SLIDE 1 – Concept of Value (Cover Page)

SLIDE 2

Concepts of Value

Market cost: The economic price at which a good or service is offered in the market. It is mainly determined by the relationship between supply and demand

Market price: The price for which a property actually sold; the final sales price

Market value: The highest price a ready, willing and able buyer, not forced to buy, will pay to a ready, willing and able seller, not forced to sell, allowing a reasonable time for exposure in the open market. Both parties well informed or well advised, and each is acting in what he or she considers his or her own best interest.

SLIDE 3

Types of Value

The purpose of an appraisal influences an estimate of the value of a parcel of real estate. This is because there are different types of value related to different appraisal purposes. Some of the possibilities are listed below.

Types of Real Estate Value

market

reproduction

replacement

salvage

plottage

assessed

condemned

reversionary

appraised

rental

leasehold

insured

book

mortgage

SLIDE 4

Market value – Market value is an estimate of the price at which a property will sell at a particular time. This type of value is the one generally sought in appraisals and used in brokers' estimates of value.

Reproduction value – Reproduction value is the value based on the cost of constructing a precise duplicate of the subject property's improvements, assuming current construction costs.

Replacement value – Replacement value is the value based on the cost of constructing a functional equivalent of the subject property's improvements, assuming current construction costs.

SLIDE 5

Salvage value – Salvage value refers to the nominal value of a property that has reached the end of its economic life. Salvage value is also an estimate of the price at which a structure will sell if it is dismantled and moved.

Plottage value – Plottage value is an estimate of the value that the process of assemblage adds to the combined values of the assembled properties.

Assessed value – Assessed value is the value of a property as estimated by a taxing authority as the basis for ad valorem taxation.

SLIDE 6

Condemned value – Condemned value is the value set by a county or municipal authority for a property which may be taken by eminent domain.

Depreciated value – Depreciated value is a value established by subtracting accumulated depreciation from the purchase price of a property.

Reversionary value – Reversionary value is the estimated selling price of a property at some time in the future. This value is used most commonly in a proforma investment analysis where, at the end of a holding period, the property is sold and the investor's capital reverts to the investor.

SLIDE 7

Appraised value – Appraised value is an appraiser's opinion of a property's value.

Rental value – Rental value is an estimate of the rental rate a property can command for a specific period of time.

Leasehold value – Leasehold value is an estimate of the market value of a lessee's interest in a property.

Insured value – Insured value is the face amount a casualty or hazard insurance policy will pay in case a property is rendered unusable.

SLIDE 8

Book value – Book value is the value of the property as carried on the accounts of the owner. The value is generally equal to the acquisition price plus capital improvements minus accumulated depreciation.

Mortgage value – Mortgage value is the value of the property as collateral for a loan.

SLIDE 9

Appraising Market Value

Market value is an opinion of the price that a willing seller and willing buyer would probably agree on for a property at a given time if:

The transaction is a cash transaction

The property is exposed on the open market for a reasonable period

Buyer and seller have full information about market conditions and about potential uses

There is no abnormal pressure on either party to complete the transaction

Buyer and seller are not related (it is an "arm's length" transaction)

Title is marketable and conveyable by the seller

SLIDE 10

Market value is an opinion of the price that a willing seller and willing buyer would probably agree on for a property at a given time if:

The price is a "normal consideration," that is, it does not include hidden influences such as special financing deals, concessions, terms, services, fees, credits, costs, or other types of consideration.

SLIDE 11

Another way of describing market value is that it is the highest price that a buyer would pay and the lowest price that the seller would accept for the property.

The market price, as opposed to market value, is what a property actually sells for. Market price should theoretically be the same as market value if all the conditions essential for market value were present. Market price, however, may not reflect the analysis of comparables and of investment value that an estimate of market value includes.

SLIDE 12

The Appraisal and Its Uses

While most appraisals seek to estimate market value, any of the types of value described earlier may be the objective of an appraisal. An appraisal is distinguished from other estimates of value in that it is an opinion of value supported by data and performed by a professional, disinterested third party.

Appraisers acting in a professional capacity are also regulated by state laws and bound to standards set by the appraisal industry.

SLIDE 13

The Market System

Price and value – In addition to supply and demand, the other critical component of an economic system is the *price mechanism*, or simply, price. A price is the amount of money or other asset that a buyer has agreed to pay and a seller has agreed to accept to complete the exchange of a good or service. It is a quantification of the value of an item traded.

Price in this context means the final trading price; it is not the preliminary asking price of the seller nor the initial bidding price of the purchaser. Asking and bidding prices are pricing positions in a negotiation between the parties prior to the exchange. The true price of an item or service is the final number the parties agree to.

SLIDE 14

Value and value determinants – Price is not something of value in itself. It is only a number that quantifies value. The economic issue underlying the interplay of supply and demand is, how do trading parties arrive at the value of a good or service as indicated by the price?

Consider consumer demand for air conditioners. Why do air conditioners have value? How do they command the price they do?

The value of something is based on the answers to four questions:

How much do I desire it?

How scarce is it?

How useful is it?

Am I able to pay for it?

SLIDE 15

Desire – One determinant of value is how dear the item is to the purchaser. Returning to the air conditioner example, the question becomes "how much do I desire to be cool, dry, and comfortable?"

To a person who lives in the tropics, it is safe to say that air conditioning is more valuable than a heating system. It is also safe to say the opposite is true for residents of northern Alaska.

SLIDE 16

Utility – The second determinant of value is the product's ability to do the job.

Can the air conditioner satisfy my need to stay cool?

How cool does it make my house?

Does it even work properly?

Of course, I won't pay as much if it is old or ineffectual.

SLIDE 17

Scarcity – The third critical element of value is a product's availability in relation to demand. The air conditioner is quite valuable if there are only five units in the entire city and everyone is hot. On the other hand, the value of an air conditioner goes down if there are ten thousand units for sale in a 500-person market.

SLIDE 18

Purchasing power – A fourth component of value is the consumer's ability to pay for the item. If one cannot afford to buy the air conditioner, the value of the air conditioner is diminished, since it is financially out of reach. If air conditioners are too expensive, consumers are forced to consider alternatives such as ceiling fans.

SLIDE 19

Transferability. How readily or easily title or rights to real estate can be transferred affects the property's value. Property that is encumbered has a value impairment since buyers do not want unmarketable title.

Similarly, property that cannot be transferred due to disputes among owners may cause the value to decline, because the investment is wholly illiquid until the disputes are resolved.