Monthly Meetup "5-Star Mastery" – April 2024

"Multi-Family Valuator" with Nick Skalkos

Nick's introduction to multi-family buildings with Scott McGillivray

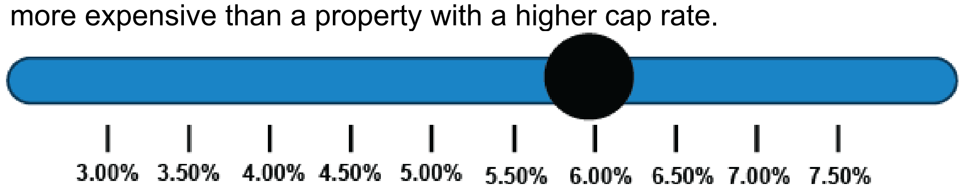
- Through his connection with Keyspire, Nick bonded with Scott McGillivray over music. One day, Scott invited Nick to go look at multi-family buildings together.
- As they looked at property after property, Nick noticed that Scott would use his calculator quickly.
- Scott explained that he was calculating the value of the property using cap rates.

In this Monthly Meetup, Nick shares two quick calculations he uses to help him decide whether he wants to consider a multi-family building more thoroughly:

1. **Determine the actual value of the multi-family property**
2. **Where your primary sources of income are coming from**

What Is a Cap Rate?

- The capitalization rate that your income producing property is bought and sold at. Cap rate is set by the market and is different for every market.
- You can use the relationship between a property's NOI and cap rate to determine the property's value if you know what cap rates similar properties (those of similar vintage and asset class) are trading for in that submarket.
- For instance, if a property is at a 10 cap rate, that could mean that it would take 10 years for the investor to recoup the investment. Alternatively, if it's at a 3.5 cap rate, it would take the investor 3.5 years to recoup the investment.
- Do not get overwhelmed by the definition of "cap rate" – instead focus on how you can use cap rates to determine the actual value of a property.
- In terms of pricing, a property that has a lower cap rate, generally means that the property is more expensive than a property with a higher cap rate.



Multi-Family Building

- A multi-family building that has 5 or more units requires commercial financing.
- When looking at multi-family unit, you need to assess its actual value using an income approach. To do this, you need the cap rate and NOI.

Where to Find Cap Rates and NOI

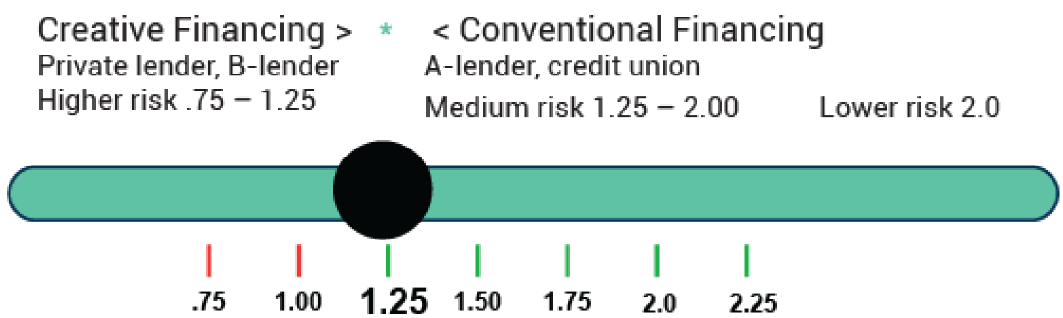
- Your goal is to find the cap rate that an appraiser would use to value a property. There is no one correct cap rate, so you'll have to look at different sources and find a range, and value the property for that range.
- You can look up cap rates online (for instance, CMHC and Turner Drake in Canada). You can also check in with your realtor to see if they have access to this information.
- You can get the NOI from the property listing if it's available or from the realtor.

How To Find the Value of A Multi-Family Building

- To figure out the value of a property, you need to divide the NOI by the cap rate.

How Are You Going to Finance a Multi-Family Building? DSCR

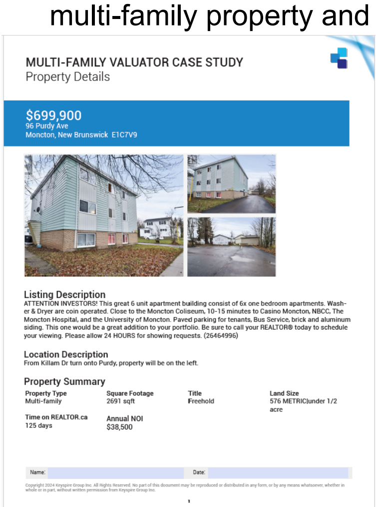
- Institutional lenders will only finance a multi-family building if it’s not too risky. For them to determine this, they need to know what the debt service coverage ratio (DSCR) is.
- A DSCR is a metric used in commercial and multi-family real estate to calculate a project’s cash flow compared to its expenses. DSCR is one of the primary metrics used to underwrite commercial and multi-family real estate loans.
- To calculate DSCR, you need to divide NOI by the Total Debt Service.



- If the property gets a DSCR score of 1.25 or higher, then you know you can get financing through an A-lender.
- If you plan on adding value to a property and you get a DSCR that a conventional lender wouldn’t finance, you might consider creative financing for the first little bit, until you can raise the NOI of the property and obtain conventional financing then.

Case Study:

- In this session, members were asked to review a case study to determine the value of a multi-family property and determine the DSCR based on that property value.


