

Capitalization Rate

Capitalization Rate can sometimes go by two different definitions. Capitalization rate is a term used in real estate to describe the net operating income of a property relative to the cost of that property. It is very similar to a return on assets ratio, and it looks like this:

$$\text{Capitalization Rate} = \frac{\text{Net Operating Income}}{\text{Cost (or Value)}}$$

In stock analysis, (according to Graham and Dodd) capitalization rate refers to the last step in a simple stock or firm valuation. The analyst first determines an appropriate level of earnings or dividends to capitalize and then applies a capitalization rate to this number. The capitalization rate denotes the factor used to determine the present value of the earnings (a multiplier) or the dividends (a discount rate).