

REAL ESTATE NEWS



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Fine Homes



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If the stock market is a leading indicator, then home building stocks may forecast the future direction of the housing market. Here are the symbols for 9 home builders. BZH, CTX, DHI, KBH, LEN, PHM, TOL, SPF, HOV.

Inventory Low and Prices Rise... What's a buyer to do?

By *John Dumke*

There is nothing on the horizon that gives any indication that the market is going to soften. If you are a buyer waiting to purchase, you may have to wait until Leisure World becomes the desired location. So if you need to bite the bullet and purchase a new home, then there are some precautions you may take. It is simple supply and demand equation, and there is nothing on the horizon that appears to tip the scales in favor of buyers.

Here is the bottom line with Long Beach Real Estate at this time. The number of transactions remains steady, yet down slightly from 2003's breakneck pace. Inventory remains very low at around 300 unsold homes in all of Long Beach. This is VERY low, just above the all time low last spring of only 200 unsold homes and down considerably from last falls significant uptick of 700 unsold homes, which temporarily slowed the market.

This steady buying, coupled with a lack of inventory has once again driven prices up this spring. Is this latest move up sustainable? As long as the supply/demand pictures stays the same, well yes.

On the supply side there simply is no more land within commuting distance to work, so SoCal can't build it's way out. The only other option is people leaving. During the early 90's downturn, there were a significant number of retirees that moved out of the area, this coupled with a very large slowdown in the Aerospace Industry, produced a net outflow of

people from Southern California, for the first time in memory. Yet there are no indications that this is happening at all. Yes retiring out of the area is an attractive alternative, but it is not happening on any kind of scale to be significant. Neither does there appear to be any significant business outflows from the area

in excess of the incoming traffic. During the early 90's downturn, there were a lot of people that were sour on the SoCal way of life. However, there is no negative sentiment like this today. So it is likely the market will remain plagued by low inventory, this bodes well for prices.

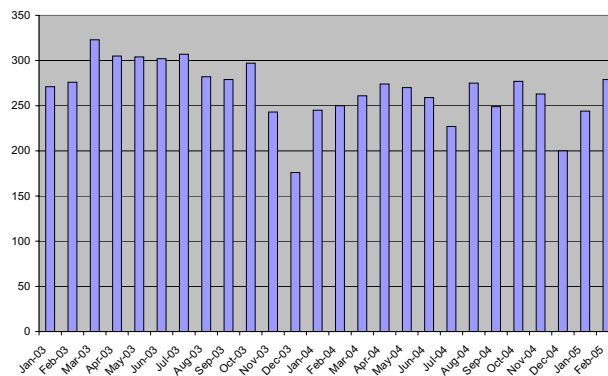
How about the demand side of the equation? The

biggest factor remains interest rates. Which for all of Greenspan's short term rate increases, long term mortgages still remains at all time lows. The bond market doesn't seem to be bothered by short term rates moving up as much as one would think. So mortgage rates remain low. Yet there does seem to be a slight disconnect between the bond markets lack of concern with inflation and the overall backdrop of higher oil prices, and higher material prices across the board. The bond market is saying that inflation will not be a problem, yet commodities indexes suggest otherwise. So this is the only source of major concern, but no determination can be made as of yet.

The current market does not show any signs of imploding, yet knowing that SoCal Real Estate can show signs of booms and busts, some basic defensive strategies may be in order.

First let's put an historical prospective on our last

SFR Sales in Long Beach



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bust, 1990-1995, and pretend you had rode out this last storm. During the last downturn (1990 - 1995) prices dropped by 25%. Let assume that you bought a typical 3 bedroom, 2 bath home at the peak in 1990 for \$250,000 with \$50,000 (20%) down. During this painful 5 year period you watched as your homes value fell to \$190,000. Your down payment gone, you couldn't even sell your home, without coming up with another \$15,000 to close escrow. You kicked yourself on a daily basis for having been so stupid.

Fast forward to 2005 and your home, that you wisely chose not to sell, is now worth \$625,000. You look back and say \$190,000, \$220,000, \$250,000, who cares, I should have bought the whole neighborhood. In hindsight that \$60,000 theoretical drop was just a blip on the radar screen and today hardly warrants consideration. **But that is not how it felt at the time.**

So in hindsight, what is the moral of the story? That everything has worked out overtime, but on a short term basis, if you had folded, the results would have been tragic.

So here are some thoughts on taking a more defensive posture if you are in the market for a new home.

