

# Spring 2014

## First Assignment Form

<b>Name</b>	David Longinotti	
<b>Course</b>	Commercial Real Estate Transactions	
<u>Required Text/Reading</u>	<ul style="list-style-type: none"><li>-Section 12, Modern Real Estate Finance and Land Transfer (for 1/6/14 class)</li><li>- Article on Real Estate Financial Analysis (below, for 1/6/14 class)</li> <li>-Section 13, Modern Real Estate Finance and Land Transfer (for 1/8/14 class)</li></ul>	

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# Introduction to Real Estate Investment Deal Analysis

by [J Scott](#) on June 30, 2010 · [43 comments](#)

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Have you ever wondered what a *Pro-Forma* or a *Cap Rate* is? Are you trying to figure out what *NOI* means? Do you want to know how to calculate the various types of *ROI*, like *Cash-on-Cash Return* and *Total Return*?

If yes, then read on...

We get a lot of posts on the [BiggerPockets forums](#) asking about [evaluating deals](#) — everything from single family homes to large apartment complexes. Oftentimes, the posters and the readers of the posts have a reasonable understanding of the basic building blocks of a financial analysis, but all-too-often, I find myself (and others) reiterating some basic concepts around deal analysis.

While I love answering questions, I figured it would be easier to document the basic financial analysis process in one place, so that in the future, I can just refer readers here when they have basic questions. Below is a primer that I put together a couple years ago while I was learning the process of financial analysis; while this should by no means be considered a comprehensive review of the subject, it should serve as a good introduction for most readers.

So, without further ado, let's jump in...

## INTRODUCTION

Have you ever considered buying investment real estate? Are you curious about how you would go about analyzing the financial details of the property you are considering buying? How you would go about figuring out if the property were a good deal or rip-off?

The following is a detailed tutorial on how to do a thorough financial analysis of any multi-unit residential rental property you might be considering purchasing. While different sized properties require more or less analysis than you'll find here, the information presented in this document is the basis for analyzing any sized multi-unit residential property, from two-unit duplexes to 500-unit apartment complexes.

While this analysis will certainly work for single-family rentals (in fact, this type of analysis will work for most investments, in general), the market value of single family homes is generally determined differently than multi-family properties. The value of single family homes (investment or not) is generally determined by market "comps." Comps (or "comparables") are those properties in the same area that have similar characteristics – same floorplan, same number of bedrooms/bathrooms, equivalent garage size, same amenities, etc. So, a single family investment home will generally rise in value if similar homes in the same area are rising in value, and lose value if similar homes in the area are losing value.

Larger investment properties (those with at least two units, and especially those over four units) are priced/valued differently. The value of larger investment properties is directly related to how much income/profit it produces for its owner. So, it's possible that an apartment building in a neighborhood where house prices are dropping could be increasing in value — especially if the components of the market that drive income are improving.

The fact that multi-family properties are valued based on their income potential demonstrates how important good financial analysis of these properties is. You can't just compare your apartment building to others down the street to see how much it's worth.

I should also mention that, while this analysis will work for any multi-unit residential rental property, it is not sufficient for analyzing all types of commercial property; for things like office, industrial, or retail space, there's a lot more you need to know, and I would recommend you find some additional resources.

The goal of this document is to teach even the most novice real estate investor how to analyze the financial components of a rental property, but I expect more experienced investors will also find some good information in here.

## GATHERING YOUR INFORMATION

The first step in being able to analyze the value of a rental property is to understand what factors contribute to property value. In general, good financial analysis involves being able to input a bunch of information about your [real estate investment](#) into a financial model, and have that model kick out a bunch of information that you can then use to determine whether the investment is a good or a bad one (and whether it is the right investment for you).

