur in March 2008 assuming that work commenced according to schedule by September 2006, following the relocation of the community's existing residents by August 2006. Marketing and pre-sales of the units would likely commence in September 2007 and there would be an estimated three-to-four month sales period. An additional two months for the dissolution of the company was estimated to allow for the profits to be repatriated.

CPI's exit from the LTJV could only occur once the entire development was completed. CPI did, however, negotiate a right that would allow it to require that Hengfu buy out CPI's 56% share of the LTJV in two installments. The first would become due at the dissolution of the STJV and the second would become due by December 31st, 2008. If the exit went as planned, Hengfu's share of the LTJV would increase to 86% (Portman would retain its 14% stake) and CPI would exit with a profit of 40% over the construction cost of the LTJV (see **Exhibit 2 – Investment Timeline**). In other words, CPI's exposure to the STJV was full development and market risk, whereas the LTJV had a guaranteed buyout clause that assured it that it would realize cost plus 40% for all of CPI's shares. CPI's legal counsel had proposed a host of additional legal protections to protect CPI's investment and to ensure that the leasing and marketing risks associated with the retail and serviced apartments transferred to Hengfu, but most of these would have to be deferred for negotiation at a later date.

The construction timeline and exit was crucial for CPI. Given their investment criteria, delays and unforeseen complications would negatively impact returns. The exit structure of the LTJV in particular made Guy uneasy given that CPI's exit from the LTJV was predicated on it being able to exercise a contractual agreement with a local Chinese developer (Hengfu). There was ample precedent that these types of agreements were seldom honored as negotiated. Equally concerning for Guy was the fact that because Hengfu was a state-owned developer, the sale of the LTJV would subject to approvals outside the control of the joint venture partners.

As CPI began to conduct due diligence on the Jian Ye Li project, these and other risks became increasingly concerning for Guy. In the early years of his career he would have been much less anxious and more risk tolerant, especially given his solid track record of overcoming obstacles with other complex projects. However, age and wisdom had instilled an intimate awareness of the variety of expected and unexpected issues that often plague otherwise well structured projects. He picked up the telephone and called Qing Ma, a young Analyst who he had assigned to the due diligence team. When she picked up, Guy

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issued his instructions, “Qing, I’d like you to do me a favor. I’d like you to prepare a memo that outlines all of the likely and potential risks that we might face with the Jian Ye Li project. I’d also like you to explain how each these risk elements can be mitigated. This will be a great opportunity for you to gain an appreciation for all of the things that can go wrong with a project like this and how developers manage to keep their heads above water. Please send me the memo by the end of next week.”

Citi Property Investors (CPI)

CPI was the real estate private equity unit of Citigroup Inc., a multinational financial services firm headquartered in New York City. CPI raised equity capital from institutional clients, high-net-worth individuals and from Citigroup itself to make equity and debt investments in real estate. By 2006, CPI had approximately USD $3 billion in assets under management and investment professionals stationed in Asia, Europe and North America. Citigroup had been active in China for over 100 years, so it was natural for CPI to explore real estate investments there. Furthermore, David Schaefer and his team of professionals, including Guy also had extensive experience investing in China, particularly in residential projects in the Shanghai region.

The Jian Ye Li project was being considered as an investment for one of CPI’s flagship funds: CPI Capital Partners Asia Pacific, L.P. (CPI Asia Fund). The CPI Asia Fund was established to provide investors with exposure to Asian real estate markets. As an opportunistic fund, CPI Asia Fund would invest in emerging markets and take exposure to development projects. In addition to investing in China, the Fund would pursue investment opportunities in India as well as more established real estate markets in Asia such as Hong Kong, Tokyo and Seoul. In undertaking a development project, as a matter of policy the Fund would always form a joint venture with an experienced local developer. In order to meet the return expectations of CPI Asia Fund’s limited partners, CPI would look for a project-level before-tax IRR in excess of 20%.

Portman Holdings, LLC (Portman)

Founded in 1953 by John Portman, Portman was a vertically integrated, full-service real estate development company with an international presence and a rich history of developing premier projects. The company’s full service approach to real estate development integrated diverse disciplines such as project conceptualization, debt and equity financing, project management, construction management, leasing, property management and asset management into a unified development regimen. Portman’s experience extended over five decades and included the development of hotels, office buildings, retail spaces, and residences.

Portman opened its first Asian office in Hong Kong in 1978 to cultivate opportunities in China and Southeast Asia. This expansion coincided with a period of economic reform in China under the leadership of Deng Xiao Ping. The firm’s initial project was the design of a mixed-use complex in Shanghai. The client that had commissioned the work ran into difficulty securing financing and asked Portman to become a partner on the project. Portman helped it to secure the necessary financing and provided development expertise. Portman later re-located its Asian operations to Shanghai. Portman’s Shanghai subsidiary, Shanghai Portman Consulting Company, Ltd. also had an extensive track record in the region.

As the Project Developer for the Jian Ye Li project, Portman would supervise and oversee the design process, financial and budget management, construction management, marketing, sales and leasing over the course of the development. Portman would also appoint the construction contractor for the project. Portman would adopt an 'architect as developer' approach as its affiliate, John Portman & Associates would serve as the architectural firm. These responsibilities would potentially give Portman considerable control and discretion, something that concerned Guy (see **Exhibit 3 – Portman Responsibilities**). As compensation for its services, Portman would receive an acquisition fee (1% of total project costs), development fee (5% of hard costs, plus the cost of a project manager), architectural fee (4% of hard costs), and a sales & marketing fee (1.2% of the value of disposed property).

Portman had a reputation for designing and developing premier international projects. It developed both Shanghai Centre and Tomorrow Square, two successful mixed-use projects just north of the French Concession. Shanghai Centre was an immediate success upon its completion in 1990. It was the largest foreign project completed to date at the time in China and featured a landmark building. With a hotel, apartments, offices, retail space, exhibition space, and a Broadway-type theater, it catered to the sizable and growing international business community. Portman was considered a 'star-chitect', and its commitment to quality and creating cachet projects was expected to bring with it considerable pricing premiums. Guy wondered: in Jian Ye Li, had Portman discovered another 'winner'?

Hengfu Property Company (Hengfu)

Hengfu was owned by the XuFang Group, a large wholly state-owned enterprise with registered capital of USD $286 million, which was in turn controlled by the state-owned Assets Administration Commission of the Xuhui District in Shanghai. The Xuhui District was one of nine central districts that made up the Municipality of Shanghai. Its core business was construction, renovation and property management. It was formed in 1996 and at the time of the Jian Ye Li project managed 8 million square meters of property. XuFang was the current holder of the title of the land for Jian Ye Li. Title was to be transferred to the STJV and LTJV when the first payment of registered capital was made.

Of some concern to CPI was the fact that Hengfu had experienced significant cost overruns at its last construction site, and it was rumored to be quite interested in tightly controlling costs at Jian Ye Li. Guy wondered whether Portman, a prestigious international developer with architectural responsibility for the project and Hengfu, a value-oriented local contractor, would have different visions and priorities for Jian Ye Li. If conflict arose between the parties, how much influence CPI would have in resolving it? Also of concern was the somewhat mysterious nature of Hengfu, a newly formed company specifically tasked with the renovation of Jian Ye Li. CPI admittedly knew relatively little about the company, despite best efforts in their due diligence. Although CPI were assured of their legitimacy and competence, it felt strange for CPI to be so intimately involved with a potential joint venture partner who it ultimately wasn't familiar with.

