APPRAISING

Looking Inside the Appraiser's Crystal Ball

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Relocation appraisers give serious consideration to past and current data on interest rates, unemployment figures, political atmosphere, and trends when determining the anticipated sales price of a home. Martin spoke to appraisers from many regions of the country to get their forecast on the real estate market.

How does an appraiser forecast? What crystal ball is used? Within the development of each ERC Summary Appraisal Report, the appraiser must use forecasting in estimating an opinion as to the "anticipated sales price."

The appraiser has in mind the typical marketing time and the reasonable marketing time not to exceed 120 days. The amount of marketing time used will be the lesser of the two.

Marketing time is a reflection of the existing inventory of homes and demand for homes in that particular area. When demand is significantly more or less than the available supply of homes within the 120-day marketing time, a forecasting adjustment is considered appropriate.

When reviewing current listings and sales, as well as those at previous times, the appraiser can draw a conclusion as to the direction of the market. For example, in my own marketplace for Orland Park, IL, according to the Multiple Listing System (MLS) of Northern Illinois, 392 single-family attached homes (condominiums and town homes) sold during the 12 months that preceded November 12, 2001. The range in sales price was between $71,000 and $498,750. The average of the mean sales price was $161,003. The average marketing time was 43 days.

In comparison, the period for nearly one year earlier (the 12 months that preceded November 30, 2000) the average of the mean sales price was $147,337—based on 396 sales—and had an average marketing time of 66 days. The recent 12 months reflected a 9.3 percent average price increase and a drop in marketing time of nearly 35 percent (from 66 days to 43 days).

Currently, there are 125 homes priced from $92,900 to $429,900 with an average asking price of $200,705 and an average time on the market of 59 days. A year earlier, there were 202 listings with an average marketing time of 63 days for homes on the market. This indicates that the market for town homes and condominiums in Orland Park is excellent.

However, there is the anticipation of a significant deterioration in the market after the September 11 terrorist attacks. Therefore, the current statistics compared to a year ago indicate a significantly stronger market. While it is possible some deterioration might occur within the market, this is not borne out in either the current listings or the current sales as compared with the same data the same month a year ago.

Only by analyzing the aforementioned data—and more specifically, data within the immediate marketing area—is the appraiser able to make a reasonable forecast. The evidence within the market not only suggests what adjustments might be appropriate to the present, but also what might be a reasonable forecast.

Other indicators that might be used when market forecasting include, but are not limited to changing interest rates and the likelihood of additional changes; changes in unemployment figures; and the political atmosphere locally, regionally, nationally, and internationally.

Toward the end of 2001, I tried to gauge where the national and regional housing markets were headed by asking several active relocation appraisers for their thoughts on forecasting.

These appraisers were asked in late December and early January to keep in mind the following:

"In light of where we are now with the discount rate cut by the Federal Reserve Board to a 40-year low, and rising unemployment: What is your outlook? Are you forecasting a decrease, increase, or neither? Does your MLS or other service show any downtrends in your market area? Please offer any statistics or articles that show developing trends since September 11."

10 Percent Reduction in 2001
Nancy L. Zawaski, CRP, Zawaski & Zawaski Real Estate Appraisers, Western Springs, IL. "I find that in some instances, there has been as much as a 10 percent reduction in property values since the beginning of 2001. This appears to be especially true in the 'upper-bracket' housing price range or when properties are competing with new construction.

However, in other instances, there has been no decrease at all. Properties that have held their values are generally those in the 'starter' price range or when there is very little available for sale in a given market area."