Below are the very high level inputs necessary to perform a thorough financial analysis of a residential rental property:

- **Property Details:** This is information about the physical design of the property, including number of units, square footage, utility metering design, etc
- **Purchase Information:** This is basic cost information about the property you are considering, such as the purchase price, the price of any rehab or improvement work you'll need to do, etc
- **Financing Details:** These are the details of the loan you will obtain to finance the property. This includes such things as total loan amount, downpayment amount, interest rate, closing costs, etc
- **Income:** This is the detailed information about the income the property produces, such as rent payments
- **Expenses:** This is the detailed information about costs of maintaining the property, including such things as property taxes, insurance, maintenance, etc

Getting good data out of your model requires that the information you put into your model is highly reliable and accurate; gathering accurate data can often prove the difference between making the property look great on paper and look horrible.

### Pro-Forma vs Actual Data

Remember from the introduction of this tutorial that the value of multi-unit properties is directly related to how much income/profit it produces for its owner. Because of this, it's often in the seller's best interest to provide numbers that are more "appealing" than they are accurate; for

example, a seller may give high estimates of rental income or neglect to mention certain maintenance expenses to give the impression that the property is more valuable than it is.

So, part of your job is to make sure you have the best information available when doing your financial analysis.

How do you do that, you might ask?

Well, while you may rely on “pro-forma” data (basically, pro-forma means “estimated”) from the seller to kick off a discussion about a property, you should ensure that before you actually close on the property that you get actual data about income and expenses. You should ask to see previous years tax returns, property tax bills, maintenance records, etc. Hopefully all the actuals will prove similar to the pro-forma data you had previously been given, but don’t be surprised if it doesn’t. Remember, the seller is trying to make a sale, and will oftentimes get creative to make the numbers seem better than they are.

In addition to getting actual data from the seller, you should do your best to ensure there are no surprises if you were to buy the place. For example, when was the last time the property was assessed for taxes? If it was a while ago, and values have increased significantly since then, it’s possible that the property will be reassessed very soon, and property taxes will increase. Remember, even small changes to the income and expense numbers can mean big changes in your bottom line.

## Where to find your data

In terms of the input data we discussed above, here is where you should be looking for each of these:

- **Property Details:** This information should be available from the seller, but more comprehensive and detailed information can also be obtained from your local County Records Office
- **Purchase Information:** Obviously the seller is going to name a purchase price (which will likely be negotiable, of course), but the more important information here will be any upfront maintenance or improvement work that needs to be completed to ensure that the property can (or continue to) meet its income potential. While there may be no extra cost here for properties in good condition, it’s worth having the property inspected by a professional building inspector to ensure that there are no hidden issues or problems
- **Financing Details:** You’ll want to talk to your lender or mortgage broker to get an idea (or better yet a letter of approval) about the cost of the loan and the necessary downpayment
- **Income:** Details about income should come directly from the seller, but as mentioned above, don’t rely on pro-forma data for final analysis. You can also talk to the property management company currently running the property (if there is one) to get this information
- **Expenses:** Similar to income, details about expenses should come directly from the seller (last warning not to trust pro-forma data!) or the property management company

currently running the property. This is another place where a building inspector could help warn you about any major repairs that may be coming due in the near future (new roof, new heating/AC, etc)

## Example Property

While it will be your responsibility to do your own due diligence in gathering the necessary data when it comes to evaluating real properties, I'm going to take the liberty to create a fictitious apartment building for sale to use as an example for this tutorial.

Here are the high-level details on the building ([click here to download flyer](#))...

For reference, this is similar to what a seller might provide in terms of pro-forma data on a property for sale (though a good seller would hopefully have something a little more professional looking).

## Example Financing

The flyer above contains most of the data you'll need for this analysis (though again, remember that this is just pro-forma data; you'll want actual data before signing any contracts). The one thing the seller can't tell you is what your financing will look like for your property; that's something you'll need to determine with your lender or mortgage broker. For the sake of this example, let's assume we've also spoken with our lender, and have secured a loan with the following properties:

- Price: As listed in the flyer
- Improvements: \$10,000, as listed in the flyer
- Finance Amount: 80% of total cost
- Interest Rate: Fixed 7% over 30 years
- Closing costs: 2% of total property cost

Based on that here are the calculations we'll need later in our analysis:



Now, using this fictitious building and our assumed financing options, let's jump into our analysis!