Shanghai & The French Concession

Shanghai was a bustling 21st century port city located at the mouth of the Yangtze River. It was first incorporated in the 8th century and remained a fishing and textiles town for many years. It grew significantly in importance during the 19th century. At the conclusion of the First Opium War, the Treaty of Nanking opened Shanghai to foreign trade and the city flourished as a trans-oceanic commercial hub. By the 1930s it was the undisputed financial center of the Asia-Pacific region. Shanghai's commercial power and international culture waned with the Communist Party's takeover of the mainland in 1949, but returned anew with the economic reforms instituted by Deng Xiao Ping beginning in the late 1970s.

The French Concession neighborhood was a foreign settlement in the city established in 1849 and expanded twice before its relinquishment by the French in 1946. The area eventually came to encompass a large swath of the center, south and west of urban Shanghai in what became the Xuhui and Luwan districts. A small strip extended eastward along the Rue de Consulat (eventually renamed East Jinling Road) to the Huangpu River (see **Exhibit 4 – French Concession**). To the north of the French Concession was the British Concession, which would eventually merge with the U.S. Concession to become the International Concession.

Although the French Concession originally began as a settlement for the French, it eventually attracted residents of various nationalities. During the 1920s the area was developed into Shanghai's premier residential neighborhood. With its expansion in the 1920s, many British and American merchants chose to relocate there. Additionally, many Russians settled in the area in the wake of the Russian Revolution. Avenue Joffre (eventually renamed Huaihai Road) was one of the most famous retail and commercial districts in Shanghai. The road was originally built as Rue Sikiang in 1905 but was renamed in honor of the French General Joseph Joffre in 1922. During the 1920s Avenue Joffre became an enclave for the Russian community in the French Concession as well as its commercial center. Throughout the 20th century it would retain that status, despite frequent redevelopments. The area retained a distinctive character and became a popular tourist destination.

Shikumen Architecture

The Jian Ye Li development was originally built in the early 1920s as a residence for middle and high-income Chinese families. It was designed by a French architect and was one of the city's finest examples of Shikumen-style housing. Shikumen design was unique to Shanghai and represented a blend of traditional Chinese residential elements and functional western concepts. Shikumen translated literally as 'Stone Warehouse Gate', referring to the stone archway gates at the entrance of each alleyway (see **Exhibit 5 – Shikumen Architecture**). Shikumen homes were two or three-story structures that resembled western-style townhouses. Each residence abutted one another and were arranged with straight side alleys. At the height of their popularity, Shikumen buildings comprised almost 60% of the housing stock of Shanghai. Many of these structures were hastily built and kept in ill repair, while others featured sturdy construction and modern conveniences.

During and after World War II, population increases led to extensive subdivision of Shikumen homes. The spacious living rooms were often split into three to four rooms, each rented to a separate family. Such cramped conditions gave Shikumen homes a reputation for gritty and dirty urban living. However, developers eventually began to successfully re-develop Shikumen sites. In the early 2000s developer Shui On Land and architect Ben Wood set the bar for redevelopment of historic districts with the XinTianDi project in Shanghai. A cluster of Shikumen homes was renovated into an affluent, pedestrian-oriented shopping, dining, and entertainment district. The narrow lanes and stone gates were maintained, while the interiors of the homes were converted to trendy cafes, bookstores, restaurants and bars. XinTianDi was a tremendous success and became one of Shanghai's key attractions.

As disclosed by Portman at the outset of its discussions with CPI, the Jian Ye Li site had been designated as a historical preservation area, thus any redevelopment would have to maintain the original Shikumen design, facades, alley-scale and proportion. There were numerous preservation projects rumored to be planned for Shanghai under new government programs at the time, however Jian Ye Li would be among the first of this Shikumen-style of project to come to market. Guy didn't see this as disconcerting, believing that that the preservation of the Shikumen elements would make Jian Ye Li unique and appealing to prospective residents. However, it was obvious that these elements would also act as constraints to creating an efficient and modern layout and range of amenities. Specifically, the alleyways were exceedingly narrow and could not be widened. Moreover, there would be no room for street parking and since the townhouses were adjacent to one another, above-ground garages were also out of the question. Portman's proposed design was innovative to say the least, but could it be accomplished in practice?

The Site

The Jian Ye Li site had many favorable attributes. For example, transportation linkages were excellent - the Heng Shan Road Station of Metro Line 1 was approximately 10 minutes away on foot, many bus routes ran through the area and taxis were readily available. The site was centrally located downtown, but off the main thoroughfare of Hengshan Road (see **Exhibit 6 – Jian Ye Li Site**). This resulted in a relatively quiet intersection, allowing for a less crowded and more tranquil feel for residents. The site was also adjacent to the Xu Jia Hui business district and was within a 20-minute walking radius to many public facilities. These included the Shanghai Library, the Shanghai Music Academy, the Medical School of Fudan University, the Zhong'shan Hospital, the International Health Care Center for Women and Children, the Global East Asia Fortune Hotel and Xu Jia Hui Park. The neighboring retail area could be divided into two categories, one comprised mainly of small, scattered street stores that catered mostly to daily consumption by nearby residents, and the other consisting of bars and restaurants that catered to a younger, more upscale crowd.

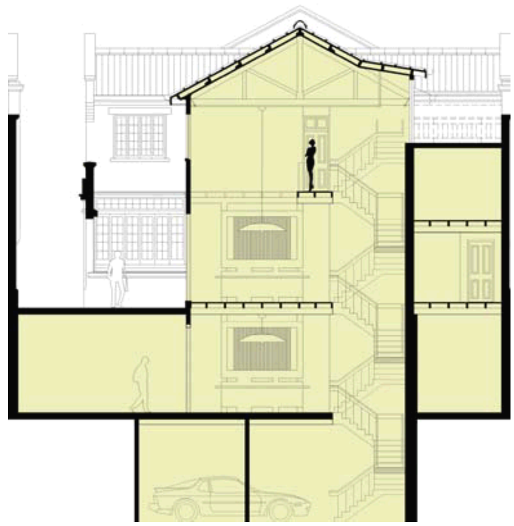
Despite its prestigious location, being within one of the wealthiest residential areas of the city, the site itself was in ill repair and suffered from aesthetics that were far from consistent with the luxury-oriented concept that the redevelopment would seek to accomplish. The majority of the homes had been subdivided numerous times and the subdivisions were of ad-hoc construction and were often illegal. Conditions were cramped and squalid, with three to four families living in each house. The residents were generally working-class and many had only recently moved to Shanghai from the rural provinces in search of employment. Many of these residents would have to be relocated in order to facilitate the project, which caused Guy considerable concern. Portman advised CPI that the fact that the site had been designated by the local government for redevelopment, and that a state-owned entity was acting as partner should give it comfort, but Guy was still troubled by the potential for public backlash due to the relocations and how this might affect the marketability of the residential units and leasing of the retail space.

The Product

The proposed redevelopment would include residential townhouses fronted by one to two rows of retail shops along Jian Guo Road in the eastern and central sections of the site, and hotel-style serviced apartments for the western section (see **Exhibit 7 – Redevelopment Map**). While the exterior façade of the buildings needed to be preserved close to the original design, the interiors could be outfitted with modern amenities. The project would also have to incorporate a great deal of below-grade space as living area, which was atypical for the market. Although this type of basement area would normally be considered unmarketable as high-end living space, Portman felt that unlike many other developments the Jian Ye Li space would benefit from access to natural light that would overcome this issue. The below-grade component of the design was crucial to the marketability of the project but the current title was insufficient because the existing structures did not have basements. The title for the units in the STJV would have to be amended to allow for below-grade development. It was also crucial to secure the right to develop below-grade space because the target market for the residential units were expected to have one or two cars and on-street parking was impossible due to the narrow alleyways.

