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COMMERCIAL BIG BOX

A GUIDE TO MARKET BASED VALUATION



COMMERCIAL BIG BOX

- KENNETH VOSS, MAI, SRA, AI-GRS, CAE
- KVOSSATL@AOL.COM
- 404-869-7970 (OFFICE)
- 404-822-9595 (CELL)

COMMERCIAL BIG BOX

WHAT WE ARE GOING TO TALK ABOUT TODAY

- DEFINITIONS
- HIGHEST AND BEST USE
- METHODOLOGY
- TRANSACTIONS
- MARKET SEGMENTATION

PREPARATION IS THE KEY TO SUCCESS

BOY SCOUT MOTTO: BE PREPARED!

DEFINITION: BIG BOX

- A BIG BOX FACILITY IS ESSENTIALLY A BIG BOX WHEN VIEWED FROM ABOVE
- GENERALLY OPEN WITH HIGH CEILINGS, MINIMAL INTERIOR FINISH, CONCRETE FLOOR, FLUORESCENT LIGHTING, HVAC, SPRINKLERS, LOADING DOCKS
- NORMALLY A SINGLE USER STORE, TYPICALLY 10,000 AND 100,000 SQUARE FEET OR MORE
- NUMEROUS IMPROVEMENTS FIT THIS CRITERIA; THE KNOWN BIG BOXES INCLUDE: HOME DEPOT, LOWE'S, AT HOME, BRANDS-MART, WALMART, TARGET, SPORTS AUTHORITY, BEST BUY, SEARS, JC PENNEY, DICKS, GANDER MOUNTAIN, K-MART, CABELA'S, KOHLS, ET AL.

DEFINITION: BIG BOX

- APPRAISERS TEND TO ASSUME THAT ALL BIG BOX PROPERTIES ARE THE SAME
- THESE PROPERTIES, IN THE EYES OF THE OWNER AND APPRAISER TEND TO HAVE DIFFERENT VALUES BASED UPON CURRENT USE CONCEPT OF MARKET VALUE
- NO SINGLE DEFINITION
- REFERS TO LARGE SCALE, STAND ALONE RETAIL ESTABLISHMENTS

DEFINITION: BIG BOX

- **BIG BOX CATEGORIES**
- **DISCOUNT DEPARTMENT STORES**
- **REFERRED TO AS GENERAL MERCHANDISE STORES**
- **NORMALLY RANGE IN SIZE FROM 80,000 TO 200,000 SQUARE FEET**
- **WALMART, K-MART, TARGET, ETC.**

DEFINITION: BIG BOX

- **SPECIALITY STORES**
- **ALSO CALLED “CATEGORY KILLERS”**
- **SIZE RANGE FROM 20,000 TO 120,000 SQUARE FEET**
- **BARNES & NOBLE, TOYS “R” US, LOWE’S, HOME DEPOT, ETC.**

DEFINITION: BIG BOX

- OUTLET STORES
- SIZE RANGE FROM 20,000 TO 80,000 SQUARE FEET
- NIKE, BURLINGTON COAT FACTORY, ETC.

DEFINITION: BIG BOX

- **WAREHOUSE CLUBS**
- **SIZE RANGE FROM 100,000 TO 200,000 SQUARE FEET**
- **COSTCO, SAM'S**

DEFINITION: BIG BOX

- **POWER CENTER**
- **GROUPING OF VARIOUS BIG BOX RETAILERS**
- **SIZE RANGE FROM 250,000 TO 1,000,000 SQUARE FEET**
- **CONTAINS AT LEAST FOUR ANCHOR STORES**
- **TRADE AREA 5 – 10 MILES**

DEFINITION: BIG BOX

- REGIONAL CENTER
- SMALL GROUPING OF BIG BOX RETAILERS, BUILT AROUND TWO OR MORE ANCHORS
- SIZE RANGE FROM 400,000 TO 800,000 SQUARE FEET
- USUALLY ENCLOSED
- TRADE AREA 5 – 15 MILES

DEFINITION: BIG BOX

- **SHOPPING CENTER**
- **GROUP OF RETAIL AND OTHER COMMERCIAL PROPERTIES THAT ARE PLANNED, DEVELOPED AND MANAGED BY ONE GROUP**
- **SIZE RANGE IS BASED ON DEMOGRAPHICS AND LOCATION**
- **GENERALLY ENCLOSED CENTERS OR OPEN-AIR MALLS**
- **TRADE AREA 5 – 25 MILES**