## NET OPERATING INCOME (NOI)

It's now time to jump into the analysis. And one of the cornerstone metrics of RE financial analysis is "Net Operating Income" or "NOI." In short, NOI is the total income the property generates (after all expenses), not including debt service costs (loan costs). In mathematical

terms, NOI is equivalent to the total income of the property minus the total expenses of the property:

$$NOI = \text{Income} - \text{Expenses}$$

In general, NOI is calculated on a monthly basis using monthly income and expense data, and can then be converted to annual data simply by multiplying by 12. So, now that we know we need NOI, and we know that NOI is calculated using property income and expenses, let's jump into our income and expense calculations.

## Assessing Property Income

Gross income is the total income generated from the property, including tenant rent, other income from such things as laundry facilities, parking fees, etc, and any other income that your property will produce on a regular basis. From our example property, we have 8 units renting for between \$525-650 per month, as follows:



Unit	Rent
1	\$525
2	\$550
3	\$575
4	\$600
5	\$625
6	\$650
7	\$650
8	\$650

Plus, we have \$200 per month (\$2400 per year) in additional income from laundry facilities in the building, for a total monthly income of \$4700 (and annual income of \$54,000).

Because the majority of a property's income generally derives from tenant rent, it is very important that your income calculations take into account the rent you won't be collecting due to unit vacancy. In any area, there is some average vacancy rate; the vacancy rate for the property you are evaluating may be higher or lower than the surrounding area, and if it is, you need to decide how you'd like to factor that into your analysis.

For example, if building vacancy is listed as lower than average local vacancy, the first question you should ask is whether the data you are looking at is pro-forma or actual? If it's actual, what is the current management doing to keep the building filled? Is the rent lower than market rents? When do current leases expire? In any regard, you need to determine what you think is a reasonable vacancy rate going forward; my suggestion would be to err on the side of conservative for this, and not assume that your vacancy rate will be any lower than the local average vacancy rate.

So, to assess total income on the property, you want to subtract out the income that you likely won't see due to vacancy. In our example property, only 7 of the 8 units are listed as vacant (which equates to about 12% vacancy), so we'll go with that for our analysis. So, our total monthly income for this property would be:



Category	Amount
Total Monthly Income	\$4160

With the total monthly income \$4160, the total annual income would be \$49,920.

## Assessing Expenses

Now let's calculate our total expenses for this property. In general, expenses break down into the following items:

- Property Taxes
- Insurance
- Maintenance (estimated based on age and condition of property)
- Management (if you choose to employ a professional property manager)
- Advertising (to advertise for tenants)
- Landscaping (if you hire a professional landscaping company)
- Utilities (if any portion of the utilities is paid by the owner)
- Other (anything else we may have missed above)

Any expenses listed as monthly should be converted to annual, and then we can total our expenses to find the annual cost of operating the property:



So, the total annual expenses for this property would be \$12,751.

## Calculating NOI

Now that we have our total annual income and expenses for the property, we can calculate NOI using the formula above:

NOI = Income – Expenses

= \$49,920 – \$12,751

= \$37,169 (the property generates \$37,169 per year)

While NOI doesn't give you the whole picture (or even enough information to make any decisions), it is the basis for calculating most of the important metrics in our analysis.

In the next section, we'll examine those key metrics...

## COMMON RE PERFORMANCE MEASUREMENTS

We now have all the key pieces of information necessary to determine if this property meets the financial bar you've set for making an investment. If you remember from the beginning of this tutorial, I listed a number of key outputs you will want from this analysis. In this section, I will focus on the first two of these – Cash Flow and Rates of Return.

In the last section, we learned that NOI was the total income the property produced, not including the debt service (loan) costs. You might have been wondering, “Why doesn’t NOI include the expense cost of the loan, since that will ultimately affect your bottom line?”

## **Cash Flow**

The reason we don’t include debt service in the NOI calculation is that NOI dictates what level of income the property will produce *independent of the owner’s particular financing model*. Because the monthly or annual debt service amount is going to be specific to the particular financing plan (it will be dependent on the downpayment amount/percentage, interest rate, amortization schedule, etc), if we included debt service in the NOI, then NOI would only be meaningful in the context of that particular financing plan. And because different buyers will no-doubt have different financing, it’s important to have an income metric that is specific to the property, not the buyer.

