

# NON-STATUTORY URBAN & RURAL VALUATION

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# Non Statutory Valuation

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## Resources

1. PowerPoint Lecture Notes
2. Slide Notes
3. Sample Valuation Sheets 1-4
4. International Valuation Standards
5. Any University Valuation text book
  1. The Appraisal of Real Estate-Appraisal Institute
  2. The Appraisal of Rural Property-Appraisal Institute

# Objective

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Stop!

This is not intended to teach, but to recap your knowledge of valuation for the following two reasons.

1 - Academic Knowledge: All of you have University or University-equivalent training in Valuation

2 - Practical Skills: And you have also trained for not less than two years under competent principals

I therefore invite you to share your experiences in this session.

# Objective-cont.

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Upon satisfactory completion of this course together with the other courses in this program you will be eligible for:-

- Award of the Diploma of the ISK
- Full Membership of the ISK
- Registration and Licensing by the VRB
- Registration and Licensing by the EARB



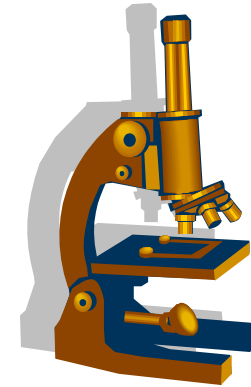
# Introduction

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What is valuation ?

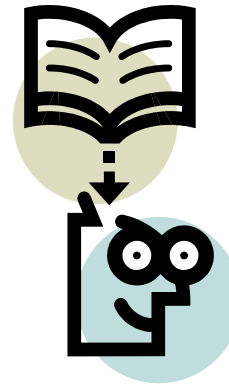
A Science ?

An Art ?



Non Statutory Valuation

No statutory direction ?



Urban Valuation

Rural Valuation

# Introduction

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## Types of Assets:

### 1 - Real Estate (Fixed Assets)

Land, Buildings and site works (improvements)  
Permanent Crops, Forests, Quarries? etc

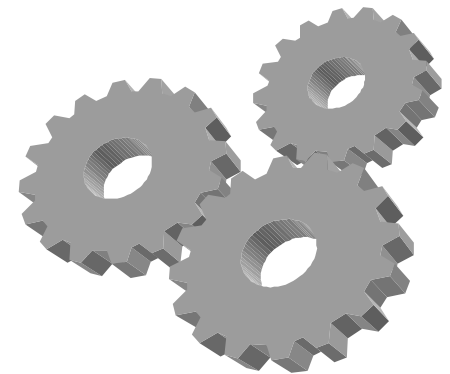
### 2 - Chattels (Movable Assets)

Plant and Machinery, Equipment  
Furniture, Fittings and Stock

### 3 - Business

### 4 - Intangible Assets

Goodwill e.t.c.



# Real Property Ownership

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## Freehold Interest/Absolute Proprietorship

- Perpetual ownership
- No rent payment

## Leasehold Interest

- Ownership defined by term (period)
- Payment of consideration

## Co-ownership

- Joint tenancy
- Tenancy in common



# Purposes of Valuation

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## Market Value

- Sale/Purchase
- Mortgage Lending
- Accounting (book keeping)

## Rental Value

- Rent negotiation
- Rent dispute resolution- tribunals

## Insurance Value

- Replacement
- Indemnity

**Note: Purposes of valuation are innumerable**





# Nature of Value

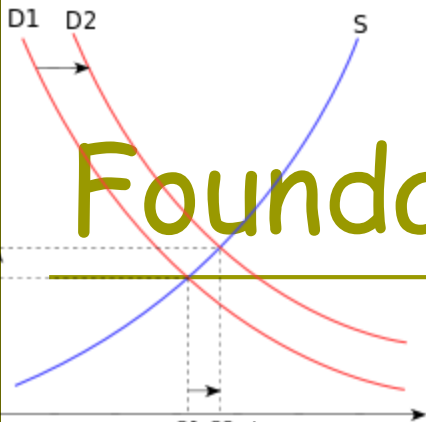
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Price, Cost and Value

