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Appraising using hindsight, during improving real estate market

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A poignant and sometimes inherently contradictory method of appraising real estate requires the appraiser to take historic sales data and apply it to current and proposed transactions. Clearly pulling data out of a declining or stagnant market does not accurately reflect the appreciation of current transfers in a growing market.

We have several tools to project historic transfers into the future, but lack the tools, in many projects (more specifically the time), to forecast historic data. Projecting data: A prediction of the future that is an extension of current and historic trends. Forecasting data: a prediction of the future based on the fundamental forces of demand. The process of projecting data is relatively simple, as it relies wholly on historic data. Forecasting data into the future, comparatively, is an entirely different animal which requires an amplified research phase including inventorying and analyzing an entire market worth of comparable property types. Given the nature of our work is mostly done behind-the-scenes, its no wonder our clients do not appreciate the breadth of research required to forecast real estate values vs. projecting historic real estate values into the future. In many ways, not having the users of our appraisals understanding of these fundamental differences leaves the appraiser with a time window that is too small, and a fee which cannot hope to cover the time invested in such an exercise. This problem is more relevant specifically at the beginning of an ascending market, which is exactly when our clients need the most meaningful and realistic analysis of the subject's value.

I have to say, I think we are more or less coming to the end of the beginning of our market appreciation cycle and some, if not many of the markets we work in actually include hard data on which to base and project a good estimate of market appreciation. Namely, the single-family residential market. In my experience during this current upswing houses were the first to transfer en masse, quickly shedding the economic constraints of this most recent recession. Land as well has begun to transfer, mostly in response to pent-up demand for future development. With that in mind, the most active appreciation markets include buyers of single-family homes. I also have the feeling that many of the transfers have been put on hold, mostly by wise buyers and sellers who could afford to hold their real estate through the recession and this turbulent period when negative values stabilize and begin their ascension into a growing market.

Given the relatively low ratio of improvements per square mile and while considering a special use property, say retail or restaurant in a smaller Maine town, the difficulty of identifying appreciating sales of similar property types defiantly lags behind lease rates on these properties. More often than not, the income-generating potential for a property is seen by an investor and quickly transformed into income based comparable which we can use in our valuation process.

Appraisers as well as clients should understand we are bound by a set of imperfect professional standards which are accurate and appropriate most of the time, whilst falling short during specific period in a market's cyclical cycle, namely during a rebounding market. It has always been my opinion that at least banks, probably brokers, and maybe some end users of appraisals should understand more about what it is we do, and the tools available to appraisers. Having the time and funding to take adequate time developing an appropriate market (macro view) and marketability study (micro view, specific property) will allow us to develop the most appropriate valuation model and provide our clients with the most accurate and relevant appraisal of our abilities.

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