That is why we have the cash flow calculation. Cash flow is equivalent to NOI adjusted for the expense of debt service. Specifically, cash flow is the NOI minus the debt service payments:

$$\text{Cash Flow} = \text{NOI} - \text{Debt Service}$$

As might now be obvious, cash flow is the total profit you will see at the end of the year from this property. As is also probably obvious, the higher your debt service payments (the larger your loan, higher your interest rate, or shorter your amortization period), the smaller your cash flow. If you pay all cash for a property (don’t take any loan), your cash flow will equal the NOI – this is the maximum cash flow on the property.

If you recall from our financing data, our monthly debt service would be \$2129 on this property, and therefore our annual debt service would be \$25,548. For this property, our cash flow would be:

$$\text{Cash Flow} = \text{NOI} - \text{Debt Services}$$

$$= \$37,169 - \$25,548$$

$$= \$11,621 \text{ (at the end of the year, we'd have \$11,621 in our pocket from this property)}$$

Hmmm, paying all cash will minimize my debt service (it would be \$0) which would therefore maximize my Cash Flow. So, if paying all cash maximizes Cash Flow, and if you have the means to pay all cash for the property, why wouldn’t you?

Read on to find out...

## **Rates of Return**

Cash flow isn’t the only important factor when it comes to analyzing the property. What is more important than cash flow is rate of return (also known as return on investment or ROI). Think of

ROI as the amount of cash flow you receive relative to the amount of money the investment cost you (your “basis”). Mathematically, that would be:

$$\mathbf{ROI = Cash Flow / Investment Basis}$$

Obviously, ROI is going to be higher when one or both of the following is true: Cash Flow is higher or Investment Basis is lower. You can see that from the equation above, but it should also be obvious when you think about it: if you can make a lot of money from a small investment, things are good!

What is a reasonable ROI, you might ask. Well, we already know our ROI from several other types of investing vehicles. For example, if you put your money in a high-interest savings account, your return (in this case, your interest rate) is about 5%. In mathematical terms, for every \$100 you “invest” in your savings account, you get \$4 in cash at the end of the year:

$$\text{ROI} = \text{Cash Flow} / \text{Investment Basis}$$

$$= \$4 / \$100$$

$$= 4\%$$

We know that a savings account will have an ROI of about 4%. A CD will have an ROI of about 5%. And if you do a little research, you’ll find that investing in the stock market will have an average ROI of about 8-10%.

So, what would our ROI be on this property?

There are actually three ROI numbers that you should be concerned with; let’s explore each of these individually.

### **Capitalization Rate (Cap Rate)**

Just like we have a key income value (NOI) that is completely independent of the details of the financing, we also have a key ROI value that is also independent of the buyer and the details of the financing. This value is known as the “Capitalization Rate,” or “Cap Rate.” Cap Rate is calculated as follows:

$$\mathbf{Cap Rate = NOI / Property Price}$$

If there is a single number that is most important when doing a financial analysis of a rental property, the Cap Rate may be it. Because the Cap Rate is independent of the buyer and the financing, it is the most pure indication of the return a property will generate.

Here is the cap rate for our example property:

$$\text{Cap Rate} = \text{NOI} / \text{Property Price}$$

$$= \$37,169 / \$418,000$$

$$= 8.89\%$$

Another way to think about Cap Rate is that it is the ROI you would receive if you paid all-cash for a property. Though, unlike cash flow, where the value is maximized by paying all cash, the Cap Rate is *\*not\** necessarily the highest return you'll get on a property. This is because Cap Rate assumes that the investment amount is the maximum (the full price of the property), and we learned above that the value of ROI calculations goes up as the investment amount goes down.

So, what is a good Cap Rate? It really depends on the area of the country you're in, but in general, most areas see maximum Cap Rates in the 8-12% range. And just like the value of single family houses are based on the prices of comparable houses in the area, the value of larger investment properties are usually based on the Cap Rate of comparable investment properties in the area. So, if the average Cap Rate in your area is 10%, you should be looking for at least an 10% Cap Rate for your property (barring other more complex situations and considerations).