## Factors of Value:

1. Utility
2. Scarcity
3. Desire
4. Effective purchasing power

# Foundation of Valuation



**1 - The principle of supply and demand**

**2 - Factors that Influence Real Property Values**

1. Social factors
2. Economic factors
3. Governmental controls and regulations
4. Environmental factors

# Markets and Neighborhoods

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**Real Estate Markets, Money Markets, and Capital Markets**

**Market Areas, Neighborhoods, and Districts**

# Market Value.

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International Valuation Standards - 1 January,  
2012



The estimated amount for which an asset or liability should exchange on the valuation date between a willing buyer and a willing seller in an arm's length transaction after proper marketing wherein the parties had each acted knowledgeably, prudently and without compulsion.

# Definitions-cont.

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## Highlights of the definition



The **estimated** amount-value/price  
An asset should **exchange-transaction**  
On the valuation **date**  
Between a **willing buyer**  
And a **willing seller**  
In an **arm's-length** transaction- *special purchaser?*  
After **proper marketing- why?**  
Where the parties had each acted **knowledgeably,**  
**prudently**  
And **without compulsion**

# Highest and Best Use

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## Fundamental Questions to ask:

- 1 - Should the land be developed or left vacant? (if yes) then,
- 2 - What kind of improvements should be built?

*-The highest and best use is the use of an asset that maximises its productivity and that is possible, legally permissible and financially feasible*

*-The highest and best use may be for continuation of an asset's existing use or for some alternative use.*

# Three Bases of Value

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(a) Exchange in a free and open market.

*Market value.*



(b) Entity specific: may have no relevance to market participants in general.

*Investment value and special value*

(c) The price reasonably agreed between two specific parties.

*Fair value as*

# Other Values

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## **IVS 2 Valuation bases other than market value.**

*Investment Value*

*Fair Value*

*Special Value*

*Synergistic Value*



## **Other Valuation provided by valuers.**

*Mortgage Lending Value*

*Forced Sale Value*

*Insurance Value*



# Other Values.

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## **Mortgage Lending Value:**

The value of the property as determined by the valuer making a prudent assessment of the future marketability of the property by taking into account long-term sustainability aspect of the property, the normal and local marketing conditions, and the current use and alternative appropriate uses of the property. Speculative elements may not be taken into account in the assessment of the mortgage lending value.

The mortgage lending value shall be documented in a transparent and clear manner.

(This is also cited: Directive 98/32/EC of the European Parliament and of the Council of 22 June 1998)

# Other Values.

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## Liquidation or Forced Sale Value:

The amount that may reasonably be received from the sale of a property within a time frame too short to meet the marketing time frame required by the market value definition. In some states, forced sale value in particular may also involve an unwilling seller and a buyer or buyers who buy with knowledge of the disadvantage of the seller.

The term Liquidation/Forced Sale Value is defined under the 6th Edition of the IVS but has subsequently been expunged from the 8th Edition of IVS (current edition).

# Assumptions

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## **Assumptions**

### **Special assumptions**

Assumptions and special assumptions must be reasonable and relevant having regard to the purpose for which the valuation is required.

# Valuation Process

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## 1 Terms of Reference

- Instructions-must be clear and understood
- Defines the purpose of the valuation
- Forms the basis of valuation and the methodology

## 2 Inspection

- Objective is to understand the property
- Collect all the facts of the property
- Includes: searches at Land Registries and Local Authorities

# Valuation Process-cont.

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## **3 Information**

Development parameters- Highest and best use  
Comparables (sales, lettings, costs), planning parameters, etc  
The quality of your valuation lies here

## **4 Data analysis/Calculations**

Sales comparison, Income capitalization, Cost Approach  
Reconciliation of the value indications-Final value estimate  
(the judgment)

## **5 Report the value**

Should meet your clients requirements.

# Methods of Valuation

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## 1 Market Approach

provides an indication of value by comparing the subject asset with identical or similar assets for which price information is available.

## 2 Income Approach

provides an indication of value by converting future cash flows to a single current capital value.

