

**L-T S V**

# Long-Term Sustainable Value Network

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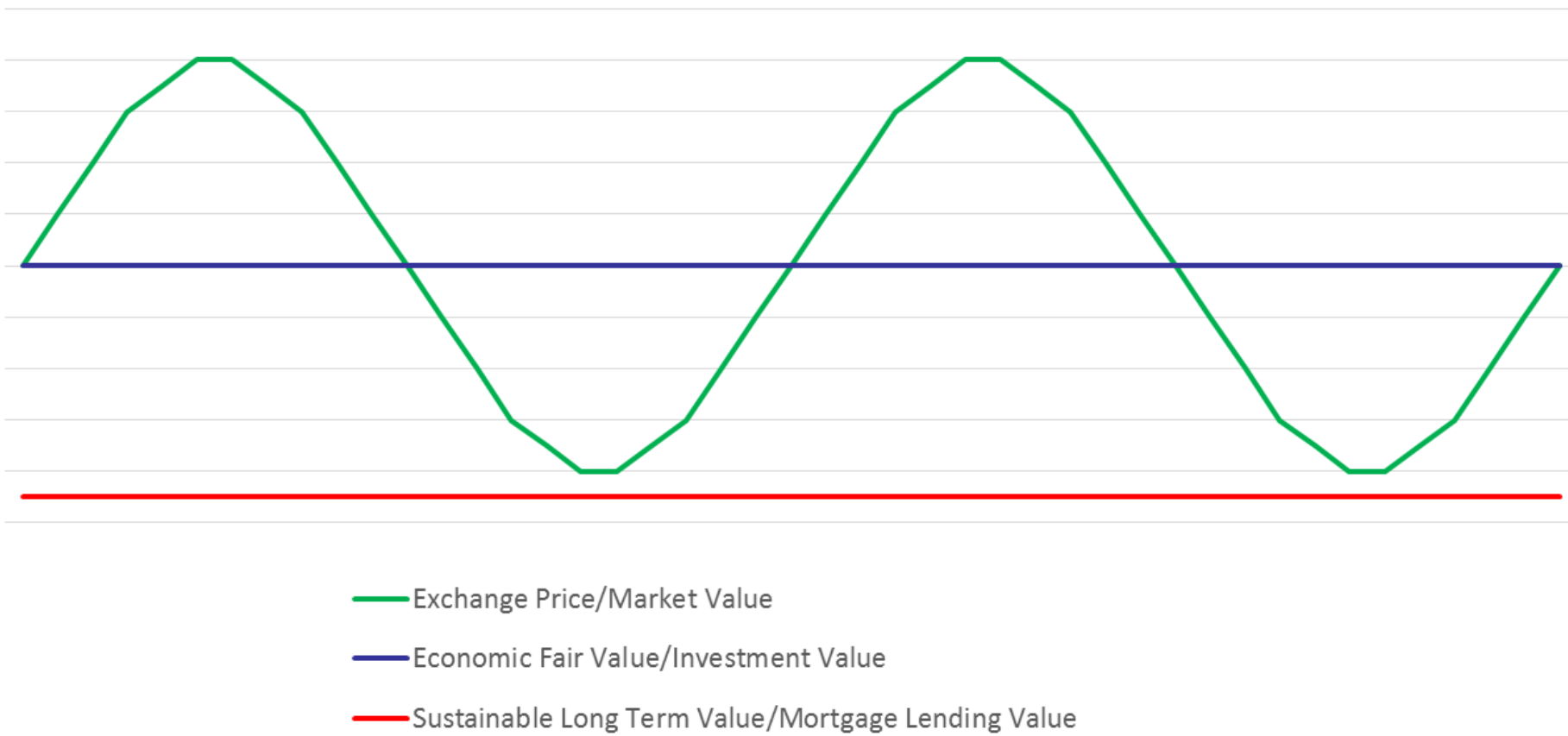


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### 1. L-TSV Network

- Objectives
- Background
- Status Quo

### 2. Methodology



# Market Cycle Pattern





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### 2. Methodology

- Support of a Long-Term Sustainable Value as a basis for valuation for lending purposes
- Discussion of an European methodology to determine LTSV on national and international level
- Support of training/ education in the area of LTSV - valuation

- The concept of a sustainable value for valuation for lending purposes can **generally be implemented in every country**
- *L-TSV Network* **encourages achieving a common understanding** of how to determine the underlying principles and parameters of a LTSV and might therefore also **increase acceptance and application** of L-TSV internationally
- A **full harmonisation** of the L-TSV methodology at European level is **not the purpose** of this initiative. The results of this project contribute to a further international discussion about valuation for lending purposes and could also serve as a basis for **further discussions at national level** about the potential of L-TSV be introduced in more states.