### **Cash-on-Cash Return (COC)**

Just like there are multiple measures of income — NOI (financing independent income) and Cash Flow (financing dependent income) — there are also multiple measures of return. As we've discussed, the financing independent rate of return (the theoretical return on a fully paid property) is the Cap Rate, and of course there is the real (not theoretical) rate of return as well. This is called the Cash-on-Cash (COC) return, because it is directly related to the amount of cash you put down on the investment.

For example, we discussed that if you took \$100 and put it in a savings account, you'd receive \$4 per year, or 4% ROI. The COC is the equivalent measure of how much return you would make if you put that \$100 into the property.

COC is calculated as follows:

$$**COC = Cash Flow / Investment Basis**$$

In our example, the annual Cash Flow was \$11,621, and the investment of cash that we had to apply upfront on the property was \$98,000 (this includes the downpayment, the improvements, and the closing costs). So, our COC is:

$$\text{COC} = \text{Cash Flow} / \text{Investment Basis}$$

$$= \$11,621 / \$98,000$$

$$= 11.86\%$$

As this return is directly comparable to our savings account return, we can see that we are getting a better return than either a savings account or in a diversified stock portfolio (albeit with a lot more time and energy spent).

While it's completely up to you on what rate of return you need to purchase a property, it should be obvious that if you're getting less than a 10% return on a property, it's probably not worth your investment (you'd rather take that money and invest in the stock market where you can do a lot less work).

But, before you run off and make any final decisions based on COC, consider that the Cash Flow you make on a property isn't the only thing that affects your bottom line...

## **Total ROI**

In addition to Cash Flow, there are several other key financial considerations that affect a property's performance. Specifically:

- Tax Consequences (depending on your situation, you may gain or lose money to taxes)
- Property Appreciation (you may not be able to predict this, but if you can)
- Equity Accrued (remember that your tenants are paying off your property for you)

The difference between COC and Total ROI is that COC only considers the financial impact of Cash Flow on your return, while Total ROI considers all the factors that affect your bottom line. Total ROI is calculated as follows:

***Total ROI = Total Return / Investment Basis,***

where "Total Return" is made up of the components we discussed (Cash Flow, Equity Accrual, Appreciation, Taxes).

Let's use the following for our Total Return calculation:

- Let's assume we would expect a 2% appreciation on the value of the property this year, based on the improvements that we would do upon purchase (2% appreciation is \$8360)
- We can calculate that the equity accrued in the first year of the mortgage is \$3251
- Let's also assume that for the sake of this example that there are no tax breaks (or extra taxes due) by owning this property.

The Total Return of the property for this year would be:

Total Return = \$11621 + \$8360 + \$3251 + \$0 = \$23,232

And, therefore the Total ROI would be:

Total ROI = Total Return / Investment Basis

= \$23,232 / \$98,000

= 23.71%

Not too shabby, huh?

## FINANCIAL ANALYSIS SUMMARY

We now have all the data to assess the value of this property, but keep in mind that our assessment is only for the first year of ownership of this property. In subsequent years, accrued annual equity will increase, expenses may rise (with inflation), rental rates may increase or decrease, depending on the market, your tax situation may change, and a host of other factors may contribute to the return on your investment either increasing or decreasing.

While you can't predict the future, you should extend your analysis out a couple years, using trend data or demographic data that indicates the direction of the market, inflation, etc.

For example, [here is a full financial analysis of this particular property](#), using a spreadsheet I've put together to easily create a financial model for any property.

As you can see, based on the assumptions that revenue will rise 3% per year (rental rates will increase) and operating expenses will increase 2% per year (inflation, cost of services, etc), our cash flow (and our rates of return) are increasing each year as well. An even more thorough analysis would take into account things like taxation issues, where with the tax deductions you'll likely receive on the interest portion of your loan, your return may be even better.

Introduction to Real Estate Investment Deal Analysis by J Scott

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By [J Scott](#)

**J's Website:** <http://www.123flip.com/>

**J** has written **28** articles for us.

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Mike McKinzie [June 30, 2010 at 1:02 pm](#)

J

Excellent article explaining the basics of analyzing a real estate investment. You took what some people make a 200 page book out of and turned it into a easy to ready essay. Great job.]

