LESSON 5

AIM

On completion of this lesson the student will be able to determine the following returns on investment for an investment property:

1. Initial yield (IY)
2. Equivalent yield (EQVY)
3. Equated yield (EQTY)

INITIAL YIELD (IY) MODEL

1. Retrieve previous DCF file eg DCF1.WK1
2. The initial yield return on investment is the most common used in industry. It has 3 important assumptions:

   * The expected net annual income to be derived from the subject property is the starting (initial) amount.

   * The initial amount will remain level from 0 to perpetuity.

   * The end market value always = the starting market value. That is, it is assumed that there are no capital gains.

3. Therefore, the initial annual amount in the previous cash flow was 166 (000). Under the initial yield model it is assumed that 166 will continue into perpetuity:

NET ANNUAL INCOME - INITIAL YIELD

166 000 per annum -->

0 --> perpetuity

4. The starting market value and the end market value are the same:

   166 * 100/8.3 = 2000

ANALYZING SALES - INITIAL YIELD

Sales are analyzed to determine the discount rate in the DCF. This can be equated with the capitalization rate. DCF1 can be used to analyze a sale to find the market discount rate.