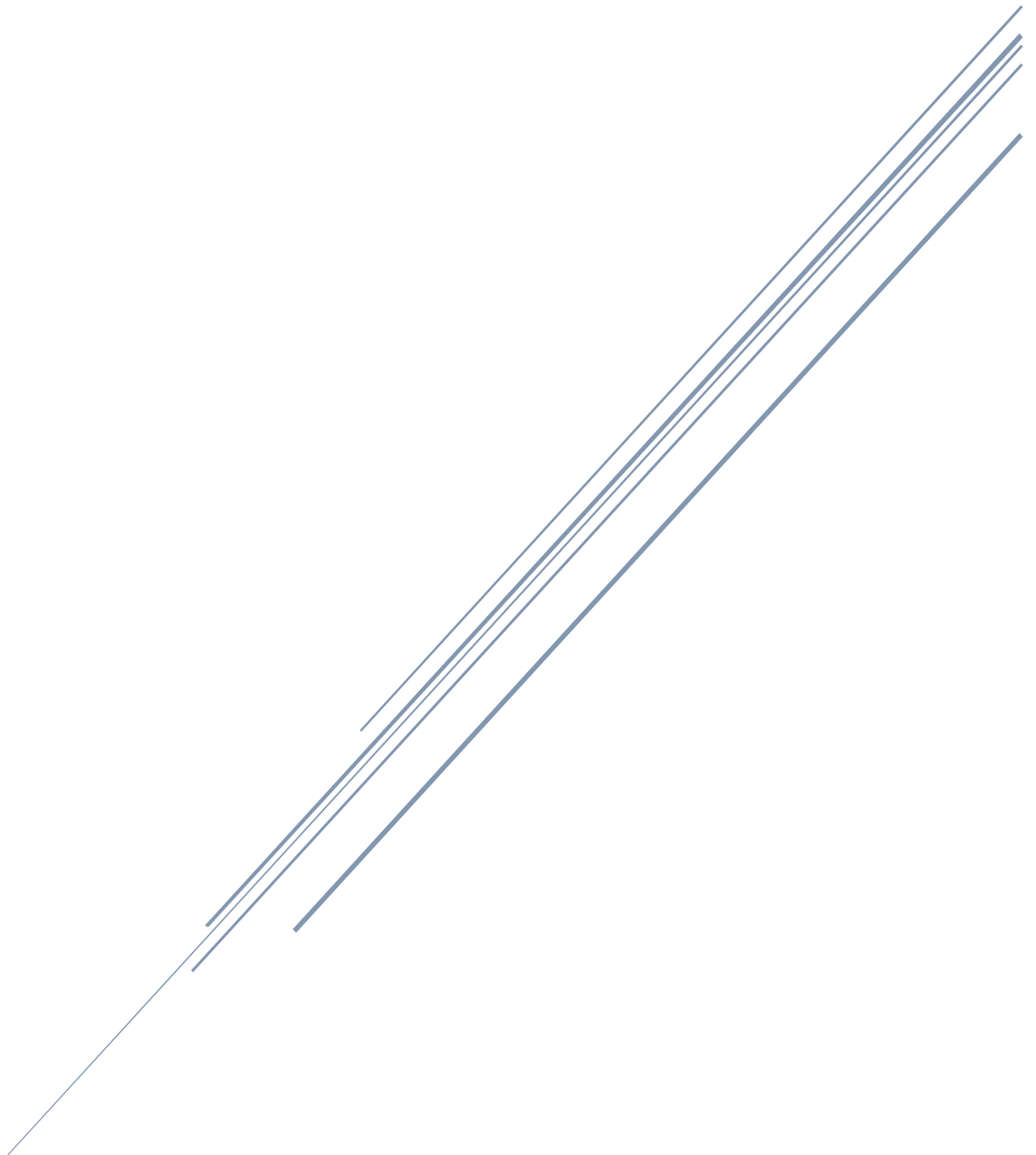


# Real Estate Valuation: The Case of a Marina with Development Potential

Capstone Project

Ms in Finance



## **Project introduction**

My capstone project was completed at the capital markets division of a multinational, commercial real estate firm in Budapest. I got to participate in a project where the firm represented a seller side client and was hired to value, market, and sell their property. The subject property consisted of multiple plots of land at the shore of Lake Balaton with its own, operating marina. With the existing local building regulations the property had great potential for further developments creating value for the land. Due to the information sensitivity of the project, the report summarizes the findings and results without specific numbers.

