

INCOME APPROACH

The income approach to value is applied to those real properties which are typically viewed by market participants as "income producing", and for which the income methodology is considered a leading value indicator. The first step in the income approach pertains to the estimation of market rent on a per unit basis. *This is derived primarily from actual rent data furnished by property owners and from local market surveys conducted by the district and by information from area rent study reviews. This per unit rental rate multiplied by the number of units results in the estimate of potential gross rent.

A vacancy and collection loss allowance is the next item to consider in the income approach. *The projected vacancy and collection loss allowance is established from actual data furnished by property owners and local market survey trends. The market derived stabilized vacancy and collection loss allowance is subtracted from the potential gross rent estimate to yield an indication of estimated annual effective gross rent to the property.

Next, a secondary income or service income is considered and, if applicable, calculated as a percentage of stabilized effective gross rent. The secondary income estimate is then added to effective gross rent to arrive at an effective gross income, when applicable.

Allowable expenses and expense ratio estimates are based on a study of the local market, with the assumption of prudent management.

Subtracting the allowable expenses (inclusive of non-recoverable expenses and replacement reserves when applicable) from the annual effective gross income yields an estimate of annual net operating income to the property.

Return rates and income multipliers are used to convert operating income expectations into an estimate of market value for the property under the income approach. These include income multipliers, overall capitalization rates and discount rates.

Capitalization analysis is used in the income approach models to form an indication of value. This involves the direct capitalization of net operating income as an indication of market value for a specific property. Capitalization rates applicable for direct capitalization method and yield rates for estimating terminal cap rates for discounted cash flow analysis are derived from the market.

Hays CAD will review the income approach method when requested by the property owner comparing actual rent rolls and expense data with pro-forma estimates.

** Surveys and renditions received from property owners and local market surveys are considered confidential and not available to the public.*