



STRATHMORE BUSINESS SCHOOL

BACHELOR OF COMMERCE

END OF SEMESTER EXAMINATION

AMS 3102: REAL ESTATE AND PROJECT FINANCE

DATE: Fri, 26th July 2024

TIME: 13:00 – 15:00

INSTRUCTIONS

- 1) Answer question **one** and any **other two** questions
- 2) Question one is compulsory and carries **30 marks**
- 3) All other questions carry **20 marks each**

QUESTION ONE

.....The case involving KCB Bank's auction of 78 Greatwall Apartments stems from a legal battle with Erdemann Property Limited over an unpaid loan. In 2015, Erdemann secured a loan of KSh 1.3 billion from KCB to construct 2,190 units. As part of the agreement, 100 units were to be held as security for the loan. However, Erdemann mistakenly sold these 100 units to homeowners who were unaware of the existing charge against the properties. When Erdemann defaulted on the loan repayment, KCB sought to exercise its statutory power of sale to recover the outstanding balance of KSh 1.9 billion. The homeowners, who had purchased the units between December 2019 and January 2020, challenged the auction, claiming they were innocent buyers and had no knowledge of the bank's interest in the properties. Despite their appeals, both the High Court and the Court of Appeal ruled in favor of KCB, allowing the auction to proceed. The auction, scheduled for May 21, 2024, involves selling the units individually, with the proceeds intended to settle the loan. The home owners continue to seek legal remedies to prevent the sale, arguing that their interests should be protected against the bank's claims

- (i) From the above extract explain between the bank's interest and the home owners interest as it has been represented **(2 marks)**
- (ii) Describe the term security as used in the extract above **(2 marks)**
- (iii) Why did the court fail to protect the home owners interest? **(2 marks)**

- (iv) Distinguish the difference between the terms Estate and Real Estate (2 marks)
 - (v) Your friend is facing a risk to undergo foreclosure for a defaulted mortgage. Discuss to him options that he may consider as an alternative (12 Marks)
 - (vi) Describe the **two** types of estates not yet in possession (4 marks)
 - (vii) Compare between reverse mortgage loans and negative amortizing loans. (2 marks)
 - (viii) A company has a mortgage loan of ksh 56 million made at a nominal interest rate of 15.4% for 20 years. The mortgage loan is paid monthly. What is the balance of the loan after 9 years assuming fully amortizing pattern is applied? (4 marks)
- (TOTAL 30 MARKS)**

QUESTION TWO

- (i) Real estate and property investors seek to value properties either to know how much they must pay as a buying price or the best price they must sell at. The valuation process is sometimes complex and time consuming. Discuss **three** approaches that can be used to value properties (9 marks)
- (ii) Explain the contents of a mortgage (4 marks)
- (iii) Explain assumption of mortgage (3 marks)
- (iv) Explain tilt effect (2 marks)
- (v) Consumer Price Index (CPI), can be used to adjust mortgage interest rates. Explain two problems of using CPI (2 marks)

(TOTAL 20 MARKS)

QUESTION THREE

- (i) Under property financing, the bank would wish to appraise properties to ascertain the value against the amount they wish to lend. Describe the steps they may follow in the property appraisal. (3 marks)
- (ii) Explain the main factors that influence interest rate on mortgages (5 marks)
- (iii) Real estate can be classified under three groups, namely Economic characteristics, Physical characteristics and Investable assets. Discuss the characteristics in each group. (8 marks)
- (iv) What is the balance of a 20-year loan at interest rate 14.5% of ksh 15 million after 12 years assuming partial amortizing pattern is applied where a balloon payment of ksh 3.5 million at maturity? The loan repayments are made monthly. (4 marks)

(TOTAL 20 MARKS)

QUESTION FOUR

- (i) In property discuss three alternatives methods of financing projects. **(6 marks)**
- (ii) Differentiate between the following terms
- A. Freehold estate and Leasehold estate **(2 marks)**
 - B. A mortgage and a promissory note **(2 marks)**
- (iii) Distinguish a foreclosure from a default **(2 marks)**
- (iv) Explain **two** types of foreclosure **(2 marks)**
- (v) An individual with loan of ksh 13,500,000 borrowed for 14 years at 13%. The interest rate is adjustable after every one year based on the Consumer price index (CPI). If the CPI is 4% after year 1,
- a. Calculate the monthly repayment for year 1 **(2 marks)**
 - b. What is the loan balance after year one? **(2 marks)**
 - c. Calculate the loan repayments for year two **(2 marks)**

(TOTAL 20 MARKS)

QUESTION FIVE

- (i) Discuss the contents of a promissory note **(5 marks)**
- (ii) Explain a composite rate of interest distinguishing from a teaser rate. **(4 marks)**
- (iii) A mortgage loan has the following information
- Loan Amount = Sh 37,650,000
 - Starting Rate = 7%
 - Term = 25 Years
 - Adjustment Interval = 2 Year
 - The loan also has an interest rate cap : 3.5 % Annual Rate Cap

Required:

- (a) Compute the monthly payments for year 1 **(3 marks)**
- (b) Compute the loan balance at the end of year. **(4 marks)**
- (c) Explain the effect of the annual cap rate if composite rate rise to 15% **(2 marks)**
- (d) What will be the effect if a payment cap of Ksh 65,000 per month is introduced **(2 marks)**

(TOTAL 20 MARKS)