DEFINITION: BIG BOX

- **BIG BOX CHARACTERISTICS**
- **LARGE FREE-STANDING. SINGLE FLOOR, ON A CONCRETE SLAB**
- **LARGE WINDOWLESS, RECTANGULAR SHAPED BUILDING**
- **FLAT ROOF, STEEL WITH CONCRETE BLOCK WALLS**
- **SIZE RANGE FROM 50,000 TO 200,000 SQUARE FEET**
- **LAND-TO-BUILDING RATIO: 4:1 AND HIGHER**

DEFINITION: FEE SIMPLE

- FEE SIMPLE IS A TERM OF OWNERSHIP
- FEE SIMPLE IS NOT A TERM OF OCCUPANCY
- FEE SIMPLE IS NOT A TERM OF VALUE
- FEE SIMPLE IS A PROPERTY RIGHTS CONCEPT
- FEE SIMPLE OWNERSHIP MAY BE SUBJECT TO MARKET RENT OR CONTRACT RENT
- WHEN THE FEE SIMPLE INTEREST IS VALUED, IT IS MARKET VALUE. THE PRESUMPTION IS THAT THE PROPERTY IS AVAILABLE TO BE LEASED AT MARKET RATES

DEFINITION: LEASED FEE

- **LEASED FEE INTEREST**
- **IF THERE IS ARE LEASES IN PLACE, EVEN AT MARKET RATES AND TERMS, THE INTEREST IS A LEASED FEE INTEREST, THAT IS, FEE SIMPLE WITH A LEASE.**
- **ONCE A PROPERTY IS LEASED, THE OWNER NO LONGER HAS THE RIGHT TO LEASE OR RIGHT TO OCCUPY THE PROPERTY, UNTIL THE END OF THE LEASE.**
- **WHAT THE APPRAISAL PROFESSION REFERS TO AS LEASED FEE IS REALLY JUST FEE SIMPLE SUBJECT TO A LEASE.**

DEFINITION: LEASE

- **LEASE IS A POSSESSORY RIGHT THAT DOES NOT DIMINISH FEE SIMPLE OWNERSHIP**
- **A LEASE AND THE RENT IT PROVIDES TO THE FEE SIMPLE OWNER IS A BENEFIT TO THE OWNER AND THE PRIME REASON FOR THE INVESTMENT.**
- **THE LESSEE HAS THE BENEFIT OF POSSESSION OF SPACE IN WHICH TO OPERATE THEIR BUSINESS.**
- **A LEASE MAY IMPACT VALUE, BUT HAS NOTHING TO DO WITH FEE SIMPLE**

DEFINITION: BUNDLE OF RIGHTS

- **BUNDLE OF RIGHTS: CONSIDER THE BUNDLE OF STICKS AS A PIN CUSHION.**
- **THE PIN CUSHION REPRESENTS "FEE SIMPLE." THE CUSHION MAY HAVE LEASES, EASEMENTS, ETC. THAT WILL TRANSFER WITH THE SALE OF A PROPERTY.**
- **THE TRANSFER IS STILL FEE SIMPLE, SUBJECT TO A DEED RESTRICTION, EASEMENT, LEASE, OR WHATEVER THE ENCUMBRANCES MAY BE.**

DEFINITION: HIGHEST AND BEST USE

- **A THEORETICAL CONCEPT THAT UNDERLIES VALUATION ANALYSIS. AN APPRAISER MUST FIRST PERFORM GENERAL MARKET ANALYSIS IN ORDER TO ANALYZE THE CHARACTERISTICS OF THE MARKET THAT CAUSE THE SUBJECT PROPERTY TO HAVE VALUE.**
- **HIGHEST AND BEST USE IS THE USE THAT GENERATES THE HIGHEST NET RETURN TO THE PROPERTY OVER A REASONABLE PERIOD OF TIME.**

DEFINITION: HIGHEST AND BEST USE

- A PRINCIPLE OF APPRAISAL AND ASSESSMENT REQUIRING THAT EACH PROPERTY BE APPRAISED AS THOUGH IT WERE BEING PUT TO ITS MOST PROFITABLE USE. GIVEN PROBABLE LEGAL, PHYSICAL, AND FINANCIAL CONSTRAINTS.
- THE PRINCIPLE ENTAILS FIRST IDENTIFYING THE MOST APPROPRIATE USE, AND, SECOND THE MOST PROFITABLE USE WITHIN THAT MARKET.
- THE CORRECT DETERMINATION OF ITS HIGHEST AND BEST USE IS ONE OF, IF NOT THE MOST IMPORTANT STEPS IN THE APPRAISAL PROCESS.

