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Trending Up

Optimism builds for a revitalized real estate market in 2014

By Joe Follansbee

Tyler Zoellin watched the Seattle housing market for two years before getting serious about buying a home. The 32-year-old IT consultant and his family wanted to find the classic American single-family home with a nice back yard to raise their 4-year-old. They lived in a condo in Seattle, and starting in the summer of 2013, began their new home search in urban residential neighborhoods. At first, they discovered what industry observers have been noting for a year now—the market has been heating up.

"It seemed like every good property we looked at was sold within 24 to 48 hours of listing," Zoellin recalls.

Eventually, they found what they were looking for in the Seattle suburb of Issaquah: a 2,300-square-foot house built in 1988. It had four bedrooms, two and a half baths, and a three-car garage. It was affordable, relatively near the urban amenities they had grown used to—and, with Issaquah's location at the foot of the Cascade Mountains, it was also close to their favorite recreational options. "We're really outdoorsy and it definitely feels like those things are a lot closer now," Zoellin says, happily. The family moved in last December.

Meanwhile, Supriya Uchil wanted to live on top of a hill—but not just any hill. After three years renting a restored 1920s-era one-bedroom apartment below Seattle's prosperous Queen Anne neighborhood, the Amazon employee decided to move up. "It was time for me to buy a house, to own a home," she says. Uchil needed a bigger place to entertain guests and host extended visits by family and friends from as far away as her childhood home in India. She wanted to walk to work, and find a place that showcased the mountains and water landscape that makes Seattle special. "My heart was set on top of Queen Anne Hill." After looking at 10 houses, she found a 2,800-square-foot house and picked up her keys in February.

Their stories exemplify several conspicuous trends in the real estate market today:

• Market activity is shifting from the high-profile major metro areas of the early part of the decade—New York, San Francisco—to cities such as Seattle and Portland.

The urban village, where work, shopping and recreation cluster, exemplifies the growing strength of the U.S. real estate market.

RADIUS IMAGES / ALAMY

The many advantages of condominium living have proven appealing to the millions of Gen Y members now entering the housing market.

• While families such as Zoellin's are happy to head to exurban areas for their American dream single-family home, other Gen Y professionals such as Uchil remain committed to the in-city advantages of urban neighborhoods—nearby services and amenities and even employment options that do not require use of a car.

• So-called "move-up buyers" constitute the majority of activity. These are young families with wage earners in tech professions whose kids will soon enter public schools; or "millennials" such as Uchil desiring to expand their living quarters while retaining a central location. Although the condos and apartments that have burgeoned so visibly in urban areas the past decade served their needs admirably for a while, these young professionals are now ready for stand-alone homes.

"I'd say 'move-up' buyers are 60 percent of the business we're seeing these days," reports Lance Morgan, area manager and mortgage consultant at Windermere Realty's Sandpoint office in Seattle. "The demand is strong, and the biggest problem is that inventory is tight enough that buyers often cannot wait on contingent sales of their existing homes." Sometimes, Morgan adds, buyers are so anxious to accomplish their move-up mission that they sell their existing home and rent until they find a new home to buy.

So, with activity such as this becoming common, is 2014 the year the real estate economy returns to normal after its half-decade slump? Many economists

Real eStats

1 The highest-priced major metro area housing market at the end of 2013, according to National Association of Realtors statistics, was San Francisco, with a median listing price of \$799,000. Los Angeles was \$450,000; Seattle was \$350,000; Portland, \$289,000.

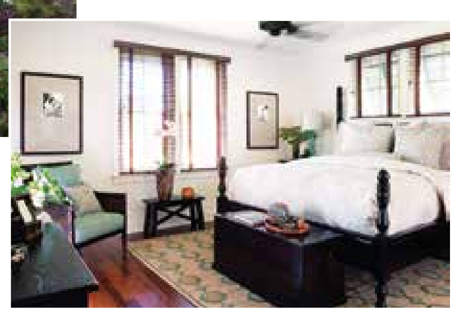
2 Time on market, a key expression of market activity, was lowest in Honolulu (64 days) and San Jose (70 days). Highest were Philadelphia (145 days) and Newark (124 days).

3 The national median list price, \$195,000, was 8.1 percent higher at the end of 2013, compared to December 2012.

4 Total housing inventory at the end of 2013, according to the U.S. Census Bureau, was 132.9 million units—362,000 above 2012, a 0.27 percent increase.

5 The rental vacancy rate at the end of 2013 was 8.2 percent, down from a high of 11.1 percent in 2009. Homeowner housing vacancy rate was 2.1 percent, down from a late 2008 high of 2.9 percent.

COURTESY: KUKUI'ULA (2)



Second homes, such as these deluxe cottages at Kukui'ula on Kaua'i, are proving very popular with the baby boom's many empty nest couples.

believe so. In 2013, low inventory and low interest rates, as well as a slowly improving broader economy, drove much of the increase in house prices from the lows of 2009. In 2014, "inventory should gradually stabilize and return to traditional seasonal levels," predicts Realtor.com, which adds that the tide of "underwater" mortgages is likely to continue ebbing. In 2013, foreclosures nationwide reached their lowest point since 2007, before the bubble burst. At the end of 2012, 1.2 million U.S. homes were in foreclosure; by the end of 2013, that number had dropped dramatically to just 837,000. The "serious delinquency" rate, a different measure than outright foreclosures, was also at a five-year low of 2.52 percent, compared to 3.2 percent two years prior.

Add all these factors up and, according to a report by the nonprofit Urban Land Institute, this year the national real estate market will be "recovering from the recovery," that is, the market will respond less to the echoes of the deflated bubble and more to economic fundamentals such as demographics and continued low interest rates.