- Increasing focus of banking regulation and supervision in technical issues such as property valuation for lending purposes:

*Art. 124 (4) CRR.*

*"EBA shall develop draft **regulatory technical standards (rts)** to specify the rigorous criteria for the assessment of the mortgage lending value..."*

Source: REGULATION (EU) No 575/2013 OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL of 26 June 2013 on prudential requirements for credit institutions and investment firms (CRR)

- Asset Quality Review (AQR) undertaken by the European Central Bank (ECB) in the year 2014



2014

- According to CRR draft regulatory technical standard (RTS) shall be finished until end 2014

Apr 2015

- First draft was stopped due to open fundamental questions regarding scope of application and level of detail

Oct 2015

- Opinion on MLV was published by EBA:
  - Scope of application of the RTS should be limited to the credit risk area, the credit risk mitigation and the large exposure framework (**exclusion of Covered Bonds**)
  - EBA discusses whether the right to decide about the application of Market Value or Mortgage Lending Value is on the level of the bank or member state
  - EBA asks the **European Commission to initiate appropriate legislative steps** to clarify these issues

## Definition of Value in the context of Basel III

*„Value of the property: the valuation must be appraised independently using **prudently conservative valuation criteria**. To ensure that the value of the property is appraised in a prudently conservative manner, the valuation must **exclude expectations on price increases** and **must be adjusted to take into account the potential for the current market price to be significantly above the value that would be sustainable over the life of the loan**. National supervisors should provide guidance setting out prudent valuation criteria where such guidance does not already exist under national law. If a market value can be determined, the valuation **should not be higher than the market value**“*

- Many European countries do not use the concept of L-TSV
- Little practical experience in its implementation on European Level
- So far no common European understanding of L-TSV and its approaches/principles
- Difficult to discuss a common European understanding and methodology of L-TSV in the existing European networks on the basis of detailed expert knowledge