Arizona Market Strong
Jay K. Delich, SCRP, SRA, Delich Appraisal Services,Scottsdale, AZ. "Our top-end market shows extended market times and stair-step decreasing asking prices, in addition to a shift to an oversupply [There are more than 900 homes for sale in Maricopa County, AZ, which have an asking price of more than $1 million.]. The market for homes priced up to $500,000 is slower, but remains active. However, some in the industry think that the September 11 tragedy is having an effect, while others think this is the normal seasonal time for a slow down. We will break a record with nearly 36,000 new housing starts this year, and our local economists still say that the market shows appreciation and that our market is strong because owners are using their equity appreciation to move up. Go figure...I comment in the forecasting section within the ERC Summary Appraisal Report that 'the forecasted market assumes continued homesale activity and stable economic factors.' I have had two appraisals with negative forecasting adjustments, and both anticipated sales price estimates exceed $750,000."

Sitting on a Fence
Scott Pettifer, CRP, MAI, SRA, Pettifer & Associates, Santa Ana, CA. "In Orange County [CA] it varies from neighborhood to neighborhood. There is no specific evidence at this time to warrant a forecasting or discount adjustment to the majority of sub-markets. But it's like we are sitting on a fence. Things could go either way. In a lot of neighborhoods, inventory is still so low most properties sell in 120 days. Condominiums and lower-priced homes are selling in less than 30 days in many neighborhoods. We are seeing some luxury home markets [those with units priced at $750,000 and greater] with typical market periods exceeding 120 days. In those cases, a negative forecasting adjustment would be warranted.

"In most markets, buyers clearly are not as aggressive as they were earlier in the year. The only things keeping the market from a serious downturn are the low-mortgage interest rates and our county's unemployment rate, which is lower than most other areas of the country. In many areas, home prices have risen so fast it's hard to believe there is more room for home prices to rise in the short term. Many areas would seem to be inflated, but because of the strong local economy, we have not experienced much softening in home prices. I think the complete picture will be much clearer by the first quarter of 2002. There is just no concrete evidence right now to apply a forecasting adjustment in most neighborhoods. We are keeping a close eye on our residential sub-markets. If mortgage interest rates stay low and people still have their jobs, the residential market will be fine. If rates rise and the local economy experiences significant job losses, we may be in trouble."

About a 30 Percent Reduction
Jeffrey G. Otteau, SCRP, IFA, president, The Otteau Appraisal Group, Inc., East Brunswick, NJ. "We've seen about a 30 percent reduction in contract sales activity during the past month or so. I attribute about half of that to the backdrop of recession-driven economic trends, and the other half to the aftereffects of September 11. I've been applying negative forecasting adjustments since September 11, because the expectation that the high-water mark of prices in spring and summer of 2001 won't be maintained in this new environment."

Everything Is 'Normal'
Patrick J. White, CRP, SRA, White Appraisal, Inc., Cincinnati, OH. "For one, I probably have negative-forecasted only twice out of the 30 appraisals I've done since September 11. Second, there was no 'direct' tie with September 11. Third, the negative forecasting I have done is due to 'micro' judgments of supply and demand, i.e., supply high with plenty of competition from builders; dampened demand based on days on market of actives; and conversations with agents saying that the phones are quiet, showings are down, or buyers are being slow and picky. Fourth, there is some consideration because of the perennial downturn of demand during November,

December, and January.

Finally, it is price range-driven—partly. Everything is 'normal' in the greater Cincinnati market of homes priced up to around $250,000.

"In other words, supply-and-demand is balanced or even good up to that level; the demand seems to drop as the price goes up. These items would cause me to negative forecast in any time period. If September 11 has had an impact, it is indirect.

"The measures that should be used still should be locally extracted. I'm doing a lot of listening to Realtors about what it is happening at their office. Are the phones ringing? Are people looking [for homes]?

"The thought occurs to me that we are busy because of refinance appraisals. This large block of property owners is digging in with these low rates [The national average on a 30-year mortgage fell below 7 percent in mid-January, its lowest level since Thanksgiving.]. This may have an impact on demand for other and new housing. Should the rates go even lower, they might cause even more damage to future demand, if most consumers are refinancing.

"I may be wrong in my logic. Just the opposite happened in the auto sales sector—the zero percent financing helped General Motors, for example, have its best October sales figure in years. But people don't refinance cars—they get a new one. I read an article about the soon-to-be glut of used cars on the market and the good deals to the consumer to be found there if the new car sales keep up."

