Single Family Home ("SFH") Comparative Market Analysis ("CMA") / Deal Analysis

Purpose - The whole CMA/Deal Analysis process will help determine the following key data points to truly do a deal deep dive analysis and decide if the target property is a good investment:

1. Sell Side Sales Price or After Repair Value ("ARV")
2. Rehab, Financing, Holding and Closing Costs
3. Buy Side Purchase Price Range or Maximum Allowable Offer ("MAO")
4. Flip Deal Analysis
5. Rental Deal Analysis and P&L
   a. Using the Buy, Rehab, Rent, Refinance, Repeat ("BRRRR") Strategy

Prerequisites/Inputs - To begin, you will need the following tools/data to utilize this process:

- "Deal Analysis.xlsx" template – The model that will guide and generate the deal analysis
  o When starting a new analysis save a new copy in this format "Target Property Address – Target Property City – Deal Analysis – Date" into the "Current Projects" folder in the shared Google Drive
- Target Property Address
- Access to Zillow – Property Data, Rental Comps, Zestimate (terribly inaccurate but a valuation data point sellers often quote)
- Access to the MLS – For Comparable Sales/Transactions ("Comps"), Property Data
- MAO Equation: Buy Side Purchase Price = (ARV * 70%) – Rehab Costs
  o The 30% discount is our built in margin for a flip or BRRRR

Deliverables/Outputs:

- Completed "Deal Analysis"
- Property Valuation: ARV, Rehab Estimate and Purchase Price

Process:

One of the first steps of the valuation or CMA process is to work backwards and come up with a very good estimate of the target property's ARV which is essentially the retail price of the property after repairs have been completed.   The ARV is what we estimate the property's sale price (or to appraise for during the refinance in a BRRRR) when the rehab is complete and we exit the investment via a flip or BRRRR. Once we have locked in a pretty good estimate of ARV we can back into what we should pay for the property.

Since SFHs are valued based on comps, we need to find comps that can be used to value the target property.   The key here is to try and use the same methodology that an appraiser would use as at the end of the process it is the appraiser that will make or break the deal with the comps and valuation they

set. Since the properties were are purchasing have ARVs less than $425k we are usually selling to a buyer with financing (requiring an appraisal) or refinancing ourselves (when doing a BRRRR), so the final valuation is crucial and why we aim to use the same appraisal methodology.

Here is the process L. Grace Properties ("LGP") follows to determine the comps:

1. Type address into Google and find the Zillow listing.
2. Copy the Zillow listing into the "Assumptions & Summary" tab in the "Deal Analysis" model for future reference.
3. While on the Zillow page, take all the property features and enter them into the "Assumptions & Summary" tab on "Deal Analysis" model. Features include:
   a. Address
   b. School District
   c. Square Footage
   d. Number of Beds / Baths
   e. Garage
   f. Foundation Type
   g. Taxes (make sure you gross 20-30% up for Non Homestead)
   h. Style of Property
   i. Last Sold Date (not necessary in a comp, but helpful in negotiations)
   j. Source of Lead
4. Pull up the MLS to find the comps:
   a. Go to the "Quick Search" feature and enter the address to set the geography
   b. Enter the following initial parameters:
      i. Distance = .25 Miles
      ii. Sold = 90 Days
      iii. Type = Sale
      iv. City = Type in the city
   c. If you can pull at least 2-5 results with that search, do some verification of the results:
      i. Are they on the same street or a busy/worse/better street?
      ii. Are they the same style?
      iii. Are any of them updated?
      iv. Is there anything about them that would not make them a good comp (style, beds/baths, other features)

If you're not happy with results there are several possibilities. Maybe there not enough comps in the initial parameters, or you can't find a comp that aligns with your initial assumptions or you can't find a comp that is truly comparable. If that is the case, you can adjust the search parameters:

- Move distance from .25 miles to .50 miles
- Move Sold date range from 90 to 120 or 180 (or up to 365 if needed)

Some other rules of thumb when pulling comps:

- Make sure comps are as "apples to apples" as possible
  o If a 3 bedroom, don't use a 4 bedroom comp

- o If on a corner lot/busy street try and find a similar comp
- o If the property is a 900 sq. ft. property, don't use 2,000 sq. ft. comps
- Don't base a deal on using the max per sq. ft. comp, give yourself some upside
- Sometimes there's value (or lack there of) outside of the square footage that you need to take into account
  - o Finished basement
  - o Garage
  - o Style (ranches in certain areas are highly desirable)
  - o Is it non conforming to the neighborhood, etc.
- Sometimes it helps build confidence in your comps looking at the Pending and For Sale comps. You shouldn't base your ARV on these as they are not sold transactions but they might give you confidence in your assumptions. Same goes with Zillow's "Zestimate."

