

Waiting for the Rebound



Luxury continues to thrive in some areas. But other markets have seen declines. In our annual year-end assessment, we talked with industry leaders about what's in store for 2008 and beyond.

BY CAMILLA McLAUGHLIN

Homes in prized San Francisco neighborhoods sometimes sell within weeks, occasionally garnering multiple offers, even though sales in California are projected to decline by 23 percent in 2007. | In Palm Beach, July's condo sales tumbled by 16 percent from the prior year with a 5-percent price drop; yet, a new luxury building in an exceptional location is experiencing brisk pre-construction sales. | In the Bay Area, some locales such as Berkeley, Piedmont and St. Francis Wood have an inventory of only several months, a sign of a white-hot market, while the backlog in some others can be counted in years rather than months.

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Such is the contradictory nature of real estate going into 2008. From Seattle to Boston, high-end sales are outperforming other price brackets, particularly in cities, a trend that DataQuick, a La Jolla, Calif.-based firm that tracks changes in the real estate industry, sees “playing out across much of the West and the nation.”

“Luxury has been the good news in real estate for 2007, and will most likely continue to be in 2008 at the highest price points,” observes Mary Tennant, president and COO of Keller Williams Realty.

“The frenzied market is gone and we’re in a more normal market. I think 2008 will be a very robust market. Plus, it’s an election year and the economy is always good in an election year,” says Brian Losh, publisher of LuxuryRealEstate.com and owner of Seattle brokerage Ewing & Clark.

Certainly, for real estate in general, 2007 has not been a good year. Slow markets got even slower and an oversupply of new construction and investor-owned properties stalled others. Mid-year brought a few, fleeting positive omens—a slight upswing in new home sales and stabilizing pending sales. “The downswing in home sales that began in 2005 appeared to be losing momentum,” said David Seiders, chief economist for the National Association of Home Builders. But the wallop of the subprime dilemma and ensuing credit crises sent the markets into a tailspin in August with sales tumbling to 5.5 million, the lowest in five years. New home sales fell 8.3 percent, down 21.2 percent from August 2006. The inventory of unsold homes rose to 10 months, a level last seen in the early 1990s. “The prospects for the rest of the year darkened considerably,” was Seiders’ assessment.

“Even areas such as Seattle that were doing well are feeling some pain now,” comments Bernard Markstein, senior vice president for forecasting at NAHB.

With overall prices expected to decline by 0.3 percent and sales falling back to 2002 levels, it would be easy to classify 2007 as one of real estate’s worst years; yet the National Association of Realtors says it will also be the fifth best on record.

“You read a lot that the sky is falling when in fact there are tons of transactions

being completed,” observes Laurie Keenan, president of Prudential Real Estate, noting that the forecast calls for nearly 6 million sales. “There are still lots of new households being created” and trillions of dollars in equity in real estate, she says.

“From the luxury standpoint, we’ve seen that market being less impacted than the general market and we believe that will continue to be the case in 2008,” says Michael Good, CEO of Sotheby’s International Realty Affiliates. “What we see is that many pockets will continue to be very strong in 2008 and there will be other pockets that will be impacted by the general economy and by the media.”

Data from NAR and the Office of Federal Housing Enterprise Oversight, according to Good, shows that in markets such as those in California and Florida that had the hottest growth in luxury, there is in fact an adjustment underway even in luxury price brackets. “In these markets there is now a bulge in inventory, which naturally causes more competition,” he says.

Luxury sales are strongest in urban areas, which, according to Paul Boomsma, president of Luxury Portfolio at Leading Real Estate Companies of the World, “are doing well this year and old traditional luxury areas are doing really well. People are looking for authenticity and quality.”

“Location has become even more critical. Today, if you define luxury by price, you would find healthier sales activity closer in to cities. Old-money areas are especially strong,” says Terry Morris,



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president and CEO of GMAC's company-owned brokerages.

As the year winds down, shock waves from the subprime crisis continue to reverberate with expectations that delinquencies will continue to rise. Although luxury is traditionally more insulated than real estate overall, the turbulence in the mortgage market does spill into the luxury price bracket, particularly the lower end, since buyers are required to bring more equity to the closing table. Also, says Jim Gaines, an economist at the Real Estate Center at Texas A&M University, “People who might have been in the luxury price bracket are being forced down into the next lower price loan.”

At press time, uncertainty continues to hover over housing. Speaking at the Economic Club of New York in mid-October, Fed Chairman Ben Bernanke said he expects “that the further contraction in housing is likely to continue to be a significant drag on the economy through the end of the year and into early 2008.” Treasury Secretary Henry Paulson echoed his comments saying, “Working through the housing correction will continue to take time.”

Jim Smith, chief economist at Parsec Financial Management in Asheville, N.C., has been consistently ranked by The Wall Street Journal as the most accurate forecaster. Smith believes the greatest impact of the housing downturn is behind us, although he does acknowledge that repercussions will continue to be felt in some markets. The consensus among economists and industry experts is that it will take 24 months or longer for some of the hardest-hit locations in Florida and California to recover.

Sieders expects home sales to hit bottom early in 2008 and slowly improve as the year continues. However, he doesn't expect to see a solid recovery year until 2009. NAR's Chief Economist Lawrence Yun expects to see slow gains in home sales next year.

Such a long recovery doesn't surprise Jim Gillespie, president and CEO of Coldwell Banker Real Estate. “I have been in real estate for 32 years and this is my fifth market correction. And they are all the same. The usual bull run is three to five years, followed by 12 to 18 months of modest correction. With the recent 10-year bull run, it makes sense that the correction would also double to about 36 months, which would take us into mid-2008, which is the same time NAR and most other prognosticators and economists are predicting real estate to take off again.”

“What I see for the coming year is continued adjustment in overheated markets, but really there is a return to a healthier pace,” says Boomsma. “I think we are beginning to approach a really good mix, very much like a traditional market in many areas.”

Already some encouraging numbers are showing up in Massachusetts, one of the first states to experience the downturn. Sales in July and August were up 7.7 and 6.6 percent with even some price improvement. The number of single-family homes on the market was down by 16 percent to an 8.6-month supply, bringing the state closer to the magic 7.5-to-8-month number that reflects a balanced market.

The challenge for the real estate industry, and one that will continue into 2008, according

to Good and others, will be to help sellers adjust their expectations. “It is always most difficult in the early stages of these changes.”

Still, spend time with agents in the field and one also begins to sense that change is underway. “I think we're bumping along the bottom,” says Andrew Miller, a broker with Coldwell Banker Lake Oconee Realty in Georgia. Even though the number of homes for sale continues to be high, Kim Davis, owner of Ponte Vedra Beach Realty, says she senses that the Florida market has bottomed out. In San Francisco, prices might be a little soft versus 2005 and 2006's high water market, but Charles Moore, CEO of McGuire Real Estate in San Francisco, says things in the upper-end are selling, and, most importantly, properties that have been on the market for awhile are selling—as was the case with a home that had been on the market for 153 days for \$12.97 million and sold for full price.

Looking ahead, a number of trends will continue to support luxury. Thanks to a weak dollar and lower home prices compared to other countries, American real estate is a bargain for foreign buyers. Luxury is expanding to new areas throughout the country. “In the past, luxury was relatively isolated and confined to specific areas, now there are pockets of luxury everywhere,” says Mike Reagan, senior vice president, Brand Marketing and Event Management at RE/MAX International.

Lastly, the longer buyers remain on the sidelines means more delayed purchases. Keenan says, “The sense at NAR is that there is a lot of pent-up demand and it will come forth. You can't hold that back forever.” **UH**