Title would also have to be converted from 'allocated' to 'granted' status, as well as re-zoned for a mixed-use project, as the current zoning allowed for only residential uses. Hengfu had disclosed this issue in its bid solicitation materials but had promised would-be partners that it could resolve it. Hengfu was a state-owned entity, so it appeared sensible that it would be able to secure this sort of entitlement with ease. However, Guy knew enough about the Xuhui District building department to be skeptical - individual officials and entrenched interests could often obstruct projects that were otherwise well supported.

(i) Townhomes



Typical Unit Layout

The townhouse units were designed with two above-grade floors and two below-grade floors, one of which was to be a garage that could accommodate two automobiles. There would be three bedrooms in each unit. Two bedrooms would be on the second level and one bedroom would be on basement level one. The first level would include a living room and kitchen, while basement level one would include a games/family room. Parking spaces would be located on basement level two and would be directly accessible from each unit. The average size of the units would be 391 square meters, comprised of 184.96 square meters above-grade and 206.04 square meters below-grade.

It was expected that demand for the townhouses would be primarily from high-end buyers wanting to acquire a nostalgic, well-located, historically preserved home within the French Concession. The homes would serve as an alternative to buyers of high-rise apartments, suburban villas and old houses. Demand was expected to come from a niche market of senor Asian professionals and foreign expatriates who had access to limited supply due to market constraints and barriers to entry.

(ii) Retail

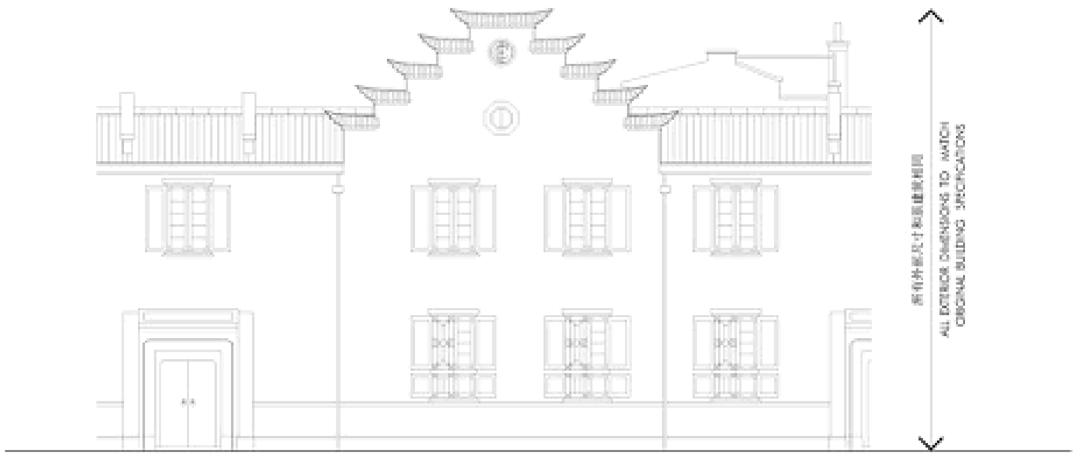
The retail component of the LTJV would encompass 4,666 square meters of retail in two above-grade levels and one below-grade level in structures fronting West Jian Guo Road. As per standard conventions in Shanghai, these spaces would be handed over in a bare shell condition, allowing tenants to undertake their own fitout. In terms of a provisional retail mix, the French Concession location lent itself well to food and beverage, high fashion, beauticians, and design conscious boutique uses. Other retail sub-markets in the Xuhui District had used this type of retail mix with great success, in particular the XinTianDi project, which had become a popular tourist destination.

Guy wanted to be certain that there would be sufficient demand drivers for the retail component of the project. As the site was somewhat isolated at the time within a swath of residential buildings, access, visibility, demographics and of course parking would all become important variables. Portman had assured CPI that it was very confident in the leasing dynamics that the submarket offered, but Guy would continue to play devil's advocate until he had more comfort that the projected lease-up could be accomplished and that the retail tenants ultimately secured would be of good credit and would add to a desirable 'sense of place' for the development.

(iii) Serviced Apartments

Unlike the townhouses and the retail uses, the serviced apartments would not include any below-grade, development. The work would be more along the lines of a renovation than a redevelopment. However, as with the residential and retail sections the unique design aspects of the facades would be preserved. The 40 units would range in size from 97 to 127 square meters. Portman designed most of the units on the first level as two-bay units comprised of one bedroom with an en suite bathroom, a small kitchen and a sitting and dining area. Compared to other units in the market this was spacious-to-average for a one-bedroom unit. However, the current design did not provide the flexibility of larger units due to the historical preservation requirements. The first level units would be accessed at ground level by walking from the check-in lobby along the covered corridor.

The units on the second level would also be two-bay units and would be similarly sized to those on the ground floor. However, the configuration of these units was different. These units would include a third level, which would provide a small outside sundeck. Similar to a large balcony in a regular apartment, this sundeck could be used during six to nine months of the year. The second level units could also be accessed by the covered corridor, which currently existed at that level.



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Too Many Cooks in The Kitchen?

During the construction phase of any development, cost overruns and delays could substantially affect initially forecasted returns, something that Guy was acutely aware of. Portman had prepared a construction budget that accompanied its design proposal. Given Portman's extensive experience, Guy was certain that the budget reflected Portman's business practice of employing high-quality construction and modern interior finishes. However, considering Portman's 'quality first' approach, he couldn't help but wonder if costs might spiral out of control once construction began. Looking over the budget (See **Exhibit 8 – Development Budget**), he wasn't able to pinpoint anything egregious but he wanted to ensure that Portman didn't lose sight of its partners' interests as it oversaw the development process. That's where KLR Asset Management came in.

KLR Asset Management (KLR) was a Shanghai-based firm that provided a broad array of real estate professional services. It specialized in helping international capital sources invest in China. Guy felt that the development consortium (CPI, Portman, and Hengfu) was strong, but he knew that development in China could be an opaque business. Frequently, the extent and strength of one's contacts was crucial to achieve one's aims. Guy hoped that KLR would apply a critical eye to the development budget, exert cost control throughout the development process, help to secure entitlements and ensure that CPI's interests were protected.

Jiangrui Bai, KLR's General Manager, had served as a financial controller on similar redevelopment projects in Shanghai. Guy felt that Mr. Bai could provide focused resources and local contacts for the Jian Ye Li project. If KLR were hired, it would function as the 'owner's representative'. CPI would maintain full control over all major decisions but KLR would aid in the design process, handle relations with the local government, monitor tendering and project progress, provide regular reporting and data, and assist in the marketing strategy. The fee for its representation would be 0.25% of CPI's invested equity, or approximately USD $84,250. In addition, KLR had expressed an interest in investing in up to 5% of CPI's equity position. Guy knew that it was always good if everyone had 'skin in the game'.

