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Time to Buy an Investment House in Pacific Palisades?

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Not sure where to invest your cash? Are you looking for a way to diversify your portfolio? Now may be the best time to buy an investment home in Pacific Palisades.

While no one knows for sure what will happen with real estate values in the next few years, the chart below outlines real estate prices from the past 20 years as well as our prediction for the next five years.

Based on historical data, if you were to buy an investment home in the Palisades this spring and rent it out over the next five years there's a possibility, assuming we're close to the bottom of the market, it could appreciate approximately 15 to 20 percent over that time period. This may not sound like much but when you consider the effect of leverage, if you put 25 percent down, then you are really getting about a 60- to 80-percent return on your money over the five years. You need to factor in carrying costs, vacancies, home repairs and other expenses, but the return could still be a decent one.

Pacific Palisades housing prices are currently at 2004 price levels, whereas prices peaked in 2007, which was considered the height of our market. Since property values have dropped approximately 25 percent in the past 24 months, even if we are not exactly at the bottom we seem to be close.

Many stock market investors have repaired their portfolios in the past year but are still wary about the market's volatility, and are unhappy about the low returns they are getting for their cash (e.g., a three-year CD paying about 2.57 percent, a five-year CD paying about 3.25 percent). They know that historically, real estate has been a good investment, especially when one can purchase a home near a market bottom, as appears to be happening in Pacific Palisades, at least for entry-level homes.

The best indicator of our local current market is the supply and demand chart (see below). For the past 13 months the number of homes for sale is down 41% while the number of homes sold is up 7%. This trend indicates that real estate prices, at least for entry-level properties, have started to bottom out and have stopped declining. Additionally, interest rates are close to all-time lows, helping to make this an excellent time to purchase an investment property. Many lenders are seeing that consumer confidence in entry-level price ranges is coming back, so we are slowly seeing banks lending again which will be the key to our real estate recovery.

The upper end market will take longer to recover because there is more risk for a lender to lend. This is why lenders are requiring 40- and 50-percent down payments on higher-end homes. If someone was able to put 20 percent down on a $3 million home and it declined another 20 percent, the bank would lose all of its equity. Lenders know that higher priced homes typically have more room to decline then an entry-level home.

Buying real estate, much like stocks, can include a great deal of risk and we recommend you speak to your accountant and financial planner before deciding to invest in real estate.

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