What is comparative market analysis (cma)?

Business

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Comparative market analysis, known in short as CMA, is a tool used in the real estate industry to estimate the value of a home. The basic premise of comparative market analysis is to calculate a property's value based on the average price per square foot or price per square meter of similar, recently sold properties in the same geographic region. Although comparative market analysis is never 100% accurate, it gives a simple and reliable framework for real estate valuation.

In this complete guide to comparative market analysis, we'll go in-depth on how to carry out comparative market analysis, when it should be used, and why — answering many other questions along the way.

How to Conduct Comparative Market Analysis

As we touched on above, comparative market analysis is used to generate an estimated value for a property, typically a home. The most reliable way to do so is by referencing the sale prices of nearby, recently sold properties that can be considered " similar". In fact, it's this comparison to recently sold properties which puts the comparative in comparative market analysis.

The steps for conducting a comparative market analysis are actually very simple. They are:

- Search sold property records for at least three recently sold properties that can be considered “ similar.” All of the properties which you are comparing should be located in the same geographic region as the property being valued, but we’ll talk more about what makes properties similar in a second.
- Calculate the price per square foot or price per square meter for each similar property. For each of the similar properties, calculate the price per unit area (unless this is already included in the sale record). You can do this by dividing the property’s total sale price by its total area.
- Calculate the average price per unit area across similar properties. You may find that the price per unit area differs between the similar properties. As such, you now need to calculate the average price per unit area across those properties. You can do this by summing up the similar properties’ prices per unit area and dividing by the number of similar properties, or with the help of spreadsheet software.
- Multiply the area of the property being valued by the average price per unit area of similar, recently sold properties. This will give you a rough estimate for the value of the property, which even accounts for the current strength of the real estate market.

In fact, those steps make up the easy part of comparative market analysis. The difficult part of comparative market analysis is choosing three or more properties that are similar. We’ll discuss what makes a property “ similar”, and how you can find them, just now.

What Are Similar Properties?

The key assumption in comparative market analysis is that you compare the property being valued to other, recently sold properties which are sufficiently “ similar”, ensuring an accurate valuation. There are several factors you should review when determining the similarity of two properties:

- Location

Finding properties in the same geographic location is key for them to be considered similar. If possible, the properties you’re comparing to should be located on the same street as the property you are valuing. If you can’t find recently sold properties on the same street, aim to find recently sold properties in the same neighbourhood.

- Size

Although comparative market analysis corrects for discrepancies in the sizes of properties, it’s best to choose similarly-sized properties for comparison. This is because smaller properties may have a higher price per unit area or vice versa.

- Beds and baths

One of the most important factors for those comparing properties is the number of beds and baths. Typically, the more bedrooms and bathrooms a property has, the higher its price per unit area.

- Finish

The most difficult factor to evaluate in determining the similarity of properties is the quality of the finish inside the properties. Whether the windows are double- or triple-glazed or the bathrooms are finished with granite or tile can make a big difference to the price per unit area of a property.

Also make sure that the properties you're using for comparison purposes have been sold recently. This is because fluctuations in the real estate market may change the actual value of a property over time. As a general rule, aim to compare to properties that have been sold within the last two or three months.

Adjustments in Comparative Market Analysis

While comparative market analysis can be an extremely accurate valuation tool in built-up, liquid real estate markets, the lack of comparable properties in sparser or more illiquid real estate markets may cause poor valuations. As such, if you can't find comparable properties, you should use so-called adjustments to adjust the discrepancy in values of the properties.

For example, if you are valuing a three bedroom, two bathroom property, but can only find two bedroom, two bathroom properties for comparison, you may choose to make an adjustment. You can assume that the extra bedroom in the property you are valuing adds value, so you can add a flat adjustment onto the valuation produced by comparative market analysis.

There is no easy way to calculate accurate adjustments for comparative market analysis. It takes years of experience in the real estate market. With that in mind, real estate agents can be of great help when conducting comparative market analysis.

When to Conduct Comparative Market Analysis and Why

You should carry out comparative market analysis before buying or selling a property. If you’re buying a property, comparative market analysis can be a useful tool to ensure you don’t overpay. On the flipside, comparative market analysis can be a valuable tool when selling a property, to ensure you receive a fair price. Also, in both cases, a better understanding of how the property’s value is derived can make you a more powerful negotiator.

Conclusion

To wrap up, comparative market analysis is a real estate valuation tool that draws on the sale prices of similar, recently-sold properties. While the process itself is surprisingly straightforward, finding comparable properties can often be quite tough. However, whether you’re buying or selling a property, you’ll find that comparative market analysis could save you quite a bit of money!

If you want to perform market analysis in industries other than real estate, we highly recommend you first check out what market analysis is in general.

Photo by Staff Sgt. Teresa J. Cleveland