DEFINITION: HIGHEST AND BEST USE

- **HIGHEST AND BEST USE IS DEFINED BY IAAO AS:**
- **A PRINCIPLE OF APPRAISAL AND ASSESSMENT REQUIRING THAT EACH PROPERTY BE APPRAISED AS THOUGH IT WERE BEING PUT TO ITS MOST PROFITABLE USE (HIGHEST POSSIBLE NET PRESENT VALUE) GIVEN PROBABLE LEGAL, PHYSICAL, AND FINANCIAL CONSTRAINTS. THE PRINCIPLE ENTAILS IDENTIFYING THE MOST APPROPRIATE MARKET, AND SECOND THE MOST PROFITABLE USE WITHIN THAT MARKET.**

DEFINITION: HIGHEST AND BEST USE

- THE CORRECT DETERMINATION OF THE HIGHEST AND BEST USE IS ONE OF, IF NOT THE MOST IMPORTANT STEPS IN THE APPRAISAL PROCESS.
- HIGHEST AND BEST USE SHOULD NOT BE ASSUMED TO BE THE CURRENT USE.
- WHEN YOU TRANSITION FROM MASS APPRAISAL TO SINGLE PROPERTY APPRAISAL FOR PURPOSES OF DEFENDING AN APPEAL, THE DETERMINATION OF THE HIGHEST AND BEST USE IS REQUIRED AS PART OF THE PROCESS.
- THIS ANALYSIS MUST BE DONE ON THE SUBJECT PROPERTY AND THE POTENTIAL COMPARABLE PROPERTIES USED TO ESTIMATE THE VALUE.

DEFINITION: HIGHEST AND BEST USE

- **PHYSICAL POSSIBLE**
- **LEGALLY PERMISSIBLE**
- **FINANCIALLY FEASIBLE**
- **MAXIMALLY PRODUCTIVE-GENERATING HIGHEST RETURN TO THE OWNER**

DEFINITION: HIGHEST AND BEST USE

- **PHYSICALLY POSSIBLE**
- **THE FIRST STEP IN DETERMINING THE HIGHEST AND BEST USE OF A SITE IS TO IDENTIFY THE PHYSICALLY POSSIBLE USES OF THE SITE.**
- **CHECK TOPOGRAPHY, CONFIGURATION, ETC.**
- **MOST ANY USE RELATIVE IN SIZE IS PHYSICALLY POSSIBLE**

DEFINITION: HIGHEST AND BEST USE

- **LEGALLY PERMISSIBLE**
- **WHICH OF THE PHYSICALLY POSSIBLE USES ARE LEGALLY PERMISSIBLE.**
- **CHECKING THE ZONING CLASSIFICATION, SETBACKS, LOT COVERAGE, BUILDING HEIGHT, ETC.**
- **THE ZONING CLASSIFICATION DETERMINES WHAT CAN BE PUT THERE, THE APPRAISER DETERMINES WHAT CAN PHYSICALLY BE CONSTRUCTED.**

DEFINITION: HIGHEST AND BEST USE

- **FINANCIALLY FEASIBLE**
- **THE APPRAISER SHOULD HAVE A GROUP OF POTENTIAL USES, THAT IS, PHYSICALLY POSSIBLE AND LEGALLY PERMISSIBLE**
- **THE APPRAISER MUST DETERMINE WHICH OF THESE USES ARE FINANCIALLY FEASIBLE.**
- **THE GREATEST INFLUENCE ON POSSIBLE DEVELOPMENT OF THE SUBJECT SITE ASSUMING IT IS UNIMPROVED, IS THE ZONING, LOCATION WITHIN A COMMERCIAL CORRIDOR AND THE NEIGHBORING USES**
- **NOTE: THE PRINCIPLE OF CONFORMITY SUGGESTS THAT A CONFORMING USE WILL PRODUCE THE MAXIMUM RETURN FOR AN OWNER.**

DEFINITION: HIGHEST AND BEST USE

- **MAXIMUM PRODUCTIVITY**
- **THE TEST OF MAXIMUM PRODUCTIVITY IS APPLIED TO THOSE USES THAT HAVE PASSED THE FIRST THREE TESTS.**
- **OF THE FINANCIALLY FEASIBLE USES, THE HIGHEST AND BEST USE IS THE USE THAT PRODUCES THE HIGHEST RESIDUAL LAND VALUE CONSISTENT WITH THE MARKET'S ACCEPTANCE OF RISK AND WITH THE RATE OF RETURN WARRANTED BY THE MARKET FOR THAT USE GIVEN THE ASSOCIATED RISK.**