After careful consideration, CPI elected to appoint KLR in this capacity. This gave Guy considerable comfort that CPI would have expert eyes and ears on the ground on a more regular basis than it otherwise would absent KLR's involvement. The decision was easy – the difficulty lay in figuring out how KLR would effectively interact with Portman and Hengfu and how decision-making and control would be managed. Despite the good relationships between the parties and their respective reputations as companies with a high degree of professionalism, performance and integrity the potential for conflict certainly always existed. With such a tight development schedule and the sensitivity of returns to delays CPI wanted some assurance that everyone would get along. Aligning everyone's respective interests would be a challenge.

Relocation of Existing Residents

Despite China's rapid economic growth and modernization, relocation remained a sensitive subject. A week prior, Guy had read headlines in the international media that screamed of abuses related to the relocation of residents in advance of construction for the upcoming 2008 Olympics in Beijing. The Beijing Municipal Construction Committee estimated that 15,000 residents would have to be relocated to prepare for the construction and renovation of over 30 different sports venues. The authorities claimed that the vast majority of residents moved voluntarily and were glad to accept generous compensation packages for their displacement, noting that they would have enough money to pass up government-funded affordable housing in favor of higher-quality private apartments. Many would even have enough money to purchase an automobile.

However, international human rights groups painted a very different picture and utilized international media to promote their cause. In one of the articles that Guy had read, a researcher from Human Rights Watch, a New York City-based non-governmental organization decried the lack of transparency in the relocation process in China. Residents received money and were resettled, but the process often wasn't voluntary. Many faced heavy-handed tactics such as intimidating trips to police stations and threats of job dismissals. Many others received only a portion of what they had been promised with the rest being embezzled by unscrupulous local officials. The chief complaint was that residents were powerless to contest the valuation of their residences. Some received compensation based on a smaller area than the actual size of their home.

Although the local media was characteristically silent and physical protests and violence were rare, Guy knew that this was the type of issue that could easily boil over at a moment's notice. In the case of Jian Ye Li, he did not want to be in a situation where popular outrage delayed construction or worse, harmed CPI's corporate reputation. The difficulty was that this issue was somewhat out of CPI's control since the local government held title to the land and Hengfu was responsible for relocating residents. Guy wondered how CPI could ensure that residents were relocated in an expedient yet fair manner. As far as he could gather, Hengfu's strategy for the relocation of the approximately 1,000 residents was to determine occupancy rights for each of the units and offer a reasonable compensation based on the respective area of each dwelling. As to the specifics, Hengfu was unclear, aside from their contention that it would have the site clear by August 2006 so that construction could begin, a mere 8 months later. Guy knew that relocations in Shanghai typically took at least a year and sometimes as much as two or three years depending on scale, degree of negotiations and unforeseen complications.

Political & Economic Climate

Guy paid close attention to the political and economic climate in China. To date, the Communist Party had largely suppressed criticisms of the booming development and physical protests were rare. When protests of any sort did occur they were often located in rural areas of the provinces. However, income inequality between the provinces and urban areas had been growing and the potential for local protests was always present. China had made great strides in reforming its legal and political systems, in large part to facilitate its entry into the World Trade Organization just a few years earlier. But trepidation on the part of foreign investors and other observers had not completely disappeared.

At the time, real estate investment in China was seen as being relatively safe by international development standards. China, and Shanghai in particular was experiencing remarkable growth. Inflation, interest rate and currency dynamics were for the most part considered favorable. Currency exchange risk was often addressed by international investors through expensive hedging strategies, however in the case of Jian Ye Li, CPI benefited from the townhouse sales being managed in U.S. currency, which avoided the devaluation issue. The retail and apartment rents, however were to be levied in Chinese Yuan and would be subject to certain financial risks, including inflation unless acceptable solutions could be devised.

The Municipality of Shanghai and the Xuhui District (which the French Concession fell within) were both considered firmly pro-development at the time. Construction had been booming in the city since Deng Xiao Ping's economic reforms, and by 2005-06 had reached a fevered pitch. However, although both levels of government ostensibly supported development, political concerns remained, especially with regard to recent measures that the Chinese government had taken to cool speculation in the residential market. Streams of negative press regarding residential real estate had been released in order to add bluster to the government's discouraging tone to speculators. The government had also expressed a commitment to strictly limit the amount of new development in the area and the 4.3 kilometers surrounding it by closely monitoring and controlling the height and density of surrounding buildings.

Supply of high-end residential product in Shanghai was expected to decline over 2006-2007, as no new plots had been sold during the previous year due to the government imposing a moratorium on land to be released for construction. Ironically, this had the opposite effect of driving up prices in the more desirable downtown areas. There were 12 areas at the time in Shanghai that had been designated for renovation similar to Jian Ye Li, however none had yet been formally named and the relocation of the existing residents (typically a one to three year process) had not even commenced. Jian Ye Li was the largest single Shikumen-style area within Shanghai and would be the first of the set to be redeveloped, serving as the model case.

There was also a potential issue regarding land appreciation tax. The tax had been in existence in China for over 10 years but was only levied selectively during 2005 in order to cool the residential market. It was impossible to know ahead of time whether this tax would be levied at the time that the units were sold, however based upon initial discussions with Hengfu it was unlikely to be an issue.

Market Dynamics & Competition

Guy and his team busily studied the local market to help them to gauge the economic and competitive metrics that would influence their decision-making. Guy wanted to gain a better level of comfort that the market would support the proposed product mix and that there weren't excessive competitive threats that would endanger their financial expectations once the product came online. KLR proved to be extremely helpful in this regard, providing a wealth of information about the submarket and what could be expected over the ensuing years.

CPI and its partners found themselves having to sort through the distortion of negative press and the measures imposed by the government to quell speculation in the Shanghai residential market. They felt that underlying demand was still robust even though there had been a drop in transactions from April 2005, when the latest measures were announced.

It was widely accepted in the market that these measures had the desired effect and that it was highly unlikely that new ones would be introduced. Transactions had actually increased starting in September 2005, and the top end of the market had been less affected than other segments.

(i) Townhomes

The residential townhouses in the Jian Ye Li redevelopment would be projected to sell for approximately USD $1.85 million each, based on an average price per square meter of USD $4,730 (USD $7,000 per square meter for the above-grade space and USD $2,450 per square meter for the below-grade space). When comparing the above-grade pricing only against the competitive set, Jian Ye Li looked expensive. However, at the blended average (discounted for the below-grade area) USD $4,730 was considered to be an attractive price for such a unique product. This pricing strategy was unconventional though, as pricing in Shanghai was usually only based on the above-grade area.

Portman was confident that its pricing for the townhouses reflected market conditions, given the data that it had studied and the alternatives that buyers had to consider. Other options for buyers in the USD $1.5 million to USD $2 million range included downtown apartments, suburban villas, and old-style detached or terraced housing (see **Exhibit 9 - Townhouse Comparables**). In the Xuhui District, in the trailing twelve months, there had been approximately 300 registered transactions in the USD $1.5 million to USD $2 million price range. However, Guy knew that the actual number could be considerably higher given transactions that had not yet been registered by buyers in order to minimize tax liability. The projects listed among the comparable product that had come to market in the previous 18 months had shown strong sales rates despite the government regulations to curb residential speculation.

Data provided by KLR indicated that there was a supply overhang of 209 units in the USD $1.5 million to USD $2 million range. Moreover, an additional 2,996 units were in the development pipeline (See **Exhibit 10 – Townhouse Competitive Development Pipeline**). However, not all of these units would be in the USD $1.5 million to USD $2 million range. Since most of the units were apartment buildings, it was likely that only 10% to 20% of them would be greater than the 250 square meters required to fall in the price range exceeding USD $1.5 million, based upon pricing guidance of USD $6,000 per square meter.