Build a strong game plan. If you buy today, make sure you are comfortable with the payment, and are happy with your home. Will you be comfortable living there for 5-7 years? If this is the case who cares if the market is down 10% or up 30%, But don't buy in a bad neighborhood that you don't want to live, or settle for a 2 bedroom, 1 bath when you really need more, telling yourself, that it is just temporary to get into the market and in two years we will trade up. Two years has an easy way of becoming 7 years.

Don't Follow the Crowd. Don't buy just because you think you have to. Let's say you are 25 years old, single and have a great apartment for only \$500 or maybe even live at home. You have a steady job in a well paying profession, but it kills you to hear your slightly older married co-workers talk about the killing they have made. Your happy where you are, but have a hard time dealing with your gloating co-workers and your tax accountant says you need a write off.

Ignore then. Because of your low living expenses you are able to sock away \$1,500 - \$2,000 per month because you don't have a home or condo payment. You are happy with your living situation and the only pressure to buy is your co-workers telling you, you are getting behind. Don't fret. While \$50,000 in appreciation makes your hard fought \$20,000 of annual savings feel like chicken feed, this can't go on forever. Houses can only go up at the same rate as peoples incomes. Lately appreciation has greatly outstripped income growth, so at some point in the future it is likely that home price appreciation will stagnate in which case your extra \$20,000 in saving will be money in the bank and looking pretty good.

Beware of excess leverage. Another danger area is excessive leverage when you trade up and rent out your existing home. (If you have a home worth \$500,000 and you only owe \$100,000 and you have

a 20% down payment for your next home, then I am not talking about you.) But what is more typical, is for somebody to have bought their existing \$500,000 home for \$300,000 and they have a \$270,000 loan and they are considering a \$700,000 purchase. They feel really smart about their current home purchase, it is their best investment. *"We turned a \$30,000 down payment into \$230,000 of equity, so I want to keep this home and do it again"*. What often happens is that this buyer will borrow off their existing home for the down payment to purchase their next home. In essence financing 100% of their new home.

How well will this buyer be able to weather a storm? Let's compare scenario's.

#1 - Sell and trade up	#2 - Keep and trade up
\$700,000 New home	\$1,300,000 in 2 Homes
\$500,000 Loan	\$1,100,000 in Loans
\$200,000 Equity	\$200,000 Equity.

Now there is no indication that there is an early 1990's bear market in Real Estate in our future, but let's just pretend that something bad happens. We buy life insurance and fire insurance not because we plan on dying or burning our house down, but simply as sound financial planning. Real Estate investing is no different.

Should the market turn south for a protracted period of time, debt is likely to bury a buyer in scenario #2. If the market goes down even 15% all equity has vanished. Second, it is likely that this financial picture severely craps ones cash flow to the point where the loss of a job or other financial hardship might result in foreclosure. Paying high mortgages feels purposeful when prices are going up, but when there is no equity left, after 5 years of a downturn, most people just say, "what is the point?"

The third factor against keeping an existing home with a low purchase price are the tax considerations. In the above example there is \$200,000 of capitol gains that if sold as a principle residence would be exempt from taxes. But if rented out for 3 years, the gain becomes taxable at a rate of about 25% for federal and state taxes. Imagine this. You refinanced the \$500,000 home and pulled \$100,000 out to buy your next home. Over the next 5 years the value of this home goes down 20% and is worth only \$400,000. The total payment runs about \$3,000 every month and rents for \$2,000 per month. So when the property is rented and there is no maintenance, you still have to fork over \$1,000. After 5 years (or 60 months) of forking over \$1,000 / month and watching it go down \$100,000 you just can't take it any more. Why throw good money after bad? So you decide to sell.

But because the home is worth \$400,000 and you owe \$400,000 you now you have to bring in \$25,000 in to close escrow. Then while you are down the IRS kicks you by wanting another \$25,000, to pay the taxes on the \$100,000 in gain.

Beware of 100% financing and adjustable rate loans.

Market Activity

The following information is from the Multiple Listing Service as of 3/14/2005.