DEFINITION: HIGHEST AND BEST USE

- **MAXIMUM PRODUCTIVITY-EXAMPLE**
- **THE SUBJECT SITE HAS CURRENT DEMAND FOR APARTMENTS AND DEMAND FOR RETAIL IS ESTIMATED IN FIVE (5) YEARS, IN THE FUTURE, THE HIGHEST AND BEST USE CAN BE TESTED BY USER SALES DATA.**
- **APARTMENT LAND IS SELLING FOR \$3.50/PSF TODAY TO USERS AND RETAIL LAND IS SELLING FOR \$7.50/PSF TO USERS.**
- **IF THE LAND WAS HELD FOR FIVE (5) YEARS AT A DISCOUNT RATE OF 20%, THE PRESENT VALUE OF RETAIL LAND IS \$3.00/PSF (5-N, 20-I, 1-FV, 0-PMT, PV-0.4019, X \$7.50), WHICH SUGGESTS THE HIGHEST AND BEST USE TODAY IS TO DEVELOP APARTMENTS OF THE SITE.**
- **THE USE THAT PRODUCES THE HIGHEST RESIDUAL LAND VALUE IS THE HIGHEST AND BEST USE.**

METHODOLOGY

- **THE SALES COMPARISON APPROACH IS A PROCESS WHEREBY PRICES AND RENTS ACTUALLY PAID FOR PROPERTIES SIMILAR TO THE SUBJECT ARE USED TO ESTABLISH AN INDICATED VALUE FOR THE PROPERTY YOU ARE APPRAISING.**
- **THIS APPROACH HAS ITS FOUNDATION IN THE PRINCIPLE OF SUBSTITUTION WHICH STATES THAT A PRUDENT INVESTOR WILL PAY NO MORE TO BUY OR RENT A PROPERTY THAN IT WILL COST HIM TO BUY OR RENT A COMPARABLE PROPERTY SOMEWHERE ELSE IN THE MARKET.**
- **THE SALES COMPARISON APPROACH CAN BE AN EFFECTIVE APPROACH TO VALUE, ASSUMING THE DATA GATHERED IS PROPERLY ANALYZED AND VERIFIED.**

METHODOLOGY

- **THE INCOME CAPITALIZATION APPROACH**
- **THE INCOME APPROACH IS A TECHNIQUE IN WHICH THE ANTICIPATED NET OPERATING INCOME TO BE GENERATED BY THE SUBJECT DURING ITS PROJECTED PERIOD OF OWNERSHIP IS CAPITALIZED INTO A VALUE ESTIMATE.**
- **THE ACCURACY OF THE INCOME APPROACH IS RELATED TO THE ESTIMATION OF INCOME, VACANCY, EXPENSES, AND CHARACTERISTICS OF THE NET INCOME STREAM; ITS ECONOMIC LIFE SPAN, THE CAPITALIZATION RATE (R_0); AND THE METHODOLOGY USED IN CONVERTING THE NET INCOME INTO VALUE.**

METHODOLOGY

- **INCOME APPROACH**
- **THE APPRAISER MUST MAKE AN ADJUSTMENT FOR PROPERTY TAXES.**
- **DO NOT DERIVE A CAPITALIZATION RATE FROM THE MARKET AND ADD THE EFFECTIVE TAX RATE. REMEMBER THE CAPITALIZATION RATE INCLUDES A LINE ITEM EXPENSE FOR PROPERTY TAXES, THEREFORE, YOU MUST MAKE AN ADJUSTMENT.**
- **IF RESERVES FOR REPLACEMENT ARE INCLUDED YOU MUST CONSIDER MAKING AN ADJUSTMENT, AS MOST FINANCIAL STATEMENTS DO NOT INCLUDE A LINE ITEM EXPENSE FOR RESERVES.**