Establishment of  
international L-TSV  
expert network

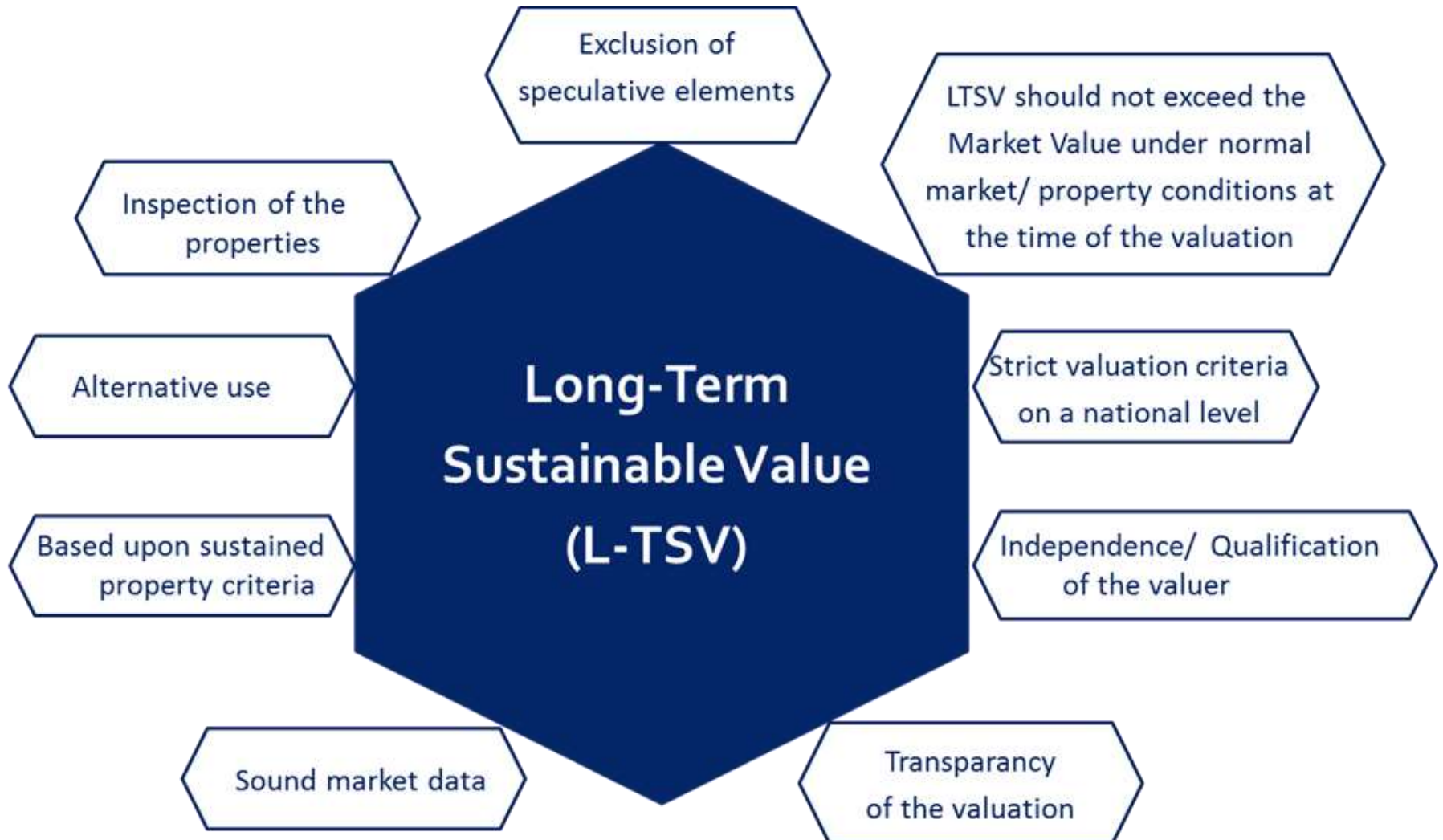


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<b>Alternative use</b>	<ul style="list-style-type: none"><li>▪ Discussion of <b>sustainable qualities</b> of the property</li><li>▪ Consideration of its <b>flexibility and potential for alternative use</b></li><li>▪ If substantial alteration works would be required to change the property from a specialised or obsolete use to a readily marketable one, such cost implications must be addressed in the assessment of L-TSV</li></ul>
<b>Inspection of the properties</b>	<ul style="list-style-type: none"><li>▪ The valuer must undertake a <b>property inspection and research</b> to a sufficient extent</li></ul>
<b>Exclusion of speculative elements</b>	<ul style="list-style-type: none"><li>▪ “Abstract” the relevant parameters adopted in the valuation to a level which would be <b>acceptable to the majority of occupiers, operators, tenants, purchasers</b> etc.</li><li>▪ <b>No speculative assumptions</b> which may enhance future value</li></ul>

L-TSV should not exceed market value under normal market/property conditions at the time of the valuation

- L-TSV should not exceed Market Value at the time of its determination
- In **special circumstances** at the date of valuation, whereby a **higher L-TSV** in relation to Market Value results, normal market conditions and/ or factors relating to the state of the property have to be taken into account to adhere to this principle (**Explanation!**)

Strict valuation criteria on a national level

- Joint **European methodology** to determine L-TSV based upon **broad principles**
- **More precise valuation guidelines on a national level** to ensure that national characteristics of property markets and valuation practices are properly accounted for

## Independence/ Qualification of the valuer

- The valuation should be prepared by a qualified valuer, who, in respect of his professional training and experience over a longer period, possesses **special knowledge and experience in the field of property valuation with a special focus on determination of L-TSV**
- The valuer must **not be involved** either in the loan acquisition, lending decision or in the brokerage, sale or letting of the property.
- Any conflict of interest in this respect must be avoided.
- The valuer has to ensure and confirm that he is **independent of any party interested in the outcome** of the valuation.

