Real Estate Portfolio Financial Performance Measurement –

A New Frontier for Appraisers?

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Don Guarino, MAI, FRICS, CRE, CCIM
Jeremy McCarty
Welcome! Bienvenue! Bienvenido! 歡迎！환영！

Speaker Introductions

• Doug Potts
• Don Guarino
• Jeremy McCarty
Disclaimer

The materials presented in this seminar are for educational purposes only.

They are solely the opinions and research of the authors and do not represent the opinions of the author’s employer or the Appraisal Institute, neither of which guarantee the accuracy or reliability of information herein.
LOAN PORTFOLIO MANAGEMENT
A Risk Perspective

Douglas Potts, VP, MAI, AI-GRS
Portfolio Monitoring – General Options & Risks

- Monitor assets separately or aggregate level?
- Frequency – Annual? Anniversary? Daily? RT?
- Financial position -- unleveraged? Equity only? Debt only?
- Value-setting or value-stressing?
  - Mark to market requirements – FASB / IVSC / Basel III
- Discrete or aggregate monitoring?
- Applied methods (more on this later)
  - Owner-occupied assets v income-producing?
  - Income-based assets v sales-based?
Risk Management in Banking

- Loan concentration risk managed by
  - Borrowing sector (C & I, CRE, HVCRE)
  - Geographic diversification (operating or lending footprint)
  - Loans retained (portfolio) v loans sold (2ndry market)
- Underwriting policy / process
- Real Estate collateral underwriting policy / process
  - LTV requirements
- Alignment -- Policy to Regulation to Operating Practices/Procedures
- Follow-Through & Portfolio Penetration
  - Capture all relevant lending activity
  - Consistent / appropriate handling of new / existing loan events
Portfolio Management – Loan Risk

• Fundamental Loan Classes
  1. New Loans
  2. Existing Extensions
  3. Problem Loan Management

• Only #1 = New Risk to a Bank --

• #2 & #3 already in Portfolio
  • Money is already is invested = Recovery Risk

• What generates most bank’s profits?
  • Loan Class #1? or
  • Loan Classes #2 & #3?
What is required after the origination? *(excerpts below)*

- **12 CFR 34.43 (a)** –
  “An appraisal performed by a State certified or licensed appraiser is required for all real estate-related financial transactions except those in which:” *(emphases added)*

- **(7)** The transaction involves an **existing extension of credit** at the lending institution, provided that:
  
  (i) There has been no obvious and material change in market conditions or physical aspects of the property that threatens the adequacy of the institution’s real estate collateral protection after the transaction, even with the advancement of new monies; or

  (ii) There is no advancement of new monies, other than funds necessary to cover reasonable closing costs;

- **12 CFR 34.43 (b)** –
  “For any transaction that does not require the services of a State certified or licensed appraiser under paragraph ... (a)(7) of this section, the institution shall obtain an appropriate evaluation of real property collateral that is consistent with safe and sound banking practices.”
Loan Portfolio Evaluations – Risks & Rewards

Should an evaluation opinion replace an appraisal??

• You have an appraisal on file at origination.
• Loan is up for renewal or subsequent transaction.
• Appraisal is ideal but not required.
• Evaluation is not ideal but is permitted.

• Other Risk Considerations
  • Loan grade (pass credit v troubled asset)
  • Loan exposure risk (shifts in Supervisory LTV)
  • Collateral re-marketing risk (exit strategy)
Appraisal Orthodoxy v New Approaches

• Appraisals = well-worn path
  • A “value finding” tool -- designed to establish value
  • Ideally suited to the high-risk moment of loan origination
  • Well-suited to replace any prior estimate on file (assuming ≥ quality)

• What’s best for the stuff already in the portfolio?
  • Replace a particular value-finding method with different method?
    • Appraisal v evaluation v AVM? Other? -- Strengths v weaknesses

• Are there other possible options?
A New Option? -- Portfolio Stress-Test

• Value stress-testing of existing values on file.
• Existing values on file established by prior valuations
• Measurement of change only
• Strengths & weaknesses

