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ASPECTS OF MARKET APPROACH - LAND & BUILDING

Market changes from time to time. Earlier, knowledge of the variations or causes of variation were few known, so analysis could be easily made but was improper. Whereas nowadays, with widening of knowledge, the aspects of market analysis need to be analyzed more skillfully and professionally. Also, the market value differs from time to time according to demand and supply.

The market approach plays a very major role in analyzing the immovable assets such as land & building. Till now, about 70% of the valuation works arise from Banking/ Finance sectors. We already know that finance companies consider market value or rather fair market value as the basis of amount of finance to be provided to their clients. So, it becomes very important for us valuers to carry out valuation of immovable assets very carefully, skillfully and professionally.

Moving ahead, the easiest approach is to value a property is to base it on the value actually assigned to other properties in the market i.e., the **comparable sales approach**. However, because no two properties are the same and significant differences exist between properties, this approach is not appropriate for all properties and must be used with caution. The market approach excels in situations where abundant data is available on comparable transactions. When that data is not available, alternative approaches may be required. In situations where limited data is available, the valuator may need to rely on alternative methods such as the cost approach or discounted cash-flow analysis (DCF).

There are many aspects involved in Market Approach. Few of them are discussed below along with a case study:

1. Principle of substitute: - Market approach involves principle of substitution because in this method, we may substitute the cost of acquiring of another equally desirable substitute on the basis of proximity with time and location.

2. Utilization Area: - It is generally suitable for estimating value of open lands or agricultural lands, where reliable net income data is not easily available. However, It can also be combined with cost approach or income approach to find value of buildings or property on the whole.

3. Relation to cost approach: - In case of buildings, market value can be estimated by substituting the cost of another equally desirable comparable sale instance the basis of proximity with time and location.

4. Sources of information of sale instances: - Some sources of information include:

- i. Index-II Register of Registrar Office: This can be used by valuers to find the Market Rates of particular area but challenge is that these values might not be true because people tend to make record of lesser rates to save imposed stamp duty taxes.
- ii. Local real estate agents: They tend to provide higher values than actual market rates because of their own commission interests.
- iii. Newspaper advertisements: Newspaper often contains market rates but area of interest distinguish from time to time.
- iv. Land acquisition cases in the area: The values for land acquisition cases in the area can be considered for analyzing market value if total value minus solatium - compensation.

- v. Auction Sale Transaction: The values for auction sale of land acquisition cases in the area can be considered for analyzing market value but these values should not be a forced sale transaction.
- vi. Valuer's own data bank: Valuer's generally have their own data bank but it needs to be updated from time to time. Valuers may share data with one another if relied upon good and friendly relations.
- vii. RESIDEX: It is an index published by the National Housing Bank (NHB) about prices of residential properties in India.

5. Valuer's success mantra: - Valuer's success mantra is said to be "INSPECT BEFORE YOU VALUE" which means that valuer should inspect market before analyzing value of a certain subject property so that he can easily collect comparable sale instance and understand the genuine sale instances out of those. If a seller is under duress because of the threat of foreclosure, or if a private sale is held, the property may sell below its market value. So, this kind of comparable sale instance may or may not be the genuine sale instances.

6. Steps of Market Approach: -

- i. Follow success mantra.
- ii. On Site visit, obtain copies of sale transactions if available and find out if there are any false or fake transactions been made and eliminate them.
- iii. Analyze rate of sale in genuine sale transaction.
- iv. Compare the subject property with each of the comparable sale instances considering the favorable and unfavorable features.
- v. Arrive at the final estimated value for each sale by comparison and form final opinion.

7. Open market Transaction: - All transactions/ sale instances should be of open market in which a property was exposed to many prospective buyers and both buyer and seller acted willingly with full knowledge of all details about the property and were under no pressure.

8. Type of information collected during site visit: -

- i. Physical aspects which include size, shape, orientation, access, frontage, topography, vastu aspect, etc. It also depends on the specialties in the building such as water supply, sewer and electricity etc.
- ii. Legal aspects include verification of property no., owner's detail, boundaries and dimensions with title deed and also built-up area and permissible built-up area.
- iii. Social aspects such as lifestyle of area, reputation of area, stigma attached if any.
- iv. Economic aspects such as land rate, circle rate, guideline rate, etc.

9. Permissible Built-up Area: - On Site visit, one should must check whether property is built-up according to sanctioned plan or not. If area as per site increases than sanctioned- plan, then said extra area should be ignored or valued as a scrap.

10. Effect of size and frontage on market value: - Smaller properties with larger frontage attract larger no. of buyers. Hence, those properties fetch better per unit price. A plot with double frontage along two opposite boundaries or the Return frontage meaning corner plot fetches higher values of price. Valuation of a building also depends on the height of the plinth, height of the building, thickness of its walls, nature of structure (such as load bearing or framed structure), type of flooring, roofing, doors and windows etc.

11. Effect of topography: A plot should be either leveled or having a gentle slope to permit drainage. Steep slopes add to cost of construction or a plot is in low lying area where water may stagnate with time, they fetch lower price.

12. Effect of status of land: - Land without improvements is called virgin land and land with improvements is called married land. Virgin land is more valuable than married land. For partially developed properties, means where FSI/FAR has not been fully utilized fetches higher prices than fully developed properties.

13. Age of the property: - Age is another factor that impacts the worth of a property. An old construction would cost much less than a new construction in the same location.

14. Meaning of vista: - Property having vista meaning an unobstructed view of building from front, impresses its viewers and fetch better price. If road width is larger, then greater unobstructed view of building from front is easily obtained. The value of land in India, especially in urban regions, has grown exponentially over the past two decades, on the back of the terms like ‘land scarcity’ and ‘space crunch’. Such has been the demand for land that its values have continued to show appreciation, in spite of a multi-year slowdown in the real estate market in India, which has been aggravated by the Coronavirus pandemic and its fallout on human lives and the economy. In fact, the impact on value appreciation on new property has also been negligible as reflected in numbers below.