A Dramatic Downturn
A.L. "Chip" Wagner III, SCRP, IFA, A.L. Wagner Appraisal Group, Naperville, IL. "I am able to track downturns in markets through many methods and sources. First and foremost, I talk to the real estate agents working with buyers to get a feeling for the mood of the market. Most that I spoke to said that the market stopped between September 11 and October 1, but started to pick up again. Also, I study inventory levels very closely on each and every assignment. I do an absorption rate on the entire community, the price range 10 percent above and below what my home is being appraised for, and another on the immediate market area and/or subdivision. Also, it is imperative to stay current with economic factors relating to our global economy through published articles and news briefs.

"Because I do so many relocation appraisals, it is easy to see market trends. For example, the Naperville market, which continued to be one of the communities with the highest in demand and lowest in supply in all of the Chicago metropolitan area, was in November 2001 up to a 3.3-month supply, which is the highest level it has been since 1996. I consider a three- to four-month [90- to 120-day] supply to represent a balanced situation. I've watched the months-supply inventory level rise this year in Naperville from 1.2 months to more than 3.0 months after September 11.

"I also analyze the days on market and analyze listings more than I do sales. I place strong emphasis on selecting good listings in a relocation appraisal—even more so during a down market.

"Listings are very important during a down market. I adjust out the listings just as I do the closed sales to estimate an adjusted list price. If my three sales are adjusting out higher than my three listings are adjusting out, this may lead to either a market change adjustment for a declining market and/or a forecasting adjustment for market that is softening and continuing to soften.

"I make sure that my subject is not appraised above the adjusted list price of my competitive listings. This tells the true story. If the appraiser has a difficult time finding good listings, or if they are under contract, market conditions may be good.

"I have not seen a market turning downward as dramatically as I am seeing with this one. I also find certain pockets and areas remaining strong. It seems as though the first-time homebuyer market is still strong. Renters are looking to get out of apartment buildings, and are taking advantage of the low-interest rates to purchase [a home or town home]. The move-up and luxury buyers are standing pat, waiting it out to find out whether or not they have a job tomorrow.

"As far as hard statistics, much is in our MLS system. But the secret is to understand how to use and interpret the data, and to run these statistics all along, so that you can see the trends. Overlook the seasonal trends by looking at where we were at this time last year. By pulling up appraisals that I did [one year ago], I find my answers are all there. All of this with some common sense and a bit of luck, and the basis for your forecasting adjustment is covered."

In summarizing what each of the appraisers wrote, each market must be analyzed to determine what is happening prospectively in the market and what has happened in the market retrospectively.

Using benchmarks, particularly in markets that have seasonal changes such as in the Midwest, it is imperative to consider what has happened at the same time a year and even two years earlier. Changing interest rates, general public opinion, unemployment figures, and general growth rates might give some direction or anticipation for the direction of the market, but cannot by themselves reliably predict change.

Even sub-markets within markets must be analyzed. What may seem obvious in a specific community, may be contradicted to some extent by the specifics occurring within a particular development or even a portion of a particular development.

The crystal ball we started with might have seemed clearer at the beginning of the article, rather than at the conclusion. While there are no absolutes in forecasting the "anticipated sales price," neither are there absolutes in the forecast of value for stocks, bonds, or other publicly traded commodities.

Nearly all appraisers indicate that they have some markets to which they have applied negative forecasting. But at the same time, nearly all say they have had markets that had either no change forecast or a positive forecast.

The important thing is for the appraiser to consider all of the evidence within the market to make sure the transferee is being treated in a manner that is consistent with the market. In that most of our clients choose two or more appraisers to perform an ERC appraisal, a consensus of opinion and consistency within the appraisal process can be determined.

Editor's note: Nationwide existing homesales for January 2002 increased by an all-time record rate of 16.2 percent, compared to December 2001.

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