Should a portfolio asset get = treatment to a new loan? Shouldn’t we do a replacement valuation? Is a Stress-Test enough?
Everything is a Value Algorithm

• All value methods are essentially algorithms with unique user inputs
• Each algorithm inputs & methods = determines the nature of its result
• Differences in inputs & methods = differences in value conclusions
• Input & Methods Risks
  • Appraiser inputs & methods
  • Evaluation inputs & methods
  • AVM inputs & methods
  • Data availability v density quality v transparency

Orthodoxy v Stress-Tests -- Weighing Risks

Do new valuations create new risks?
Algorithm Determinism – Pick Your Methods

- Picking your value method = picking your algorithm
- Your chosen algorithm determines your outcome reliability
- Same methods but by different appraisers → Opinions differ.
- Reasonable v unreasonable basis for variation & disagreement

The Algorithm Devil is in the Differences!

- More differences between inputs & methods = more outcome variance
- More outcome variance = lower reliability & trust in new values

How do we reduce algorithm difference?
Exploding Alternatives – Bottling the Edge

• Challenge of $2^n$
  • $n = $ each factor where disagreement exists ...
  • Disagreement can be caused by either differing algorithm or
  • Differing ways of applying similar algorithms
  • Exploding alternative opinions.

• How can exponentially expanding alternatives offer consistency & reliability?
Perceived Risk & Algorithm Choices

• Risk Drives the Goal → Goal Drives the Scope

• Relating Goals to the 3 Perspectives on “Value”
  • Point - Range – Relationship

• Origination = Higher Perceived Risk =
  • Need for greater precision / accuracy
  • Mark to market; updated precision
  • Scope = traditional point valuation

• Subsequent Transaction = Lower Risk =
  • New point valuation? Range valuation?
  • Relationship valuation?
  • Emphasis on efficiency in Time / Cost
Point – Range – Relationship

Challenges in the choices

• New Point Valuation is subject to algorithm determinism risk

• Range Valuation – why nobody uses it
   • Oops – you have to make at least one point value (been there did that)
   • Regulated lenders will always race to the bottom for safety & soundness

• Relationship Valuation – How do we incorporated this?

How about  Portfolio Value Stress-Test?
Evaluations & Relationship Value-Stress Tool

• The Nexus of Accuracy v Adequacy
  • Existing collateral & the subsequent transaction
  • Transaction cost v flat profitability shift
• Floor values on file as adequacy filter
  • Against current balance? Increasing balance?
  • Declining value? Physical deterioration?
• “no obvious and material change in market conditions or physical aspects of the property that threatens the adequacy of the institution’s real estate collateral protection after the transaction, even with the advancement of new monies” [[12CFR34.43(a)(7)(i)]]

Could we stress-test the values – “let them ride?”
Stress-Test Evaluation – Portfolio Tool

• Same asset – with its value from prior point of intake
• Value reliability established at loan origination
  • Now we measure only “change” rather than “value”
  • Minimizes numbers of inputs → increases reliability

• Tests a past appraisal’s crystal ball
  • Was the NOI forecast proved up by later performance?

• Tests a past appraisal’s editorial choices
  • What comps were available for consideration but not used
Relationship Value – Metrics Are Key

• Change (since loan inception) is a dynamic thing
  • Physical Condition
  • Market Forces
  • Asset’s Economic Performance

• Minimizing Risk - Maximizing Reliability
  • Risk scoring the stress test
  • Risk scoring the Asset
  • Risk scoring the Predictive Data
  • Risk Scoring the Predictive Model Algorithm

• Identify the black swans
“We realize it is an unnecessary department but the acronym was just too cool to shut it down.”
Key Acronyms