## 3 Cost Approach

provides an indication of value using the economic principle that a buyer will pay no more for an asset than the cost to obtain an asset of equal utility, whether by purchase or by construction.

# Methods of Valuation - cont.

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## Other Methods

- Profits
- Residual
- Discounted Cash Flows etc

**These are variations of the three methods above.**

# Market Approach-Steps:

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1 Comparables

2 Adjust for differences

- Financing terms
- Condition of sale
- Market condition
- Location
- Physical characteristics
- Income characteristics

3 Apply to subject

4 Market Value

1 Subject Property

2 Apply Comparable

3 Adjust for differences

- Financing terms
- Condition of sale
- Market condition
- Location
- Physical characteristics
- Income characteristics

4 Market Value



# Market Approach-Example:

## ANALYSIS AND APPLICATION OF COMPARABLES To value LR 14970/D In Evergreen Estate bordering Runda

Comparable					Application		
LR Number	Date	Acre	Price	Value per sqft	Acre	value	Call
14970/A Evergreen	Apr-08	0.4873	6,500,000	306	0.7868	10,494,929	10,500,000
7785/B Runda	Sep-07	0.4964	6,500,000	301	0.7868	10,302,139	10,300,000
7785/C Runda	Nov-07	0.7425	9,000,000	278	0.7868	9,536,562	9,500,000
<b>Average</b>				295	0.7868	10,111,210	9,766,667
<b>CALL</b>							<b>9,500,000</b>
Discount 5% for inferior immediate road 5% for shape disadvantage							8,550,000
Market Value- call							8,500,000

# Income Approach-

## Steps:

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Arriving at a value by multiplying the incomes from the property by suitable multipliers.

You must understand the (sub) market.

1. Establish the total income flows
2. Establish the reviews
3. Establish voids which are lettable and give rent
4. Establish the rate of return
5. Apply the rate of return to the incomes

# Income Approach-

## Steps:

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### Rental Incomes

#### Rent reserved

- Reviews if any
- Protected tenancy

#### Market rent

- Comparable rentals

#### Outgoings

- Actual outgoings
- Market

Usually expressed per annum

### Rate of return

#### Rate of return:

- Net Income/Sale Price
- Expressed in %

#### YP:

- Sale Price/Annual Income
- Expressed as ratio

#### You need to obtain:

- Comparable sales
- Comparable lettings

Differs for each (sub) market

# Income Approach-

## Steps:

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### 1-Valuation of property not under lease

1. Establish the market rent of the property pa
2. Establish the rate of return (or YP)
3. Multiply YP (or inverse of rate of return) with the rent
4. Result: **Market Value**

# Income Approach-

## Example:

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### Simple Calculation

$$MV = \text{Market Rent pa} \times YP$$

Market Rental Value	120,000
	<u>x12</u>
Annual Income	1,440,000
Less o/g @15%	<u>216,000</u>
Net income	1,224,000
YP@6% in perp	<u>16.667</u>
Capital Value	20,400,400
<i>Call</i>	<i>20,500,000</i>

### Or Simple Calculation

$$MV = \text{Market Rent pa} \times YP$$

Market Rental Values	120,000
	<u>x12</u>
Annual Income	1,440,000
YP@7% in perp	<u>14.286</u>
Capital Value	20,571,840
<i>Call</i>	<i>20,500,000</i>

# Income Approach-

## Steps:

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### 2 Valuation of leased Property

#### 1 - Term

Establish all the fixed period incomes

Rent reserved  
(contract)

Reviews

Protected

Apply appropriate rate of return

*Usually a lower rate of return since rent is secured*

#### 2 - Reversion

Market rent

Apply market rate of return deferred by term

*Usually higher than term since the rent after contract is rather riskier*

*Note: Do not loose focus:- the rate of return is market driven*

# Income Approach-

## Example:

### Valuation-property under lease

#### Term (first 2 years)

Rent Reserved	5,000sq.ft@50/-pm	3,000,000 pa	
YP in 2yrs @6%		<u>1.8334</u>	5,500,200