If you are content with the comps, have looked at their pictures and made sure you have 2-5 "apples to apples" comps, export them into CSV/XLS and copy the data into the "Sale Comps" tab of the "Deal Analysis" file. Once the data is copied into this tab, on the "Assumptions & Summary" under the ARV ranges section you will now see potential ARV ranges (Mean, Median, Mean and Max). This is calculated based on the square footage of the target property and the price per square foot of the chosen comps. This isn't an exact science though as you will need to do more analysis. If they are really good comps, I try and set my ARV as close to mean or median but I try and make sure I have removed any outliers (distressed sales). Even if the max comp is an updated property and our project will have better finishes it is dangerous to use the max comp. That should be your deal upside. Set the ARV at or slightly above the mean/median and enter it into cell K2 (Yellow Cell).

So in the MAO equation we now have the ARV, we can proceed to estimate the Rehab cost in order to come up with our Buy Side Purchase Price.

- Buy Side Purchase Price = (ARV * 70%) – Rehab Costs

While I have tried to build a model to estimate rehab costs (see tab "Rehab Estimation" in the "Deal Analysis" model), it is not ideal. Right now we will need come up with our rough estimate and then lock in a detailed estimate once we can get a contractor to walk through the property. In a perfect world we have the contractor walk through the property before we put an offer in and not waste the seller's time or our time, but that isn't always an option. So if we can walk the property with contractor, use his quote and build a 10-20% cost overrun contingency.

If we cannot have a contractor walk the property and get a detailed rehab quote, we can do one of the following:

- Use the model on tab "Rehab Estimation" and give a 20% cost overrun contingency estimate
- Take the square foot of the target property and multiple by $30-$40
- Read J. Scott's book on Rehab Costs!
- Some things to note:
  - o Does it need a new roof?
  - o Does it need any new windows or doors? (How many?)

        o   Does it need any new mechanicals (Furnace, Hot Water, etc.)

        o   I assume we are installing a new kitchen/bath and paint, is that correct?

        o   Does it need all new electrical or plumbing?

        o   Does it need a new driveway?

        o   Is there evidence of water damage?

- Deal Breakers: Foundation issues

Once we have a decent rehab estimate (that allows for cost overruns) enter that data point into the "Assumptions & Summary" tab on the "Deal Analysis" model. Now we can now solve for the purchase price. Again, the MAO equation is:

- Buy Side Purchase Price = (ARV * 70%) – Rehab Costs

Now that we have the three main numbers in the MAO equation, let's analyze the deal. We must fill out the other assumptions that take into account whether the property is a good investment for a flip or a BRRRR. The assumptions to fill out or alter are:

- Timing:
    - Purchase Date
    - Finance Date (if different than Purchase Date)
    - Expected Sale or Refi Date
- Quality of neighborhood (for a sample key - A=Grosse Pointe, B=SCS, C=Eastpointe, D=Detroit)
- Financing terms (default is 12%)
- Financing amount (default is 100% of Purchase Price and Rehab)
- Holding costs (taxes, utilities, etc.)
- Sell Side Closing Costs (default is 8%)
- Rental Insurance Monthly Estimate (default is $1,000)
- Property Management fee (default assumes we are not self-managing and included Epic's rate of $99/mo. per property plus $750 placement fee annually)
- Vacancy Rate (default is 8% of rent)
- BRRRR Refi Amortization (default is 20 years)
- BRRRR Refi Interest Rate (default is 5.5%)
- Maintenance for Capex for BRRRR (default should be $1,000-$2,000/year)
- Rental Rate (search MLS or Zillow for comps)

After you have filled out all the assumptions, you are ready to analyze the deal. Here is what we are looking for:

- Flip - these don't have to be mutually exclusive and resources (labor, financing) can play a factor too:
    - Are we all in (purchase + rehab + financing cost) under 70%-75% of ARV?
    - Are we profiting at least $20,000?
    - Is the total Return on Invested Capital (or Cash on Cash Return) above 15%?
        - This comes into play if there's an opportunity cost to the borrowed capital. If there's not a shortage of capital then this can be adjusted.
- BRRRR
    - DSCR above 1.25%
        - This assumes we are doing a portfolio loan refi. If not, we are looking for cash flow of over $200/mo. (NOI – Financing Costs)
    - Are we all in (purchase + rehab + financing cost) under 70%-75% of ARV?
    - Can we get most of our capital back in the refi? If not, can we pay back that capital after 48 months?
    - Is the neighborhood a C+ or better (i.e. will it appreciate?)?

Once we have completed this analysis, we can play with the major assumptions (sensitivity analysis is provided to purchase price and rehab costs in the model). Most of the time we have to adjust of offer (Buy Side Purchase Price) down to make the numbers work.