2004 Stats

Address	Br/Bth	Sq Ft	Lot Size	List Price
Alamitos Heights				
388 Ultimo	3/3	1691	3250	759,000
335 Flint	3/2.5	2242	3250	775,000
775 Havana	3/2	1850	6400	799,000
400 Flint	4/3	2718	6500	1,100,000
5375 E. 4th St	4/3	2451	7200	1,150,000-1,250,000
356 Santiago	4/3	2560	8100	1,300,000
528 Havana	3/2.5	2849	9750	1,395,000
427 Orlena	4/3.5	3020	6500	1,450,000
379 Manila Ave	5/4.5	3350	5740	1,599,000
425 Ultimo	6/5.5	5679	13000	1,899,000
621 Havana	4/4.5	6419	9750	2,295,000
La Marina Estates				
1421 Iroquois	4/2	1624	7150	695,000
1411 Josie	3/2	1488	7150	705,000
1315 Hackett	3/1.75	1682	7035	749,500
Los Altos (S. Fwy)				
2231 Iroquois	3/2	1207	8337	529,900
1809 Knoxville	4/3	2100	6758	675,000
2065 Fidler	3/2	1960	6046	719,900
1857 Knoxville	3/2	1300	6758	569,500
1809 Nipomo	3/2	1633	5600	647,000
1885 Lave	3/2	1700	6080	699,900
6945 El Cedral	4/2	1360	5904	475,000
6400 Madera	3/2	1077	6104	485,000
2220 Senasac	2/1	1239	6000	495,000
1867 McNab	3/1	1176	6600	495,000
6400 Fairbrook	2/2	1198	5665	500,000
2080 Gondar	3/1	1314	6380	515,000
6917 El Cedral	3/2	1280	6200	549,000
5804 Garford	3/1	1622	6450	584,000
2261 Lomina	3/2	1226	6400	589,900
1802 Litchfield	3/1.75	1676	6830	599,000
1840 Vuelta Grande	3/2	1424	5900	599,000
2044 Carfax	3/1.75	1292	5985	609,000
2211 Gondar	4/1.75	1795	6000	629,000
1872 Marber	3/2	1464	6044	639,900
University Park Estates / College Park				
6840 E. 11th St	4/2	1857	5985	685,000
695 Silvera	4/3	3147	7040	950,000
845 Lees Ave	3/1.75	1517	6270	609,000
6850 Lees Way	3/2	1525	6000	659,900
6301 Vermont	3/2	1566	6930	695,000
Park Estates				
5371 El Parque	4/3	2888	15040	1,575,000
1411 Greenbrier	3/2.5	2562	6900	715,000
5411 Las Lomas	3/3	2100	10820	949,000
1430 Ramillo	2/3	1867	7800	785,000
5231 Vista Hermosa	3/1.75	2031	8090	869,000
5210 El Roble	3/2	2001	7490	898,000
5241 El Roble	3/2	2241	10500	949,000
5330 El Parque	3/2.5	2846	10110	1,329,000
1410 Bryant Dr	3/4	4771	22500	2,375,000

(Based on closed sales from 2004 - SoCal MLS)

Alamitos Heights

*Number of Sales - 45
Low Price - \$425,000
High Price \$1,350,000
Average - \$839,079
Average Sqft - 2,213*

La Marina Estates

*Number of Sales - 7
Low Price - 569,000
High Price - \$770,000
Average - \$665,571
Average Sqft - 1,969*

Los Altos (all)

*Number of Sales - 191
Low Price - \$360,000
High Price - \$749,900
Average - \$511,504
Average Sqft - 1,457*

Univ Park Estates

College Park

*Number of Sales - 20
Low Price - \$528,000
High Price - \$825,000
Average - \$661,720
Average Sqft - 1,776*

Park Estates

*Number of Sales - 24
Low Price - \$625,000
High Price \$1,425,000
Average - \$903,366
Average Sqft - 2,357*

Along the same line of building a strong financial game plan, these are two areas that could get you in trouble. While you can buy a home with nothing down plus several thousand dollars in closing costs, it does cost about 6-7% to sell. What if the property doesn't appreciate? How will you sell it? The answer is that you can't, without coming up with cash or letting it go in to foreclosure. If a buyer couldn't save for a down payment will their savings strategy be any better with a mortgage payment?

The second area of a weak financial planning is getting a loan other than a 30 year fixed mortgage which run around 5.5% right now. Sure that 2.95% start rate makes your house payment more palatable, but can you afford the home should that adjustable go to 6%. If so, then you have nothing to worry about.

I love the past example of 1990-1995's bust. It reminds us that even the worst downturn in memory in hindsight was nothing more than the best buying opportunity. But this was only the case if you were able to weather the storm and stay in the Real Estate market. Make sure that any purchase is based upon a sound long term game plan.