Presentation

What is an Appraisal:

Let us start out with the boring, official dictionary definition. The Dictionary of Real Estate Appraisal, 6th ed defines appraisal as. “The act or process of developing an opinion of value; an opinion of value.”

Boiled down, an appraisal is simply an opinion of value. But before you rush into things and say, “Well, if it is just an opinion, then who cares? Everyone has an opinion, right?” Absolutely! Everyone is entitled to their own opinion. However, the appraiser must complete an appraisal (opinion of value) that is supported. We do not have the luxury of simply pulling a number out of thin air and saying “that’s my opinion, so therefore, it’s an appraisal!” Appraisers are bound by our standards of professional practice that state we must provide credible results to our client. Those results must be supported by the market, and not just our own opinions and/or feelings.

As defined in Uniform Standards of Professional Appraisal Practice (USPAP), an appraisal is the act or process of developing an opinion of value. The valuation process is a systematic procedure the appraiser follows to answer a client's question about real property value. The most common type of appraisal assignment is the development of an opinion of market value. It may be said that value is the present worth of all rights to future benefits, arising out of property ownership, to typical users or investors.

An appraisal report is usually a written statement of the appraiser’s opinion of value of an adequately described property as of a specified date. It is a conclusion which results from the process of research and analysis of factual and relevant data. Real estate appraising methods are being standardized by virtue of the experience and practice of qualified people in all parts of the country who encounter the same types of valuation problems, and who by various methods and processes succeed in solving them in an equitable manner. It is natural, however, that differences of opinion may exist as to the value of specific parcels of real estate and the means of estimating their value.

Real estate appraisal is the process of developing an opinion of value for real property (usually market value). Real estate transactions often require appraisals because they occur infrequently and every property is unique. The location also plays a key role in valuation. However, since property cannot change location, it is often the upgrades or improvements to the home that can change its value. Appraisal reports form the basis for mortgage loans, selling a property, settling estates, divorces, and taxation.

An appraisal is an objective and professional analysis of a property’s value. An appraisal aggregates an array of information including details on the home/property itself (the floor plan, quality, condition, and amenities), a visual inspection, real estate trends in your area, and how much nearby homes in your area sold for.

The licensed or certified appraiser, by reason of professional training, experience, and ethics is responsible for furnishing clients with an objective third party opinion of value, arrived at without pressures or prejudices from the parties involved with the property, such as an owner or attorney. The appraiser has a heavy personal and professional responsibility to be correct and accurate in opinions of value. Otherwise, the appraiser’s clients may easily suffer loss and the appraiser’s professional reputation may also suffer.

Steps in the Appraisal Process

1) Frame the purpose or identify the problem.
2) Record the data needed and its sources or references.
3) Collect, document, and verify the data.
4) Collect, document, and verify the data for each approach.
5) Examine and analyze the data.
6) Reconcile data for the final estimate.
7) Draft an appraisal report
8) Sample Appraisal Report

The three approaches to value, Sales, Income, and Cost

Basically, there are three approaches to property valuation used by appraisers. Each gives a separate indication of value, yet the approaches are all interrelated and all use market comparison techniques. All three approaches are considered in each complete assignment. However, all three are not always employed, depending upon the property type and the process and report type agreed to by the client and the appraiser.

The sales comparison approach is based primarily on the principle of substitution. This approach assumes a prudent (or rational) individual will pay no more for a property than it would cost to purchase a comparable substitute property. The approach recognizes that a typical buyer will compare asking prices and seek to purchase the property that meets his or her wants and needs for the lowest cost. In developing the sales comparison approach, the appraiser attempts to interpret and measure the actions of parties involved in the marketplace, including buyers, sellers, and investors.

The cost approach was once called the summation approach. The theory is that the value of a property can be estimated by summing the land value and the depreciated value of any improvements.

The income capitalization approach (often referred to simply as the "income approach") is used to value commercial and investment properties. Because it is intended to directly reflect or model the expectations and behaviors of typical market participants, this approach is generally considered the most applicable valuation technique for income-producing properties, where sufficient market data exists.

Are all Appraisers' Created Equal

The basic differences in appraisers are the different types of Appraisal Licenses (in the State of California, we have a Certified General License (AG), Certified Residential License (AR), Residential (AL) and a trainee (AT)) and the length of time in the appraisal industry and area.

It is necessary that appraisers be exceptionally sensitive to their roles in accurately assessing the true forces affecting value. In accomplishing this, the appraiser cannot allow the general neighborhood composite of ethnic, religious, or minority populations or the general condition of neighborhood improvement to detract from a clear and objective evaluation of the property appraised on its own merits. The appraiser is responsible for keeping the appraisals timely in a changing market. It is no longer prudent to rely solely on past sales of comparable property. The appraiser must use all pertinent data and appraisal methods to ensure the appraised value is, in fact, the closest estimate of the price the property would bring if freely offered on the open market. Recent world events have resulted in property appreciation spirals to historic highs, along with creative financing approaches to generate sales, which has been followed by a collapse in property values and extraordinary levels of foreclosure and bankruptcy. Such times required exceptional appraiser sensitivity to the true market forces.

How do appraisers make, adjustments?

Paired sales/matched pair analysis, Excel MLS, and HP 12C Financial Calculator. I use the local MLS and local contractors and builders to help determine a more specific adjustment to my market area. Generally, place at least 6 in the grid. Also, cost less depreciation is a common methodology I use. I utilize a functional depreciation by measuring the presence of a specific feature. Textbook methods for adjustment support are not usually practical in our area. I also use matched pairs within the report and statistical analysis including single line linear regression analysis to support my adjustments. When possible, I have found the matched pair analysis to be the most reliable method for supporting adjustments. It is data directly from the market that is driven by the market. Other ways include:

- Allocation method
- Depreciation
- Cost to build
- Market knowledge/research
- Market extraction
- Interviews
- Experience

Common errors or ways to manipulate the appraisal result.