METHODOLOGY

- **COST APPROACH TO VALUE**
- **STEP #1: AN ESTIMATE OF THE MARKET VALUE OF THE LAND**
- **IN ORDER TO ESTIMATE THE MARKET VALUE OF THE SUBJECT LAND, ASSUME THE LAND IS UNIMPROVED AND AVAILABLE FOR DEVELOPMENT TO ITS HIGHEST AND BEST USE..**
- **THE APPRAISER MUST ASSEMBLE DATA FOR THE SALE OF SIMILARLY LOCATED UNIMPROVED PROPERTIES SURROUNDING THE SUBJECT PROPERTY.**
- **COMPLETE A LAND SALES GRID CHART, EXPLAINING THE FOLLOWING: TIME/MARKET CONDITIONS, SIZE, PHYSICAL CONDITION, ZONING, AND LOCATION.**

METHODOLOGY

- **COST APPROACH-CONTINUED**
- **STEP #2: ESTIMATE THE COST OF REPLACING THE EXISTING IMPROVEMENTS UNDER CURRENT MARKET CONDITIONS**
- **THE APPRAISER NORMALLY WILL USE 'REPLACEMENT COST.'**
- **THE REPLACEMENT COST ESTIMATES ARE GENERALLY ON A SQUARE FOOT BASIS, WHICH INCLUDES "SOFT COSTS" SUCH AS ARCHITECT'S FEES, CONTRACTOR'S OVERHEAD AND PROFIT, INTEREST DURING CONSTRUCTION AND LOAN FEES.**

METHODOLOGY

A DEVELOPER IS MOTIVATED BY THE ANTICIPATION OF PROFIT, WHETHER HIS EFFORT WILL BE REWARDED OR NOT. ESSENTIALLY, ENTREPRENEURIAL PROFIT IS A MARKET DERIVED FIGURE THAT REFLECTS THE AMOUNT THE ENTREPRENEUR, OR DEVELOPER, EXPECTS TO RECEIVE IN ADDITION TO COSTS.

DEPENDING UPON THE MARKET PRICE, THIS TYPE OF PROFIT MAY BE MEASURED AS A PERCENTAGE OF--

- 1. DIRECT COSTS**
- 2. DIRECT AND INDIRECT COSTS**
- 3. DIRECT AND INDIRECT COSTS PLUS LAND VALUE**
- 4. VALUE OF THE COMPLETED PROJECT**

METHODOLOGY

- **ENTREPRENEURIAL PROFIT**
- **DIRECT AND INDIRECT COSTS, A FIGURE MUST BE ADDED WHICH REPRESENTS THE ENTREPRENEURIAL OR DEVELOPER'S PROFIT FEE.**
- **A DEVELOPER IS MOTIVATED BY THE ANTICIPATION OF PROFIT, WHETHER OR NOT HIS EFFORT MAY BE REWARDED.**
- **ESSENTIALLY, ENTREPRENEURIAL PROFIT IS A MARKET DERIVED FIGURE THAT REFLECTS THE AMOUNT THAT THE ENTREPRENEUR, OR DEVELOPER, EXPECTS TO RECEIVE IN ADDITION TO COSTS.**
- **DEPENDING ON THE AREA, THE PROFIT MAY BE MEASURED AS: 1. A PERCENTAGE OF DIRECT COSTS; 2. DIRECT AND INDIRECT COSTS; 3. DIRECT AND INDIRECT COSTS PLUS LAND VALUE; OR 4. THE VALUE OF THE COMPLETED PROJECT.**

METHODOLOGY

- **STEP #3: DEPRECIATION**
- **AN ESTIMATE OF DEPRECIATION FROM ALL CAUSES WHICH INCLUDES PHYSICAL DETERIORATION, FUNCTIONAL OBSOLESCENCE AND EXTERNAL OBSOLESCENCE.**
- **PHYSICAL DEPRECIATION: DETERIORATION AS EVIDENCED BY WEAR AND TEAR, DECAY, DRY ROT, CRACKS, ENCRUSTATION, OR STRUCTURAL DEFECTS**

METHODOLOGY

- **PHYSICAL DEPRECIATION-CONTINUED**
- **CURABLE (DEFERRED MAINTENANCE) ITEMS OF WEAR AND TEAR ON A PROPERTY THAT SHOULD BE FIXED NOW TO PROTECT THE VALUE OR INCOME PRODUCING ABILITY OF THE PROPERTY.**

METHODOLOGY

- **PHYSICAL DEPRECIATION-CONTINUED**
- **INCURABLE (SHORT LIVED ITEMS) COMPONENTS OF THE BUILDING STRUCTURE WHICH HAVE SHORT LIVES, INCLUDING ROOF, PARKING LOT, HVAC, FLOOR COVERING/FINISH, ETC.**
- **INCURABLE (LONG LIVED ITEMS) A BUILDING COMPONENT OR SITE IMPROVEMENT EXPECTED TO HAVE THE SAME USEFUL LIFE AS THE ENTIRE STRUCTURE**