Mike

[Reply](#)



Julie Broad [July 1, 2010 at 11:28 am](#)

WOW!! This is a mini-course on the basics of real estate analysis. I am incredibly impressed. I will definitely be sharing this with our readers because there are a lot of people who don't understand these terms. Great job!!!

We don't usually formally do more than a first year analysis but we usually do that analysis with a higher interest rate than what we're getting and a conservative rent rate estimate plus we build in a 2 to 3 month rent contingency fund into the whole plan to help cover bigger expenses that might come up. The last couple of years our expenses have gone up more than our rents have in most of the properties we own. In some cases our expenses have gone up 5% and our rents have gone down 5% ... (amazing how taxes keep going up even when the economy is slower!) so I don't put much weight on

forecasts we do. I think it's more important to build in a buffer and put in a contingency fund.

Good post!! Thanks!

[Reply](#)



Richard Warren [July 1, 2010 at 1:31 pm](#)

Hopefully Josh can put a link to this post where it's easy for people to see. Outstanding job!

[Reply](#)



Joshua Dorkin [July 1, 2010 at 7:25 pm](#)

I made this a sticky post on the Real Estate Deal Analysis forum, Rich.

[Reply](#)



Peter Giardini [July 1, 2010 at 5:58 pm](#)

J., what a fantastic job you did with explaining, in clear simple terms, how to evaluate income producing properties. This post should be made "sticky" somewhere here on Bigger Pockets.

Pete

[Reply](#)



J Scott [July 1, 2010 at 8:24 pm](#)

Thanks folks...I appreciate the kind words and feedback!

J

[Reply](#)



[Daniil Kleyman](#) July 4, 2010 at 2:54 pm

Very well-organized and concise article! Every real estate investor should have a basic understand of everything in this article, yet you'll be amazed how many do not. Great job spreading the knowledge!

[Reply](#)



[James Scholl](#) July 5, 2010 at 5:25 am

Very nicely done.

I have noticed that some of my real estate appraisals on legitimate flipped properties that sold have had selling prices well below market. They sell fast and the investor gets his money out quickly but I wonder if there is another reason to leave that much money on the table ? (I. E. a property that sold for \$80000 that could easily have sold for \$90000)

I am also wondering if anyone has done a similar post to J Scott's above, but on marketing.

[Reply](#)



[Tom](#) July 5, 2010 at 12:08 pm

Really we'll done simple language explanation of the ways to analyze different property. I would love to know how to get a copy of the spread sheet you put the link of. Is it in your business plan on your blog.

[Reply](#)



[Jason](#) July 8, 2010 at 12:50 pm

JScott,  
I didn't think it was possible to outdo your previous analytical skills and gift for explaining things, but this post really sets you in a field of your own. Extremely well done.

Jason

[Reply](#)



Melinda Smith [October 3, 2010 at 6:49 pm](#)

This may already be posted somewhere, but is there any way we can get that spreadsheet template? That is so awesome! Thanks.

[Reply](#)



J Scott [October 4, 2010 at 9:32 am](#)

Melinda -

Here you go:

<http://www.biggerpockets.com/forums/88/topics/51334-sfh-rental-analysis-spreadsheet->

[Reply](#)



Nancy Yavorsky [February 25, 2011 at 11:42 am](#)

Excellent article. Thank you very much.

[Reply](#)



Jim Simcoe [April 11, 2011 at 3:42 pm](#)

This is great info, thank so much for posting!

[Reply](#)



george [May 27, 2011 at 10:55 am](#)

i downloaded the spreadsheet, but cell F43 (equity accrued) is giving me error. is anyone else getting this error? the formula is “=-CUMPRINC(H6/12,12\*H7, H4, 1, 12, 0)” and the error is #NAME?

please let me know..

[Reply](#)



Litia [June 22, 2011 at 8:26 am](#)

Thank you very much J Scott for taking time to teach me all these concepts.  
Again thank you.