IFRS
International Financial Reporting Standards

FASB
Financial Accounting Standards Board

NCREIF
National Counsel of Real Estate Investment Fiduciaries

GIPS
Global Investment Performance Standards

INREV
European Association for Investors in Non-Listed Real Estate Vehicles

IVS
International Valuation Standards
Key Terms

Book Value

Mark to Market
  Debt
  Equity

Fair Value
REGULATORS

SECURITIES AND EXCHANGE COMMISSION

NATIONAL ASSOCIATION OF INSURANCE COMMISSIONERS (NAIC)

STATE INSURANCE REGULATORS
Trend is the new Trend

Jeremy McCarty, Founder / CEO

VALLIGENT
DEFINING THE FUTURE OF PROPERTY VALUATION
Portfolio Regulatory Requirements

An institution should:

- “Monitor collateral risk on a portfolio and on an individual credit basis”
- “Obtain current collateral valuation information to understand its collateral position over the life of a credit”
- “Demonstrate that sufficient information is available to support the current market value”
- “Demonstrate classification of a problem real estate credit.”
- “Can use a variety of techniques for monitoring the effect of collateral valuation trends on portfolio risk”
- “Demonstrate that it has sufficient, reliable, and timely information on market trends to understand the risk associated with its lending activity.”
AVMs – The Perfect Solution?

• Individual AVM & cascade due diligence
• Quarterly testing
• Validation
• Cost
• Hit rate
• Confidence score threshold (FSD)
What’s the Point?

The problem with point values over time

AVM, BPO, Desktop Appraisal, Evaluation, Traditional Appraisal

<table>
<thead>
<tr>
<th>6 Month BPO Results</th>
<th>Mo. 1</th>
<th>Mo. 2</th>
<th>Mo. 3</th>
<th>Mo. 4</th>
<th>Mo. 5</th>
<th>Mo. 6</th>
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<tbody>
<tr>
<td>123 Maple Leaf Street</td>
<td>$247,000</td>
<td>$262,000</td>
<td>$229,000</td>
<td>$254,000</td>
<td>$270,000</td>
<td>$250,000</td>
</tr>
</tbody>
</table>
Risk Analysis Solution – A different form of valuation services

- Rather than a point value, measure the change in the market as it affects collateral.
- Has the value significantly increased or decreased from the baseline/origination value?
  - If increased, no further action required
  - If decreased beyond a given threshold, recommend a new valuation.
- Has there been a change in the risk profile since origination?

<table>
<thead>
<tr>
<th>Market Risk</th>
<th>Property Risk</th>
<th>Valuation Risk</th>
</tr>
</thead>
<tbody>
<tr>
<td>Fraud Activity</td>
<td>Zoning</td>
<td>Distant Comparables</td>
</tr>
<tr>
<td>Significant REO Activity</td>
<td>Property Condition</td>
<td>Dated Comparables</td>
</tr>
<tr>
<td>Population Density</td>
<td>Possible Non-Permitted Addition(s)</td>
<td>Dissimilar Comparables</td>
</tr>
<tr>
<td>Local Economic Risk</td>
<td>Commercial Uses or Influence</td>
<td>Unsupported Adjustments</td>
</tr>
<tr>
<td>Declining Property Values</td>
<td>Manufactured Dwelling</td>
<td>Unreported Subject Sales/Listings</td>
</tr>
<tr>
<td></td>
<td>Atypical/Unusual Design</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Adverse External Influences</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Subject Prior Sales</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Acreage &gt; 5 Acres</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Leasehold Estate</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Highrise Condominium</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Health &amp; Safety</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Non-Owner Occupied</td>
<td></td>
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<tr>
<td></td>
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<td></td>
<td></td>
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</tr>
</tbody>
</table>
Market Risk

Market Analysis

Inventory Analysis
- Avg # Sales per Month: -14.3%
- Inventory of Listings: -6.9%
- Months Supply: 0.0%
- Avg Days on Market: 45.5%

Price Trend Analysis
- Median Sale Price: 0.6%
- Median List Price: -3.8%
- Median Sale to List Price %: 4.6%

Distressed Activity
- % of sales that are distressed: 0.0% SS 5.3% Total 5.3%
- 1 distressed out of 19 sales in the past 90 days - 5.3%

