

## **Real Estate Within 10% of the Market Top!**

By John Kamin

If you have improved property you are considering selling, you probably don't want to be **caught** in a **downturn** in the real estate cycle. Ordinarily, you have about 3 or 4 good years in every 7 to 10 year property cycle. That's what we've had so far in this cycle.

The **risks** and **dangers**: If you get caught trying to sell property in the down part of the cycle, a number of things happen. **Prices** may not go down much, but they can get **softer**. **Negotiating** becomes **harder**. Many more solid **prospects** are **replaced** by lookie-loos, people who can't make up their minds. Potential **sales** go into escrow, and then **fall apart** at the **last minute**, just before the sale is completed.

**Listings increase**. Banks and other **lenders**, **stuck** with increased foreclosures, suddenly become **skittish** on making **new loans**. They examine everything on buyer/borrower applications with a fine tooth comb.

### **UP CYCLE DIFFERS, BUT TEMPORARY!**

In the UP part of the cycle, banks and lenders are **anxious** to **push out money**. Open houses near major job centers attract **crowds** of potential **buyers**. **Auctions attract** many qualified bidders, who **bid enthusiastically**. Some properties are sold as soon as someone hears about them, without even the time to put them into the Multiple Listing Service.

**Listings shrink**, so buyers have less to pick from, This is a great time for owners. There is **less supply**, but **more demand**.

Prices seem to rise, not only year-by-year, but month-by-month. In this area, for example, median prices of homes sold rose 25% over last year. When you consider that those sales are mostly highly leveraged, 5% to 20% down, that's a **huge** increase in **profits**, sometimes over 100% per year on the down payment!

During the good times, you can even get **excellent bids** and **plenty of prospects**, sometimes even for lousy properties; neighborhoods changing for the worse; vacant lots; neglected buildings; houses with years of deferred maintenance, leaking roofs, obvious problems and bad neighbors.

However, once the cycle turns down, you can't even get people to come and look at those poorer properties. Those who do look usually don't have the money to buy and won't qualify for the necessary financing to do the deal!

### **EARLY WARNING SIGNS OF THE TOP**

What **signs** do I see that the present cycle may be within 10% of topping out?

Interest **rates** are **choppy** at present low levels. Up 3 weeks, down 1 week. They're **fluctuating** instead of staying stable. This is a precursor to **higher** interest **rates ahead**. Higher interest rates would mean that **fewer buyers** would **qualify** for the loan, and monthly **payments** would be **higher**.

Homebuilders have been going great guns. **New homes** are in **direct competition** with the resales, older homes. The more new homes that are built, the more new housing starts, the fewer buyers for competing older homes. Fact: D.C. leaders will be the first to admit that the housing construction boom is **propping** the rest of a still soggy economy.

### **THE INVISIBLE RECOVERY?**

The oft-anticipated recovery has not yet appeared. It's coming, but so slowly as to be almost invisible. What happens if the recovery is further delayed by another 6 to 12 months? (e.g. Japan has been in a "coming recovery" for 10 years, which never seemed to show up.)

Many buyers who are being lent big money can't pay the mortgages. Their **incomes** are **not secure**, or they may be laid off in the near future.

Many buyers are putting only 5% or 10% down, and living a **lifestyle** commensurate with **huge credit card debt** pile-up. Any contraction in their income and they may not pay their big home loans. Some will become "walk-aways" (just handing over the keys to the lender).

### **CURRENT OUTLOOK**

Trees do not grow to the sky.

**PREDICTION:** While all property owners are very happy about 1999-2003 gains, potential profits, I predict that at some time in 2004-2006 many potential **buyers** will grow **dismayed** at ever-increasing prices, and just abandon the idea of buying now.

**FORECAST:** In most states, **property taxes** are on the **increase** as deficit-plagued state governments and local government leaders try to get more and more from taxpayers. Property owners are fixed targets. Those who own more than one property are often labeled “wealthy”, considered ripe for piracy and targets for increased taxes and fees!

**FORECAST:** In the 10 largest cities, **commuting** will become **more** of a **nightmare**.

**PREDICTION:** **Rising gas prices** add to concerns. Ever-farther-out developments may become unattractive as commuting woes worsen.

**Listings** are starting to **increase, slightly and barely noticeable**. But when listings increase greatly, **more supply** will tend to hold down soaring prices, at about the same time that demand could falter.

### **UNPREDICTABLE EVENTS CAN AFFECT DEMAND**

**Natural disasters** may discourage buyers in certain areas. (e.g. After the January 1994 Northridge earthquake, buyers took off and went to other areas. Owners of damaged homes often took 1-3 years to get checks from insurance companies. Many badly damaged homes had no earthquake insurance. Earthquake insurance can run added multi-\$1000s per year.)