Guy estimated that if 20% of the oncoming supply (261 units) and the current overhang (209 units) were considered for 2006, the total supply available would be approximately 470 units. If 20% of the oncoming supply for 2007 were added, there would be approximately 808 units in the USD $1.5 million to USD $2 million range available during 2006-2007. Given the 300 transactions anticipated for the next 12 months, it did not seem that there would be an excess supply situation at the high end of the market over the 2006-2007 period, when Jian Ye Li would be marketed in the downtown area, although it was likely that some more remotely located and inferior villa projects would struggle. Guy hoped that Hengfu would share Portman's commitment to quality throughout the development process, given that it was extremely important for the project to accomplish a level of quality that would attract the wealthy expatriates that they were relying on to purchase the townhouses. Otherwise, CPI might be stuck in the STJV for longer than it anticipated or could justify to its investors.

Also of some concern was the relative disadvantage that Jian Ye Li would have in terms of amenities. Comparable projects offered additional amenities not available for Jian Ye Li residents, including swimming pools, tennis courts, and children's playgrounds. To compensate for the lack of amenities, club memberships for in-town fitness centers would be offered to purchasers at Jian Ye Li. Suburban villas also offered much larger living and yard areas and were located near international schools and areas that offered childrens' activities and school facilities. However, the buyer profile at Jian Ye Li was expected to be dominated by senior Asian professionals and foreign expatriates who preferred downtown living over suburban housing alternatives. Perhaps the best comparable for Jian Ye Li was the market of old houses, which typically had no facilities, were well located, but operated in a much more opaque market. Prices for old houses varied from under USD $4,000 per square meter to over USD $8,000 per square meter.

(ii) Retail

Overall vacancy in the Shanghai retail market stood at approximately 6.8% at the time. The sector had been deregulated by the authorities countrywide and looked poised for solid growth into 2006. Most of the data that Guy and his team had sourced, however pertained to prime malls located in Shanghai's top commercial areas and relatively little had been found regarding street-style retail similar to that which was proposed for Jian Ye Li.

While there was a large amount of retail supply coming onto the market (670,000 square meters in 2005) the majority of this space was located in outlying areas. New retail supply in downtown areas continued to be limited. The relative lack of supply and strong demand, particularly from foreign retailers, had increased rents in the retail sector by over 30% since 2000. Rents stood at USD $100 to USD $180 per square meter per month for prime ground floor space, depending on location, and USD $60 per square meter per month for prime first floor space.

The forecast for the retail rental market remained strong, according to DTZ's Shanghai retail property forecasts. DTZ predicted that the sector overall would maintain an annual growth rate of 8% to 10% through 2010. The key drivers would be increased buying power amongst Chinese consumers, expansion of foreign retailers following the elimination of some licensing restrictions, increased tourism and travel among Chinese and the growth of retail driven by infrastructure developments, for example the development of shopping malls at new subway stations.

The analysis of the retail market led Guy to conclude that at USD $60 per square meter per month, the retail space at Jian Ye Li was priced conservatively, as was the project sales price of USD $5,000 per square meter, which indicated a yield of 14.4%. The issue would be more about the speed at which the retail space could be leased at this price, given that current foot traffic in the Jian Ye Li area was quite low. However, Portman felt confident that as the houses were sold and the community developed, they would be able to lease out the retail space in a manner consistent with the underwriting for the project.

(iii) Serviced Apartments

The quality of serviced apartments was extremely variable in Shanghai and many developments that purported to be serviced apartments were little more than residential blocks in fringe locations with minimal services. Some offered fitness facilities but no cleaning or meal services. Some units were generally too large to be considered genuine serviced apartments and were simply family apartments with simple services by unbranded developers. These types of 'serviced apartments' rented in the USD $25 to USD $30 per square meter per month range. Average serviced apartment rates were approximately USD $25 per square meter per month, while vacancy rates were around 8% at the time.

Higher-quality properties such as Tomorrow Square (Marriott Hotel), Shanghai Centre, the Westin, Lanson Place and Grand Pacific Suites had meal and daily cleaning services similar to what one would find in a hotel. These types of serviced apartments were able to command slightly higher rates, in the range of USD $35 to USD $53 per square meter per month. Portman designed the serviced apartments in Jian Ye Li along these lines. At USD

$45 per square meter per month, the pricing at Jian Ye Li was considerably higher than market average and further analysis was needed to justify that rental rate. But Portman felt that Jian Ye Li rents were justifiable, even without a clubhouse, given the unique product offering and the chance that it would give guests to stay in what was essentially a charming boutique serviced apartment development reminiscent of a bygone era of Shanghai.

Planning an Exit

The return analysis for the project (see **Exhibit 11 – Return Analysis)** assumed STJV exit prices of USD $7,000 per square meter for above-grade space and USD $2,450 for below-grade space. It was also assumed that the townhouses would be sold upon completion in March 2008. Based on those dynamics the STJV was expected to yield a before-tax IRR of 29.5%. The LTJV, meanwhile was expected to yield a before-tax IRR of 20.30%, based on Hengfu purchasing CPI's shares at cost plus 40% as planned. After taking into account KLR's fees and equity stake, the final return to CPI for the entire project would be 23.47%. This confirmed Guy's initial gut feeling that the returns for Jian Ye Li would be strong. However, were they worth the significant risks, and how certain were those returns anyway (see **Exhibit 12 – Return Sensitivity**)?

Balancing The Risk-Return Scale

It was New Years Eve and Guy had just received a memo from Qing Ma outlining the risks that CPI would have to either eliminate, or get comfortable with in order to proceed with the Jian Ye Li project. "Excellent work!" thought Guy, as he reviewed the well-crafted memo. Qing had diligently outlined all of the financial and other risks that they might encounter with the project, including those specific to international development. None of the risks identified in the memo were news to Guy, but it was helpful for him to reconcile his own thoughts with that of another risk averse CPI professional.

All development projects of course involve risks, often alarming ones. For Guy, like other development and investment professionals, the challenge was in deciding whether the risks were tolerable in light of the projected returns. Each element exerted pressure on the other, and both had to be considered in the context of the needs and objectives of the investors, in this case the LPs of the CPI Asia Fund. No project was ever completely safe and no assumption was ever completely certain. There would always be reasons not to proceed with a given project, and it was the astute investors and developers who had the ability to identify which projects could overcome those risks and who could devise ways to mitigate them through savvy negotiation, creative deal structuring and sound strategy.

With extensive risk analysis and various other resources in hand, Guy synthesized the information with the financial modeling that CPI had prepared. In his mind he played out a variety of scenarios and how they might affect the return metrics. Each risk could be imagined as enormous or minute, however his years of experience had equipped him with the ability to apply an objective perspective and measure each risk appropriately. He had also learned much about the peculiarities of real estate development in China, which allowed him to appreciate the importance of the roles that each of the participants would play in the project. With the glow of his computer illuminating his office that lonely evening, he put the finishing touches on an E-mail to the Investment Committee members outlining his recommendation in respect of the Jian Ye Li project.

