Letter

Dear Lloyd:

Let me commend you for your article "New Perceptions of Value" in *Real Estate Issues* (Spring/Summer 1981).

As advisor to one pooled real estate fund and involved with appraisals in other ways, I come in contact with few MAIs who seem to know that appraisals based on debt equity, band of investment, and comparative sales going back four or five years ago "adjusted" by inflation factors are totally irrelevant.

For the pooled real estate investment fund, I have been urging our appraisers to give us one thing only — their best estimate of the present worth of all economic benefits of ownership of the property, with a holding period from 10 to 15 years. If they insist on adding depreciated reproduction costs and comparable sales figures which are meaningless, we allow it but pay them scant heed.

Actually, real estate is like any other pure investment — whether it be stocks, bonds, gold bars, diamonds, postage stamps, etc. If one casts aside any utilization or pride-of-ownership factors as irrelevant, the owner of the particular investment can benefit in only two ways:

1. He gets a predictable stream of income which may fluctuate, may be zero or negative, but can be predicted reasonably and its present value can be calculated; and
2. He gets something from nothing to possibly a demolition cost at the time his holding period comes to an end, which also can be projected and discounted.

I would like to question your statement in the concluding section (perhaps because I do not understand it). "Attempts to explain changes with new complicated mathematical formulas are noble but artificial for two key reasons: Investors or sellers do not employ these formulas in arriving at buy-sell decisions ..." If you are referring to relatively simple discounting techniques that bring projections back to present value, I disagree. Investors can and do make buy-sell decisions today more on a total return or IRR basis than on our traditional cash-on-cash method. This is not true for all investors, but it is valid for institutional and many foreign ones.

On the other hand, if you are referring to some of the formulas that expound into four pages of mathematical equations and symbols which only the most erudite appraisers use and understand, you're absolutely correct. Neither buyers nor sellers understand them, are suspicious of them, and simply don't use them.

As a reviewer and user of appraisals, I would be delighted if your suggestions — a detailed section on the financing market, an analysis of any existing assumable debt or locked-in debt, in-depth analysis of a typical purchaser market, a supplementary section with impressions and reasons for probable future market changes, qualifications of all assumptions — were common to all appraisals. But I have yet to see one used and one reason is that most appraisers wouldn't know what to do. A bigger and better reason is that a lot of users won't pay enough to permit the appraiser to do this and still make a living.

In our own practice we do little if any appraising. Several times when I have been asked by people to whom I owe particular attention to do an appraisal, I have been told after quoting a price, "Heavens, we didn't think it would cost more than a few hundred dollars. All we want you to do is tell us what it is worth. Don't call us, we'll call you."

Very truly yours,

Bruce

This letter by Bruce Hayden comments on an article by Lloyd D. Hanford, Jr., CRE, which appeared in the last edition of Real Estate Issues. *Mr. Hanford is the owner of Lloyd Hanford, Jr. & Co., a real estate counseling and appraisal firm in San Francisco.*

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