

# SIFF Insight

NOVEMBER 2006

## Reacting to the Real Estate Market Correction

### PART 1. EVALUATING



Many of our clients have asked us when they should buy another investment property or should they sell existing properties. The answer to this question really depends on their lifestyle and retirement goals. Where you are financially versus where you need to be

will help you make the best investment decisions. Every type of investment has its own characteristics and risk.

As part of our commitment to real estate investment education, we have developed SIFF Insight to help you make sense of the current market and media and what it all means to you. At SIFF, we believe that real estate investing is for the long haul, but that doesn't mean you shouldn't change your real estate investment portfolio, or some aspect of it, such as financing. Factors such as your current and future income, cash flow, lifestyle, retirement goals as well as actual and projected real estate market growth should all be closely monitored to ensure you're making the best bet with your money.

The current SIFF Insight, "Reacting to the Real Estate Market Correction," is a multi-part series that will help you decide what to think about and do as we face a correction in the real estate market. With changing conditions, it's only natural to want to take action, but also remember analyzing and deciding to stay the course may also be a reasonable response. As we've said before, it really comes down to your personal financial situation. Are you ahead or behind in retirement savings? Do you want to take advantage of the run up on your income property to allow a spouse to take time out of the workforce? Do you want to re-balance your overall investment portfolio to put more money into securities? Do you have other financial goals such as buying a business or paying down debt? These are just some of the important qualitative answers that need to be addressed along with the numbers.

In Part 1 of the series, we'll address our approach to evaluating the situation to help you make the best choice. The factors fall into three main categories: 1) Current Market Conditions; 2) Your Investment Options; 3) Your Personal Investment Plan; and 4) SIFF Investment Indicators.

### CURRENT MARKET CONDITIONS

Everywhere we turn we read about the softening of the real estate market. This is definitely true as a broad statement. But speaking in broad terms doesn't help the investor in different parts of the country. What is happening in the Bay Area, or elsewhere for that matter, has very little correlation to what is happening in Vancouver, Washington or Portland, Oregon. And when you hear the news, what should you do if anything at all?

With low inventory, limited land, and affordable housing, Portland Metro Area appreciation remains strong at 16.4% according to RMLS August 2006. This is a strong vote of confidence given that many metro areas across the US are not only experiencing slowing growth rates, but negative growth. One key metric that points to market strength is inventory. Although Portland Metro inventory has increased to 3.6 months this is still very low when we compare it to the national average over the past 6 months. The average property is on the market for 39 days, which is virtually unchanged from last year.

We at SIFF believe the Portland Metro real estate market will remain in positive growth territory for the next 12 to 18 months. As we've shared with you, Portland was one of the last metro areas to experience strong real estate gains, and so we expect the softening effect to lag many leading metro areas as well. And because it's a stable, growth market and not a hyper growth market, we don't expect the sharp declines you're reading about in other areas such as Las Vegas and Phoenix.

## INVESTMENT EXPECTATIONS

What are normal expectations for real estate investing? Historically, residential real estate appreciation is about 6% per year on a national basis. So, if you're a relative newcomer to acquiring residential real estate in the Bay Area, you've seen appreciation over the last 5 to 7 years hit the 20% and above mark. We're currently seeing appreciation hold fairly steady in the 15% to 16% range in the Portland corridor, which is good. We still see Portland as a healthy market in terms of opportunity and lifestyle and for all the reasons we've cited in past articles and newsletters. It continues to offer our investors good value.

Realistic expectations go hand-in-hand with long-term investors. They're not expecting to flip. They're not worried about changing appreciation. Money made in the Bay Area real estate market over the last 6 years is unprecedented. You're fortunate to have experienced the enormous gains, but don't count on it in the future. In other words, alter your expectations about real estate appreciation, and you'll be in a position to make more reasoned choices.

## POSITIVES OF A SOFTENING REAL ESTATE MARKET

So, what's good about this market? First of all, as we've projected, rents are usually move in the opposite direction of housing demand and that has proven to be the case. We've raised rents on average 6% for all of our properties under management. While appreciation may be tapering off, cash flow may be stronger. In addition, with fewer speculative investors in the market, investors will have more opportunities to negotiate on price and property condition. All strong reasons for acquiring real estate as it makes sense. Stay tuned, and we'll delve into this investment option in the series.

In the next few years, we will have fewer short-term, speculative investors and those investing for the long-term. We believe this will make for a more rational market for both buyers and sellers.

## YOUR INVESTMENT OPTIONS

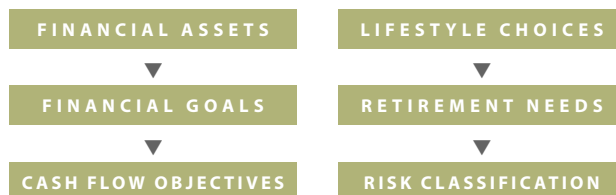
So now that you have one or more investment properties in your portfolio or you're looking to acquire your first, you must be thinking what does this market mean for me? And what are my investment options? The long-term investor will most likely hold given the current market conditions, unless there's a change in lifestyle. Below we've highlighted the primary options that come to mind; of course, they aren't all mutually exclusive:

- Sell Your Income Property
- Re-Balance Your Real Estate Portfolio
- Invest in More Income Property
- Hold – Don't Buy or Sell
- Refinance
- Refinance and Take Cash Out

## YOUR PERSONAL INVESTMENT PLAN

We like to go back to the plan of record, that is the plan we develop with you that looks at your financial assets, cash flow goals, lifestyle choices and retirement needs. Further, in the planning stage, we attempt to draw up a profile of how risk tolerant or risk averse you may be and how long your investment horizon is. So, when you ask, "should I sell, buy or hold?" we have a foundation for giving you our best advice.

### ELEMENTS OF YOUR PERSONAL INVESTMENT PLAN



## SIFF INVESTMENT INDICATORS

At SIFF, we believe that income property investing is a different animal, even different than other types of real estate ownership. It's not like investing in resort destinations or your own home. By stripping away the glamour of owning real estate, we can better analyze the property as an investment, pure and simple. The emotional part is what you can earn in wealth and lifestyle as a result of controlled, disciplined investing. When we apply our financial lens to your specific financial situation, we've come up with the following key indicators, variables we look at in conjunction with your plan. We'll use these variables to draw up scenarios to give you our best assumptions based on conservative estimates and market trends.

- Transaction Costs
- Tax Implications
- Inflation
- Type of Loan
- Interest Rates
- Retirement Goals
- Rent Management
- Projected Real Estate Market Growth

## NEXT

We have summarized our approach to analyzing the decision of what to do in a changing market. First, we analyze the current market, and taking a local perspective, we look at Portland Metro data against national data. Second, we outline the range of investment options. Third, we review the financial plan. And fourth, we bring our SIFF Investment Indicators into the picture to confirm the numbers and the goals. Please look to SIFF Insight Part 2 to learn how we can help you navigate the decision of whether to hold or sell your property.



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