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## Amid Market Uncertainty, a New Hedge

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In a week when the Federal Reserve cut rates by half a point and confusion has reigned on Wall Street, a new index has come online that allows investors to hedge against a drop in real estate values.

Created by Radar Logic, the index enables investors to bet on the future values of real estate in New York City and 24 other metropolises. It is the second attempt to create a market where large investors such as hedge funds, and eventually individual people, can bet on the future of real estate prices much in the way that investors now bet on the future prices of commodities like corn and gold.

"What this will do is give you an ongoing view of what's happening in the real estate marketplace," a vice president at GFI Group in charge of U.S. real estate derivatives, Philip Barker, said. "The market for Radar Logic is gaining liquidity much faster than anything we've seen on the residential side before."

The index aims to create a derivative market — investors place bets derived from the value of real estate but no real property is ever bought or sold. Like the stock data that scrolls across tickers, the index has a simple numerical output — in this case, the average price a square foot. The New York City region's reading yesterday was \$301.69, while Chicago, for example, was listed at \$184.11.

Radar Logic spent four years creating the technology and algorithms that enable it to calculate the values on a daily basis. The data, which comes from public sources such as taxes and building assessors' offices, reflects the average price per square foot trailing 63 days, as it takes that amount of time for the transaction to close and the data to be entered into the system.

The Radar Logic index, known as the Residential Property Index, or RPX, is the second such financial tool to measure real estate futures. Last year, ratings agency Standard & Poor's teamed up with two prominent economists, Robert Shiller, a professor at Yale, and Karl Case, a Wellesley College professor, to create the S&P/Case-Shiller Index. That index, which is monthly and is displayed in terms of appreciation since the beginning of the year, has seen a "relatively low" amount of activity, Mr. Case said.

While the S&P index has agreements with Goldman Sachs and the Chicago Mercantile Exchange, the RPX has agreements with every bulge bracket investment bank, including Morgan Stanley, Lehman Brothers, and Merrill Lynch.

The key to making indices such as these work is liquidity. As more investors bet on the real estate derivatives, its accuracy improves, and it can be used as a predictor of where the financial community believes the market is headed. While only four days old, a number of bets have already been placed using the RPX, the head of property derivatives for ICAP, Andrew Aymen Samawi, said. "The timing of the product is good given the nature of the volatile markets, and we expect to see the number of deals grow."

The president of the appraisal firm Miller Samuel, Jonathan Miller, a research partner at Radar Logic, said the RPX is an important tool, particularly in periods of turmoil.

"After having been in the valuation business for 21 years, I understand and have seen problems with the way markets are tracked," he said.

The subprime mortgage woes, for example, are a perfect example of why knowledge of risk is important.

"The whole issue in the subprime chaos is that there wasn't a great understanding of risk," he said. "We are providing tools that interpret information in a way that can be used to assess that risk in residential real estate."

While the index is off to a good start, some are more critical in their assessment of it.

"I'm not overly sanguine about it working," the director of research at UCLA's Richard S. Ziman Center for Real Estate, Stephen Cauley, said. "It could make a major contribution or it could make a small contribution." Part of the problem, he said, is that the RPX is too broad. It looks at real estate prices in the New York City region, for example, which does not allow investors to bet on the value of a particular neighborhood.

Mr. Case, who has been involved with research into real estate indices since the 1980s, said the RPX caters more toward dealers, but includes more "unpredictable random error" by using complex mathematics to calculate the values on a daily basis.

"They add fancy math, but they don't add data," he said.

Still, while there are kinks to work out, a real estate index like this could change the way property deals are conducted. The president and chief executive of Radar Logic, Michael Feder, said that while the index is available only to institutional investors at the moment, down the road developers or individual buyers could use it to hedge any losses in their investments.

A buyer of real estate may one day be able to buy an insurance policy that includes a hedge on the local real estate market, for instance. If prices start to slide, the buyer would earn money and be able to stabilize their finances.

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