VALOCITY

THE FUTURE OF VALUATIONS

Global Valuation Reporting Trends and the Increasing Use of Technology in the Valuation Space

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Valocity Limited
Auckland, Delhi, Mumbai, Sydney

Kerry.Stewart@valocityglobal.com
hello@valocityglobal.com
www.valocityglobal.com

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Introduction

When you consider mortgage lending over the past few years, apart from house prices rising globally, little has changed. Yet, two big trends have emerged:

- Post GFC, the need for increased regulatory compliance and best practice in mortgage lending is now a part of every lender's DNA
- Increased expectations of customers for seamless and relevant digital experiences

Consequently, we have seen developments in the valuation and appraisal space to solve this, including:

- The introduction of Valuation Ordering Platforms
- The development of various Valuation Models in structured markets
- The creation of new kinds of technology to allow in-field digital data capture and reporting

Further technological developments are on the horizon or are now coming to market, including AI, blockchain, valuations where physical inspection is not required, and analytics. How will this impact the role of the valuer?

Property continues to be the most valuable asset in the world. As such, client expectations are changing with a focus on understanding likely future values, the sustainability of those values, and value enhancement reflected in environmentally responsible and resource-efficient buildings. Are valuers ready?

The Purpose of Valuations

While the theme of this paper is the discussion of the future for valuers and appraisers (using the term valuer for this paper), it would be remiss not to consider the profession as it currently exists - specifically the why do we exist?

Institutional investors and banks require valuations reflecting the current value of assets as an intrinsic part of most financial reports, transaction support, litigation support, and to assist with secured lending decisions. Critical to the delivery of the valuation, a report must be prepared by a suitably qualified and experienced valuer following appropriate professional and valuation standards. Most importantly, the report must be prepared independently, objectively, and with transparency in terms of the approach or approaches selected. It defines the basis of value, should include any special assumptions and material considerations, and disclose all relevant matters and where the valuation may be relied upon by a third party.

The main valuation purposes include: [1]

Institutional Investors	Banks
Financial reporting	Mortgage origination for property purchase
Performance measurement	Quality control as a part of mortgage origination
Securing finance	Regulatory capital requirement purposes
Enterprise value	Balance sheet asset review
Management reporting to stakeholders	Bonds and securitisation transactions
Regulatory authorities	Underwriting of non-purchase mortgage loan products
Corporate acquisitions	Feasibility study support
	Risk management
	Non-performing loans
	Investment property fund and asset management
	Arrears management
	Accounting (IFRS)
	Estimating cash flows

While there are many different property types that valuers are requested to value, including residential, commercial, rural, and specialised, the focus of this paper is specifically on the valuation of residential properties for mortgage purposes.

Post GFC, there has been a growing awareness of the need for increased regulatory compliance by banks – in fact, by all deposit-taking institutions. Lending secured by mortgages over residential property (residential mortgage lending) constitutes the largest credit exposure for most banks. This concentration of exposure warrants banks paying particular attention to residential mortgage valuation and lending practices.

The GFC laid bare the vulnerabilities of the international banking system. Major banks entered the crisis with excessive, mismeasured levels of leverage and insufficiently stable funding sources. Crisis-related losses accumulated rapidly, contagiously spreading across markets and countries and forcing public sector intervention. What started as strains in US subprime mortgage markets turned into a full-blown financial crisis.

Twelve years on, the post-crisis reforms of the regulatory framework for internationally active banks - Basel III - have been completed with most banks meeting the more stringent capital requirements and new liquidity standards. Basel IV introduces additional changes to global bank capital requirements that were agreed in 2017 and are due for implementation in January 2023.

In Australia (and New Zealand, due to the Australian ownership of most of New Zealand's major banks) the moves to tighten lending processes resulted in the production of a prudential practice guide (PPG) by the Australian Prudential Regulation Authority (APRA) and which detailed prudent lending practices in residential mortgage lending. This included: the need to address credit risk within banks, risk management framework, sound loan origination criteria, appropriate security valuation practices, the management of hardship loans, and a robust stress-testing framework. In developing this PPG, APRA has had regard to the international Financial Stability Board's (FSB) Principles for Sound Residential Mortgage Underwriting Practices.

