

Short- and Long-Term (Sustainable) Property Valuation

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Short- and Long-Term (Sustainable) Property Valuation

Dennis A. Webb, ASA, MAI, FRICS

Primus Valuations, USA

Dennis A. Webb, ASA, MAI, FRICS

Introduction

We understand sustainability and the
natural world

This Paper is about sustainability in the
financial world, what valuers can do to
support it

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Introduction

How many of you knew that 2005 property
values were out of sight?

And that a day of reckoning was due?

What good did it do anyone?

What's the problem?

Do you think we'll continue to have real
estate bubbles?

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Introduction

- What does a market value appraisal tell us?
- What if the entire market is wacko?
- How do buyers and sellers make decisions?
- What determines risk for a 10-year loan?
- What has happened to commercial investors? To homeowners?
- What's wrong with this picture?

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Long-Term/Sustainable Valuation

- ◆ Market value – a short-term premise
 - Buyers and sellers on *their* terms
 - Changes over the life of the loan/investment
 - Conditions of sale? Cash equivalency?

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Long-Term/Sustainable Valuation

- ◆ Market value – a short-term premise
 - Buyers and sellers on *their* terms
 - Changes over the life of the loan/investment
 - Conditions of sale? Cash equivalency?
- ◆ What might be a different premise?
 - How about a long-term “baseline” value?
 - If current market is over/under, what is risk?

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Long-Term/Sustainable Valuation

The appraiser as fortune teller? Not really

- ◆ Forecasts and Unexpected Events
- ◆ Mortgage Lending Value
- ◆ Value Trending
- ◆ Cycle Analysis
- ◆ Value Impairments

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Unexpected Events

- ◆ Risk & uncertainty – the “Black Swan”
- ◆ Taking the long-term view incorporates past unexpected events; examples?
- ◆ More past observations = reduced future vulnerability to unexpected events

“The longer you can look back, the farther you can look forward” – Winston Churchill

- ◆ 11% annually is not sustainable? Really?

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Mortgage Lending Value

- ◆ Provided for in Basel II Accord, IVS 2
- ◆ A “long-term risk assessment technique”

“The mortgage value of a property is the value that can be expected with a high level of surety, derived from the historic perspective of market events at the time of the valuation, on the basis of the durable characteristics, and which will be achieved in normal property transactions over a long period in the future.”

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Mortgage Lending Value

- ◆ German Pfandbriefe Banks
- ◆ HypZert valuers
- ◆ Specific rules:

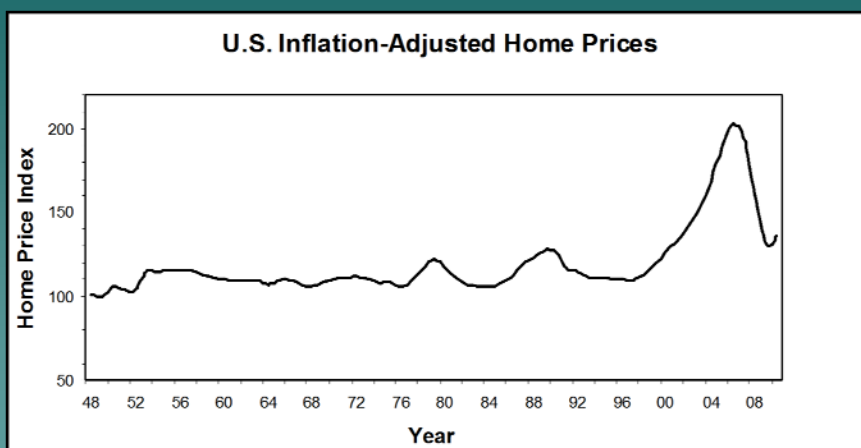
“In determining the gross income only the income may be taken into consideration that the property is capable of yielding to any owner on a sustained basis assuming proper management and permissible use.”

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Value Trending



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Value Trending

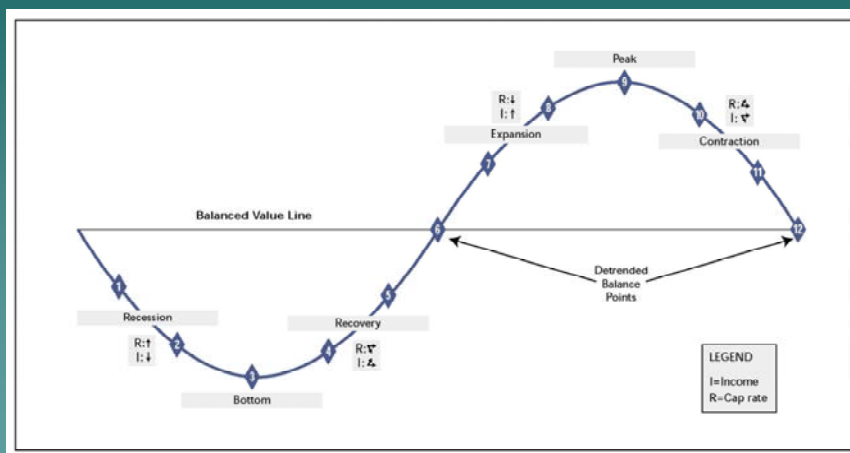
- ◆ More explicit about trajectory than MLV
- ◆ Example: Case-Shiller Index
 - Can spot reactions to past unexpected events
 - U.S. nominal value increase 4.1% 1948-1998
 - Real value increase drops to 0.2%
 - Suggest other trends, correlations, local issues

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Cycle Analysis



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Cycle Analysis

- ◆ Shorter periods, commercial properties
- ◆ Example: PWC Real Estate Value Cycles
 - Demand/supply cycle
 - Capital market cycle
 - Historic vacancy a proxy for values
 - Intended to provide support for management and investor assumptions

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Value Impairments

- ◆ Additional ways to deal with below-trend
- ◆ Common application—real estate damages
 - Transactional conditions
 - Distress and sociological conditions
 - Legal conditions
 - Building/site/infrastructure
 - Environmental/biomed/conservation

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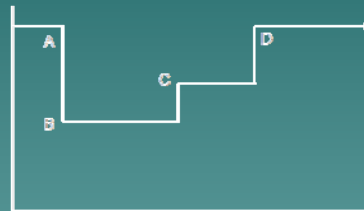
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Value Impairments

Analysis based on stages of cure over time

- A – Value is unimpaired
- B – Discovery
- C – Remediation begins
- D – Value returns to unimpaired level



Similar to discounting process for noncontrolling interests – analysis of risk and holding period

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Conclusions

- ◆ Market value vs. long-term value
- ◆ The long view reveals unexpected events
- ◆ A realistic view of risk
- ◆ Existing system, established techniques
- ◆ Push against bubbles
- ◆ Lift out of ditches
- ◆ Contribution to financial sustainability

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Thank you for attending!

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Dennis A. Webb, ASA, MAI, FRICS

011-949-443-0800

dwebb@primusval.com

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Primus Valuations, USA

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