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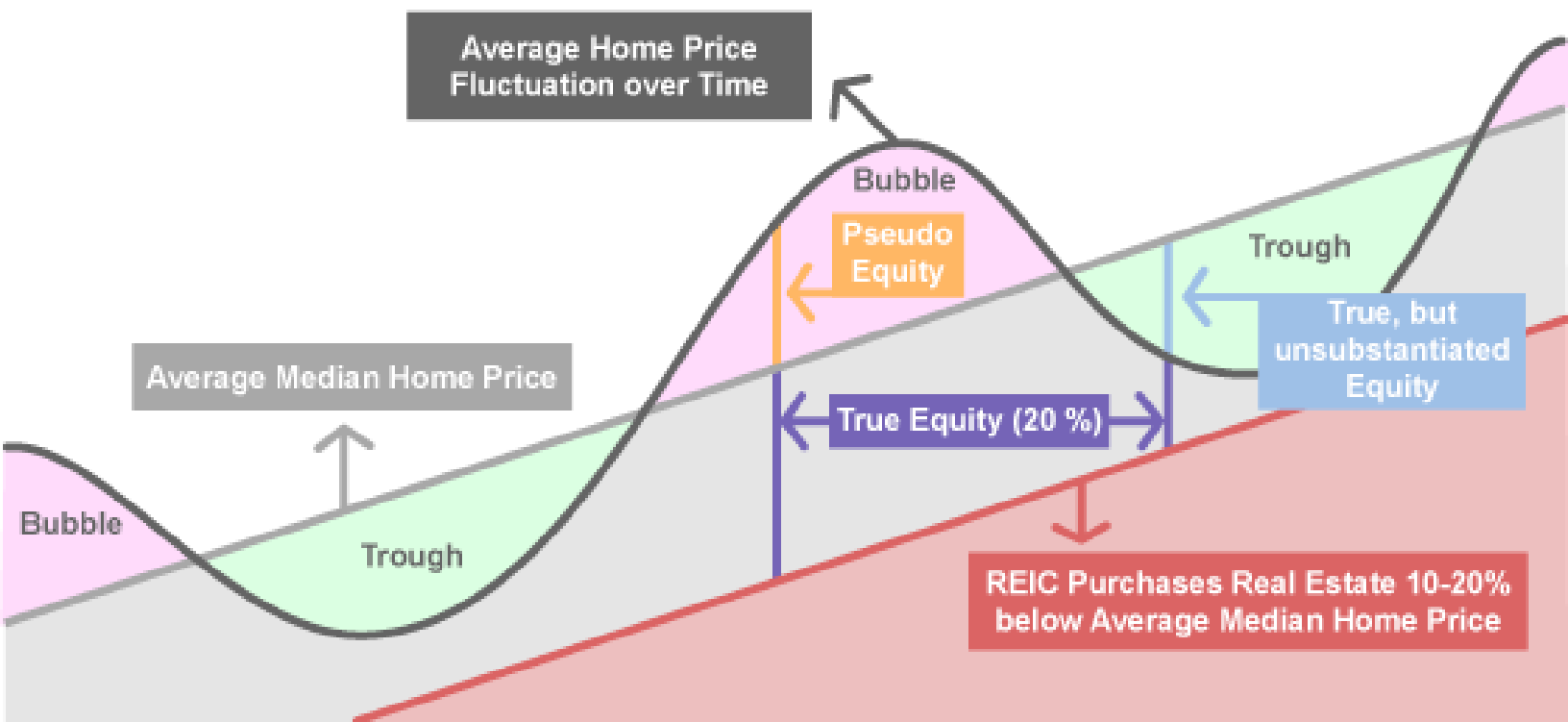
Real Estate Market Cycle