## Based upon sustained property criteria

- **Disregard** any factors affecting value that are either of a **temporary nature**, or **related only to specific parties** and not to the market as a whole.



## Transparency of the valuation

- The valuation approach adopted and the main valuation parameters and assumptions must be **clearly stated and justified**.
- The recipient of the valuation report must be able to understand the valuer's reasoning as to the choice of parameters adopted and how they have arrived at the L-TSV

## Sound market data

- Use of **reliable market data** sourced from current and previous market activity to provide property benchmarks, which can then be extrapolated to determine long term trends.
- The valuer's objective is to identify the factors influencing changes in prices and values among various property types and to use this incite to **form an "opinion" upon the future development** of markets and value

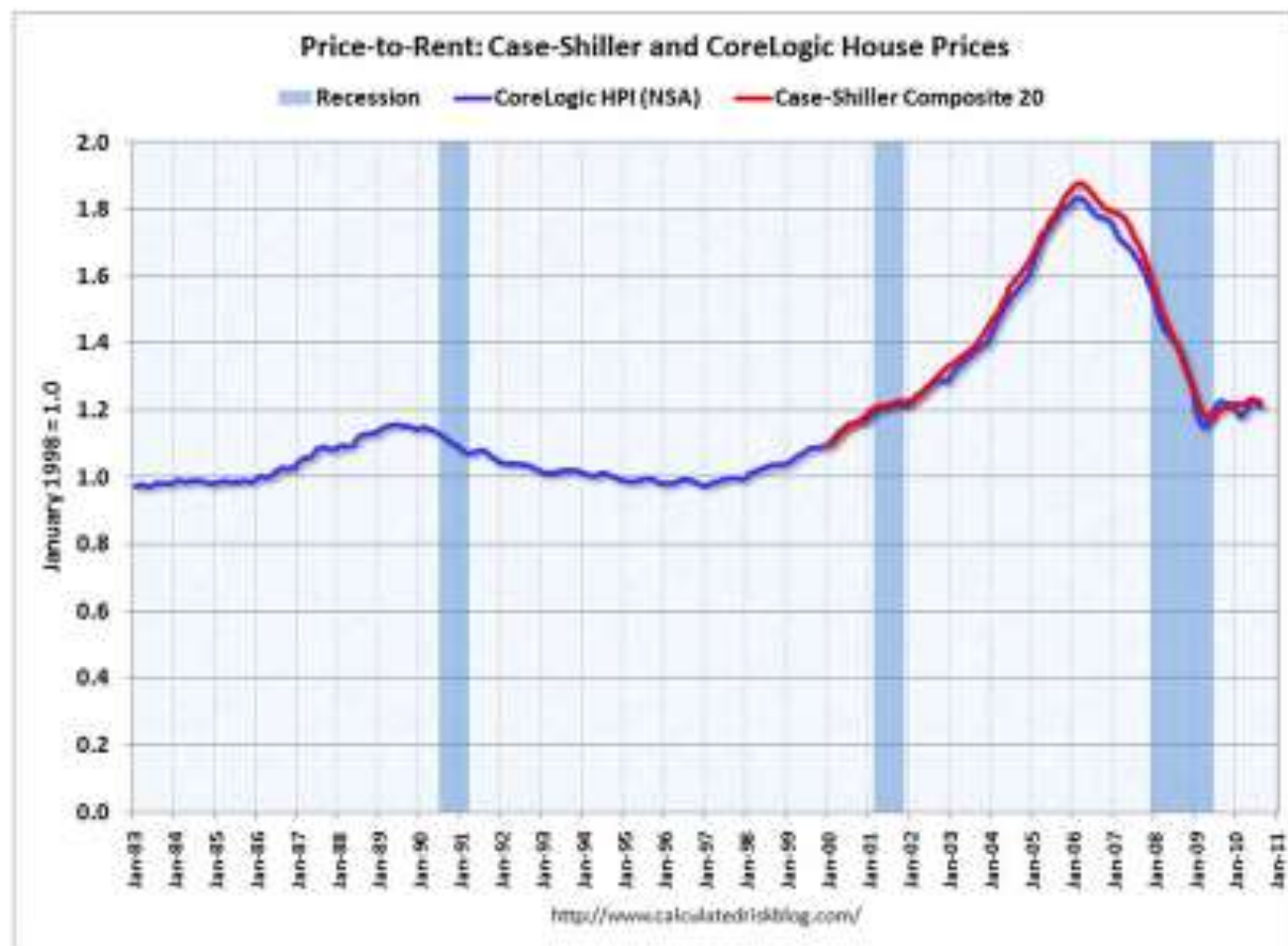
## *Draft Approach to Determine Long-Term Sustainable Value (L-TSV)*