METHODOLOGY

- **USEFUL LIFE:** THE PERIOD OF TIME OVER WHICH A STRUCTURE OR A COMPONENT OF A PROPERTY MAY REASONABLY BE EXPECTED TO PERFORM THE FUNCTION FOR WHICH IS WAS DESIGNED.
- **ACTUAL AGE:** THE NUMBER OF YEARS THAT HAVE ELAPSED SINCE CONSTRUCTION OF AN IMPROVEMENT (HISTORICAL OR CHRONOLOGICAL AGE)
- **EFFECTIVE AGE:** THE AGE OF PROPERTY THAT IS BASED ON THE AMOUNT OF OBSERVED DETERIORATION AND OBSOLESCENCE IT HAS SUSTAINED, WHICH MAY BE DIFFERENT FROM ITS CHRONOLOGICAL AGE.
- **REMAINING ECONOMIC LIFE:** THE ESTIMATED PERIOD OVER WHICH EXISTING IMPROVEMENTS ARE EXPECTED TO CONTRIBUTE ECONOMICALLY TO A PROPERTY; AN ESTIMATE OF THE NUMBER OF YEARS REMAINING IN THE ECONOMIC LIFE OF A STRUCTURE AS OF THE EFFECTIVE DATE OF VALUE
- **REMAINING USEFUL LIFE:** THE ESTIMATED PERIOD DURING WHICH IMPROVEMENTS WILL CONTINUE TO PROVIDE UTILITY.

METHODOLOGY

- **FUNCTIONAL OBSOLESCENCE: FUNCTIONAL OBSOLESCENCE MAY BE DUE TO POOR FLOOR PLAN DESIGN, MECHANICAL INADEQUACIES OR SUPER-ADEQUACIES, FUNCTIONAL INADEQUACIES OR SUPER-ADEQUACIES DUE TO SIZE, STYLE, AGE, ETC.**
- **NOTE: ARGUMENTS OF LIMITED NUMBER OF POTENTIAL USERS WITHOUT SIGNIFICANT MODIFICATION; THIS COULD LEAD TO EXTERNAL OBSOLESCENCE (NOT ACHIEVING SUFFICIENT INCOME)**

METHODOLOGY BEFORE RETROFIT

Photo taken 5/28/2014



METHODOLOGY AFTER RETROFIT



METHODOLOGY

- **EXTERNAL OBSOLESCENCE**
- **EXTERNAL OBSOLESCENCE IS CAUSED BY CHANGES EXTERNAL TO THE PROPERTY SUCH AS CHANGES IN PROPERTY TYPE, LAND USE, LEGISLATION, ETC.**
- **A CALCULATION OF EXTERNAL OBSOLESCENCE COMPARES THE NET OPERATING INCOME ASSUMING A MARKET RENTAL RATE AND MARKET VACANCY ALLOWANCE TO THE NET OPERATING INCOME NECESSARY TO SUPPORT THE DEPRECIATED REPLACEMENT COST.**
- **NOTE: ANY ESTIMATE OF EXTERNAL OBSOLESCENCE WILL BE CLOSELY TIED TO THE INCOME APPROACH.**

METHODOLOGY

• DEP. REPLACEMENT COST NEW	\$3,643,881
• REPRESENTATIVE RO	<u>8.0%</u>
• NOI REQUIRED TO JUSTIFY NEW CONSTRUCTION	\$ 291,510
• PROJECTED NET OPERATING INCOME	<u>\$ 166,049</u> (FROM INCOME APPROACH)
• NET OPERATING INCOME DIFFERENTIAL	\$ 125,461
• REPRESENTATIVE RO	<u>8.0%</u>
• INDICATED EXTERNAL OBSOLESCENCE	\$1,570,000 (ROUNDED)
• CALCULATION OF EXTERNAL OBSOLESCENCE	

TRANSACTIONS: BUILD-TO-SUIT

- **BUILD-TO-SUIT SALES ARE BASED UPON THE ACTUAL CONSTRUCTION COSTS INCLUDING THE COST OF THE UNDERLYING SITE (LAND). THE FACILITIES ARE CONSTRUCTED BASED ON A PROTO-TYPE BUILT TO THE EXACT STANDARDS AND DESIGN OF THE RETAILER GOING INTO OCCUPANCY.**