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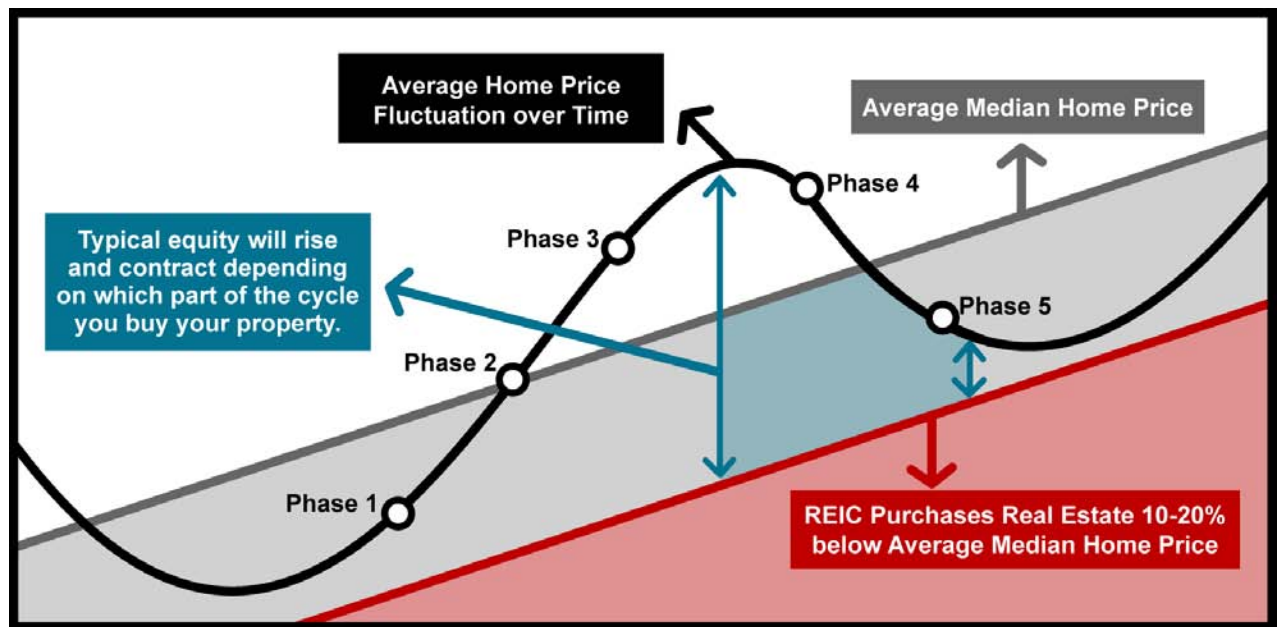
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Real Estate Market Cycle

We have often heard the adage “buy low, sell high.” If Real Estate Investors understand the wealth cycle of the Real Estate Market, they are able to capitalize on the greatest financial opportunities available. As Warren Buffet Says, “buy on fear and sell on greed.” Applying this market advice requires an understanding of typical market cycles. Below is a description of the 5 phases

of a complete real estate market cycle. **Remember:** It is possible to invest successfully in **any** market if you are purchasing real estate significantly below market value. The Real Estate Investors Club purchases all of its real estate below market and uses a short term buy and hold strategy to protect its investments from market changes.



Phase 1: Market Activity Picks Up. When a market comes out of a corrective period good real estate deals can be found. Professional investors recognize early that this is still a good time to be purchasing real estate. Consumers do not respond as readily to the market due to fear, unless their circumstances force them to.

Phase 2: Market Confidence Accelerates. As home prices increase from the response to buyers entering the market, consumers gain confidence and begin feeling comfortable purchasing real estate.

Phase 3: Market Approaches Peak Volume. Consumers now lead the charge believing the market will always continue to go up. Some of the most fearful consumers

decide to try real estate investing as a viable investment option as the market begins to wind down. This market presents the worst investment options at Fair Market Value (FMV).

Phase 4: Market Begins to Slow. As the market slows down so does the value of homes. As the number of home sales decrease on the market, consumers panic and begin flooding the market with homes to sell. This provides good opportunities for investors to negotiate good deals.

Phase 5: Market Approaches the Bottom. This is the best time to buy. As the real estate market approaches the bottom, the best deals on the market appear, especially if

you have a short term buy and hold strategy as opposed to flipping real estate. Those that buy real estate at this market time will make the greatest returns over the next few years as the market recovers and catapults forward. An interesting characteristic of this up-and-down cycle is that as the market falls in value, the number of houses

listed and sold decreases. This is because homeowners seek to hold off selling their property if they will realize profit or even lose money. Because of this slow-down, you will see a much higher percentage of desperation sales such as short sales, foreclosures, bank-owned sales, and auctions.



REIC Property Valuation

How do we establish a property's value?

“Evidence” of a property’s value is typically established by running a “Comparable,” also called a comp or CMA (Comparable Market Analysis). A CMA takes the prices of multiple properties in the same neighborhood as the property in question and averages them together to demonstrate what it would be worth if it were sold.