Exhibit 1

Project Concept

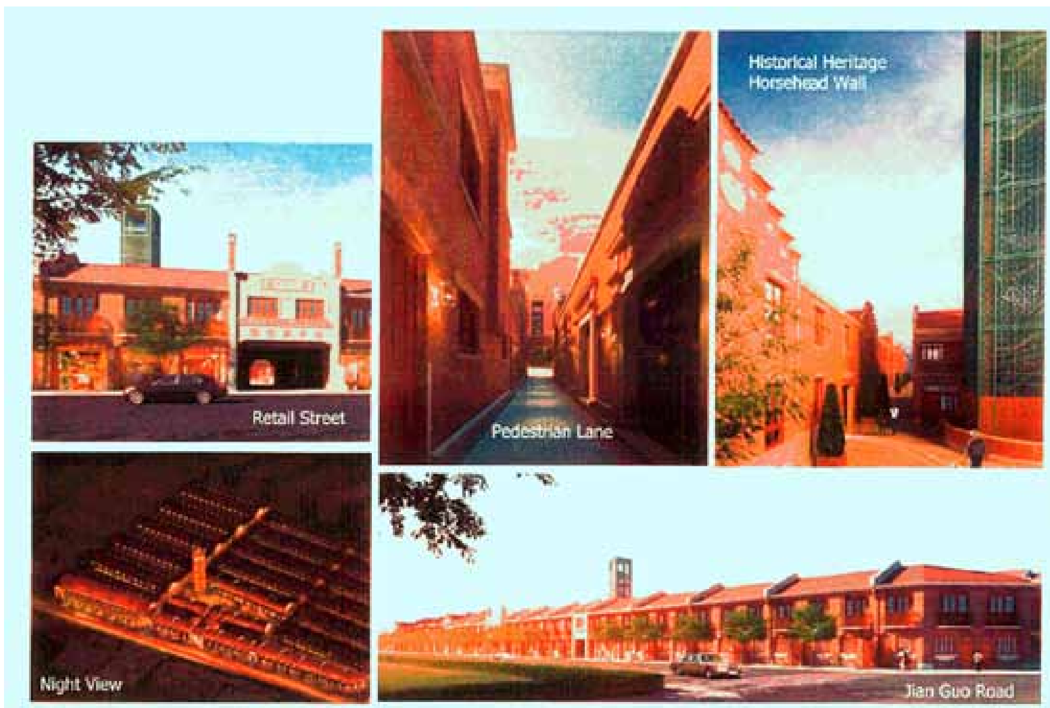

Exhibit 2

Investment Timeline

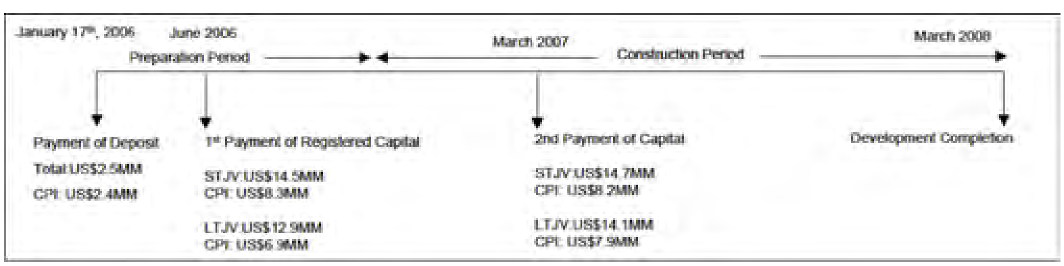

Exhibit 3

Portman Responsibilities

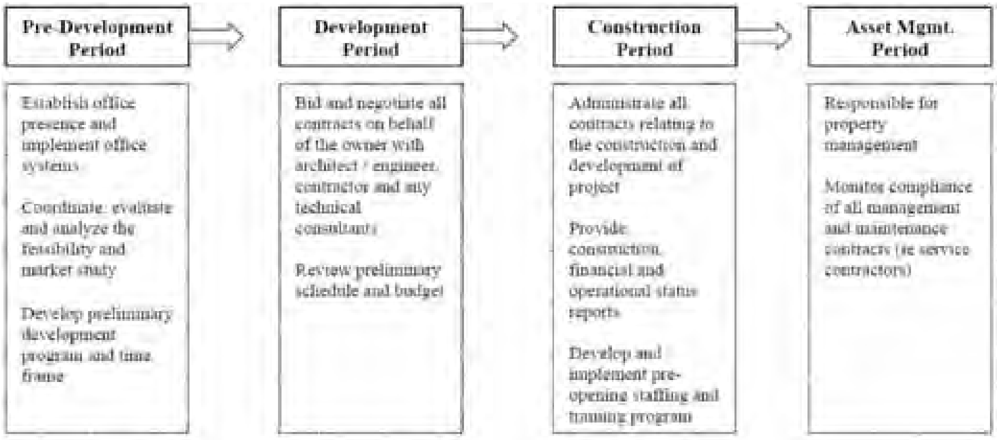

Exhibit 4

French Concession

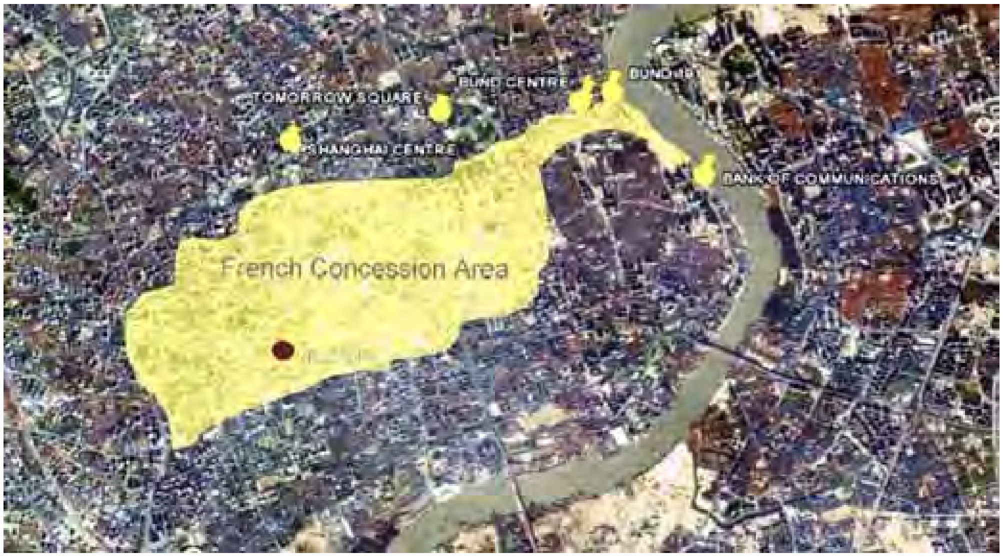

Exhibit 5

Shikumen Architecture

Exhibit 6

Jian Ye Li Site

Exhibit 7

Redevelopment Map

Exhibit 8

Development Budget

Item	STJV - US$	p/sellable sm	LTJV - US$	Total - US$
Land Cost	**$ 29,304,637**	**$ 1,498**	**$ 28,190,449**	**$ 57,495,086**
Hard Costs				
Construction Cost - Above Grade	$ 2,874,400	$ 147	$ 3,482,800	$ 6,357,200
Construction Cost - Below Grade	$ 5,972,000	$ 305	$ 3,028,000	$ 9,000,000
Fixture and Equipment	$ 7,278,400	$ 372	$ 5,678,800	$ 12,957,200
Interior and Furnishings - Apartment	$ -	$ -	$ 2,644,000	$ 2,644,000
Interior and Furnishings - Townhouses	$ 3,799,200	$ 194	$ -	$ 3,799,200
Interior and Furnishings - Retail	$ -	$ -	$ -	$ -
Interior and Furnishings - Below Grade	$ 2,160,400	$ 110	$ 741,200	$ 2,901,600
Landscape, Internal Roads, Outdoor Features	$ 284,960	$ 15	$ 325,520	$ 610,480
Total Hard Costs	**$ 22,369,360**	**$ 1,144**	**$ 15,900,320**	**$ 38,269,680**
Soft Costs				
Pre-Development Costs (% Land and Hard)	$ 355,370	$ 18	$ 317,954	$ 673,324
Development Fee to Portman (% Hard)	$ 1,523,855	$ 78	$ 1,078,022	$ 2,601,877
Architecture and Engineering (% Hard)	$ 870,774	$ 45	$ 616,013	$ 1,486,787
Interior Consulting (% of Interior and Furnishing)	$ 172,788	$ 9	$ 98,556	$ 271,344
Specialty Consulting (% Hard)	$ -	$ -	$ -	$ -
Other Technical Services (% Hard)	$ 108,847	$ 6	$ 77,002	$ 185,849
Legal and Accounting (% Land and Hard)	$ 178,759	$ 9	$ 152,568	$ 331,327
Marketing and Sales (% Sales)	$ 1,112,411	$ 57	$ -	$ 1,112,411
Public Relations and Entertainment (% Land and Hard)	$ 255,370	$ 13	$ 217,954	$ 473,324
Other	$ 127,685	$ 7	$ 108,977	$ 236,662
Total Soft Costs	**$ 4,705,859**	**$ 241**	**$ 2,667,046**	**$ 7,372,905**
Finance Costs				
Commitment Fee	$ 72,653	$ 4	$ 50,075	$ 122,728
Interest During Construction	$ 1,796,700	$ 92	$ 1,282,436	$ 3,079,136
Total Finance Costs	**$ 1,869,353**	**$ 96**	**$ 1,332,511**	**$ 3,201,864**
Contingency	**$ 1,213,597**	**$ 62**	**$ 1,023,156**	**$ 2,236,753**
Total Project Costs	**$ 59,462,806**	**$ 3,040**	**$ 49,113,482**	**$ 108,576,288**

Exhibit 9

Townhouse Comparables (Comparison to Downtown Apartments)

Name	District	Total Units for Sale (Units)	Main Unit Size (sqm)	Transaction Price (US$/sqm)	Total Price (US$)	Opening Date	Sales Speed (units/mth)	Sales Rate	Future Supply (units)	Facilities Available	No. of bedrooms	No. of bathrooms	No. of car parks/unit
Fortune Residence [illegible]	Pudong	306	317	4,194	1,333,600	Dec/04	23	75%	76	Indoor pool, Tennis court, Sauna, Gym, Playground.	2-3	3	850 (overall)
Rich Gate [illegible]	Luwan	106	362	6,425	2,325,995	Dec/04	3.5	52%	51	Indoor pool, Tennis court, Sauna, Gym, Playground.	4-5	3	NA
Central Park [illegible]	Luwan	217	391	4,473	1,748,990	Apr/04	13.5	100%	0	Outdoor pool, Tennis Court, Squash Court, Gym, Indoor/Outdoor Playground, Club house	2-4	2-3	NA
Lan Ting [illegible]	Changning	52	305	5,629	1,722,429	Feb/05	4.5	69%	16	Indoor pool, Tennis court, Sauna, Gym, Indoor/Outdoor Playground.	4-5	3	NA