Buyers absconded. After the last 3 major earthquakes in various areas of California, in those particular areas, **buyers** became much **scarcer** for up to **5 years later**. Then, because memories are short, the demand grew, finally!

9/11 reminded us that many people hate America, especially big city job centers.

**PREDICTION:** Any terrorist attacks centered on a specific area could discourage new buyers in that area and lessen demand for 4 to 7 years.

### **SPREADING RISKS**

**Geographical diversification** on multiple growth-property ownership may afford some strategic protection. Fires scare buyers. But, if your only asset is one building, one home, or concentration is within a few blocks, that can hardly be called diversification.

Even so, most insurance policies do not cover “acts of war”. Beleaguered insurance companies in general, in my experienced opinion, don’t like to pay out huge claims. Many times they will delay as long as possible if there is a no-pay loophole in your coverage!

### **ARE YOU CASH-POOR, PROPERTY RICH?**

Since real estate is illiquid, you don’t want to find yourself in a situation where you are property-rich but cash-poor. If you **need liquidity, build liquidity**. Properties are usually **illiquid**, less so in the good part of the cycle, much more illiquid in the downward part of the property cycle, even if prices do not fall much.

**Inflation** may help **bail** you out over the long term, even if you make mistakes buying and owning. But, inflation also affects buyers in other ways (such as raising interest rates). Inflation could lessen demand, unless buyers are inflation-hedgers and want to own more tangible assets!

**Competing borrowers** may take money out of the property market, Wall Street, diamonds or franchises. Factories either contracting or moving to other countries. Be careful here.

### **PROLONGED WARS AFFECT PROPERTY**

**War** can have unusual after effects on the property markets. During and after WWII, there was a tremendous shortage. Building materials could not be obtained as everything went to the military. Most building was curtailed.

In late 1960s and early 1970s, the Vietnam War took many young men and women out of the home-buying market. The property markets stagnated until the soldiers were sent home. Then it boomed. But during the 1968-1973 Vietnam War, the housing market sagged, often badly and transactions crumbled and collapsed.

During housing **boom** times, **speculation** becomes rampant. People take out huge equity loans to the max, loans they may find difficult to repay later. “Property flippers” rush in and out for

quick profits. A downturn may catch them flatfooted. Could a future war expansion or “flipper” demolition reoccur? Decidedly, so.

### **STRATEGIC MOVES**

**Selling properties takes time.** To get full ticket, you often have to repaint, repair, re-carpet and add other amenities. Appliances on their last legs often must be replaced. Listing brokers must be compared and evaluated. In a hot market, **maybe** they can sell properties in 1 to 3 months. But when market begins to sag, listings times grow longer ... 6 months, 12 months, 24 months. Therefore, I suggest a) it's better to **sell into strength**, b) sell into a **rising market**, and c) **prep early**.

**FORECAST:** If we are within 10% of the top of this housing cycle, you would be well advised to do your prep work now; a) push your listing interviews, b) get signs, advertising and flyers ready, and c) put properties on the market.

Once the cycle turns, you may find brokers who should be working **for** you, not start beating you over the head to cut prices, \$10,000s, \$50,000s, \$100,000s or more to “move the property”.

The sooner you start, and the sooner you can take advantage of a hot-hot property market, the less likely you are to be beat over the head to cut your prices. Sometimes, in a sagging, soggy market, even cutting prices doesn't work.

**FORECAST:** The more you cut, the more brokers/buyers want you to cut!

**SUMMARY:** If planning to sell a house, other improved property, or your worst properties, get started early and prep for the market to get them on the market right now!

**PREDICTION:** Late 2004-2006 could be a completely **different** kind of market.

If you are in your properties for the long term, and they're all good properties, you don't have to sell them now, because it may be hard to replace them quickly. Instead, **sell your worst properties now, keep the best.**

Long term: If you plan to hold through several more real estate cycles, **no need to dump** now. But, for those of you who plan to sell near the top of this market, I think you're within 10% of the cycle's top. What could be clearer?

*John Kamin is a Consulting Economist and publisher of The Forecaster, 19623 Ventura Blvd., Tarzana, CA 91356, (818) 345-4421. \$180 per year. For more money making ideas, order his latest book Active Money Strategies & Hidden Wealth Builder Secrets For Young Adults: What They Were Afraid To Teach You In School. If They Ever Knew! \$20 + \$4 s & h Add \$1.65 tax. 95 pages.*

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