[Reply](#)



Ryan Bowman [September 12, 2011 at 7:45 pm](#)

Great article. I found it very useful. Well written, concise and easily understandable.  
Thanks for sharing.

[Reply](#)



Justin Yin [July 8, 2012 at 4:03 pm](#)

Hello, I was wondering what the formula was for Equity accrued?

Thank you,  
Justin

[Reply](#)



Kelvin [February 24, 2013 at 8:05 pm](#)

debt service payments made for the year minus interest charged over the year = equity.

[Reply](#)



EVE [September 21, 2012 at 6:10 am](#)

Hi J:

Can you please explain how did you get the Accrued Equity of \$3251 in this example?  
Whats the formula to it? Thank you in advance!

[Reply](#)



Ivan [November 14, 2012 at 9:34 pm](#)

This is a great post J, very very informative!

[Reply](#)



Roger Goldberg [November 27, 2012 at 10:59 pm](#)

Thanks for this very informative and easy to read article. I am just curious about why the xls template provided in the comments is for a single family home, whereas the article describes a multi unit property. I am a complete beginner so apologies if this a very simple question. What is the difference between this SFH template and the one used in the article?

Thanks!

[Reply](#)



SF [December 5, 2012 at 3:00 pm](#)

Serious question, where are you getting a 30 year fixed note on NOO investment property?

[Reply](#)



Anthony [February 12, 2013 at 12:52 pm](#)

J

Great article. The article gives new meaning to the old adage "... to truly be an expert on something, try to teach someone..."

You take a very complicated and intricate subject and explain it in a way that makes sense to people who may not have the same knowledge base you do.

[Reply](#)



Christila Milne [February 20, 2013 at 10:47 am](#)

Excellent!!

[Reply](#)



Paula [February 20, 2013 at 1:41 pm](#)

Wondering the “equity accrued in first year of mortgage” was calculated. I’m having a problem with the Total ROI because of this. EVERYTHING ELSE was so clearly explained that I’d already started a spreadsheet like the one you have before I’d even seen it.

Thanks for the information really!

[Reply](#)



John D [February 26, 2013 at 11:05 am](#)

7 of the 8 units are vacant (empty)? Doesn’t that mean that 87.5% vacancy? Thanks for the article, I must be easily confused with numbers.

[Reply](#)



John D [February 26, 2013 at 11:52 am](#)

Also, to me as a young guy it seems important to account for how our profits will change once the loan is paid off. Does a place that old fall apart or become undesirable after another 20-30 years or do we then have a lot more of a retirement income?

[Reply](#)



John D [May 12, 2013 at 8:58 pm](#)

bump.

[Reply](#)



david [March 7, 2013 at 10:44 am](#)

Excellent article. I've got one rental property and am looking at buying another. I have been trying to calculate my real return on investment to see if it is worthwhile, and even after reading this article I CAN'T SEE ANY REASON TO INVEST IN RENTAL PROPERTY IN LOS ANGELES, CA IN 2013 (or ever)...

Maybe you can help me? The best place I've found so far was a duplex (with illegal third unit) that had 9 offers and sold for \$775k (this month). One unit rented out for \$2200 and the other rented for \$2000 (so said the real estate agent, but she was a little unclear). The illegal unit was a studio in the basement that rented for \$1000. The location is very hipster, and very desirable for walking to lots of shops. The price sold was below Zillow estimate (yeah i know) and similar to its projected price in 2008 (i.e. nearly full recovery to pre-bubble bursting price).

When I run the numbers, I get a cap rate below 6% and a COC of zero (unless you count the basement studio). Remember, this is the BEST looking investment I'd found in 8 months of shopping. Please help! What don't I get about LA rental property?

[Reply](#)



[J Scott March 7, 2013 at 2:32 pm](#)

David,

In high-priced markets like LA, cash flow is nearly impossible to get. Most people who are investing in these markets are banking on appreciation, not cash flow.

[Reply](#)



[david March 12, 2013 at 11:10 am](#)

Thanks for your response!