Zip Code (91913)

<table>
<thead>
<tr>
<th></th>
<th>2016 Q3</th>
<th>2016 Q4</th>
<th>% Change</th>
</tr>
</thead>
<tbody>
<tr>
<td>Avg # Sales per Month</td>
<td>28.0</td>
<td>24.0</td>
<td>-14.3%</td>
</tr>
<tr>
<td>Inventory of Listings</td>
<td>29</td>
<td>27</td>
<td>-6.9%</td>
</tr>
<tr>
<td>Months Supply</td>
<td>1.0</td>
<td>1.0</td>
<td>0.0%</td>
</tr>
<tr>
<td>Avg Days on Market</td>
<td>33</td>
<td>48</td>
<td>45.5%</td>
</tr>
</tbody>
</table>

Price Trend Analysis
- Median Sales Price: 586,214 589,923 0.6%
- Median List Price: 610,000 587,000 -3.8%
- Median Sale to List Price %: 96.1% 100.5% 4.6%
## Property Risk

### Subject & Client
- **Address:**
- **City:**
- **County:**
- **State:**
- **Zip:**

### Evidence of Listing Status
- **Evidence Type:**
- **Subject For Sale:** Yes
- **Yes, Disseminated Listing:** Yes
- **List Price:** [ ]
- **List Date:** [ ]

### Market Influences
- **Boarded Up Homes In Area:** Yes

### Subject Condition
- **Excellent / Like New:** Yes
- **Good / Very Good:** Yes
- **Average:** Yes
- **Fair / Below Average:** Yes
- **Poor:** Yes
- **Uninhabitable:** [ ]
- **Not Viewed:** Yes

### Exterior Maintenance
- **Roof Damaged:** No
- **Siding Damaged:** Yes
- **Porch:** Yes
- **Deck:** Yes
- **Roof:** Yes
- **Exterior Paint:** Yes
- **Foundation Damaged:** Yes
- **Under Construction:** Yes

### Interior Features and Appointments
- **No Interior Inspection:** N/A
- **Trim / Finish:** [ ]
- **Heating:** [ ]
- **Appliances:** [ ]
- **Bathroom:** [ ]
- **Total Rooms:** [ ]

### Exterior Factors
- **Exterior Only From Street:** Yes
- **Walk-In Interior and Exterior:** Yes
- **Security Gate or Driveway Only:** Yes
- **Exterior Only From Street:** Yes

### Property Type
- **SFR - Detached:** Yes
- **SFR - Attached:** Yes
- **SFR - Semi-Detached:** Yes
- **SPR - With Accessory Unit:** Yes
- **Manufactured:** Yes
- **Duplex:** Yes
- **Triplex:** Yes
- **Quadplex:** Yes
- **Commercial / Mixed Use:** Yes
- **Other:** [ ]
- **Use Taxable Area:** Yes

### Subject Site / Lot
- **Lot Size:** [ ]
- **Lot Shape:** [ ]

### Utilities
- **Electricity:** [ ]
- **Gas:** [ ]
- **Water:** [ ]
- **Sewer:** [ ]

### Additional Improvements
- **Garage/Carport Design:** [ ]
- **Detached:** [ ]
- **Attached:** [ ]

### Floor Area
- **Square Feet:** [ ]

### Subject Improvements
- **Foundation / Basement:** [ ]
- **Design:** [ ]
- **Exterior Walls:** [ ]
- **Roof:** [ ]
- **Windows:** [ ]
- **Doors:** [ ]
- **Additional Features:** Yes

