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Appraisal Insights for Real Estate Professionals

Will a "Declining Market" Kill the Deal?

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While it may be more noticeable in some areas than others, or within certain value ranges of a community; for the first time since World War II, the U.S. real estate market is experiencing declining property values nationwide.

What should you look for? How should the appraiser address the market conditions? Why should it be addressed?

Appraisers have a responsibility to the lending community to accurately reflect current market conditions so that proper investment decisions can be made. This includes unfavorable conditions such as declining markets, which is typically addressed early in the appraisal process. In most residential loans, it is found on the first page of the appraisal report and is consistently considered throughout the remainder of the analysis. In the comparable sales grid section of the appraisal report, see the "Date of Sale" line for negative adjustments. This reflects the decline in market value between the date the "comparable" sold and the effective date of the appraisal.

In depreciating markets, adjustments may be made on a monthly basis, a quarterly basis, or in slightly declining markets but still "soft" areas, a yearly basis. The appraisal report should clearly detail the necessity of the adjustment with support through statistical analysis, and/or paired sales analysis. One of the best examples of a Paired Sales Analysis is a case where the same home sold twice without any meaningful property changes completed. Appraisers can analyze changes in market values and buyer attitudes by comparing these sales.

If a declining trend is accurately analyzed within an appraisal report, is it going to "kill my deal?"

By accurately analyzing the market, the appraiser provides both clients and investors with sound decision making tools. Secondary lenders have no restrictions on purchasing loans in declining markets if proper analysis is provided. This is clearly indicated in the Fannie Mae Single Family Selling Guide, Part XI: Property and Appraisal Guidelines XI, 403.03: Trend of Property Values, Demand/Supply, and Marketing Time (01/31/06) which states, in part, "The appraiser must report on the primary indicators of market condition for properties in the subject neighborhood by noting the trend of property values..." "Because we purchase mortgages in all markets, this is particularly important for market areas that are experiencing significant fluctuations in property values (including sub-markets for particular types of housing within the market area).

Proper and accurate reporting of market trends won't "kill the deal", but it will provide needed information for informed underwriting of the risks associated with the loan.



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