



# The DANTER REPORT

A Periodical of Commercial Real Estate Research

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## Being There: a Guide to Danter Company Market Feasibility Methodology

This special issue of *The Danter Report* is based on the requests of many of our clients for a concise statement about our market feasibility methodology. This special report is designed to help all those involved with interpreting a market study understand our recommendations and the process we undergo to reach them.

At its most basic level, for any given proposed project and any specific market, the market feasibility study is designed to answer two basic questions:

- 1) What is the current condition of the market?
- 2) How will the market respond to the proposed project?

### MARKET CONDITION

#### IT ALL STARTS WITH THE FIELD SURVEY

At The Danter Company, we feel that the only way to determine the current condition of a market is to go there ourselves. All our methodologies are predicated on receiving complete and accurate primary information about a market.

The field survey is the most important component of any market study. That is why we employ a professional staff of field analysts whose primary job is to travel to the site and gather the critical information about *each* project in the market area.

All our professional staff members have received extensive training about market methodology and how to gather accurate

market information. Each area project is visited and evaluated by our field analyst, usually posing as a prospective tenant. Our field analysts take pictures and collect brochures. (Our photographic database is the largest of its kind.) Should it pose difficult to pry information from management, our field analysts knock on tenant doors, count windows, count mailboxes, count cars, and read meters to get the data we need.

Each project is surveyed to determine unit mix, rents, vacancies, unit and project amenities, the year opened, floor area, utility information, the number of floors, tenant mix, and other information that might be necessary for a thorough analysis.

### THE EFFECTIVE MARKET AREA

The Danter Company has developed several key methodologies which work together with the field survey to give us a clear picture of any multifamily market. The most important of these methodologies are the **Effective Market Area<sup>SM</sup>** (EMA) and the **100% Data Base**.

The first step in any market study is defining the market area, because not all market areas are alike. Several basic methods exist for determining the appropriate market area.

One common method is radial analysis. A series of concentric circles is drawn around the site at, for example, distances of 3, 5, and 10 miles. The areas within these circles are then analyzed. This method is usually employed for one reason—it is easy.



*We don't think you can accurately determine the condition of a market without going there.*



*Determining the correct market area is critical to a market study's success: incorrect market area, incorrect results*



A second method, common in studies for governmental bodies, is to base market areas on boundaries between governmental units. In such a method, county, township or city boundaries might become the boundaries of the market area. This, too is an easy solution since most secondary data are reported by political delineations.

A third methodology, developed by the Danter Company, is the Effective Market Area. The EMA is defined as the smallest geographical area from which a project can expect to generate 60% to 70% of its support. It is not easy, but it gives us a better reading of the true market area for a project.

When we determine an EMA for a specific site, we look at several factors, including geography, demographic analysis, mobility patterns, and area perceptions

**Geographical factors**—rivers, railroads, hills, and major freeways often define neighborhood boundaries. These factors, which can play a big part in where people move, are ignored in radial analyses. In fact, geographical factors are often more important than governmental boundaries, as market areas often cross county, township, or city borders.

**Demographic factors**—population and household trends, housing and income characteristics, differences in socioeconomic

makeup of individual neighborhoods, and growth figures all are analyzed to help identify the EMA. Radial analyses cannot take all these characteristics into account, and often can skew a report by including neighborhoods of vastly differing socioeconomic makeup.

**Mobility factors**—interviews with area real estate professional and civic officials are combined with our past experience in determining mobility patterns. Mobility patterns within an area are predictable, and while individuals occasionally act counter to prevailing trends, mobility analysis can help pinpoint where the majority of tenants for a particular project are the most likely to come from. Radial analyses cannot make these distinctions.

**Area perceptions**—we conduct interviews with area officials, project managers, and real estate professionals to determine area perceptions and how they relate to the previous factors. These area perceptions, in conjunction with our past experience in hundreds of markets, help determine mobility patterns, a key component of any market feasibility study.

Our field work is critical to determining our EMA. We can determine a *preliminary* EMA before we send out our field analysts, but the interviews they conduct with area real estate professionals and apartment

▼  
*Radial analysis is fast, efficient—and very often wrong.*



▼  
*We've probably been there already. Our 8 million unit database gives us an edge in most markets we visit. Plus, we have the data to track historical market changes.*



## WHY NOT SELECTED COMPARABLES?

Many companies use selected comparables for market feasibility studies. Selected comparables is one of several methods that appraisers use to determine property value. When applied to market feasibility, however, selected comparables has several flaws. Therefore, we have developed a fully documentable methodology specifically for determining market feasibility.

First, the Danter Company methodology, based on the 100% Data Base identifies market status at all pricing and amenity levels. Selected comparables can only examine the market at certain price or amenity levels, and then only with a sample. Also, without the 100% Data Base field survey, selecting comparables is a guessing game.

Second, the larger, older projects that are functionally obsolete, having little closet or storage space, small bedrooms, and generally lacking modern floor plans and design features that fill many markets cannot be

compared with any accuracy with the potential performance of a new, well-designed project with modern design. Such properties may be critical, however, in providing step-up support for new development.

Third, poor selection of comparables can create a false picture of the market, making it subject to sampling errors. One or two poorly managed comparables can make a good market look bad. Well-managed comparables in a poor market can make it appear better than it is.