### Notes
- **remarks:** None
- **other:** None
Valuation Risk

### COMPARABLE SALES AND LISTINGS

<table>
<thead>
<tr>
<th>#</th>
<th>Address</th>
<th>Rank %</th>
<th>Sale/Listing</th>
<th>GLA</th>
<th>Bdrms</th>
<th>Baths</th>
<th>Year Built</th>
<th>Condition</th>
<th>Lot Area</th>
<th>Other</th>
<th>Price</th>
<th>Date</th>
<th>Distance</th>
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</thead>
<tbody>
<tr>
<td>5</td>
<td>2456 Cottonwood Trail, Chino Hills, CA 91709</td>
<td>N/A</td>
<td>N/A</td>
<td>1,434</td>
<td>4</td>
<td>2.5</td>
<td>1964</td>
<td>Average</td>
<td>0.10</td>
<td>None</td>
<td>$ NA</td>
<td>NA</td>
<td></td>
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<tr>
<td>1</td>
<td>2445 Hillsborough Ln, Chino Hills, CA 91709</td>
<td>30</td>
<td>Sale</td>
<td>1,434</td>
<td>4</td>
<td>2.5</td>
<td>1964</td>
<td>Average</td>
<td>0.12</td>
<td>CDS</td>
<td>$ 535,000</td>
<td>11/09/2016</td>
<td>0.02 mi NW</td>
</tr>
<tr>
<td>2</td>
<td>2511 Maroon Bell Rd, Chino Hills, CA 91709</td>
<td>30</td>
<td>Sale</td>
<td>1,382</td>
<td>3</td>
<td>2.5</td>
<td>1967</td>
<td>Average</td>
<td>0.08</td>
<td>External Inf</td>
<td>$ 520,000</td>
<td>01/19/2017</td>
<td>0.64 mi S</td>
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<tr>
<td>3</td>
<td>2209 Wandering Ridge Dr, Chino Hills, CA</td>
<td>20</td>
<td>Sale</td>
<td>1,671</td>
<td>3</td>
<td>2.5</td>
<td>1987</td>
<td>Good</td>
<td>0.13</td>
<td>External Inf</td>
<td>$ 631,000</td>
<td>01/26/2017</td>
<td>0.40 mi SW</td>
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<tr>
<td>4</td>
<td>2948 Rustic Dr, Chino Hills, CA 91709</td>
<td>5</td>
<td>Sale</td>
<td>1,840</td>
<td>4</td>
<td>2.5</td>
<td>1995</td>
<td>Average</td>
<td>0.09</td>
<td>External Inf</td>
<td>$ 650,000</td>
<td>11/18/2016</td>
<td>0.76 mi SE</td>
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<tr>
<td>5</td>
<td>2511 Stagecoach Trl, Chino Hills, CA 91709</td>
<td>5</td>
<td>Listing</td>
<td>1,658</td>
<td>4</td>
<td>2.5</td>
<td>1984</td>
<td>Good</td>
<td>0.17</td>
<td>By Gmbh</td>
<td>$ 698,000</td>
<td>12/01/2016</td>
<td>0.12 mi SE</td>
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<tr>
<td>6</td>
<td>13358 Emerald Way, Chino Hills, CA 91709</td>
<td>5</td>
<td>Pending</td>
<td>1,425</td>
<td>3</td>
<td>2.5</td>
<td>1966</td>
<td>Good</td>
<td>0.13</td>
<td>PoolExcl</td>
<td>$ 572,000</td>
<td>01/02/2017</td>
<td>0.90 mi SE</td>
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</table>