Total		**681**						**74%**	**143**				
Xian Ye Li	**Xuhui**	**50**	**391**	**4,730**	**1,849,518**	**Mid-2006**	**NA**	**0%**	**50**	**TBC-but will include retail, restaurants and small gym facilities**	**3**	**2**	**2**

Exhibit 9

Townhouse Comparables
(Comparison to Suburban Villas)

Name	District	Total Units for Sale (Units)	Main Unit Size (sqm)	Transaction Price (US$/sqm)	Total Price (US$)	Opening Date	Sales Speed (units/mth)	Sales Rate	Future Supply (units)	Facilities Available	No. of bedrooms	No. of bathrooms	No. of car parks/unit
Mandarin Palace [illegible]	Pudong	20	449	4,963	2,228,169	Dec/04	1.2	60%	8	Indoor pool, Tennis court, Sauna, Gym, Playground, Supermarket	5	5	2
Vizcaya [illegible]	Pudong	23	390	4,142	1,615,254	Sep/04	10	40%	12	Indoor/Outdoor pool, Tennis & Squash Court, Gym, Indoor/Outdoor Playground	4	4	1
Tomson Golf Villa [illegible]	Pudong	53	409	4,444	1,817,453	Jun/04	2.5	75%	13	Indoor/Outdoor pool, Golf driving range, Tennis court, Playground, Gym, Sauna, Restaurant, Supermarket	4	4	2
Dongjiao Villas [illegible]	Pudong	34	528	3,000	1,584,000	Aug/04	1.6	71%	10	Indoor/Outdoor pool, Golf driving range, Tennis court, Playground, Gym, Sauna, Restaurant, Supermarket	5	5	1
Sheshan Golf Club Villa [illegible]	Songjiang	17	335	5,167	1,730,806	Jul/04	0.6	53%	8	Indoor pool, Tennis court, Sauna, Gym, Playground	4	4	1
Shimao Sheshan Villas [illegible]	Songjiang	17	750	4,532	3,399,000	Aug/05	0.6	12%	15	Indoor/Outdoor pool, Tennis court, Bowling, Sauna, Gym.	5	5	2
Century Metropolis [illegible]	Xuhui	NA	400	4,685	1,874,160	2006	NA	NA	NA	Indoor pool, Tennis court, Sauna, Gym, Indoor/Outdoor Playground.	6	3	0
Joffer Villa [illegible]	Xuhui	20	400	6,157	2,462,780	Sep.2005	NA	100%	0	None	6	3	0
Total		192						60%	66				
Jian Ye Li	**Xuhui**	**50**	**391**	**4,730**	**1,849,518**	**Mid-2006**	**NA**	**0%**	**50**	**TBC-but will include retail, restaurants and small gym facilities**	**3**	**2**	**2**

Townhouse Comparables
(Comparison to Old-Style
Detached or Terraced Housing)

Project Name	District	Building Type	Unit Size (sqm)	Market Price * (US$/sqm)	Total Price (US$)	Transaction Date	Yard Area (sqm)	Facilities
Jianguo W. Rd/ Project	Xuhui	Old Terraced House	375	4,841	1,815,450	Sep.2005	10	None
Anfu Rd/ Project	Xuhui	Old Terraced House	360	4,881	1,757,196	Sep.2005	110	None
Yuqing Rd/ Project	Xuhui	Old Villa House	354	4,964	1,757,168	Sep.2005	200	None
Hengshan Rd/ Project	Xuhui	Old Villa House	772	5,311	4,099,706	Sep.2005	450	None
Gaoyou Rd/ Project	Xuhui	Old Villa House	271	5,619	1,522,817	Sep.2005	100	None
Huaihai M.Rd/ Project	Xuhui	Old Villa House	432	5,694	2,459,938	Sep.2005	250	None
Wulumuqi Rd/ Project	Xuhui	Old Villa House	722	6,373	4,601,017	Sep.2005	500	None
Huaihai M.Rd/ Project	Xuhui	Old Villa House	400	6,736	2,694,200	Sep.2005	280	None
Gao'an Rd/ Project	Xuhui	Old Villa House	362	7,442	2,694,113	Sep.2005	417	None
Jianguo W. Rd/ Project	Xuhui	Old Villa House	925	8,104	7,496,616	Sep.2005	1,200	None
Jian Ye Li	**Xuhui**	**New Villa House**	**391**	**4,730**	**1,849,518**	**Mid-2006**	**NA**	**TBC-but will include retail, restaurants and small gym facilities**

