

based on the most recent census information. Included are the number of people within a given radius of the proposed site, growth rates, annual incomes, number of children, whether or not they own a house, education, and so on. From these data Vista's management can proceed to make several key estimates for the proposed site.

After the site is chosen, Vista architects develop plans for the outside and inside of the complex. In the last 5 years considerable effort has been directed at blending the buildings and parking facilities with their environment.

Once the project is begun, tight cost controls are imposed. Every effort is made to complete the project within the allocated budget.

After the project is completed and after the tenants have moved into their stores, Vista's management job still continues. It coordinates promotional campaigns for its tenants including advertising, dollar days, fairs, and concerts.

Vista's interest is to make the property more valuable by building up the sales level of its tenants.

After this phase of rapid growth is over, Vista usually sells the property at a considerable profit. In general the shopping center is sold 7 years after it is opened.

#### Midvale Shopping Center

The Midvale Shopping Center project passed the screening phase some 12 months ago. At that time 140,000 square feet of land were purchased.

The shopping center is located 25 miles west of a major metropolitan area and is 5 miles from its closest competitive center. Demographic data show this to be a rapidly growing area.

Construction is scheduled to be started in 6 months and will cost \$6 per square foot. This figure does not include interior finishing work but does include the cost of parking space which is required for each square foot of interior space.

Of the 140,000 square feet of land available no more than 45,000 square feet of floor space can be used according to local zoning restrictions. The rest must be used for parking and aesthetic purposes.

The problem which the company now faces is to determine how this 45,000 square feet of space is to be divided. There are 12 possible types of stores which can be included. The list is given in Exhibit A. Since certain types of stores are considered essential, the list is divided into groups and each group has a minimum number of square feet. In group A, however, it is considered essential to have both a supermarket and a discount department store. Each of these must have at least 10,000 square feet. To prevent unreasonably large stores, maximum sizes are also given in Exhibit A.

Once it is determined how the space is to be divided, it is very unlikely that any difficulty will be encountered in obtaining tenants. Since there is a broad market for shopping center space within a reasonable distance, the

#### CASE STUDY: Vista Properties, Inc.

Vista Properties is a real estate development company currently facing several problems in the design and construction of a large shopping center. The company already owns 140,000 square feet of land on which this center will be built, and it has an option to buy an additional 20,000 square feet of adjoining land. One problem is whether this option should be exercised. The second problem concerns the use of the available space. What kind of stores should be included in the shopping center, and how much of this available space should be allocated to each of them?

##### Company Background

Vista Properties was founded in 1963 by Ted Wasser. Although the company emphasizes primarily the development of shopping centers, it has occasionally built condominiums.

Vista has had an enviable record. With the exception of one condominium project, it has earned substantial profits on all its investments. Mr. Wasser credits this success to his team of qualified managers, who carefully screen an average of 40 projects before one is undertaken.

Especially useful during the screening phase is the demographic information provided by Data Profile, Inc. For \$130, a complete printout of demographic data is supplied from Data Profile's computer. These data are

Exhibit A Shopping Center Data

Group	Type of store	(1) Cost of interior Improvements <sup>1</sup>	(2) Present value <sup>1</sup>	(3) Guarantee rent <sup>1</sup>	(4) Group minimum <sup>2</sup>	(5) Store maximum <sup>2</sup>
A	1 Supermarket	10	62	3.2	20	20.0
	2 Discount store	13	80	4.1		20.0
B	3 Fabric	12	45	3.0	3	0.9
	4 Women's specialty	8	50	3.2		3.0
	5 Men's specialty	7	48	3.2		2.0
C	6 Hardware	7	52	3.0	3	4.0
	7 Drug	9	46	3.1		1.6
D	8 Gift	9	38	2.5	3	3.0
	9 Bakery (sale only, no baking)	11	50	2.4		1.3
	10 Ice cream/Sandwich	10	40	2.6		1.5
	11 Music and hi-fi	7	46	2.3		1.5
	12 Barber	11	35	3.0		1.0

<sup>1</sup> Dollars per square foot.  
<sup>2</sup> Thousands of square feet.

rental fees are market-determined and will be readily accepted by the tenants. It is expected, therefore, that there will be no negotiation on price.

The criterion by which a shopping center is judged is the present value of its after-tax flows. These flows are shown in column 2 of Exhibit A. They represent the present value of rent revenues less fixed charges, depreciation, and taxes over the 7-year life of the project. To this is added the projected sale price of the property when it is sold. The figures are given on a per square foot basis and do not include interior improvements. Mr. Wasser has argued, however, that the net of these two figures should be used. The cost of interior improvements is given in column 1 of Exhibit A.

Vista's available capital for financing interior improvement is limited to \$450,000. It is unlikely that any additional funds could be acquired.

An essential financial consideration for these centers is that the guarantee rent must cover the fixed charges including interest charges on the debt. Each tenant must sign a lease which guarantees Vista a fixed rental payment each year. In addition, if the tenants' sales revenue exceeds a certain level, a percentage (6 percent) of this excess is paid to Vista. The guarantee rents for each type of store are given in column 3 of Exhibit A. Fixed charges are estimated to be \$125,000.

The Option

Vista has an option to purchase 20,000 square feet of land adjacent to its present parcel. Only 6000 square feet can be used for stores. The option will expire in 3 months and carries a price of \$10 per square foot of land.

Capital outlay for this additional parcel has been computed in the following way:

Land costs: \$10 per square foot x 20,000 square feet = \$200,000  
 Construction costs: \$6 per square foot x 6000 square feet = 36,000  
 Interior improvements (average): \$10 per square foot x 6000 square feet = 60,000  
 Total capital required = \$296,000

To raise this capital, Mr. Wasser would borrow as much as possible and then issue common stock for the remainder. This would add \$29,000 per year to his fixed charges, assuming an average capital cost of slightly less than 10 percent.