

## **RE95C15:**

### **Commercial Real Estate Basics: Geographic and Financial Analysis**

#### **I. Introduction:**

- a. This course focuses on commercial real estate basics to further understand the real estate decision-making tools of a commercial tenant or buyer
- b. Decision-making variables will be reviewed targeting location site selection variables, physical variables, housing availability, transportation networking, etc.
- c. Valuation methods that may be employed for the purchase of investment real estate, end-user occupied building and business asset sales.

#### **II. Business Owner to be a Buyer or Tenant:**

- a. Purpose/Goal of Business Owner and the Business
  - i. What is the long-term plan of the owner?
  - ii. Will the business be sold in a few years, merged or acquire other firms?
  - iii. Understanding the reasons to own vs. to lease?
- b. Ownership Versus Leasing:
  - i. Comparison of all Costs
  - ii. Cost to purchase vs. annual debt service vs. rental payments
  - iii. Financing Alternatives (Include Owner Financing and Documentation Required) - Value of Equity
  - iv. Formal Illustration
- c. What is the 1-3 year business plan (Including Growth and Cash Flow Analysis) to support any new location or to decide if to lease versus to own?
  - i. Evaluating the company's business plan and financials, as would a landlord, to assess leasing risk and establishing negotiating leverage
- d. What are the required building characteristics and other external variables? For example, minimally a broker should understand the end-user's need for:
  - i. Space and the amount, office, warehouse, retail, lab, medical, R&D, industrial, etc.
  - ii. Number of required parking spaces
  - iii. Signage capabilities for company exposure
  - iv. Amount of power/type of lighting/Internet access and type
  - v. Company's number of employees and living locations
  - vi. Location of the company's competition
  - vii. Utilities: public vs. private water, sewer, septic, electric, gas, etc.
  - viii. Identifying any service moratoriums
  - ix. Identifying safety issues of the property

- x. If the company is a “Start Up” then identifying location of company’s market & suppliers for the company’s products
- xi. Other examples

### **III. Location:**

- a. Site and Building Cost and Availability
- b. Visibility/Exposure Required - Traffic Counts. What type of commercial end-user is this information relevant?
- c. Access to company’s suppliers and customer market to conduct a site search
- d. Supplier availability as it relates to a target site search
- e. Location of Competition and when this information is relevant
- f. Quality of All City/Town and Local Services and Utilities

### **IV. Labor Supply:**

- a. Proximity to Labor Market and Needed Services
- b. Labor Type Needed vs. Type available
- c. Wage Levels and costs; Union vs. Non-union
- d. Seasonal vs. Year Round labor availability

### **V. Transportation:**

- a. Proximity to Major and Secondary Roads
- b. Access to airports, harbors and mass transit
- c. Road Maintenance/road construction, pending road change issues, street flow
- d. Rail service
- e. Trucking vs. passenger vehicle access

### **VI. Housing Availability:**

- a. Single family and rental housing quantity, type available and cost
- b. Affordability for company workers
- c. The use of resources such as residential agents
- d. Broker conducted apartment market survey/Vacancy rate/Rental rates/general market study

### **VII. Financing Opportunities for a Business buying real estate**

- a. Commercial lender will want a 3 Year History Including Income Taxes. There will be a check list of other loan application requests.
- b. If a public company, then real estate agent can research financial history on website of the Security and Exchange Commissions (SEC) or company’s annual report
- c. Financing options that broker can assist include: traditional commercial lender, Small Business Administration (SBA), State and Local Economic Development Agencies, Commercial Mortgage Originators and other examples.
- d. Chamber of Commerce Assistance

- e. SCORE: a non-profit association that partners with SBA

### **VIII. Real Estate and Business Valuation:**

- a. Real Estate/Business valuation employ different methods
  - i. Real Estate Valuation Methods
    - 1. Full Discussion and Example of Income Approach (Capitalization Rates, Gross Income Multiplier (GIM))
    - 2. Identifying possible income sources in a commercial building
    - 3. Identifying possible operating expenses in a commercial building
    - 4. Understanding the difference between an operating expense and capital expense
    - 5. Review of the Band of Investment Approach:  $\text{NOI/Capitalization Rate} = \text{Value}$

### **IX. Business Valuation Methods:**

- a. Broker should recommend the need to use accountants and business valuation experts as required through this process
- b. Broker may find a commercial real estate firm that has both business brokers and commercial real estate brokers that could be a time management benefit
- c. Identifying the business valuation revenues: Sales of Goods, Cost of Goods, Other income = Total Income
- d. Expenses can include: Cost of goods sold, selling, general and administrative expenses, rent, building occupancy costs, operating interest, discontinued operations, TI depreciation and equipment, etc.
- e.  $\text{Gross Revenues} - \text{Cost of Goods} = \text{Gross Profit}$ ;  $\text{Gross Profit} - \text{Total Operating Expenses} = \text{Net Profit from Operations}$ ;  $\text{Net Profit from Operations} - \text{Non-Operating Expense} = \text{Pre-Tax Income}$
- f. Considering other variables that can affect business value: revenue growth over the last 3-5 years, future book of business, new patents, expansion of customer base or product base; reduction of competition or increase of competition, market share, goodwill value, etc.
- g. Financial Ratios can include Price to Earnings, Asset to Liability ratio and others
- h. Give Detailed Example of a Business Valuation

### **Resources:**

- a. *Introduction to Commercial Real Estate Sales*, by Bill W. McCoy III, Dearborn Real Estate Education
- b. *Commercial Real Estate, Listing Properties*, by Edward S. Smith, Jr., RECS, Dearborn Real Estate Education
- c. *Commercial Real Estate, Understanding Investments*, by Edward S. Smith, Jr., RECS, Dearborn Real Estate Education
- d. *Real Estate Investing for Dummies*, by Eric Tyson and Robert S. Griswold