Presented at the FIG Working Week 2024,
19-24 May 2024 in Accra, Ghana

Commision 9:

The residual method - Opportunities and risks

Wolfgang Glunz, Germany

Publicly appointed surveyor and publicly appointed and sworn in valuer in Ratingen, Germany.

Member of the german surveyor-organisations BDVI and DVW (com. 6)

Delegate of BDVI to TEGoVA

The residual method - Opportunities and risks

Brief overview of the residual method.

Importance of the residual method in

- real estate development and
- real estate finance and –investment and
- real estate valuation.

The residual method - Opportunities and risks

The residual method is used to determine the value of vacant land ready for development or land and building/s with redevelopment or refurbishment potential.

The residual method - Opportunities and risks

Provides a financial picture

Helps in assessing project feasibility

Useful in decision-making for investments

Simple in concept:

residual value

= expected selling price - total costs of development

The residual method - Opportunities and risks

Let´s call the „expected selling price“

the **Gross Development Value (GDV)** or

the **Market Value.**

The residual method - Opportunities and risks

How to assess the GDV?

either by

- comparison or
- by the income approach.

The residual method - Opportunities and risks

Factors influencing GDV:

- Market situation and - trends
- Location
- Property type and size

The residual method - Opportunities and risks

Calculation of the total development costs:

- Land acquisition costs
- construction costs
- professional fees
- Financing costs
- Contingencies

The residual method - Opportunities and risks

Land acquisition costs	acquisition price, legal costs, taxes
construction costs	infrastructure, materials, manpower, permits
professional fees	architects, engineers, surveyors
Financing costs	Loan interest, financing fees
Contingencies	Surcharge for unexpected costs

The residual method - Opportunities and risks

Residual value

= GDV

- Total development costs

- developers profit

The residual method - Opportunities and risks

That means:

The **Residual Value** comprises the Market Value of the property/land plus related acquisition costs and finance costs incurred in holding the property over the development period (costs of borrowing for property purchase or opportunity cost). These costs then need to be deducted from the residual value to arrive at the **Market Value**.

But …

… were are the risks?

Example:

Development of a residential area on a former military site

But …

… were are the risks?

Seller´s price:

10,7 Mio. Euro

Buyer´s price:

7,5 Mio. Euro

But …

… were are the risks?

Residual Values of

Valuer 1:

10,7 Mio. Euro

Valuer 2:

7,5 Mio. Euro

The residual method - Opportunities and risks

First problem

estimating the GDV = Market Value after development

Second problem (= main problem)

estimating the developer´s costs and risk (profit)

The residual method - Opportunities and risks

GDV: 10 % Difference between Valuer 1 and Valuer 2

Surcharge for the new development area / discount for social housing?

Costs: 20 % Difference between Valuer 1 and Valuer 2

8 % Difference in infrastructure costs

12 % Difference in developer´s profit and risk

The residual method - Opportunities and risks

What do we learn from this?

The residual method is good for:

- Land acquisition decisions
- Financial planning and investment analysis
- Feasibility studies

The residual method - Opportunities and risks

What do we learn from this?

To find the market value of undeveloped land, it is necessary that the valuer uses

- accurate data
- and market understanding

The residual method - Opportunities and risks

SUSTAINABLE DEVELOPMENT GOALS

International Federation of Surveyors supports the Sustainable Development Goals

Commission 9

Valuation and the management of real estate

Thanks for listening!

Serving Society for the Benefit of People and Planet