In India, the Reserve Bank of India stated: "The issue of correct and realistic valuation of fixed assets owned by banks and that accepted by them as collateral for a sizable portion of their advances portfolio assumes significance in view of its implications for correct measurement of capital adequacy position of banks.” [2]

Valuations are arguably more important for investment in real estate than any other major asset class. For non-listed real estate vehicles, they play a crucial role in reporting to investors, monitoring portfolio strategy and undertaking transactions, and as a basis for secondary market trading.

The challenge then is to make valuations future-proof to ensure that they remain fit for purpose in a rapidly evolving real estate market worldwide.

The Valuation Profession

"Professionals play such a central role in our lives that we can barely imagine different ways of tackling the problem that they sort out for us. But the professions are not immutable. They are an artefact that we have built to meet a particular set of needs in a print-based society. As we progress into a technology-based Internet society, however, we claim that the professions in their current form will no longer be the best answer to those needs." [3]

Valuers fulfil a pivotal and responsible role, operating at the interface between clients, financial providers, and property owners. As such, a capable valuer must possess a mix of competencies: hard skills, such as gathering data through investigation, inspection, and research, tempered with analytical insight, the exercise of professional judgement, and people skills. Understanding the client's needs and expectations, as well as explaining the use and limitations of a valuation in a way the client understands and accepts, are important parts of the role.

However, valuers are generally considered conservative and slow to embrace new technologies, and if the Indian and global valuation industry is anything like Australasia's, then the average age of valuers will now be over fifty. Are we then able to respond to embrace the change that is already here, and which is gathering momentum?

Like the changes occurring in the valuation industry, the banking industry is also evolving the way they lend people money, including the rise of P2P lenders. Credit risk models are evolving and have been adjusted, both in response to the COVID-19 pandemic and to changing social and environmental awareness. This is an absolute necessity for banks, not only to minimise risk but also as a way in which they may obtain a competitive advantage.

New credit risk models are incorporating new pandemic-related data points to ensure their output remains valid and robust. Changes to these models are assisted by banks using a broader range of data as well as upgrading their data platform technologies. Banks are embracing green lending. For example, a green mortgage is a mortgage specifically targeted at green buildings. As an incentive for the borrower to either buy a green building or to renovate an existing one to make it greener, the bank may offer them either a lower interest rate or an increased loan amount. These banking evolutions need in turn be supported by the evolution of the valuer.

McKissock Learning, a USA based valuation and real-estate focused educator, undertook research to answer the following question: “If you could adopt one new technology tool for your appraisal business, what would it be?” Here are the results and some comments as quoted in that study:

1. Tablet computing device
2. Drones
3. Laser distance measuring device
4. Cloud storage software (e.g., OneDrive, Google Drive)
5. Sketching software/3D drawing software
6. Automatic adjustments tool
7. Regression analysis tool
8. Report streamlining tool
9. Time tracking tool
10. Form-filling software
11. Social media marketing
12. Self-driving car

“I would like to move to a paperless office.”

“I would like to bring a tablet on inspections that I can draw on in order to sketch floor plans for properties where official floor plans are not available.”

“The laser measure with Bluetooth is great, but it still requires me to draw the lines on the tablet. If I could just point and shoot and have the line automatically drawn (because it knew the direction to draw it), it would save me a little time.”

“I want to take more frequent mini vacations and be able to leave the office as needed. I need the ability to open reports and make revisions in a timely manner and being able to use a tablet or small laptop while away from the office, when absolutely necessary, would be a big help.”

> “Would be nice to have access to all of my appraisal files, data and computer from remote locations.”
>
> “Drone photography could better capture images of larger parcels such as factories or commercial centres as well as enable inspection of large vacant tracts during winter when access is restricted by snow.”
>
> “I am not very technologically savvy, but if a drone could be used to take photographs, it would save a lot of time driving around in rural areas.”
>
> “I need an easier way to support my adjustments than exporting to Excel.” [4]

While all the technologies and tools identified can or do enable valuers to operate more efficiently and effectively, given this is a relatively recent 2019 study, it is still remarkable how much they are missing where the real focus should lie.

The mindset of today’s typical valuer needs to shift away from the concept that a valuation is just that – preparation of usually a single value and accompanying report on a sole property. The regulatory requirements for banks to reduce their mortgage lending risk suggest they may require additional information to enable them to make appropriate lending decisions.