### UPDATED BUILDING SALES

<table>
<thead>
<tr>
<th>Address</th>
<th>Sale Date</th>
<th>Sale Price</th>
<th>Land Area (sf)</th>
<th>Bldg Area (sf)</th>
<th>Year Built</th>
<th>$/SF</th>
<th>Comments</th>
</tr>
</thead>
<tbody>
<tr>
<td>1 3203 Coveview, St. Joseph MO</td>
<td>12/23/14</td>
<td>$369,900</td>
<td>18,000</td>
<td>2,204</td>
<td>2014</td>
<td>$167.83</td>
<td>St. Joseph MO MLS 106897</td>
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<tr>
<td>2 4602 Manor Dr., St. Joseph, MO</td>
<td>6/4/15</td>
<td>$379,900</td>
<td>n/a</td>
<td>1,960</td>
<td>2015</td>
<td>$194.82</td>
<td>MLS 106925,</td>
</tr>
<tr>
<td>3 4606 Manor Dr., St. Joseph, MO</td>
<td>6/5/15</td>
<td>$375,000</td>
<td>27,007</td>
<td>2,068</td>
<td>1994</td>
<td>$181.33</td>
<td>MLS 106972</td>
</tr>
<tr>
<td>4 4707 Greystone Dr., St. Joseph MO</td>
<td>11/14/16</td>
<td>$400,000</td>
<td>11,455</td>
<td>2,256</td>
<td>2016</td>
<td>$177.36</td>
<td>St. Joseph MO MLS 111883 new construction</td>
</tr>
</tbody>
</table>

| Sales Low  | $369,900   | 11,455     | 1,960          | 2014          | $167.83    |       |
| Sales High | $400,000   | 27,007     | 2,256          | 2016          | $194.82    |       |
| Sales Median | $377,450 | 16,000     | 2,136          | 2014.5        | $173.32    |       |
| Sales Average | $381,200 | 18,821     | 2,120          | 2009.75       | $180.32    |       |
| Sales COF  | 3.5%       | 43.4%      | 6.5%           | 0.5%          | 6.2%       |       |
| Sales COV  | 3.5%       | 41.5%      | 6.5%           | 0.5%          | 6.2%       |       |
Estimated volumes of portfolio, equity loan and default servicing valuations

- 933,000 Foreclosure filings in 2016 – RealtyTrac
- 2 Million Defaulted Loans in the pipeline that need at least 1 valuation per year
- 1 Million+- Equity Loans completed per year
Many appraiser’s perception of alternative valuations

• Not USPAP compliant
• Need to see the property
• Do not have the time
• I do not get out of bed for less than $100
• I prefer what I am familiar with
Technology Advancements

• Market analytics
• Comparable search tools
• Data integration
• Mobile devices
Future Prognosis

- Long-term Sustainable Value?
- Portfolio analysis standardized format
- Appraiser as analyst
- RAPT – Residential Appraisal Project Team

“Seriously?!! No one saw this coming?!”
PORTFOLIO STRESS-TEST EVALUATIONS

A New Frontier for Appraisers?
The Case for Regulatory Reform

Doug Potts
Relationships & Floor Values – More Ideas!

• Protects Safety & Soundness
  • Baseline reference stays the official underwriting estimate
  • Minimizes speculation from inflationary markets
  • Reduces “crystal ball gazing”

• Observed Value Shift (up or down) & Recommendations

• Practical outcomes shared with
  • Long Term Sustainable Value (LTSV) aka Fundamental Value
  • Mortgage Lending Value (Beleihungswert from Pfandbrief Act)

• Compatible with Other Standards?
  • Basel requirements for M-to-M?
  • FASB? IVSC?
Residential Trending - Graphical

Trend Tracker

Date ranges from 09/07/2006 to 06/30/2010

Comp Data Ranges

<table>
<thead>
<tr>
<th>List Price Range</th>
<th>List Date Range</th>
<th>Full Basement Count</th>
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<tbody>
<tr>
<td>598000</td>
<td>04/21/2006</td>
<td>73</td>
</tr>
<tr>
<td>179900</td>
<td>05/10/2010</td>
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</table>

<table>
<thead>
<tr>
<th>Sale Price Range</th>
<th>Sale Date Range</th>
<th>Partial Basement Count</th>
</tr>
</thead>
<tbody>
<tr>
<td>57000</td>
<td>09/07/2006</td>
<td>14</td>
</tr>
<tr>
<td>168800</td>
<td>06/30/2010</td>
<td></td>
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</table>