Fourth, often selected comparables from outside a project's EMA are used. Such projects draw from a different tenant base with different socioeconomic characteristics. What works on the east side of town may not work on the west side. Poorly chosen comparables can give a false picture of a project's potential.

▼  
*Our Comparability Index rates all projects on three criteria applicable across all market areas: unit amenities, project amenities, and curbside appeal. This allows us to measure all units on the same scientific basis*  
▲

▼  
*The greatest amount of support for any multifamily project comes from tenants already residing in area apartments. Quantifying these tenants through a 100% Data Base field survey allows us to quantify potential capture.*  
▲



managers and the market trends they discover often cause our field analysts to revise the EMA to reflect market conditions

Our research indicates that tenants already residing in other modern apartments within the EMA are usually the largest single component of support for an apartment project. Typically, an apartment project can expect approximately 45% to 50% of its tenants from other apartments within the EMA. Adding support from within the EMA from new household formation, home ownership, or other non-modern rental properties, increases the total EMA support to 60% to 70%, depending on the demographic makeup of the EMA. Quantifying this support also allows us to accurately measure markets with limited (or no) modern apartment development.

### **THE 100% DATA BASE**

To determine the depth of support for new development, it is crucial to identify support at all rent and amenity levels. Most markets have a continuum of housing, starting with entry-level units, and moving to upscale units as units include more amenities and higher rents. Tenants move up the continuum as their financial status increases, or as their space needs change through marriage, children, or other socioeconomic status changes.

Our solution is the 100% Data Base. In every market area we study, we visit 100% of the modern apartments to gather the primary information necessary to analyze the market accurately.

Our analysis identifies the number of market-rate and government subsidized units in the market and vacancy rates by unit type (i.e., studio, one-bedroom). We also identify construction trends by tracking the year of construction for each modern apartment development, and the vacancy rates by year of construction. As a result, we can identify whether vacancies in the market are related to the age of the product.

Also included is a distribution of rents and vacancies by unit type. Using this distribution, we can determine how one-bedroom or two-bedroom units are performing at any given pricing level. We

can also identify price points in which opportunities for development exist.

Another analysis key to our conclusions is the regression analysis. Each apartment is rated on its existing amenities and curbside appeal, with point values assigned to each amenity. These factors combine to create the Comparability Index. We plot each project by rent and Comparability Index to determine market-driven rents at any amenity level. This regression analysis plays a key role in determining the supportability of a project and establishing comparable market rents.

The 100% Data Base gives us the ability to have expertise in every market we study. As a result, we can combine our interviews with “local experts” with the documented facts to provide a complete picture of a market at all levels based on primary information. Also, the 100% Data Base process is the easiest for a reader to follow, because the data are presented in full. The question of which property is selected is eliminated.

### **MARKET RESPONSE**

Once we have a 100% Data Base from our field survey and the necessary secondary data, our project director, who has experience analyzing hundreds of markets (not only as an analyst, but also in the field), can then make recommendations regarding expected market response.

The key result of any market feasibility study is the absorption rate. The absorption rate is the measure of how many apartments we think the project will be able to lease after opening on a monthly basis. To determine the absorption rate, we look at many factors, the most critical of which are step-up and step-down support and a rent/value analysis.

### **STEP-UP/DOWN SUPPORT**

As explained earlier, our research has indicated that the largest component of support for new modern apartment development comes from existing apartment tenants. Our 100% Data Base allows us to quantify this support using an analysis of step-up and step-down support.

Our research has indicated that apartment tenants are willing to pay more, or “step up”

their rents, for an apartment that they consider a value. The level of step-up support varies with different markets and the amenity level of the development. Tenants at the high end of the market may step up their monthly rent as much as \$150, but most tenants are only willing to step up their rent up to \$50.

We identify the number of units in the market with rents up to the step-up support level for the proposed rents for the subject site. This enables us to determine the depth of step-up support. Then, we compare the number of proposed units to the number of units of step-up support, and express this as a percentage. If this percentage is low (a small number of proposed units and a large number of units in the step-up support base), this is reflected in a higher expected absorption rate. Naturally, analyzing the competition's step-up support is also critical.

### RENT/VALUE ANALYSIS

A second important consideration in determining the projected absorption rate is the rent/value analysis. The regression analysis is used to determine the market-

driven rent for a project at any amenity level. Using this graph, we are able to determine the relative value of the proposed units. The relative value of the project is then reflected in our projected absorption.

Based on these analyses, we can recommend changes that allow a project to increase performance. For example, we can recommend rent adjustments to make a project more of a value, or to place it within a market niche experiencing less competition. We also review amenity packages, and can suggest ways to fine-tune for competitive advantage (or to head off possible disadvantages).

### IN CONCLUSION

We believe the market study is one of the most important steps in the development process. A quality study not only predicts absorption, but can fine-tune product to achieve greater success within the market. In addition, our policy of continued consulting until project finalization ensures that the market impact of all changes is fully evaluated and documented.

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*Regression analysis allows us to scientifically identify the market-driven rent at any amenity level*



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*Got a question about real estate research and our methodology? Give us a call: (614) 221-9096*



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