15. Effect of orientation: - Orientation means location of a building in relation to the direction of sunlight and wind. This helps in understanding the vastu aspect of property. In upcoming times, vastu has played a key role in buyer's interest. Generally east or south fetching properties have higher rates than west or north facing properties.

16. Social aspects: - The social forces affecting values include all the characteristics and outcomes of the people that make up the community such as family size, age group, lifestyle, law enforcement, education, etc. The neighbor's interest might sometimes create objections in fetching right value for properties. The rural areas/ undeveloped areas have very low market rates and have very low salability. So, the market rate analysis in these areas become much more difficult for us. In case of a building, the brand of the developer will also have an impact on the pricing. A project by a well-known developer will, for instance, cost more than a project by comparatively less-known developer.

17. Economic aspects: - Economic aspects such as income level, employment opportunities, level of wages, availability of credit facility and interest rates and Price level and tax burden, etc. should be clearly analyzed during market valuation. Lower liquidity would negatively affect real estate demand, so higher the price levels. Certain areas have market rates in Sq Ft. while other areas might have market rates in SqYds or Marlas. Developed areas generally have market rates in SqFt. but whereas semi developed areas have market rates in SqYds or Marlas. In agricultural areas, the market rate for land is measure in per Acre of land. A property if rented out, then income to the owner comes from rent also, so valuation must consider the amount of income the building can generate.

18. Legal aspects: - Suppose your property is jointly owned by your sibling who is not willing to sell his share in the property. Such a problem may not only stall the sale but also result in value depreciation. We have different methods of comparison and estimation of market value such as hedonic pricing model, adoption of adhoc weightages, adjustment grid model, price-quality regression model, belting method and weighted score system. The most commonly used methods are hedonic pricing model, adoption of adhoc weightage and belting method.

Hedonic Pricing Model: - It is the most popular method. In this method, value of land is estimated by analyzing recent sale prices of comparable land in the vicinity, adjusting the prices to account for any difference in size, shape, location and other features. But this method is useful where there is an active market and transaction prices are easily available. The valuation expert must check average prices over the years and check for any volatility in prices.

Adjustment Grid Model: - In this method of land valuation, the unit prices for comparable land are extracted from a developed property in the vicinity by deducting the estimated value of the built-up area from the sale price. Then the value can be adjusted for any difference in size, shape, location and any other features. The accuracy of this method depends on the quality of depreciation estimate of built-up area. That is why, this method is generally used

only for properties with newly built-up areas that have negligible depreciation, or for properties where the built-up area only represents a small component of the total value of the property.

Belting Method: - This method of valuation of land takes into account the frontage and depth of the plot. A land with higher frontage will have more value. And, the value of land decreases as the depth of the plot (distance from main road) increases. In this method, the area is divided into belts with assigned values as a proportion of the value of a land on the main road. The main challenge in this method is to arrive at the rate of decrease in land rate as the distance increases from the road. generally, the depth of first belt is equal to average depth of properties fronting on the road and its rate is adopted same as market rate whereas for middle belt the depth is equal to 1.5 times the average depth of properties fronting on the road and its rate is adopted as 2/3rd of the market rate and for rear belt the leftover depth is considered and it's rate is adopted as 50% of the market rate. Moreover, for recess land, it's rate is adopted as 75% of the market rate.

Major disadvantages of Market Approach are as follows –

1. While carrying out the market approach, it becomes quite difficult in identifying the transactions or the companies that are to be compared. There is usually a lesser number of companies or transactions that can be used for comparison.
2. The method to carry out a market approach is generally considered to be less flexible as compared to the other techniques or strategies.
3. The method is also not able to clear out the doubt about what quantity of data is available and how good the data can be.

CASE STUDY - MARKET APPROACH

This is a case for revaluation of mortgage loan with a bank. A person named as X have agricultural land measuring 32 kanal = 4 acres in a village area. His relative Y proposed to him we can implant a rice and gen. mills in that property. They both agreed and Y made all the investment related to machinery and structure in that rice and gen. mills with the help of finance from mortgage with some bank. After few years, they suffered losses in the rice and gen. mills and couldn't repay installments in time to the bank. Bank took over possession of property after non-compliance of due notices sent to them from time to time.

After possession, revaluation was required to conduct for the property. I was asked by the branch manager to conduct re-valuation. on my site visit I found that the property inside boundary was only 3 acres and clearly did not match with the area mentioned on title deed. Upon reading documentations, we came to know that the property is leasehold with the firm in which X and Y are co-partners. In the title deed no dimensions of property were mentioned but only boundary details were mentioned. The area had developed industrial and agricultural usage. The property consisted of 3 separate temporary sheds, office, labor quarters, etc. in normal condition.

Later, after investigation from site observations and information provided by villagers, we came to know that the and gen. mills was installed on only 3 acres of land and the rest of 1 acre of land was kept for agricultural use by the X at back of and gen. mills boundaries. This is against mortgage with banks. As the property is Industrial Building, **Land and Building Method of Valuation** and calculations are done by adopting **Straight Line Depreciation Method** at **Fair Market Value** of the above property on the date of valuation. It is based on the information provided by the applicant. The Valuation is derived from the Surroundings, usability, infrastructure and type of construction. For Fair Market Value various sources have been contacted such as Real estate agents, etc. So, in my final opinion I clearly stated the above situation and analyzed value of land for only 3 acres because we as property valuers are not given authority to analyze agricultural land value for banks.