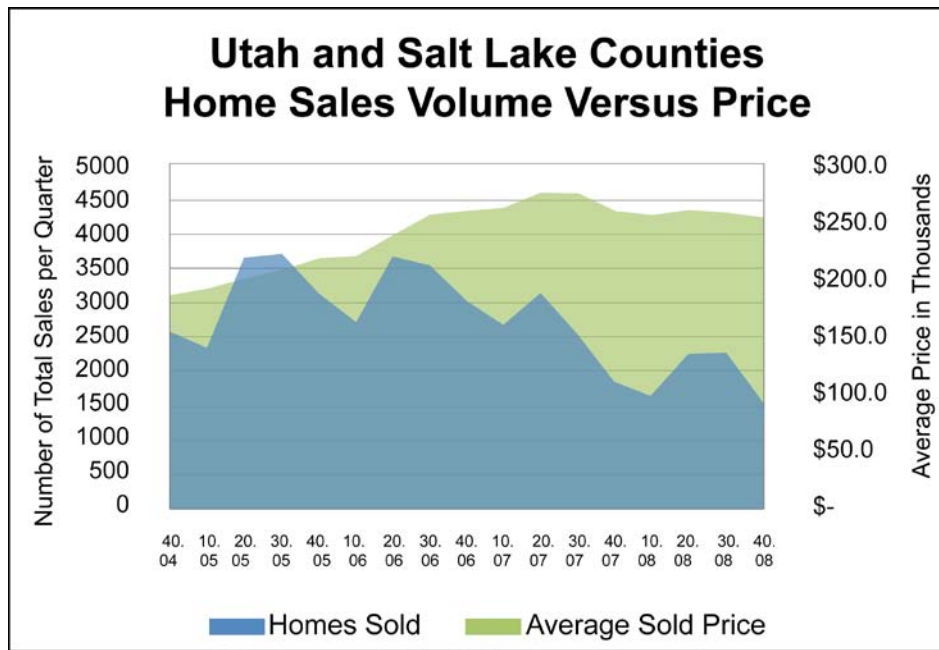
It is important to remember that CMAs are counter-cyclical to the rise and fall of market value. During times when market prices are generally low, it is extremely difficult to document a home’s true value because there simply are not enough CMAs to create an accurate profile. Also, properties that have been recently sold tend to include many underpriced properties like foreclosures or short sales, which can make the value of an excellent home artificially depressed.

Conversely, when prices are high (which is not the time optimum to purchase property), there is abundant evidence of a home’s “perceived value.” This is because neighborhoods are full of recently sold homes at inflated prices, creating a potentially false picture of true equity.

What does this mean about the property you are buying?

No matter what market we are in, REIC is buying at the bottom five percent of the bell curve. During the low part of the price cycle, the bottom five percent of homes will typically have 10-15% equity rather than the 20-30% equity you see in the high part of the cycle. This difference in percentage does not indicate the homes have less equity, but that the homes they are being compared against are less reflective of the real estate’s true value. Because there are fewer homes on the market, fewer homes being sold, and a higher percentage of desperation sales, the same amount of equity will show up in a lower percentage as compared with recent sales in that neighborhood.

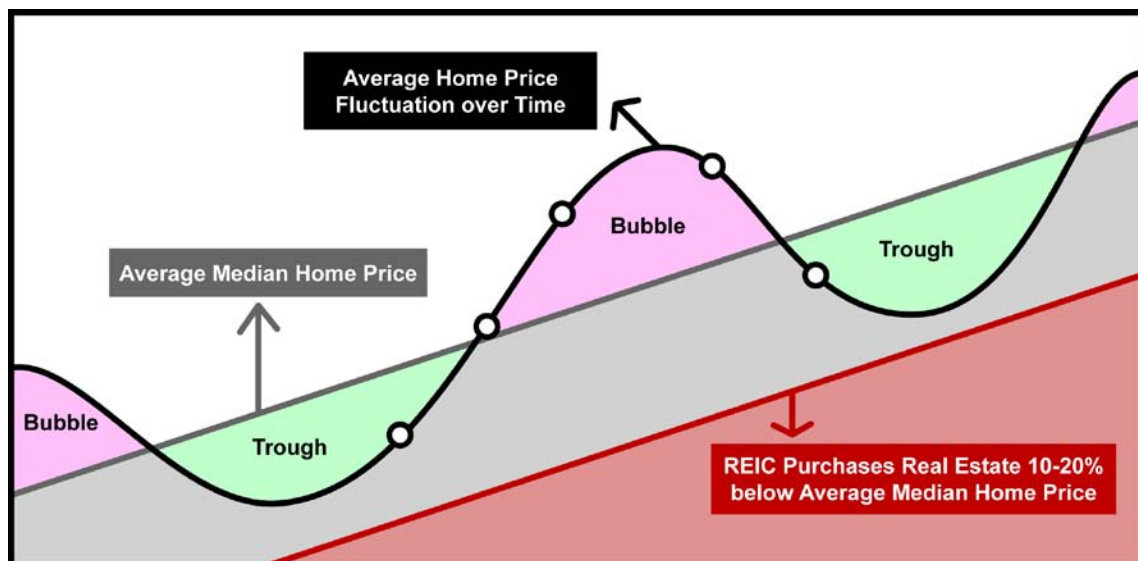
Notice that while average home sales price in Utah County has gone down only slightly, the number of homes sold has dropped by half in the last year. [Source Wasatch Front Region MLS Home Sales data.](#)