#### Review (next 3 years)

Rent Reserved review	5,000sq.ft@55/-pm	3,300,000 pa	
YP in 3yrs @6.5%	2.6648		
PV 2yrs @ 6.5%	<u>0.8816</u>	<u>2.3493</u>	7,752,649

#### Reversion to perp.

Market Rental Value	5,000sq.ft@60	3,600,000	
YP in reversion to perp. after 5yrs @7%		<u>8.8964</u>	<u>32,027,404</u>
Capital Value			45,279,889

#### Call

**45,500,000**

# Cost Approach - Steps

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This is arrived at by summing up

- 1 Market Value of Land
  - From sales comparison approach
- 2 Depreciated Replacement Cost of the Developments
  - Gross Replacement Cost
  - Less Accumulated Depreciation



# Cost Approach - Steps

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## Sources of data

### Land

sales comparison; from Estate Agents, records etc

### GRC

Quantity surveyors-IQSK

Ministry of Public Works

Contractors

Completed projects

### **Depreciation**

Physical deterioration of the structure

Obsolescence

Change in environment

**(Most difficult to measure)**

# Cost Approach -

## Example:

### Obtaining DRC Rate (comparable)

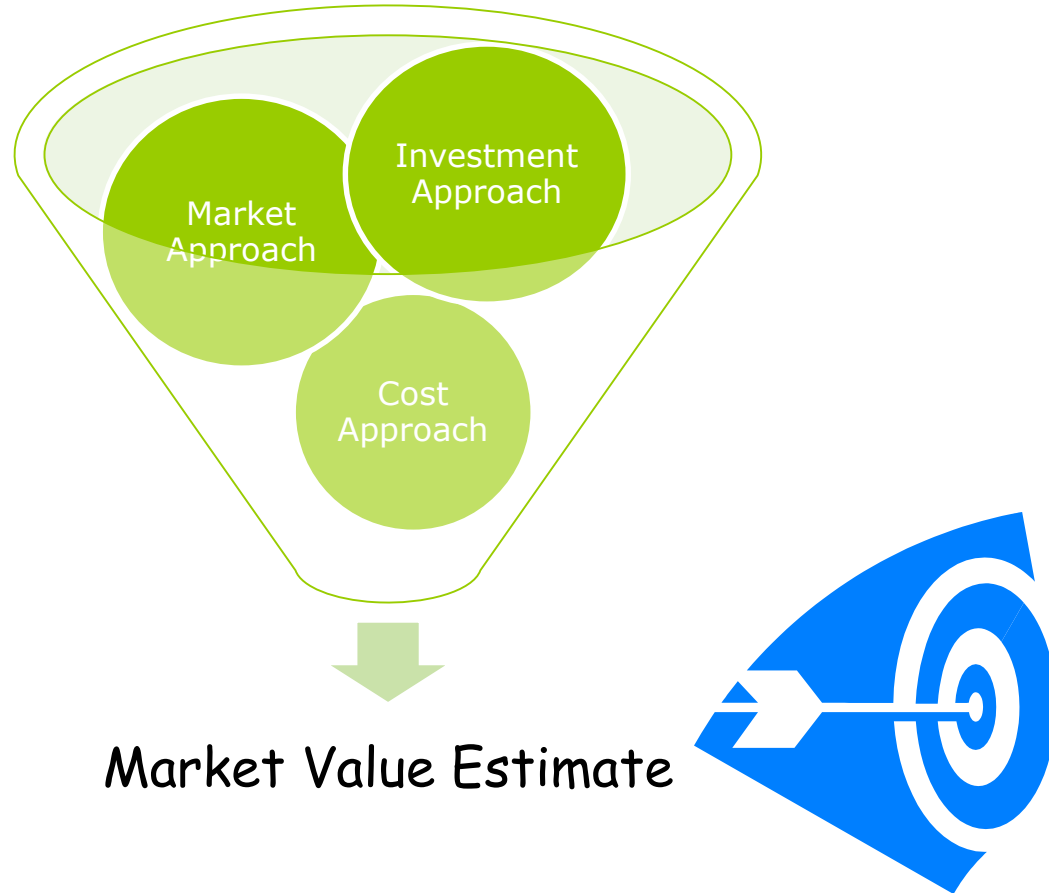
Sale Price	5,000,000
Less	
Land 0.045 ac	<u>1,500,000</u>
DRC-improvts	
	3,500,000
Less Siteworks	<u>400,000</u>
Building	3,100,000
1,200_sqft	<u>/1,200</u>
Rate psf	2,583

