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VALUATION PROTOCOL – VALUING IN A RAPIDLY CHANGING MARKET

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Valuation Protocol – Valuing in a Rapidly Changing Market

Introduction

This Valuation Protocol, and its purpose, is to provide guidance for the completion of mortgage security valuations of residential properties for banks/lenders, and their LMIs utilising the PropertyPRO Report format.

However, the general principles and guidance outlined in this protocol also applies to mortgage valuations of residential and non-residential properties outside of the PropertyPRO Report format.

When undertaking a market valuation for mortgage and loan security purposes, the Valuer is required to inspect the property, collect relevant property information, research the market, undertake at least a 'kerbside' inspection of the sales evidence and then prepare a valuation report which includes the Valuers opinion of the market value of the property.

Sales Evidence

As part of the valuation process, the Valuer is required to consider a variety of factors to understand and interpret the market, including recent sales of similar properties in the locality. The Valuer is required to research the local market and have regard to prevailing market conditions. This could include discussions with selling or listing agents to gain an understanding of market conditions and sentiment.

When analysing sales evidence, the Valuer is required to first make adjustments for differences in any physical and legal characteristics between the sale property compared to the subject property, and also, where appropriate, make allowance for market changes since the sale occurred.

When undertaking valuations in a rapidly changing market (whether that be in a rising or a falling market) it is critical that the Valuer utilise the most recent and relevant market evidence available. Older sales will often not reflect the current market. The most recent, unsettled sale(s) will provide the Valuer with the best indicator of market value. Unsettled evidence may be included in addition to settled sales and must be clearly labelled as 'under contract' or 'unsettled'.

Reliance on dated evidence in a rapidly changing market may result in an assessment of market value that does not reflect the market as at the date of valuation.

The Valuer must consider any current or recent sale price of the subject property. The API Guidance Paper: Valuation Procedures - Real Property notes *"a current or recent sale of the subject should be considered against other evidence as it has been a test of the market."*

It is the Valuers responsibility to benchmark all sales, including the current or recent sale of the subject property, against the current prevailing market and if deemed appropriate, utilise that sale as evidence in the valuation process.

To test the veracity of a sale, that is both relevant and appropriate for use in the valuation process, the Valuer should consider if the sale meets the IVS definition of 'market value' and the conceptual framework provisions contained in IVS 104 *Bases of Value paragraph 30.2*.

The selection of sales evidence for consideration and inclusion in the valuation report is a decision for the Valuer. This does not negate any requirements for sales evidence contained within the *PropertyPRO Supporting Memorandum* (PPSM) or instructions from the client.

IVS 105 *Valuation Approaches and Methods*, paragraph 30 provides details on the *comparable transaction method*, and *paragraph 30.7* outlines factors for the Valuer to consider when choosing sales. Paragraph 30.7 (g) notes *"actual transactions provide better valuation evidence than intended transactions."* This does not mean that agent advised/unsettled sales should not be considered and included in the report. As previously noted, they may provide evidence of recent market activity / direction and sentiment and should be considered and included in the valuation. They must, however, be investigated and verified by the Valuer prior to their use and inclusion in the valuation report. The status of agent advised/unsettled sales must be reported.

The basis of reliance on unsettled or reported transactions should be provided in the report

Role of the Valuer

The approach to valuing a property does not change in a rapidly rising/falling market.

It is the role of the Valuer to provide their professional opinion as to the market value of the subject property considering the prevailing market conditions and to identify and report on known or observable risks.

Risk Ratings

Valuers undertaking residential mortgage valuations utilising the PropertyPRO format are reminded to regularly review the Risk Rating Matrix and examples contained within the PPSM.

Of note is the *Market Direction (price)* risk rating which relates to the direction and strength of price movement in the market, that the property would most likely transact in, over the previous 12 months. Equally important is the *Market Activity* risk rating that relates to the supply and demand for competing product to the subject property.

Market Risk Ratings

Risk Rating Category	Market Direction (price)	Market Activity	Loca
	Relates to the direction and strength of price movement over the previous 12 months. Refers to the relevant market segment that the subject property is transacted in.	Relates to market activity with regards to supply and demand for competing product to the subject property. Refers to the relevant market segment that the subject property is transacted in.	The e econ prope Refer withi
1 - Low risk No readily identifiable adverse issue	➢ Stable, steady and consistent market prices.	➢ High demand and low supply of competing product to the subject property at date of valuation.	➢ L ➢ L t
2 - Low to medium risk Minor adverse issue only not warranting comment	➢ Consistent low to moderate increase in market prices.	➢ Supply and demand of competing product to the subject property in equilibrium at date of valuation.	➢ N
3 - Medium risk There is an adverse issue in the Report for the Client to consider before reliance upon the Report	➢ Early signs of a change (either increase or decrease) in market prices.	➢ Potential oversupply of competing product to the subject property at date of valuation or expected in next 6 to 12 months.	➢ A e ➢ E
4 - Medium to high risk There is an important adverse issue in the Report for the Client to consider before reliance upon the Report	➢ Definite signs of change (either increase or decrease) in market prices.	➢ Apparent oversupply of competing product to the subject property at date of valuation or expected in the next 3 – 6 months.	➢ S o ➢ L t
5 - High risk There is an extremely important / urgent adverse issue in the Report that could have a major impact on the current value and/or marketability of the subject property for the Client to consider before reliance upon the Report.	➢ Continuous and significant change (increase or decrease) in market prices. ➢ Steeply rising or steeply declining market prices.	➢ Known/current oversupply of competing product to the subject property at date of valuation.	➢ S ➢ C

As at the date of publication of this Valuation Protocol, the application of the Risk Ratings Matrix would result in elevated risk ratings for some of the *Market Risk Ratings* in some market segments around Australia. Valuers should review the examples in the Risk Ratings Matrix against the market segment that the subject property is transacted in and have reference to the underlying principles of risk ratings as outlined in the *PPSM*.

A property, or the market segment, may have multiple risk issues where each issue would be assigned a different risk category. It is the Valuer's responsibility to apply the risk ratings in accordance with the *PPSM* risk rating framework including providing specific comments relating to what is happening in the market, as at the date of valuation, that the property is located and transacted in (when and where additional specific comment is warranted).

If there are any comments or feedback regarding this Valuation Protocol, please do not hesitate to contact us at standards@api.org.au.

The API is committed to the promotion of best practice within the property industry and welcomes feedback to help this goal be achieved.