- *Definition*
- *Scope and Subject of Valuation*
- *The Valuer (Qualification, Independence)*
- *Valuation Report*
- *Inspection*
- *Valuation Approach*
- *Income Approach*
  - *Sustainable Income*
  - *Landlord's Costs*
  - *Sustainable Capitalisation Rate (Sustainable Yield)*

## *Draft Approach to Determine Long-Term Sustainable Value (L-TSV)*

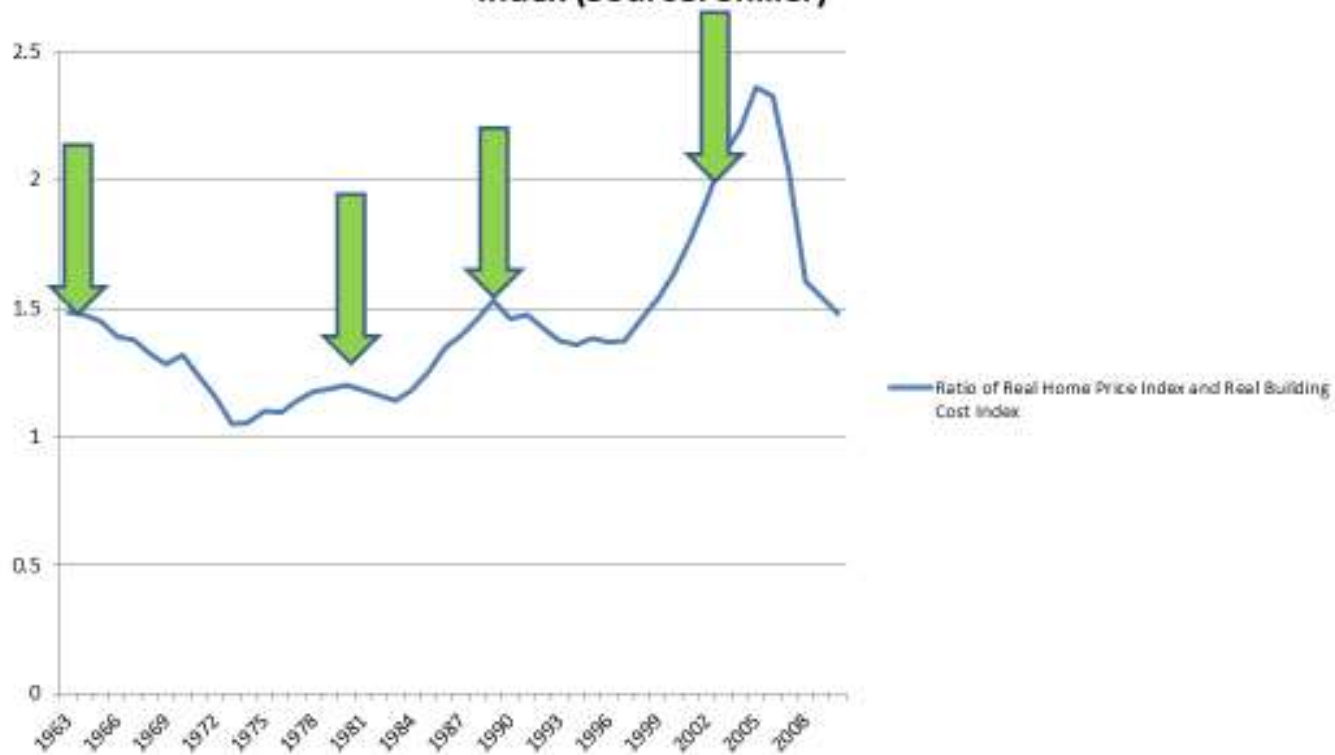
- ...
- *Comparison Approach*
- *Cost Approach*
  - *Land Value*
  - *Replacement Costs*
  - *Depreciation*
- *Remaining Useful Life of the Building*
- *Specific Aspects of Turnover Related Properties*
- *Temporary impacts on value*

