Do This Before You Order A Credit Report!

For years, the first step after obtaining a loan application from a prospective customer is to pull a credit report. This is about to all change because of a dramatic change from a top industry supplier. Through a web site, you can now obtain an AVM (Automated Valuation Model) for a given property for just $3. Previously, such products were priced at least $20 making them too expensive to pull on every new loan.

The reason that this is so significant is because at $3, it's now affordable for the entire industry to use on every single loan. At $3, it's a throw away product – it's worth buying for each loan even if it's not needed. At $3, it's a very small price to pay just to insure you know the value of the property before you even begin to prequalify the borrower. At $3, it's a great giveaway to the consumer where you can earn their appreciation for giving them an appraisal on their property. At $3, it's cheap insurance against a loan that might not otherwise fund. At $3, it's a good idea to order before spending the money and time on a real appraisal – why waste the money?

First American took a big step with this huge price drop but it's clear, they want their AVM models to become what Fair Issac's FICO score has become for the credit report. They want their model to become the defacto standard the industry uses to evaluate a property's value. It's a smart move and it might just work. AVM's have become increasingly used for home equity loans and 2nds. With a $3 price tag, we could see mainstream usage of AVM's for all loans.

Obviously, the next question is the quality of this AVM product. While I won't claim to be an expert in the analysis of AVM products, I can tell you that this product is considered among the best available and has been in commercial use since 1995. This isn't a low-end product but rather, it's a full featured solution used by twenty of the top twenty mortgage lenders in the US and it's been approved by a major ratings agency. Since First American owns the underlying data used by virtually all of the AVM products, owns the models and owns the delivery platform, it may be difficult for other AVM vendors (there are many) to match this price. Still, if the other AVM vendors are able to match this price, it will be great for our industry.

First American also concurrently announced an insurance option for this product where they will guarantee the properties value. While the cost is significantly more, it's still much less than a full appraisal and it's insured (whereas even a full appraisal isn't). Thus, lenders can remove the risk of an appraisal by using an insured AVM. This is also a significant step as it's the first appraisal alternative that carries insurance. Given the insurance component, I have to expect that lenders would adopt this product in large numbers. Why use the traditional appraisal that's not insured and costs about twice the price?

Finally, we have to look at the impact this will have on the appraisal industry. While the appraisal industry has been loosing more and more business over the years, this type of product could be the final nail in the coffin to the appraisal industry, as we know it. Clearly, we can all see a day where 80% of the loans in the industry have no traditional type of appraisal at all. Instead, they would be replaced by computers able to make instant decisions at a tiny fraction of the cost.

Because this all sounds too good to be true I have to say that there is a downside in that AVM's don't arrive at a perfect valuation every time. AVM's are all data dependent - some areas of the country will be better suited than others for their use and accuracy levels. Many AVM's use multiple methodologies to reach a value conclusion so you can get a value in every state even with minimal data available. Of course, most providers won't be charged a fee if a value conclusion is not reached. In addition, houses with very special characteristics might require a traditional appraisal. We must recognize that there are weaknesses with every valuation approach but for the intended use I am suggesting here, they aren't that significant (given the compelling cost and time savings). It is a good idea to educate yourself on what type of properties might yield a questionable value from an AVM. For example, properties that just went through a major renovation or addition might be valued to low. Obviously, houses that just had major damage (like from a flood) could be valued too high.

The AVM industry just took a huge step forward and we should begin to use AVM's on every loan. In fact, before you order that credit report you should spend the $3 first to check the property's value.