

### **Valuing the Ocean Park Terrace Apartment Complex**

You are part of a small group of private equity investors considering purchasing a small apartment complex. Your job is to come up with a valuation in order to determine if your group should buy the building.

Write a one-page memo providing your conclusions. Attach a printout of your Excel worksheet(s).

#### **Facts about the complex:**

There are 40 units in the building, with an average vacancy rate of 10%. Rent per occupied unit is \$24,000 per year. Variable cost per occupied unit is \$10,000 per year. Annual fixed costs of maintenance and other expenses is \$180,000. Assume we will receive these cash flows for 20 years, after which time the building collapses and we sell the land for \$750,000.

Assume that we are going to pay for the building now, but that annual cash flows come at the end of the year. If we discount future cash flows at 10%, what is the apartment complex worth?

If the apartment complex sells for \$2,800,000, make a graph showing the combinations of vacancy rate and monthly rent-per-unit rate for which the complex breaks even (show for vacancy rates from 0.04 to 0.16 with intervals of 0.01).

If the variable costs were actually fixed (and didn't depend whether the unit was occupied) would you expect bigger or smaller changes in the break-even-rent for a change in the vacancy rate?

In general, do you think that vacancy rates and rents are positively or negatively correlated?