

**Finance 673**  
**Real Property Valuation I**

Department of Finance  
Mays Business School  
Texas A&M University

Valuation Process

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**Definition of the Problem**

- Identification of the client and intended users
- Intended use of the appraisal
  - ▶ Manner in which client will use the information in the report
    - Price at which to buy or sell
    - Amount of loan
    - Basis for taxation
- Purpose of the appraisal
  - ▶ Estimate a certain type of value
    - Market value, use value, investment value

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**Definition of the Problem**  
***(continued)***

- Date of the opinion of value
  - ▶ Must be specified since market conditions/perceptions of future conditions vary over time
  - ▶ Prospective/Retrospective date of value
- Identification of relevant property characteristics
  - ▶ Location, physical attributes
  - ▶ Real property interests
- Extraordinary assumptions and hypothetical conditions

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## Scope of Work

- Amount and type of information researched
- Analysis applied
- Determined by appraiser/analyst given the client's intended use and the nature of the problem
- Disclose scope in report
- Helps to identify resources and data needed in assignment

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## Data Collection and Property Description

- General data
  - ▶ Social, economic and governmental forces
- Specific data
  - ▶ Information on property being valued/analyzed

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## Data Analysis

- Market analysis
  - ▶ Study of market conditions for a specific type of property
  - ▶ Supply and demand of particular product
  - ▶ Basis for feasibility analysis
- Highest and best use analysis
  - ▶ Analysis of HBU as if vacant and as improved
  - ▶ Identify improvements (optimal use) and comparables
  - ▶ Basis for valuation - value at HBU

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## Land Value Opinion

- Why value land?
  - ▶ Land value major component of property value
  - ▶ Land and building value may change at different rates
    - Land may appreciate
    - Building may depreciate
  - ▶ Many assignments require it
  - ▶ Required for cost approach

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## Land Value Opinion (*continued*)

- Land valuation methods
  - ▶ Sales comparison
  - ▶ Extraction
  - ▶ Allocation
  - ▶ Subdivision development
  - ▶ Land residual
  - ▶ Ground rent capitalization

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## Approaches to Value

- Cost approach
  - ▶ Add estimated value of land to current improvement reproduction/replacement cost less depreciation
  - ▶ Add entrepreneurial incentive (profit)
  - ▶ Depreciation
    - Physical deterioration
    - Functional obsolescence
    - External obsolescence
  - ▶ Most useful when improvements are new or not frequently sold

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## Approaches to Value *(continued)*

- Sales comparison approach
  - ▶ Identify comparable sales
  - ▶ Analyze sales prices and elements of comparability or dissimilarity
  - ▶ Price range of most comparable properties establish market range of value
  - ▶ Most useful when there are a number of similar properties having recently sold
  - ▶ Analyze conditions of sale, market conditions, location, physical attributes, etc.
  - ▶ Sales data can also be used to extract cap. rates

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## Approaches to Value *(continued)*

- Income capitalization approach
  - ▶ Present value of future benefits of property ownership
  - ▶ Capitalize income and resale price into value
  - ▶ Two methods
    - Direct capitalization
      - Relationship between one year's income and value
    - Yield capitalization
      - Discounted cash flow analysis
      - Mortgage-equity analysis
  - ▶ Estimate net operating income and reversion

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## Reconciliation and Reporting

- Reconcile of value indications from approaches used
  - ▶ Reconcile into point estimate of value
  - ▶ Range of values
  - ▶ Direction of value (more or less than a specified amount)
- Report of defined value
  - ▶ Conclusion stated in report to client
  - ▶ Written or oral reports
  - ▶ Three types of reports (complete, summary, restricted)

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