### Application to DRC Valuation

Building 1,500 sq.ft.	
@2,583/-	3,874,500
Site works	
Wall 177sqft@2,000	
Parking 265sqft@250	
	<u>420,000</u>
	4,294,500
Land 0.035 ac	<u>1,400,000</u>
Total	5,694,500
Call	<b>Kshs.5,700,000</b>

# Reconciliation of Values:

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# Insurance Valuation -

Stand alone unit:

## **Reinstatement Clause**

re-building costs

Demolition and removal of debris,  
preparation of site and professional fees

**Loss of rent/cost of alternative accommodation**  
over reconstruction period



## **Inflation Clause**

<b>E.G.</b>	<b>Replacement Cost</b>	
	Building 2,000 sq.ft.@3,000/-	Kshs.6, 000,000/-
	Site works	Kshs. <u>350,000/-</u>
	Total	Kshs.6,350,000/-
	Debris removal@5%	Kshs 320,000/-
	Loss of rent 18 months@ 30,000	<u>Kshs. 540,000/-</u>
		Kshs.7,210,000/-

# Insurance Valuation -

## Apartment:

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### *Reinstatement Clause*

Market Value

*Loss of rent/cost of alternative accommodation  
over replacement period*

### *Inflation Clause*

<b>E.G</b>	Market Value	Kshs.5, 000,000/-
	Loss of rent 18 months @ 30,000	<u>Kshs. 540,000/-</u>
		Kshs.5, 540,000/-



# Sample Valuations

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- Maisonette
- Apartment
- Office Block
- Petrol station

# Agricultural Property - Valuation Process

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## Valued in the normal way

- Sales Comparison Approach
- Income Capitalization Approach
- Cost Approach



# Agricultural Property- Challenges

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## Sales Comparisons Approach

- Sales- too few or non existent
- Difficulty in comparison due to diversity- (Adjustments)
- Sizes- too large
- Climate, whether dependent

## Cost Approach

- This is an easier method and most preferred.
- Sale of land is still less frequent
- Obtaining cost data
- Calculating depreciation
- Cost of trees, crops

## Income Capitalization Approach

- Sales- too few or non existent
- Determination of rent/income is difficult. (too many outgoings, erratic incomes dependent on external factor e.g. rainfall, diseases etc).
- Obtaining rate of return - (multiplier). Absence of sales, diversity in comparisons, complexity,



# Report Writing

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## **Land, Buildings & Siteworks**

- LR Number
- Date of Inspection
- Terms of reference
- Definition of Terminologies
- Methodology
- Situation
- Tenure
- Registered Owner
- Encumbrances
- Area
- User
- Rates
- Services

- Land
- Development
- Built-up Area
- Occupancy
- General Remarks
- Valuation(s)

## **In addition Plant & Machinery**

- S/No.
- Remaining Useful Life

# Valuation Fees

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## The Valuers Act Cap 532

- Legal Notice No. 92
  - The Valuers (Forms and Fees) (Amendment) Rules, 2011
- Legal Notice NO. 32
  - charge as per the scale of fees
- Build your profession.

# Emerging Issues

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International Valuation Standards & ISK  
International Measurements Standards

# Appendix

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Professional Practice and Law  
Financial Formulas

# Examinations Preparation

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## Read Past Papers

### Section A

Q1 - Compulsory General Questions-	25mks
Q2 - Either (Optional) (Urban Valuation)-	25mks
Q3 - Or (Optional) (Agricultural Valuation)	25mks
<b>Total</b>	<b>50%</b>