The most common errors or ways to manipulate the appraisal result that I have seen are as follows.

- Use of comparable sales that are not comparable to the subject in location, parcel size, design, quality, condition, size, room count, bathroom count and exterior improvements.
- Understating or overstating adjustments with no sound rationale. When comp price adjustments are further analyzed, there are strikingly disparate adjustment patterns between lower and higher valued transactions. Downward adjustments to higher valued comp sales are much smaller in size and increase less as the difference between the subject and comparable price widens—a proxy for potential differences in underlying housing characteristics between the two. The upward adjustments to lower valued comps appear more appropriate in magnitude and tend to rise commensurate with the subject-comp price difference. Consequently, less expensive comps typically become more price-aligned with the subject property, but more expensive comps have largely remained higher priced.
- Not bracketing sales, when possible (uses all low or high sales to support a predetermined value).

Current Real Estate Market and its challenges

In April 2023, San Luis Obispo County home prices were down 3.0% compared to last year, selling for a median price of $873K. On average, homes in San Luis Obispo County sell after 35 days on the market compared to 12 days last year. There were 172 homes sold in April this year, down from 307 last year.

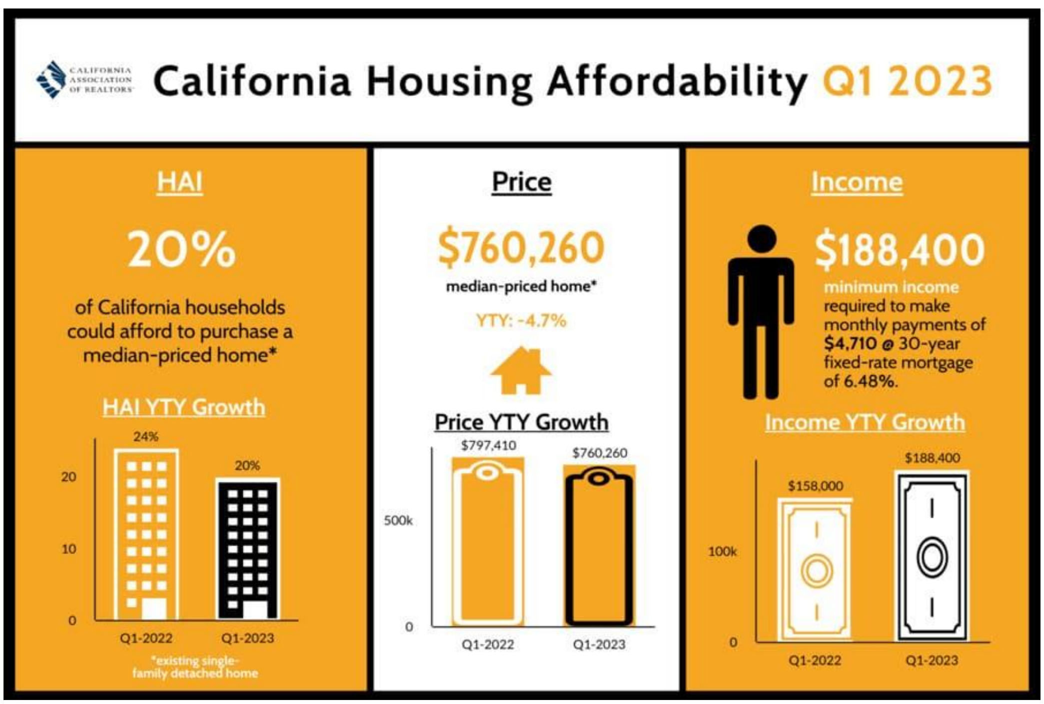
Regional sales and price activity across California has declined in sales, it was observed in all regions, with the Central Coast experiencing the most significant drop at 42.8 percent. The Far North (41.8 percent), the San Francisco Bay Area (38.5 percent), Southern California (37.4 percent), and the Central Valley (36.7 percent) also saw sales decline by more than a third compared to the previous year.

Regarding median home prices, all major regions recorded drops from the previous year. The San Francisco Bay Area experienced the most significant decline at 16.7 percent, followed by the Central Valley (8.0 percent) and Southern California (6.2 percent) and Central Coast down 3.0 percent.

Based on the latest data and market conditions, the California Association of Realtors (C.A.R.) has revised its Housing Market Forecast for 2023. The forecast provides insights into the projected trends and expectations for the housing market in the state. Overall, it indicates a challenging market environment in California, with a decline in home sales and a projected decrease in median home prices compared to the previous year. Overall, the revised forecast released in April 2023 indicates a more pessimistic outlook for the California housing market compared to the October 2022 forecast. It predicts a steeper decline in home sales and a slightly higher median home price decrease. These adjustments likely reflect the changing market conditions and factors influencing the California housing market over time.

The revised forecast considers various factors influencing the housing market, such as mortgage rates, inventory levels, buyer demand, and economic conditions. The decline in home sales is primarily attributed to higher mortgage rates and the limited availability of homes on the market. These factors have contributed to a decrease in buyer activity and overall sales volume. Despite the decline in sales, the median home price in California is expected to remain relatively high. The increase in market competition, with homes spending less time on the market and a higher percentage of homes selling above asking price, has influenced the rise in median home price. It is important to note that the forecasted figures are based on current market conditions and historical trends. However, unforeseen events or changes in economic factors can influence the actual performance of the housing market throughout the year

Housing Affordability Trends in California – 1st Quarter 2023



So, as you can see, affordability is the biggest challenge for San Luis Obispo County given the median household income in San Luis Obispo County is $82,514