## **Main tasks**

The main task of the capstone project was to determine the market land value of the property based on the existing development plan of the current owner. The development plan consisted of both residential units in the form of villas and apartments as well as a high end hotel. The final findings would be presented to the current owners of the property in a commonly used real estate document format known as a brokerage opinion valuation (BOV). The creation of the valuation model required the completion of multiple other tasks beforehand based on my own online research and by accessing internal company data. This included the research for key input variables that would directly affect the final outcome of the model, which in this case were the expected investment yield, unit gross development values, and unit construction costs individually for the development's residential and hotel components. Furthermore, the consideration of transaction comparables focused on presenting former real estate deals with similar characteristics to the subject property. This consisted of both online research for publicly available past deals as well as the firm's own internal data source. The completion of the project also required me to gather information and data from various professionals within the company mainly through shorter in person meetings.

The main valuation model was based on the residual valuation method which took into account the potential development value of the property then deducted all of its costs associated with buildings and operating together with the developer's expected profit margin to finally arrive at the land value of the property. The created valuation model was excel based with complete result responsiveness to changes in any of the input variables. Importantly, the residential units and hotel were separately valued, as they were created based on different modeling assumptions. Whilst the residential units assumed a basic construction and selling timeline, for the hotel the valuation was based on an exit yield following the construction and short operation

of the hotel with a management contract. The project also allowed me to compare the yield based discount rate technique used by the commercial real estate industry with the capital asset pricing model recommended by the financial theory and literature. Whilst the two techniques ultimately produced different valuation results, the advantage and situation appropriateness of each technique became more evident. Similarly, the use of debt financing for the construction of the development project was also examined through a market assumed loan structure, in order to highlight the use of leverage on the valuation. Due to the cheaper financing cost of debt, the leverage based development resulted in a higher land valuation.

Furthermore, an important question for the future developer of the property remained regarding the marina's operation during the building phase. The financial statements of the currently operating firm were taken into consideration, with the assumption that only the sailing boat related services would remain in the future to be in line with the new development's high end profile. The valuation focused on an income based discounted cash flow model, which was projected into the next five years with a growing perpetuity based terminal value. Lastly, I was responsible for finding contact details to a list of potential foreign investors, which included both investment firms and individuals. This was an important task of the project, as the subject property would be later marketed to them with the hopes of raising interest and receiving bids from them.

### **Final results**

Finally, the gathered information and the results of the valuation model were converted into the formerly mentioned BOV report format. The BOV consisted of 13 pages, following the structure of former company reports. The format consisted of a title page where the property was briefly described with key information, followed by an executive summary which highlighted the key findings on one slide, then slides with key inputs, a map for location description, a current macroeconomic overview of Hungary's real estate market, possible financing conditions in case of leverage, a table of transaction comparables with relevant comments, and finally the results of the valuation broken down into separate components. This report is to be shared with the current owners of the property, which should clarify the main reasons for the current market value of their property and also aid their thinking on the expected selling price they would be eventually ready to accept. In addition to the BOV report, the company also received the excel document containing all of the collected data with calculations

and the valuation models. In case of further requirements or changes in the owner's development plan the models may be adjusted accordingly.

### **Project reflection**

Taking initiative and being proactive in finding a capstone project that fit my personal interest was an important step to cooperate with a sponsor where I could perform to the best of my abilities and feel constantly motivated to strive for further challenges. The completion of the project also further convinced me about the intellectual value of the masters program at CEU, as I was able to identify the tasks and situations which related to topics covered throughout the program. Even more so, in some cases I was able to apply the financial theories to real life tasks. On the other hand, my capstone project gave me the opportunity to get a glimpse at and experience some of the diverse tasks carried out by a real estate firm. Furthermore, with the possibility to work on the project from the company's office, I was able to connect with numerous real estate professionals from various fields. I believe that the possibility for onsite project completion may be an important factor to consider, as it presents a great opportunity to get a feeling of the company's day to day dynamics. I was also fortunate enough to have a mentor like capstone supervisor who got me engaged in some other company related activities besides the capstone project, including a sell side property visits to meet potential investors and an internal education training. Most importantly, during the process of the project I was further convinced that a career in the real estate industry is the path I wish to pursue in the future. I also feel great pride for having the opportunity to contribute to a capstone project, which may even influence the final outcome of a major real estate transaction. This way I know that my submitted result materials were not only considered by the university from an academic perspective, but also used in practice by the company.