

1930 Curtis Street

Table 7.1 Land Residual Process

Property value as completed (new):	11,200 sq. ft. × \$200.00 =	\$2,240,000
Building cost:	11,200 sq. ft. × \$150 =	\$1,680,000
Plus entrepreneurial incentive:	10% of bldg. cost =	\$168,000
Less total cost to construct:		<u>\$1,848,000</u>
Indicated residual land value:		\$392,000

The land residual is positive (\$392,000). As a result, it is concluded that it would be currently financially feasible to develop the property.

incentive the buyer is willing to accept. If the land in question is 1930 Curtis Street and the land residual calculation is the one shown in Table 7.1, then the buyer would be justified in paying up to \$392,000 for the land. As a side note, the indicated residual land value is not market value since the property value as completed is not derived from an open and competitive market; instead, the \$392,000 would be investment value.

Feasibility Rent Method

Feasibility rent is the minimum rent necessary to justify new construction. New construction is not going to take place until market rent is equal to—or greater than—feasibility rent. Rents are the most time-sensitive indicator of market conditions. Market rents tend to be a leading indicator of vacancy rates since individual landlords are the first responders to changing market conditions. By comparing feasibility rent with market rent, financial feasibility is revealed:

Currently Financially Feasible if Market Rent > Feasibility Rent
 Not Currently Financially Feasible if Feasibility Rent > Market Rent

The calculation of feasibility rent is based on the relationship of development costs (including land) and the income required to attract new construction. Since any highest and best use conclusion is based on the recognition that the cost to assemble the property new is equal to the value of the property (i.e., no depreciation/obsolescence initially exists), the following formula holds true:

$$\begin{aligned}
 V_o &= I_o / R_o \\
 V_o &= V_L + V_{B(new)} \\
 \therefore I_o / R_o &= V_L + V_{B(new)} \\
 \therefore I_o &= (V_L + V_{B(new)}) \times R_o
 \end{aligned}$$

Begin with the cost of development (land and improvements), including profit/entrepreneurial incentive. Multiply the cost of devel-