MULTI-FAMILY VALUATOR CASE STUDY
Property Details

$699,900
96 Purdy Ave
Moncton, New Brunswick E1C7V9

Listing Description
ATTENTION INVESTORS! This great 6 unit apartment building consist of 6x one bedroom apartments. Washer & Dryer are coin operated. Close to the Moncton Coliseum, 10-15 minutes to Casino Moncton, NBCC, The Moncton Hospital, and the University of Moncton. Paved parking for tenants, Bus Service, brick and aluminum siding. This one would be a great addition to your portfolio. Be sure to call your REALTOR® today to schedule your viewing. Please allow 24 HOURS for showing requests. (26464996)

Location Description
From Killam Dr turn onto Purdy, property will be on the left.

Property Summary

Property Type	Square Footage	Title	Land Size
Multi-family	2691 sqft	Freehold	576 METRIC|under 1/2 acre
Time on REALTOR.ca	Annual NOI		
125 days	$38,500		

Name: Date:

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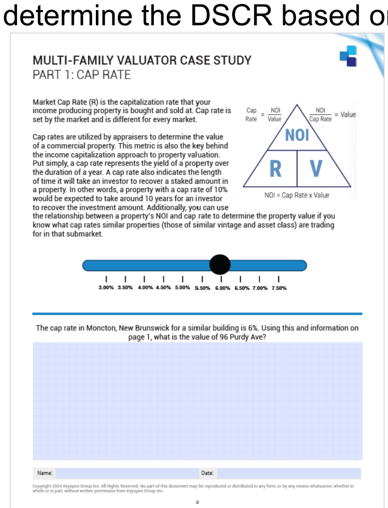
MULTI-FAMILY VALUATOR CASE STUDY
PART 1: CAP RATE

Market Cap Rate (R) is the capitalization rate that your income producing property is bought and sold at. Cap rate is set by the market and is different for every market.

Cap rates are utilized by appraisers to determine the value of a commercial property. This metric is also the key behind the income capitalization approach to property valuation. Put simply, a cap rate represents the yield of a property over the duration of a year. A cap rate also indicates the length of time it will take an investor to recover a staked amount in a property. In other words, a property with a cap rate of 10% would be expected to take around 10 years for an investor to recover the investment amount. Additionally, you can use the relationship between a property’s NOI and cap rate to determine the property value if you know what cap rates similar properties (those of similar vintage and asset class) are trading for in that submarket.

Cap Rate = NOI / Value
NOI / Cap Rate = Value
NOI
R
V
NOI = Cap Rate x Value

3.00% 3.50% 4.00% 4.50% 5.00% 5.50% 6.00% 6.50% 7.00% 7.50%

The cap rate in Moncton, New Brunswick for a similar building is 6%. Using this and information on page 1, what is the value of 96 Purdy Ave?

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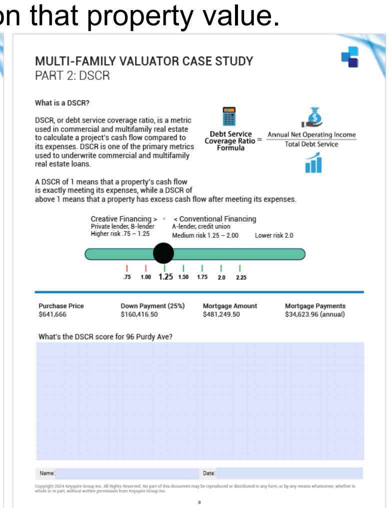
MULTI-FAMILY VALUATOR CASE STUDY
PART 2: DSCR

What is a DSCR?

DSCR, or debt service coverage ratio, is a metric used in commercial and multifamily real estate to calculate a project’s cash flow compared to its expenses. DSCR is one of the primary metrics used to underwrite commercial and multifamily real estate loans.

Debt Service Coverage Ratio Formula = Annual Net Operating Income / Total Debt Service

A DSCR of 1 means that a property’s cash flow is exactly meeting its expenses, while a DSCR of above 1 means that a property has excess cash flow after meeting its expenses.

Creative Financing > < Conventional Financing
Private lender, B-lender
Higher risk .75 – 1.25
A-lender, credit union
Medium risk 1.25 – 2.00
Lower risk 2.0
.75 1.00 1.25 1.50 1.75 2.0 2.25

Purchase Price	Down Payment (25%)	Mortgage Amount	Mortgage Payments
$641,666	$160,416.50	$481,249.50	$34,623.96 (annual)

What’s the DSCR score for 96 Purdy Ave?

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- Solutions:
  - Value of property:
  - DCSR solution: $38,500 (NOI) / $34,623 (Total Debt Service) = 1.11

Group Discussion

- Understanding the Numbers: Participants emphasized the importance of thoroughly understanding and analyzing the financial numbers associated with multi-family real estate investments, including cap rates, debt service coverage ratios (DSCR), and Net Operating Income (NOI)
- Creative Financing Strategies: The discussion highlighted various creative financing options, such as working with A and B lenders, seller financing, and strategies to increase NOI to appeal to banks or potential buyers.
- Rezoning and Property Zoning: The conversation delved into the complexities of rezoning properties and seeking opportunities in commercial real estate by understanding the zoning regulations and navigating the planning authorities.
- Building a Robust Understanding of the Market: Participants emphasized the significance of building a robust understanding of the local real estate market, evaluating opportunities, and seeking to demystify the complexities often associated with evaluating multi-family properties.
- Collaboration and Networking: The importance of reaching out to peers, networking, and seeking opportunities to connect with others in the real estate business was highlighted as a key aspect of maximizing the Keyspire experience.
- Due Diligence and Deal Structuring: The conversation emphasized the importance of due diligence, understanding the four ways to win, and structuring deals based on current property performance rather than potential future scenarios.
- Turnkey Investments: The discussion touched on the concept of turnkey investments, the need for a specific investor profile for such investments, and the importance of analyzing the numbers to determine the viability of turnkey opportunities.