When is the best time to buy or sell?

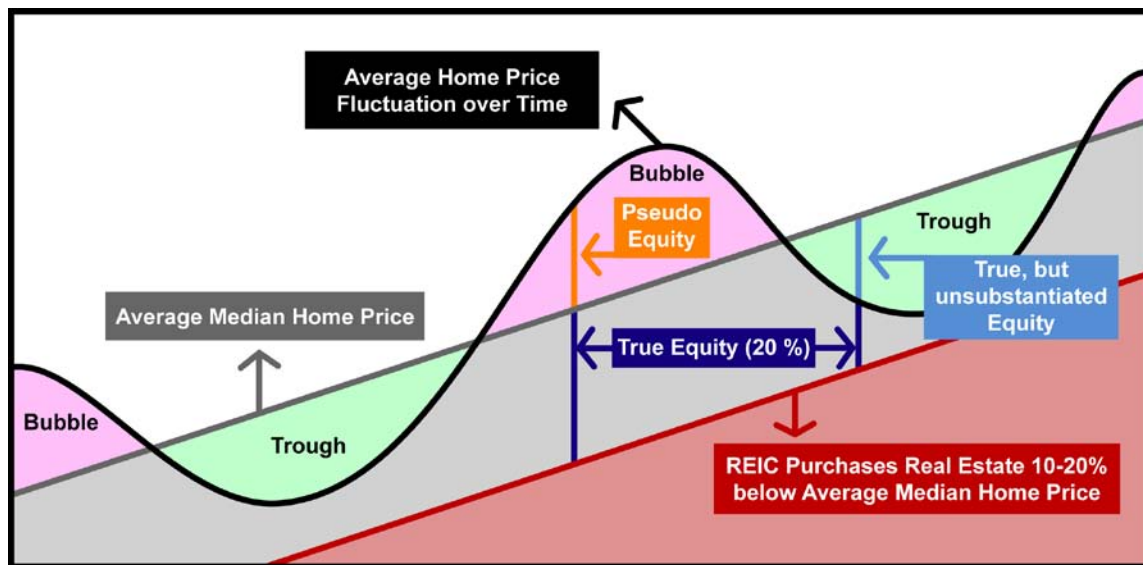
Because REIC's properties are always going to be significantly lower than the average median home price, any time you are ready to make a purchase is a good time. If your timing is such that the market is in a "bubble" (pink area of graph), you can expect the equity position will be high, typically between 20-30%. Because prices are higher than the overall average home price, however, your actual gains will be less than the equity position would indicate

as the market self-adjusts downwards over time. Conversely, if you are purchasing an investment property during a "trough" in the market (green area of the graph) your equity position will more likely be between 10-20%. This "trough" period is actually a more favorable time to buy since prices are below the average home price over time. You will see the value increase faster proportionally than the equity position as the market adjusts itself upwards.



In this example, a home bought at different times during the market cycle will have the same amount of true equity (blue line – 20%), based on the REIC purchase price versus the average median home price. However, “pseudo equity” will artificially inflate the equity during the “bubble” (pink section) and it will appear deflated during a trough period

(light green) with unsubstantiated equity. Because of this market characteristic, REIC uses a short term buy and hold strategy where homes are held for one to three years, generating cash flow through our lease-option program, then sold when market conditions are favorable to capture their true equity.



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