# Market-value-to-rent ratio: deviation from fundamental value

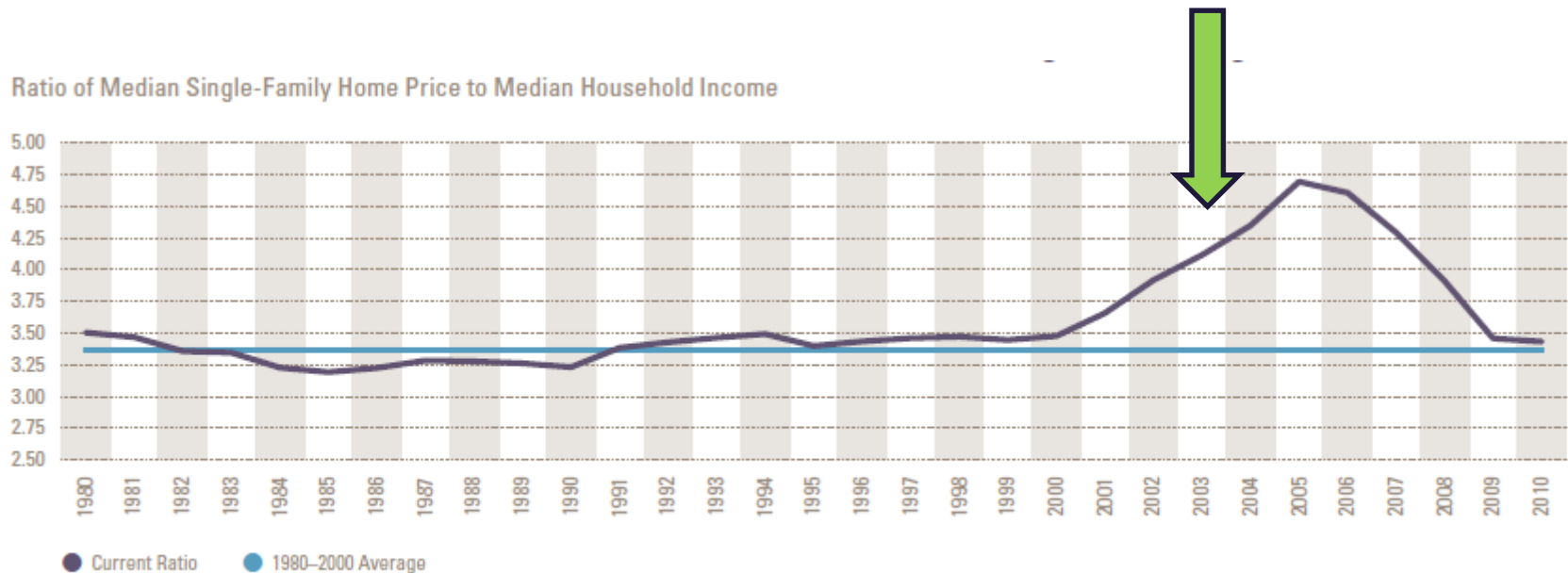


# Market value-to-replacement cost ratio: deviation from fundamental value

Ratio of National Real Home Price Index and Real Building Cost Index (Source: Shiller)

