

# Why do investors buy Real Estate?

- to generate profit, rental income, or long-term capital appreciation
- It is a tangible asset strategy that includes residential, commercial, and raw land investments, aimed at building wealth through cash flow and property value increases over time.
- It is all about NOI and Value Add

# How do we get to NOI?

- Net Operating Income (NOI) is calculated by subtracting operating expenses from gross revenue
- $\text{NOI} = \text{Revenue} - \text{Operating Expenses}$
- Types of revenue?
  - Rent Income
  - Move in Fees
  - Parking
  - Laundry
  - Pet Rent
  - RUBS

# So what are our Operating Expenses?

- Operating expenses (Op-Ex) in real estate are the recurring, necessary costs required to manage, maintain, and operate a property on a day-to-day basis
- Examples:
  - Property Taxes
  - Insurance
  - Utilities
  - Maintenance

# What do we leave out of Op-Ex?

- Capital Expenditures (Cap-Ex) in real estate refers to significant, long-term investments used to acquire, improve, or upgrade a property, such as replacing a roof, HVAC system, or major renovations
- What about the mortgage?
  - These are not Op-Ex
  - Your debt service is considered non-operating and not part of NOI

# Key reports to building NOI

- Rent Roll
  - detailed document listing all units in an investment property, including tenant names, lease terms, and rent amounts
- Income Statement or Profit and Loss Statement (P&L)
  - is a financial report summarizing a property's revenues, expenses, and net operating income (NOI) over a specific period

# Rent Roll

Unit	Lease Start	Lease End	Bed/Bath	Rent	Balance Due
1	5/15/2023	5/31/2026	1 Bed/1 Bath	\$2395.00	\$0.00
2	4/1/2023	3/31/2027	2 Bed/2 Bath	\$2750.00	\$0.00
3	7/1/2025	6/30/2026	1 Bed/2 Bath	\$2900.00	\$0.00
				\$8045.00	

# P&L - Operating Income

	Q1-2025	Q2-2025	Q3-2025	Q4-2025	Total
Income					
001 Rent Income	\$ 23,995.00	\$ 24,260.00	\$ 27,185.00	\$ 24,235.00	\$ 99,675.00
005 Non-Refundable Move In Fee			\$ 350.00		\$ 350.00
Total Income	\$ 23,995.00	\$ 24,260.00	\$ 27,535.00	\$ 24,235.00	\$ 100,025.00

# P&L - Operating Expenses

101 Management Fees	\$ 1,139.40	\$ 1,086.09	\$ 724.05	\$ 1,293.09	\$ 4,242.63
102 Leasing Commissions			\$ 2,900.00		\$ 2,900.00
103 Lease Renewals	\$ 250.00	\$ 250.00			\$ 500.00
206 Bank Fees	\$ -	\$ -	\$ 45.00	\$ 15.00	\$ 60.00
401 Service Calls	\$ 85.00		\$ 170.00		\$ 255.00
402 Materials			\$ 63.32		\$ 63.32
411 Turnover Cleaning			\$ 250.00		\$ 250.00
412 Turnover Maintenance			\$ 120.00		\$ 120.00
420 Outside Contractor		\$ 423.50			\$ 423.50
423 Appliance Repairs			\$ 250.00		\$ 250.00
430 Landscaping		\$ 70.00	\$ 210.00	\$ 105.00	\$ 385.00
440 Snow Removal	\$ 450.00				\$ 450.00
Total Expense	\$ 1,924.40	\$ 1,829.59	\$ 4,732.37	\$ 1,413.09	\$ 9,899.45

# P&L - Operating Expenses

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440 Snow Removal	\$ 450.00				\$ 450.00
800 Insurance	\$ 975.00	\$ 975.00	\$ 975.00	\$ 975.00	\$ 3,900.00
<u>900 Property Taxes</u>	<u>\$ -</u>	<u>\$ 6,735.00</u>	<u>\$ -</u>	<u>\$ 6,838.00</u>	<u>\$ 13,573.00</u>
Total Expense	\$ 2,899.40	\$ 9,539.59	\$ 5,707.37	\$ 9,226.09	\$ 27,372.45

# P&L

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Total Expense	\$ 2,899.40	\$ 9,539.59	\$ 5,707.37	\$ 9,226.09	\$ 27,372.45
Net Operating Income	\$ 21,095.60	\$ 14,720.41	\$ 21,827.63	\$ 15,008.91	\$ 72,652.55

# Review – Are these operational income?

- Tenant Rent?
- Utility Income?
- Owner Contribution?
- Parking Income?

# Review – Are these operating expenses?

- Property Taxes?
- Property Management?
- Mortgage?
- Roof Patching?
- New Roof?
- Utilities?
- Appliance Repair?
- New Appliances?

So how do we get NOI?

