

# **Understanding and Applying Cap Rates in Residential Real Estate Investing**

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## **1) *Introduction to this session***

## **2) *Scenarios that require Capitalization Rate analysis***

- Single-family homes
- Multi-family homes
- Apartment buildings
- Mixed use properties
- Commercial – storefront/office/industrial

This section discusses approaching income producing properties in the appropriate fashion, with the right questions, facing the right challenges to properly evaluate sale or longer term value for your client.

## **3) *The 3 approaches to residential real estate appraising***

- Comparable Sales approach
- Income Approach
- Cost Approach

This section will emphasize the income approach to residential real property appraising vs. the comparable sales approach that is used in a typical realtor CMA. Understanding when each approach is most appropriate, and how they differ. The differences between market value, actual market price, and cost of replacement. Examples of how insufficient data, short sales and foreclosures can influence an appraisal or valuation of a property differently than value according to just the income approach, and how the life cycle of the community can be considered.

## **4) *The “IRV” formula, and the process of calculating Capitalization Rates***

- Calculations and adjustments to attain needed variables
- Usage and checking the formula
- How changing factors will affect value and projected values

This section will review annual rate of return calculations and application examples of them. IRV formula explained in detail. Different ways the equation can be used or applied for different types of properties, solving for different variables. Checking your work. Examining change of value due to expectations of a different annual rate of return, and utilizing in conjunction with comparable sales.

## **5) *Practical application of the formula, and longer term projections***

- Unique factors with subject properties to look for
- Guidelines when formulating longer term projections and models
- Categorizing expenses of the subject property
- Making necessary adjustments to the formula for vacancy, reserve, and modernization

This section will look at real world case studies and tackle issues that could complicate the subject property. Unique factors to consider with each subject property will affect investor goals, and thus affect short and long term rate of return. Basic guidelines to consider with longer term projections and models for clients will be addressed. Understanding appraisal concepts of both functional and external obsolescence, and how those limitations will affect future planning. Common sense and effective use of multipliers and adjustments, such as rent roll increases, property taxes, and adjustments for vacancy rates and reserve funds. Developing an appropriate model for a particular subject property to assist a client in determining valuation and whether or not to invest.

#### **6) *Marketing strategies for the real estate professional***

- Using these figures for pricing during a listing presentation
- Marketing strategies for sale of income producing properties
- Financing challenges of income properties

This section will discuss a variety of strategies for the real estate professional to integrate into their business. Proper use of marketing, and within negotiations. Understanding the challenges with attaining common financing on certain types of investment properties. Factors that will affect your client's ability to purchase and realize their goals of either equity or cashflow in a particular property.

#### **7) *Utilizing Capitalization Rates to manage client relationships***

- Integration with property management
- Client portfolio management
- Building new business

Finally we'll discuss understanding and managing client needs, and goals and expectations and property management applications. Utilizing your customized formula to evaluate property performance and maximize revenue and increase cap rates to earn repeat business, and help advise your clients on when it's time to sell or buy.

#### **8) *Questions and Answers***