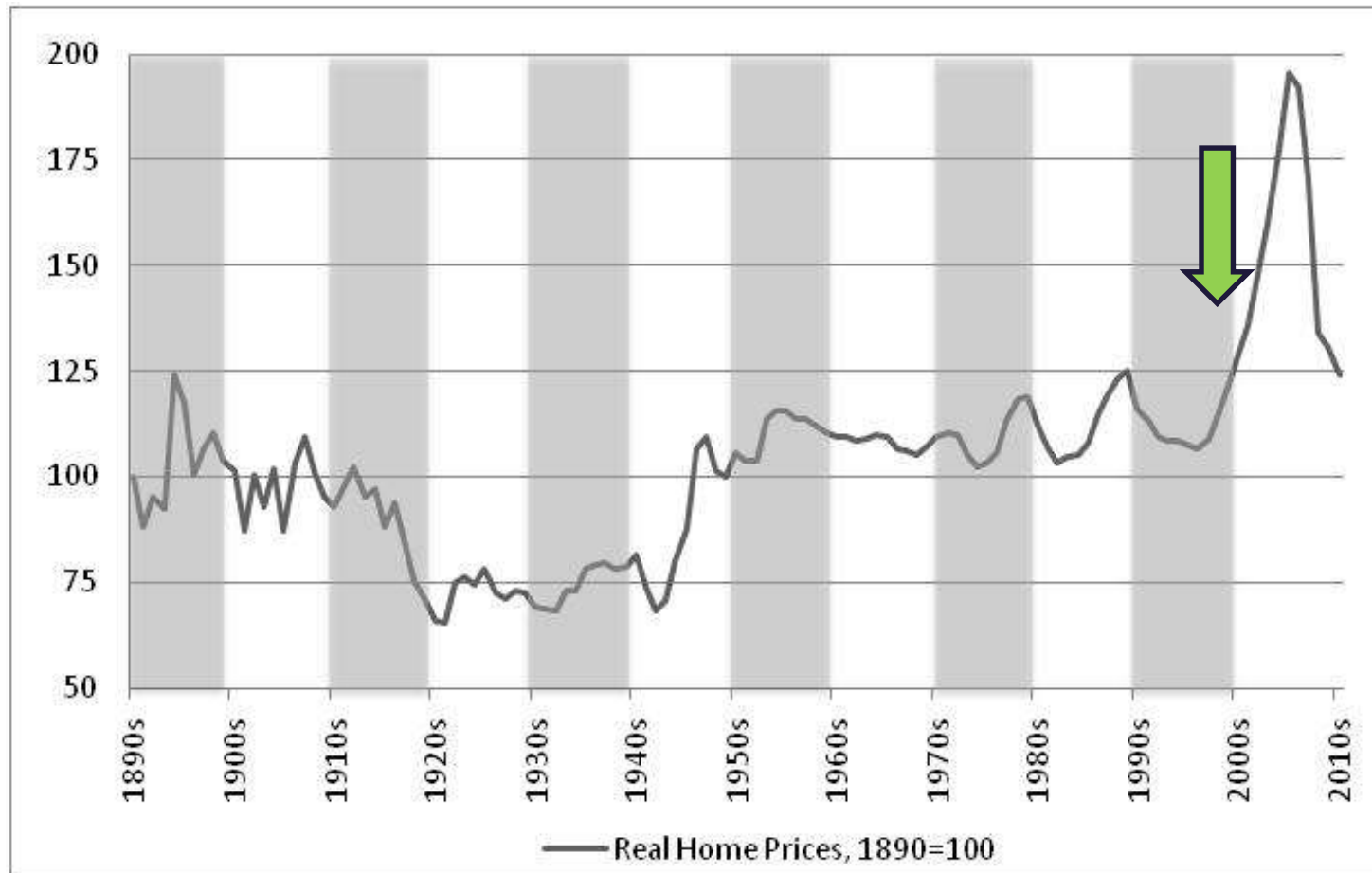


# Media home price-to-median income: deviation from the mean



Source: JCHS tabulations of National Association of Realtors®, Existing Home Sales Prices; and Moody's Economy.com, Median Household Income.

# Market value: deviation from the mean

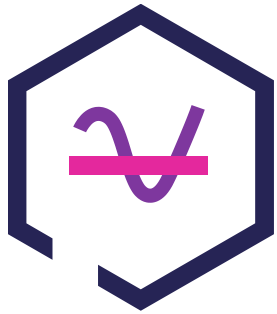


- Compiled from Robert Shiller's updated historical housing market data used in his book, *Irrational Exuberance* (Princeton University Press, 2000; Broadway Books, 2001; 2nd edition, 2005). Data available at [www.econ.yale.edu/~shiller/data.htm](http://www.econ.yale.edu/~shiller/data.htm).

**Interested ?**  
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# ltsv.info



**L-TSV**

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