Another factor that limits the valuers’ ability to provide information other than what is typically found in a valuation report, is that valuation fees are also focused on a single report and single-use case, which reduces the ability to develop new or expanded services. Furthermore, this single ‘per use’ mentality has positioned valuers and valuation reporting as a ‘must-have’ or ‘pain point’ for customers, only required in order to achieve something as opposed to something that the majority voluntarily use to ‘add value’.

A skill inherent in the majority of India's valuers is their ability to gather, interpret, and analyse data obtained as part of the valuation process. In addition to providing the value of a property, it is these inherent skills that should be focused on, to the benefit of the client and the valuer. Valuers need to stop identifying themselves as residential mortgage valuers and start thinking of themselves as property experts, as this immediately suggests the ability to provide client assistance across the property spectrum.

We believe that both bank clients and their customers need valuers to start thinking and acting in this way. The question the valuer should ask is, “How can I provide you with the advice you need, to not only allow you to make a lending decision, but to further your knowledge on both the current and future value of the property, along with supporting information to allow the bank to fully consider their risk?”. This is the time to stop resisting new technology and embrace it, to maximise the available information and provide valuer-enhanced models and reports. Along with a mindset shift, valuers should seek industry support from their governing bodies, valuation standards setters, and professional indemnity insurers, and discussions with these parties should begin now.

The changing nature of the professional services value chain has created additional complexity for valuers, with the rise of large global and national valuation firms. These firms can more readily absorb the cost of new technology in addition to offering specialist expertise, making it more difficult for the smaller valuation firms to be competitive. The need for specialist expertise and more rapid avenues for innovation has propelled the number of acquisitions, partnerships, and alliances in the industry, and as a result, firms are also faced with a growing need to operate within a chain of services and manage a more extensive set of offerings and broader governance.

However, globalisation means that those firms operating internationally now need to meet demands in different jurisdictions and cultures, serving clients with more tailored and localised services. While valuation practices are growing, the ability for small companies with minimal resources to enter a market and displace the established system lessens. Successful companies do not just meet customers’ current needs but anticipate their unstated or future needs.

New Technology Focus

The tech space continues to rapidly change, with a move away from the 'all content on one device' model - providing a single product, a valuation report - toward multi-use environments, platform marketplaces, and cloud computing. Tech is also blurring the boundaries of valuation firms as they evolve to meet the consumer demands of today. There has been a considerable focus by valuation practitioners on ways to improve efficiency, but considerably less focus on the ways we can improve valuation accuracy and provide supplementary information to assist with loan decisions. Many valuation firms have spent considerable money on developing 'in-house' collection and reporting software, but again, with a focus on a single report use case.

As valuers, we need to spend time with the valuation report end users, to define what is required in the valuation report of today. This will allow the consolidation of opportunity; it will reduce time spent on current but potentially unnecessary report inclusions by minimising extraneous information and maximising information that helps a lender make a rapid loan decision.

The rise of new technologies is rapidly providing a wealth of new opportunities for professional services firms to improve their undertakings. Technology has the potential to be a great equaliser, offering new opportunities and solutions to those that embrace it. This new technology will allow valuers to focus on areas where their expertise is paramount, i.e. market analysis, value assessment, and acting as an experienced advisor. This will increase productivity.

Information Focus

Valuers must shift toward technology that assists with the collation, storage, and retrieval of property information. The data must be able to be securely stored and efficiently retrieved and analysed. Becoming digital and data first will provide a distinct competitive advantage. Smaller valuation firms, where the ability to invest in technology is more difficult, should consider working with other valuers and jointly developing the technology and data they require. Acquiring and using property information and technology does not need to solely be the purview of the large national and international property firms.

Being open to new ways of harnessing information is likely to be just as crucial as any single technology. Look at the information that you currently collect when inspecting a property. What additional information can you access from freely available sources, from paid subscriptions, and through your own collection, and consider what you could provide to your clients in addition to the report that you have prepared? Again, speak to your clients to see their expectations in today's business climate.