<table>
<thead>
<tr>
<th>Year Built Range</th>
<th>Size Range</th>
<th>No Basement Count</th>
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<tbody>
<tr>
<td>1915</td>
<td>2100</td>
<td>1</td>
</tr>
<tr>
<td>1938</td>
<td>2676</td>
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</tbody>
</table>
Income Stress-Testing -- IRV

\[ \text{Inc} \div \text{Rate} \rightarrow \text{Value} \]
WE JUST NEED THE VALUE TO STAY FLAT

Capitalization Modeling

7.61% R₀

Imputed Growth

LOAN BALANCE

Annual Expenses
NOI

2011Q1 Appraisal Data
2012 Prior Actual
2013 Prior Actual
Forecast
Relationship Value Stress-Testing

- Stress Testing Methods
  - Repeat sales indexing
  - Broad sales trend indexing
  - Comparative sales sets trending
  - Economic performance indexing
  - Cap or IRR indexing
  - GIM indexing

*But was USPAP built for this process?*
Navigating Through Risk
Risks on the horizon --
Identify potential threats (and opportunities)
Some we see, some we don’t

Risk Appetite Trade-Offs
Complacency ....
when is playing safe “too safe?”
How much risk is OK?
Reflection Questions ...

• Have appraisers become too complacent about risk?
• Should appraisers rely on the well-worn path to solve new challenges?
• Should appraisers push for entry into non-traditional valuation practice?

*Is USPAP getting in the way of innovation?*
“The vast majority (over 75%) of residential mortgage transactions fall outside the current definition of what constitutes a federally related transaction.”

The Appraisal Foundation --
“State Legislative / Regulatory Initiatives to Recognize Alternative Appraisal Standards” -- Update for The Association of Appraiser Regulatory Officials – April 2016

“Only 11% of all financial transactions currently tracked by the FDIC are federally related transactions. If the deminimis increases, that may diminish to 4%...... We simply didn’t know...”

John Brennan, the Appraisal Foundation --
Commercial Real Estate Risk Council Meeting – (notetaking - Doug Potts, presenter)
Baltimore MD – October 2016
Appraisers in the Financial Environment

Work We See

Work We Don’t See (and mostly don’t get)

Can This Hurt Us?
Workload v Risk v Loan Profitability

Is Risk Proportional with Workload?

Stratification Data from the QBP

80% of workload

de minimis loans

6% of risk/profit

76% of risk/profit

±10% of workload*

*DP estimate; not measured by QBP
Who Will Do the Work?

The Work Has to Go Somewhere
How Can Appraisers Recapture the Market?

• Banks desperately need effective & efficient value consultation.
• Banks will find others who will do it – *and are looking*
• Should we eliminate mandatory rules linked to USPAP-only Standards?
  • Permit alternatives to USPAP -- provide flexible evaluations
• Become consultants again – reduce appraisal commoditization
• Bring appraisers out of the cold – take back our turf
• Support a more sustainable appraisal business model
• Stress-Test task segmentation will offer options in the war for talent
Needs & Opportunities

• Risk is a constantly evolving aspect of our business
  • Solutions need to evolve in order to manage them.
  • Many sectors need creativity -- financing, consultation, legal, etc.

• Lenders must provide appropriate access to credit
  • While providing appropriately scaled documentation
  • Critical for community-model lenders with limited staff

• Appraisers have the opportunity to provide those services
  • Portfolio consultation is **A HUGE VALUE OPPORTUNITY**
  • May provide an excellent way to draw trainees into the business and a pathway to making them more technically proficient & economically viable to supervisors.
The Frontier Awaits – Who is Willing?

- Change is coming – like it or not!
- Solutions need to evolve to manage them.
- Have we lost sight of all the risks we are facing?
- Have regulations stagnated our ability to respond?
- Appraisers have tools and the creativity to use them.
- Will this industry forge ahead into new opportunities?

“PEARLS” await those who navigate the “perils”
Thanks for Attending!
Merci pour votre présence!
Gracias por venir!
Danke fürs Kommen
謝謝你的到來！
와줘서 고마워！
R I S K
A Ship In The Harbor Is Safe...But That’s Not What Ships Were Made For.