TRANSACTIONS: SALE-LEASEBACK

- **SALE-LEASEBACK IS THE SIMULTANEOUS PURCHASE OF PROPERTY AND LEASE BACK TO THE SELLER. THE LEASE PORTION OF THE TRANSACTION IS GENERALLY LONG-TERM.**
- **THE SELLER-LEASEE IN THE TRANSACTION IS CONVERTED FROM AN OWNER TO A TENANT.**
- **EXAMPLE: ABC CORPORATION OWNS AN OFFICE BUILDING. IT ARRANGES A SALE-LEASEBACK FOR THE BUILDING SITE WITH XYZ PENSION FUND. ABC RECEIVES CASH AND A 25-YEAR LEASE TO THE SITE. XYZ RECEIVES AN INCOME STREAM FOR 25-YEARS AND A REVERSION OF THE PROPERTY AT THE END OF THE LEASE.**

TRANSACTIONS: SECOND GENERATION LEASED FEE SALES

- **THESE SALES REPRESENT LARGE RETAIL SPACES LEASED TO SECOND GENERATION TENANTS PRIOR TO THE DATE OF SALE. THE MAJORITY OF THESE PROPERTIES WERE ORIGINALLY CONSTRUCTED FOR ANOTHER MAJOR RETAILER. AFTER THE TENANT VACATED THE PREMISES , THE PROPERTY WAS SOLD TO AN INVESTOR.**
- **SIMILAR TO THE BUILD-TO-SUIT SALES, SALES IN THIS CATEGORY WILL BE DRIVEN BY THE NEGOTIATED LEASE RATE AND THE CREDIT WORTHINESS OF THE TENANTS.**
- **THESE TYPE OF SPACES WILL VARY DEPENDING UPON WHICH PARTY PAYS FOR TENANT FINISH/RETROFIT.**
- **IF A COSTLY RETROFIT/RENOVATION IS FINANCED BY THE LANDLORD AND AMORTIZED OVER THE LEASE TERM, SALE PRICES MAY APPROACH THE SALE PRICES REFLECTED BY BUILD-TO-SUIT SALES.**

TRANSACTIONS: FEE SIMPLE SALES

- **THESE SALES REPRESENT TRANSACTIONS INVOLVING PROPERTIES THAT WERE VACANT AT THE TIME OF THE SALE. THESE SALES PROVIDE A RELIABLE INDICATION FOR A VACANT BUILDING.**
- **THE PURCHASER OF SUCH A FACILITY MAY BE ANOTHER RETAILER (TYPICALLY LOWER QUALITY) THAT PLANS TO OCCUPY THE SPACE "AS IS" OR WITH LIMITED RENOVATION.**
- **MANY OF THESE PROPERTIES ARE PURCHASED BY ENTREPRENEURS THAT MAY HAVE A USE/TENANT FOR THE FACILITY AND PLANS TO LEASE THE BALANCE TO OTHER TENANTS,**
- **SPECULATORS PURCHASE THESE PROPERTIES IN THE HOPE OF TURNING THEM INTO "SECOND GENERATION SALES."**

TRANSACTIONS: DEED RESTRICTED SALES

- **DEED RESTRICTION: A PROVISION WRITTEN INTO A DEED THAT LIMITS THE USE OF THE LAND. DEED RESTRICTIONS USUALLY REMAIN IN EFFECT WHEN THE TITLE PASSES TO SUBSEQUENT OWNERS.**
- **IF THE SUBJECT IS NOT UNDER ANY RESTRICTION AND THE COMPARABLE IS, THE RESTRICTION ELIMINATES VIABLE USES FOR A SIGNIFICANT TIME PERIOD. IT IS DIFFICULT TO ADJUST FOR RESTRICTION. RESTRICTIONS ARE DESIGNED TO LIMIT POSSIBLE USES OF THE PROPERTY.**
- **KEY FACTOR: THE RESTRICTION MAY HAVE CHANGED THE HIGHEST AND BEST USE, AND YOU DO NOT KNOW HOW MANY POTENTIAL USERS NEVER CONSIDERED THE PROPERTY BECAUSE OF THE RESTRICTIONS.**

MARKET SEGMENTATION

- INVESTMENT CLASS A
- FIRST GENERATION SPACE
- VERY GOOD LOCATIONS
- LONG-TERM LEASES, NNN
- NATIONAL OR REGIONAL TENANTS
- ATTRACTS NATIONAL INVESTORS, SUCH AS REITS, RETIREMENT FUNDS, ETC.
- THESE ARE THE BEST PROPERTIES THAT DEMAND HIGH RENTS, AND WHEN SOLD, WILL COMMAND THE HIGHEST PRICES AND LOWEST CAPITALIZATION RATES (R0)

