Adjusting to market condition adjustments - by Bill Pastuszek

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Bill Pastuszek

Appraisal deals with the dynamism of markets. The principle of change is a fundamental appraisal concept. Appraisers operate in markets that are constantly shifting, often in very nuanced ways. Appraisers are careful, in general, to not adopt sledgehammer approaches to their work but, in doing so, often don't take advantage of many resources and techniques that are more available now than a decade, or even half a decade, ago.

Appraisers find great comfort and solace in their well-established appraisal process. A lot of technology out there isn't comfortable and feels threatening to many. And the changing landscape of GSE requirements and the promise (and danger) of AI, present challenges to residential appraising that many won't find to be easier or more fun. But the changes will represent opportunities to provide enhanced reporting in the residential environment under uncertain market conditions.

The GSEs are rolling out a new form: the form is designed to be used for all 1-4 family assignments and is designed to be interactive and flow logically depending on the type of property. (N.B. These changes are long overdue.) With the new forms, there is increased emphasis on supporting adjustments in a credible manner, including providing much more precise means of measuring market conditions (time) adjustments.

Recent guidance from Fannie May provides updates to requirements related to the market area analysis, "including establishing a 12-month timeframe for market trend derivation, identifying that the overall market trend may differ from adjustments to individual comparable sales, and including an illustration of the methodology used for time adjustments." (AI summary)

Let's take a quick look at the concept of an "overall market trend" versus "adjustments to individual comparable sales." Market condition adjustments traditionally are often based on a linear (or a constant change model) approach. Thus, an appraisal may state that prices have increased 6% in the past year based on market trends and make across the board adjustments of .5% per month. A comparable sale – let's call it #1 - that sold three months ago would be adjusted for market conditions as follows: .5%/mo. x 3 mos. = 1.5%. However, most appraisers would agree that markets do not generally perform in such a lockstep manner and the new requirements provide more flexibility and precision in arriving at market condition adjustments.

The GSEs are requiring that market condition adjustments be made from the comparable's sales date to the effective date for each comparable. Using Fannie Mae Guidance, data developed from sales may show differing levels of market increase or decrease over 12 months, for example. Thus, each comparable is viewed based on its position within the dataset. Thus, comparable #1 would be adjusted +1.5%. The data for comparable #2, which sold six months ago, shows a decrease in prices and is adjusted downwards 1%. A third comparable, having sold close to the date of appraisal, is not adjusted at all.

Undertaking a more detailed adjustment analysis requires additional data and analysis. This results in improved data gathering and analysis, as well as enhanced presentation techniques and reporting of results. Appraisers will need to employ new methods to provide supported and logical opinions. This additional requirement, while not new, represents a step forward in terms of more sophisticated analysis, which can only enhance appraisal practice and public trust.

As embattled as many appraisers have felt, given low volumes and criticisms, residential appraisers are faced with challenges that become opportunities. The new reporting formats and increased emphasis on more quantified, more comprehensive, and better market analysis and support for adjustments will result in better appraisals and better appraisal development and reporting.

Bill Pastuszek, MAI, ASA, MRA heads Shepherd Associates, LLC, Needham, Mass.