Exhibit 10

Townhouse Competitive Development Pipeline

Future Supply

High-end Villas and Apartments

Property	District	Completion Date	Current Status	Total Units	Current Asking Price	Unit Size	Purchase Price Range	Facilities	Developer
2006									
Lakeville Phase 2 (Part I)	Luwan	2006	U/C	424	[illegible]	N/A	N/A	[illegible]	Shui On Property Ltd
Lakeville Phase 2 (Part II)	Luwan	2006	U/C	250					Shui On Property Ltd
Shimao Sheshan Villas	Sheshan	2006	U/C	55	US$4900 psm	[illegible]	[illegible]	[illegible]	[illegible]
Tomson Riviera	Pudong	2006	U/C	286	US$11,600 psm	[illegible]	[illegible]	[illegible]	Tomson Group
			U/C	1,0[illegible]					
			Proposed	0					
			Total	1,0[illegible]					
2007									
One Park Avenue (P III)	Jingan	2007	Proposed	300	TBC	TBC	TBC	TBC	Keppel Land
Hui Yun Villas	Qingpu	2007	Proposed	229	TBC	TBC	TBC	TBC	Shanghai Industrial
Yuguang Villas	Qingpu	2007	Proposed	108	TBC	TBC	TBC	TBC	Zhongxing Real Estate
Zhongkai Sheshan Villas	Songjiang	2007	Proposed	79	TBC	TBC	TBC	TBC	[illegible] Group
Project of Kerry	Jingan	2007	Proposed	300	TBC	TBC	TBC	TBC	Kerry Group
Green Villa (Phase IV)	Pudong	2007	Proposed	50	TBC	TBC	TBC	TBC	Shanghai Jinqiao Group
The Emerald Park (Phase VI)	Pudong	2007	Proposed	50	TBC	TBC	TBC	TBC	Shanghai [illegible] Real Estate
Vizcaya (Phase III)	Pudong	2007	Proposed	25	TBC	TBC	TBC	TBC	Shanghai [illegible] Property
Regency Park (Phase V)	Pudong	2007	Proposed	50	TBC	TBC	TBC	TBC	Hutchison Whampoa
			U/C	0					
			Proposed	1,[illegible]					
			Total	1,[illegible]					

Exhibit 11

Return Analysis (Returns)

US$		1/15/2006	6/30/2006	3/31/2007	3/31/2008	12/31/2008
CPI Returns						
Equity Requirement						
CPI STJV Cash Flow		(1,421,790)	(8,292,765)	(8,205,298)	25,775,510	0
CPI LTJV Cash Flow		(973,322)	(6,919,290)	(7,893,326)	14,330,975	7,127,386
CPI Total Cash Flow		(2,395,112)	(15,212,055)	(16,098,624)	40,106,485	7,127,386
CPI Total Cash Flow		**(2,395,112)**	**(15,212,055)**	**(16,098,624)**	**40,106,485**	**7,127,386**
Equity Return		*24.28%*				
Equity Multiple		*1.40x*				
KLR Fees and Equity						
KLR Cash Flows	5.00%	*119,756*	*760,603*	*804,931*	*(2,005,324)*	*(356,369)*
Underwriting	0.25%	*(84,264)*				
Asset Management p.a.	0.25%	*(84,264)*		*(84,264)*		*(84,264)*
Disposition	0.00%					
Total KLR Fees		(48,772)	760,603	720,667	(2,005,324)	(440,633)
CPI Cash Flows, after KLR		**(2,443,884)**	**(14,451,452)**	**(15,377,957)**	**38,101,161**	**6,686,753**
Equity Return		*23.47%*				
Equity Multiple		*1.39x*				

Return Analysis (Returns by JV)

CPI	Cash Invested-US$MM	Cash Received-US$MM	Profit on Cost-US$MM	IRR	Equity Multiple
Investment in STJV	(17.92)	25.78	7.85	29.50%	1.44x
Investment in LTJV	(15.79)	21.46	5.67	20.30%	1.36x
Total	**(33.71)**	**47.24**	**13.52**	**23.47%**	**1.39x**

Exhibit 12

Return Sensitivity

STJV Exit Sales Price	**$ 5,000**	**$ 6,000**	**$ 7,000**	**$ 8,000**	**$ 9,000**	**$ 10,000**	**$ 11,000**
% Change	-28.6%	-14.3%	0.0%	14.3%	28.6%	42.9%	57.1%
CPI Returns	12.93%	18.13%	23.47%	28.1%	33.4%	38.65%	43.87%
CPI Multiple	1.22x	1.30x	1.39x	1.46x	1.53x	1.60x	1.67x
STJV Hard Construction Cost (MM)	**$ 18**	**$ 20**	**$ 22**	**$ 24**	**$ 26**	**$ 28**	**$ 30**
% Change	-18.2%	-9.1%	0.0%	9.1%	18.2%	27.3%	36.4%
CPI Returns	26.16%	24.88%	23.47%	21.93%	20.41%	18.89%	17.38%
CPI Multiple	1.43x	1.41x	1.39x	1.36x	1.34x	1.32x	1.29x
Combined Hard Construction Cost (MM)	**$ 29**	**$ 33**	**$ 37**	**$ 41**	**$ 45**	**$ 49**	**$ 53**
% Change	-21.6%	-10.8%	0.0%	10.8%	21.6%	32.4%	43.2%
CPI Returns	26.16%	24.88%	23.47%	21.93%	20.41%	18.89%	17.38%
CPI Multiple	1.43x	1.41x	1.39x	1.36x	1.34x	1.32x	1.29x
Construction Completion Date			**Mar-08**	**Mar-09**	**Mar-10**	**Mar-11**	**Mar-12**
CPI Returns			23.47%	13.71%	9.68%	7.47%	6.08%
CPI Multiple			1.39x	1.22x	1.18x	1.15x	1.13x
Combined Debt Finance Rate	**5.50%**	**5.75%**	**6.00%**	**6.25%**	**6.50%**	**6.75%**	**7.00%**
CPI Returns	23.53%	23.51%	23.49%	23.47%	23.44%	23.43%	23.41%
CPI Multiple	1.39x	1.39x	1.39x	1.39x	1.39x	1.39x	1.39x
STJV Debt Level	**35%**	**40%**	**45%**	**50%**	**55%**	**60%**	**65%**
CPI Returns	22.42%	22.74%	23.09%	23.47%	23.84%	24.09%	24.36%
CPI Multiple	1.36x	1.36x	1.38x	1.39x	1.40x	1.41x	1.42x
STJV Sales Velocity				**Mar-08**	**Dec-08**	**Dec-09**	**Dec-10**
CPI Returns				23.47%	20.94%	17.98%	15.78%
CPI Multiple				1.39x	1.35x	1.31x	1.26x
LTJV Mark Up	**25%**	**30%**	**35%**	**40%**	**45%**	**50%**	**55%**
CPI Returns	20.31%	21.38%	22.44%	23.47%	24.49%	25.49%	26.48%
CPI Multiple	1.33x	1.35x	1.37x	1.39x	1.41x	1.43x	1.45x

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