

# RE 614 – Real Estate Appraisal

Fall 2008

## Homework 7 – Income Approach

*Dr. Stanley D. Longhofer*

*TTh 9:30-10:45*

- 1) Trent is appraising a commercial office building in east Wichita. The building has 120,000 square feet of gross leasable area. Of this, 35,000 square feet rent for \$17.50 per square foot (psf), 65,000 square feet rent for \$16.00 psf, while the remaining 20,000 square feet rent for \$15.25 psf. All leases in this building are gross leases. Currently, the average vacancy rate for similar office space in east Wichita is 12%.

Based on the owner's past tax returns, Trent has forecasted the following expenses for the property:

|                         |            |
|-------------------------|------------|
| Depreciation allowances | 205,000    |
| Utilities               | \$195,170  |
| Maintenance             | 185,000    |
| Management expenses     | 10% of EGI |
| Mortgage interest       | 220,000    |
| Property insurance      | 135,000    |
| Property taxes          | 260,000    |

- Write out the pro forma operating statement for this property. What is its expected net operating income?
- Suppose that the property recently sold for \$10 million. What is the cap rate of this transaction?
- What is the net Income Multiplier of this transaction?
- Similar office buildings have recently been selling at an 8.50 percent cap rate. Based on this, what is the market value of this property?
- Suppose that the market (effective) gross income multiplier is 5.7. What is the indicated market value of this subject using a gross income multiplier?
- Provide two specific weaknesses of the cap rate and net income multiplier as tools for valuing an income property.
- What additional weakness does the gross income multiplier have in addition to the two just mentioned?