I get it. Appreciation is helped greatly by leverage. But when I assume that appreciation (~3.2%/yr) is about the same as inflation (~3.1%/yr from Case-Shiller data and inflation over the last 100yrs). I find that my total return for most properties peaks somewhere 10-15yrs from date of purchase.

Does that mean I should sell my property every 10-15 yrs, or is it possible to continue to re-finance and "re-leverage" my investment dollars?

[Reply](#)



Keith Ghion [April 6, 2013 at 10:03 am](#)

Hey folks for those of you wondering about the Equity Accrued calculation I was having trouble with it to but I believe I figured it out @J Scott or anyone else confirm this that would be a great help for those just learning. Since I like to fully understand calculations before I rely on spreadsheets, I did this by long hand month by month.

First step is you have to convert your APR to a monthly APR. In the example that 7%.  
.07 / 12 gives you a monthly interest rate of .0058 or rounded to .006.

Then you multiple your loan balance by your new MIR .006. In the ex that's 320,000 x .006 giving you \$1,920.

Subtract your interest from monthly debt service and you get your monthly equity accrued. The first month that = \$209.

Do this month by month making sure you multiply the new balance by your MIR. So it looks something like this:

$$320,000 \times .006 = 1,920 \{2,129 - 1,920 = 209\}$$

$$320,000 - 1920 =$$

$$318,080 \times .006 = 1908 \{2129 - 1,908 = 221\}$$

$$318,080 - 1920 =$$

$$316172 \times .006 = 1897 \{2129 - 1897 = 232\}$$

Repeat for 12 months like above and add up your principal totaling your equity accrued.

[Reply](#)



Michelle [May 5, 2013 at 9:46 pm](#)

I loved this article! Extremely detailed and so valuable! I will say anything you write I will read and apply! Thank you!!

[Reply](#)



J Scott [May 6, 2013 at 6:20 am](#)

Michelle -

If you're interested in rehabbing, feel free to pick up the books that BiggerPockets and I just released:

<http://www.biggerpockets.com/flippingbook>

[Reply](#)



[Ken Higgins](#) [May 10, 2013 at 12:27 pm](#)

This is fantastic! Thank you so much. Can you recommend a free software that allows you to plug in the numbers and get the full analysis?

[Reply](#)



[Rodwell Smith](#) [May 12, 2013 at 7:55 pm](#)

Wonderful details and explanations! I was looking for deal summary spreadsheet but after reading this string of information I am well prepared to draw a Summary Table manually. Thank you and I will continue to receive updates.

[Reply](#)



[James Tobin](#) [August 4, 2013 at 8:05 pm](#)

Awesome article. Can't say anything that hasn't already been said but thank J!!

[Reply](#)



[caleb](#) [August 28, 2013 at 4:30 pm](#)

Can you share your multi-unit spreadsheet. I can see and download the SFH spreadsheet, but I'd really appreciate getting your multi unit spreadsheet in excel form (like the image file you posted here).

Thanks,

Caleb

[Reply](#)



Becca Shaw [September 26, 2013 at 10:22 pm](#)

Thanks for tossing all the good knowledge into one brain dump! This was really helpful and I've bookmarked it so I can start to become familiar with all the steps.

[Reply](#)



William Turner [October 11, 2013 at 3:21 am](#)

Bigger Pockets, where have you been for the past six months. This was a great article for doing evaluations and it was easy to understand. This is preparing me for my first deal....

[Reply](#)



Joseph Furmansky [October 14, 2013 at 1:17 pm](#)

Thank you for the crash course. In the paragraph determining "vacancy rate", you wrote, "In our example property, only 7 of the 8 units are listed as vacant (which equates to about 12% vacancy)," I believe you meant to write, "only 1 of the eight units....." or "only 7 of the 8 units are rented".

I would love to have a copy of your spreadsheet, so that I can plug in my data.

Thank you

[Reply](#)



Brett Shepherd [November 10, 2013 at 7:55 pm](#)

Joseph. Here is a link to it.

<http://www.biggerpockets.com/files/user/JasonScott/file/20-sfh-rental-analysis>

After discussing appreciation as part of Total ROI, I wonder why Appreciation was taken off the final SS, but was shown on an earlier jpg of the example deal..

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