MARKET SEGMENTATION

- **INVESTMENT CLASS B**
- **FIRST GENERATION SPACE**
- **SLIGHTLY OLDER, GOOD LOCATIONS**
- **REMAINING LEASE TERMS EXCEED 10-YEARS**
- **ATTRACTS NATIONAL AND REGIONAL TENANTS**
- **MAY BE DESIRABLE FOR NATIONAL INVESTORS.**
- **THESE MAY STILL BE FIRST GENERATION PROPERTIES IN LESS DESIRABLE LOCATIONS.**

MARKET SEGMENTATION

- **INVESTMENT CLASS C**
- **NEARING THE END OF THEIR ECONOMIC LIFE FOR FIRST GENERATION SPACE**
- **MAY BE CLASSIFIED AS SECOND GENERATION SPACE**
- **LESS DESIRABLE RETAIL LOCATIONS**
- **REMAINING LEASE TERMS LESS THAN 10-YEARS.**
- **PROPERTIES SELL AT THE LOW END AND THE CAPITALIZATION RATES ARE AT THE HIGH END.**
- **THE CONTINUED USE AS A BIG BOX IS AN INTERIM USE.**

MARKET SEGMENTATION

- **INVESTMENT CLASS D**
- **CLASSIFIED AS SECOND GENERATION SPACE**
- **SELL AT LOW PRICES**
- **OFTEN VACANT OR SOON TO BE VACANT**
- **ORIGINAL MARKET DEMAND FOR THESE PROPERTIES HAS MOVED TO MORE DESIRABLE RETAIL LOCATIONS OR NEEDS DIFFERENT SIZE BUILDING FOOTPRINT.**

VALUATION METHODOLOGY

FIRST GENERATION

- CLASS A COST, INCOME , MARKET
- CLASS B COST, INCOME, MARKET
- CLASS C UNLIKELY HIGHEST & BEST USE
- CLASS D UNLIKELY HIGHEST & BEST USE

SECOND GENERATION

- CLASS A UNLIKELY HIGHEST & BEST USE
- CLASS B UNLIKELY HIGHEST & BEST USE
- CLASS C INCOME & SALES
- CLASS D INCOME & SALES

TYPICAL BIG BOX DATA-WALMART

TWO SETS OF MARKET SALES DATA

- 1. SALES OF UNOCCUPIED BIG BOX STORES (DARK)**
- 2. SALES OF OPERATING STORES WITH LONG-TERM NNN LEASES IN PLACE**

TYPICAL BIG BOX DATA-WALMART

1. SALES OF UNOCCUPIED BIG BOX STORES (106 SALES)

PERIOD: JANUARY 1, 2011 TO JUNE 25, 2016

RANGE OF SALES: \$8.72/PSF TO \$66.84/PSF

MEDIAN: \$26.08/PSF

MEAN: \$27.73/PSF

2. SALES OF OPERATING STORES WITH LONG-TERM NNN LEASES IN PLACE (96 SALES)

PERIOD: JANUARY 1, 2011 TO JUNE 25, 2016

RANGE OF SALES: \$48.92/PSF TO \$371.78/PSF

MEDIAN: \$104.58/PSF

MEAN: \$127.07/PSF

TYPICAL BIG BOX DATA-WALMART

SALES OF UNOCCUPIED BIG BOX STORES (106 SALES), SUBSEQUENT USE

<u>CATEGORY</u>	<u>NUMBER OF SALES</u>	<u>AVERAGE SALE PRICE/PSF</u>
BIG BOX TO BIG BOX	49	\$27.13
CONVERSION TO MULTI-TENANT	19	\$27.82
CONVERSION TO ALTERNATE USE	27	\$28.60
VACANT	11	\$28.22

TYPICAL BIG BOX DATA-WALMART

SALES OF UNOCCUPIED BIG BOX STORES (IMPACT OF DEED RESTRICTIONS)

<u>CATEGORY</u>	<u>NUMBER OF SALES</u>	<u>MEDIAN SP/PSF</u>	<u>AVERAGE SP/PSF</u>
DEED RESTRICTED	39	\$25.17	\$26.22
NO DEED RESTRICTIONS	52	\$28.38	\$28.84

QUESTIONS AND ANSWERS

PREPARATION