• NOI =

Revenue –

Operating Expenses

# So how do we find VALUE?

- Capitalization Rate (CAP Rate):

fundamental real estate metric measuring a property's expected annual return, calculated as Net Operating Income (NOI) divided by current market value or purchase price. It helps investors compare risk and profitability, with higher rates signaling higher risk/returns and lower rates indicating safer, stable assets.

$$\text{NOI} / \text{CAP} = \text{VALUE}$$

# Basic Examples of Cap Rate Equations

- $\text{NOI} = \$100,000$
  - $\text{Cap Rate} = 10\%$
  - $\text{Value} = \underline{\hspace{2cm}}$
- 
- $\text{Value} = \$2,000,000$
  - $\text{NOI} = \$200,000$
  - $\text{Cap Rate} = \underline{\hspace{2cm}}$

# Cap Rate Correlation

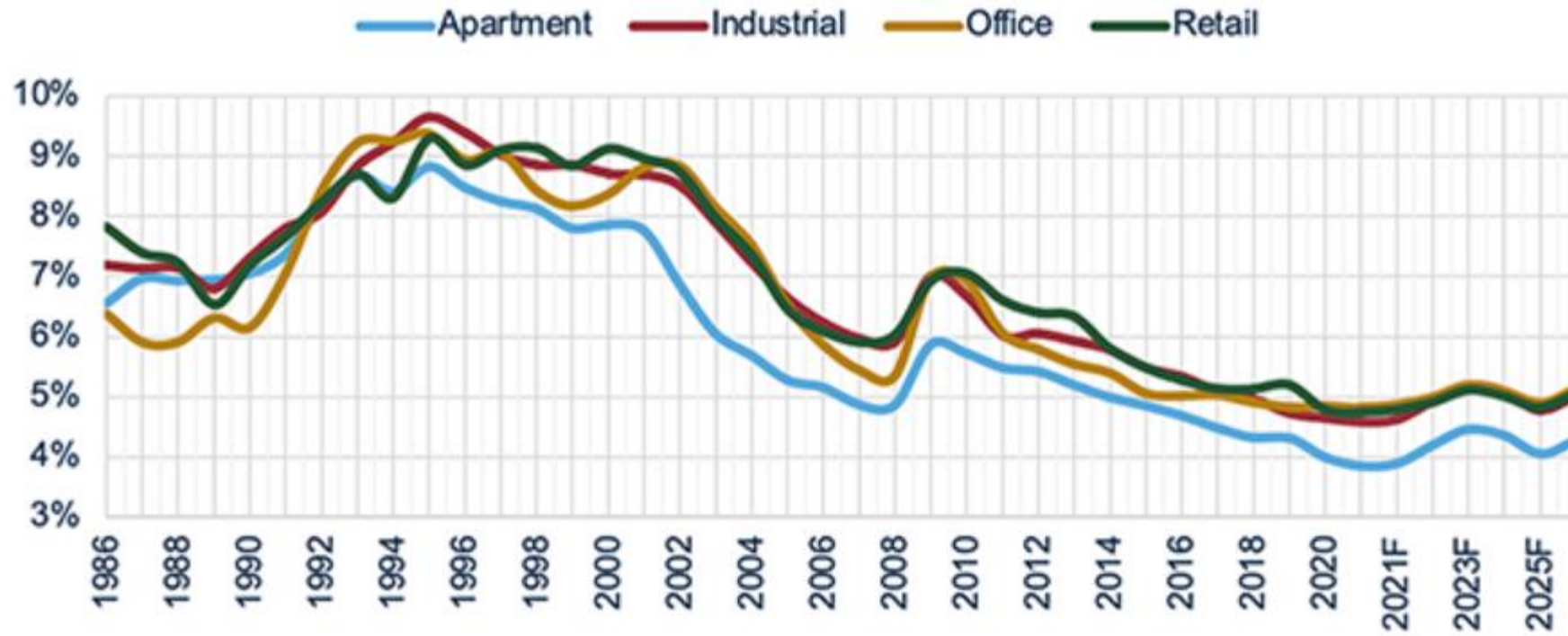
- Cap Rate is a measure of return
- Cap Rates are closely tied to risk
  - What is the return for a “safe investment”
  - What is the premium needed to take on a more risky investment?
- What has a higher cap rate? More risk or less?
- There is an inverse relationship between Cap Rate and Value
  - As CAP RATE drops, VALUE increases

# History of Cap Rates

- Cap Rates for quality real estate in US historically between 7-8%
- Since real estate is limited, cap rates have driven down recently into the 5-6% range, and even below
- Real estate is now considered less risky, plus capital is less costly

# History of Cap Rates

## Annual Current Value Cap Rate by Property Type



# Picking the right cap rate matters!

NOI = \$100,000

Cap Rate = 6%

Value = \_\_\_\_\_

NOI = \$100,000

Cap Rate = 7%

Value = \_\_\_\_\_

NOI = \$100,000

Cap Rate = 8%

Value = \_\_\_\_\_

# Lets do the math

Rents for 3 units are: \$2,500, \$2,500 and \$3,000

Property Taxes = \$15,000

Management fees = 5% of rents

Utilities = \$2,400

Insurance = \$6,000

Maintenance = \$6,000

Mortgage = \$3,000 monthly

What is NOI?????

# Lets do the math

Annual Income = \$96,000 (\$8Kx12)

Operating Expenses = \$34,200 (~35%)

NOI = \$61,800

The property is a well performing 3 unit with upgrades to all units 3 years ago. Tenants have good credit and unit is in a secondary location within Wicker Park. What is a good cap rate here?

# Lets do the math

NOI = \$61,800

5 cap = \$1,236,000

5.5 cap = \$1,123,636

6 cap = \$1,030,000

6.5 cap = \$950,769

7 cap = \$882,857

# What it's all about?

Grow NOI over time through the repositioning of units

Derisk the property and drop the cap rate

Add value

\$100,000 NOI at 8% cap = \$1,250,000

\$120,000 NOI at 6% cap = \$2,000,000