What is Value?

- Price
  - Asking or Selling
  - One person’s assessment of value
- Cost
  - Actual amount paid or actual cost to build or improve
- Value is defined as the power of a good or service to command other goods or services when exchanged in the marketplace

Types of Value

- Investment value
  - The value to a specific investor based on that investor’s requirements
- Insurable value
  - The value of those parts that are physically destructible (reproduction or replacement)
- Assessed value
  - Value established by a tax assessor
- Liquidation value
  - The likely price that could be realized in a forced sale
- Fair Market Value (FMV)

Market Value

- The most probable price a property would bring in a competitive and open market under all conditions requisite to a fair sale, the buyer and seller each acting prudently and knowledgeably, and assuming the price is not affected by undue stimulus. (The Appraisal Foundation)
- Also:
  - Both parties motivated
  - Both parties informed and acting in own self interest
  - Reasonable time for market exposure
  - Payment in cash
  - No unusual financing concessions
  - The value used for loan underwriting purposes

Key Value Considerations

- What is highest and best use?
  - Residential or commercial?
  - Depends on the party and the property
  - Highest and best use can be affected by improvements
  - Positive and negative!
  - Understand what you are buying to know what to pay

Common Valuation Methods for B&B’s and Inns

- Gross Revenue Multiplier (GRM)
- Price per Room (PPR)
- Cost / Asset Approach
- Capitalization Rate (cap rate)
- Financial and investment analysis
- Combination of all of the above
  - Informed by marketplace knowledge
  - Small B&B’s affected by local real estate values
  - Larger inns affected more by cash flow; have a more national marketplace
**Using the Tools: GRM**

- **GRM: Gross Revenue Multiplier**
  - Sale / asking price divided by gross revenues equals GRM for that B&B/inn
  - Price is $1,000,000 and room revenues are $200,000
  - $1,000,000 / $200,000 = 5.0 GRM
- Or this way:
  - Revenues are $200,000
  - You will accept GRM of 6
  - $200,000 x 6 = $1,200,000
- GRM can range from 2-10 or higher; 4-6 for businesses
- Does not consider condition, innkeeper’s quarters, land, other amenities

**Using the Tools: PPR**

- **PPR: Price per Room**
  - Sale / asking price divided by number of rooms equals price per room
  - Price is $1,000,000; 10 rooms.
  - $1,000,000 / 10 = $100,000 per room
- OR, comparable PPR times number of rooms suggests a price
  - 10 rooms; comparable PPR is $150,000
  - 10 x $150,000 = $1,500,000
- This is a crude, unreliable tool for B&Bs, which are all unique; works best for hotels / motels

**Using the Tools: Cost / Asset Approach**

- Reliable tool for lifestyle B&B's that considers most valuable assets first
- Value of real estate (as residence) plus one year’s gross room revenue if revenues exceed value of trade fixtures (FF&E, furniture, fixtures, & equipment)
- Real estate worth $500,000. FF&E worth $50,000. Gross revenues = $75,000.
- Revenues exceed value of FF&E (trade fixtures). $500,000 + $75,000 = $575,000

**Using the Tools: Cost / Asset Approach (cont)**

- Variation: value of all hard assets (RE, FF&E) plus one year’s net operating income (NOI)
- Quick lesson: Gross revenue minus operating expenses = NOI (net operating income before debt service, depreciation, owner’s compensation)
- Same as previous slide, but NOI is $30,000
- $500,000 (RE) + $50,000 (FF&E) + $30,000 (NOI) = $580,000
- Yield similar values and good tool for lifestyle B&B’s where you know the value of the house; pay premium for business

**Using the Tools: Cap Rate**

- Best quick tool to assess viability (and ability to finance) a B&B/inn business. Measures profitability
- Does not work for small, lifestyle inns
- Cap rates (on room revenue) for quality inns range 8-11%. Can go higher with restaurant.
- Capitalization rate calculated by dividing NOI (net operating income) by the price, as a %

**Using the Tools: Cap Rate Example**

- Gross revenue = $225,000; operating expenses = $125,000; NOI = $100,000
- NOI / cap rate = value
- Cap rates and value are inverse
  - $100,000 / 9% cap rate (.09) = $1,111,111
  - $100,000 / 10% cap rate (.10) = $1,000,000
  - $100,000 / 11% cap rate (.11) = $909,090
- NOI / price = cap rate (does it work?)
Use the Whole Toolbox

- Similarities between valuation methods suggest a solid valuation
- Differences require interpretation
- Sometimes differences can be averaged
- Some methods may have to be discounted
- DON'T GUESS!!!

Key Factors Affecting Value

- Location
- Condition
- Income

Key Factor Affecting Price

- Motivation

Key Factor Affecting Sale

- Price
- If you get it right the first time, the rest will fall into place!

THANK YOU!