Valuation Focus Reinvention

Valuations are largely required urgently to satisfy purchase, sale, or refinancing. Consider how you can get the "answer" to the bank/lender more quickly. Could you, if the bank is amenable, provide a short form assessment of value first showing any assumptions or conditions and then follow this up with your usual report? Realistically, most valuers think this way in practice. Focus your report on the value of the property and how you arrived at your value. While the building's condition on the property is important, too many valuation reports that I have seen spend a proportionately large percentage of their report on location, house layout, and services, and very little on the process and thinking that went into the assessment of value. Reinforce the value by analysing and providing information that you have collected for the locality.

Our clients are looking for new and improved products and services, and the list of clients that valuers can sell services to is increasing. As property experts, we must be prepared to differentiate our products and market and communicate our knowledge and expertise to this wider group of potential users.

Conclusion

As digital technology continues to develop, banks/lenders and investors expectations are also evolving and continuing to increase. Partly this reflects the increasing complexity of many real estate transactions. However, the main driver is the need by these same groups to benefit from technology's full potential for valuations, to ensure faster turnaround times, less human error, and a far greater range of evidence to support the value than is currently provided by many of us.

We all know that the valuation profession, as have many other professions, is undergoing significant change and the range of services we provide to our clients is evolving. As a profession, we must, with the help of our professional bodies, take initiative. We must continue to educate and upskill ourselves, enabling us to embrace the changes brought about through the digital and data revolution, rather than fight an inevitability losing defensive battle to resist change and preserve the status quo.

Change is a given. We know our profession will undoubtedly experience other advances and impacts, such as the further growth and consolidation of valuation firms, increasing specialisation, competing valuation products, commoditisation of some valuation types, and the growth in those providing valuation and property consulting services. Being adaptable will ensure business viability. In 2017, the Royal Institute of Chartered Surveyors (RICS) developed six recommendations for today's valuers which continue to have relevance today: [5]

1. **Embrace technology** - valuers must be receptive to changes, such as in how data is gathered
2. **Enhance the client experience** - experimenting with new ways of reporting and providing information can lead to better outcomes for the client
3. **Ensure independence and objectivity** - without independence and objectivity, there can be no trust
4. **Beware of liability** - liability needs to be in line with risk and reward, with different levels depending on the assignment
5. **Reduce timescales** - digitisation will help the profession to become more agile; reduced timescales should not compromise quality
6. **Update your skill set** - the profession must place increased emphasis on skill development, particularly in the areas of data analytics and client interaction

RICS similarly suggested that the skill set required for valuers must include:

- Conduct rules, ethics, and professional practice
- Client care
- Measurement of land and property
- Inspection
- Communication and negotiation
- Accounting principles and procedures
- Valuation
- Conflict avoidance, management, and dispute resolution procedures
- Data management
- Health and safety
- Team-working
- Sustainability

We would go even further. Valuers will need to:

- Ensure they are computer-literate to be able to embrace digitisation
- Digitise their workplace
- Work both inter-disciplinary and trans-disciplinary
- Professional development
- Be entrepreneurial & progressive
- Be collaborative

We are seeing some of the valuation firms of today already embracing these skills to meet our evolving digital and global marketplace. The skills valuers have are unique, and accepting the changes that are upon us will ensure valuers continue to be a vital part of the property ecosystem.

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Kerry Stewart

Head of Asia Pacific, Valocity

Kerry has extensive valuation experience in both the public and private sectors, and is a Fellow of both the New Zealand Institute of Valuers and the Property Institute of New Zealand. He has significantly helped develop the Valocity platform and has led the international growth of the company, in addition to working closely with both clients and valuers, helping to create this vital ecosystem.

He has been commissioned to undertake international assignments by clients such as the United Nations, the International Finance Corporation, World Bank, SOPAC, and New Zealand Aid. He has worked extensively throughout the Pacific region; in 2008, he led the valuation exercise of NZ House in London for The Treasury, as well as various properties for The Ministry of Foreign Affairs and Trade in Washington, New Delhi, and the South Pacific.

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www.valocityglobal.com

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About Valocity

Valocity is an award-winning FinTech company transforming and digitising the property decisioning process globally with customers across Australia, New Zealand, India, and Asia.

Valocity digitises the entire property valuation process with its unique cloud-based valuation platform, with bespoke solutions for residential, commercial, and agricultural lending.

It combines the best of nationwide property data with global technology and advanced analytics expertise to create digitally connected workflows, customised insights, and desktop valuations that enable data-driven decision-making and more seamless customer experiences.

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