"Tailwinds," such as good, if not great, job growth in energy, technology, health care and biological research, education, and financial services will overcome the "headwinds" of relatively high unemployment, uncertainty over government regulation and fiscal policy, and concern about rising interest rates, according to ULI.

Nationwide, house prices rose 8 percent last year; listings increased 1 percent; and time on market—a key indicator of real estate activity—declined 5 percent.

Of course, the health of real estate markets varies from town to town, and ULI predicts that investors, developers and builders will turn their attention away from so-called "gateway" cities such as San Francisco and New York, where land is tight and prices high, to more moderately priced cities such as Seattle, Austin, and the cities of Orange County, California.

Some severely stressed markets have been reporting dramatic gains. Las Vegas prices were up almost 30 percent in 2013; Phoenix, 20 percent.

In the Portland metro area, where prices rose 10 percent last year and time on market declined more than 9 percent, real estate agent Terrie Cox anticipates a good year. "I see a slow but positive growth in 2014 with an abundance of new home construction permits being issued," she says. "Builders are snapping up lots close to shopping, schools and airports."

The changing demographics of the country will play a key role in the trends that shape the housing market in 2014 and beyond. The newest buyers on the scene are the millennials, sometimes called Generation Y, who were born in the 1980s and '90s. The older members of this cohort, now in their 30s, face a home ownership environment different from their Gen X and baby boomer parents. Many are relatively recent college graduates, and affordability is a key challenge. In 2013, the National Association of Realtors Home Affordability Index dropped to a five-year low as price increases outpaced income growth. Glenn Crellin, an economist at the Runstad Center for Real Estate Studies at the University of Washington, says many millennials have put off buying. "What we're seeing is a three- to five-year delay in home ownership decisions," he says. But he remains confident that millennials will eventually own homes at about the same ratio as their parents.

The potential market is huge: Gen Y, the millennials, has 72 million members, according to ULI. The baby boom generation, once the premier economic force of our time, is now down to 73 million.

But the millennials' expectations and tastes are markedly different from older generations'. A 2013 survey by Better Homes and Gardens Real Estate found that one in three prefer a "fixer-upper." And they're ready to get calluses: 72 percent of millennials consider themselves "just as handy—if not more so" than their parents. They're also choosing different neighborhoods. Like Supriya Uchil, many want to walk everywhere, and that means downtown areas or neighborhoods with restaurants, entertainment venues and personal services. “Millennials are time-sensitive and really prefer to walk to work,” says Dean Jones, principal at Seattle-based Realogics Sotheby’s International Realty. He’s seen the transformation of Seattle’s downtown from a strictly retail and office environment to a true neighborhood with high-rise condo towers and world-class high-tech companies, such as Amazon. And neighborhoods such as Ballard, once almost completely dominated by single-family housing, now boast multistory condo and apartment complexes that have attracted hundreds, if not thousands, of new residents. When these residents move up, they may move just four blocks from a condo to a traditional single-family house.

At lunchtime and after work in the evenings, millennials crowd the sidewalks of the South Lake Union and Belltown neighborhoods next to the downtown core; and the bustling restaurant and entertainment districts such as are found in Ballard and in Portland neighborhoods such as the Pearl District. “Millennials are less interested in chasing the American dream 20 miles from work [in a suburb].”

Jones notes that many of those workers are renting, not owning, in part because they value mobility; it’s easier to pull up stakes to take a new job in a different city if you rent. However, that’s likely to change if rents continue to rise in Seattle at the current 6 percent annual rate. Owning will become more appealing, Jones says.

Millennials do share some preferences with their parents, the so-called empty nesters, middle-aged singles and couples who no longer need that big suburban house with an expansive back yard for raising a family. Many baby boomers are downsizing to urban condos and townhomes (and selling their homes to young families such as Tyler Zoellin’s). The Urban Land Institute says this trend will continue in 2014 as people 55 and older look for neighborhoods with high “walk scores” close to cultural amenities and health care services.

Harold and Laurie Linebarger are typical of these couples. They owned a 3,600-square-foot house in a San Diego suburb, and once their youngest child moved out, the house was too big. Harold remembers discussing the situation with Laurie. “This is crazy. Let’s sell,” Harold told her. “Within three days, we had multiple offers, and the house sold after five days on the market.” They rented a condo in downtown San Diego, then decided to move to Seattle to be closer to family. At first, they thought they’d rent. “But rents in Seattle are 20 percent higher than San Diego,” Harold says, leading them to a condo purchase this spring. The walkable lifestyle is perfect for their needs. “It’s great to walk to go out for dinner, rather than drive to a restaurant. You can walk off your dinner on the way home.”

Real estate developers and agents are also responding to an ongoing trend among empty nesters with means: While they are enjoying a more carefree life in their new urban-village homes, these buyers may also be in the market for second homes to enjoy a couple times a year or more. A new property development in Hawai'i has turned its attention to this segment of empty nesters. Located on the south shore of Kaua'i on a former sugar plantation, Kukui'ula sells lots from one-third to a full acre, starting just under $1 million. Lots with cottages range in price from $2 million to $4 million. Members-only amenities include an 18-hole, Tom Weiskopf–designed golf course, a restaurant, a pool, a 6-acre farm growing fresh fruit and vegetables, and a fishing lake stocked with peacock bass. Brent Harrington, president of the company developing Kukui'ula, says sales have been picking up. Many of his buyers are the heads of families "who watched their kids grow up and scatter to the four winds," Harrington says. "They are purchasing a second home which becomes a rallying point for their families." These homes may be used only a few times a year, but the concept still pencils out for his buyers, such as Randy Lert, a retired chief portfolio strategist for Seattle-based Russell Investments. He plugged the numbers into a spreadsheet and found that Kukui'ula's program of renting out owners' cottages when they're empty (akin to the classic fractional ownership vacation properties) means the investment pays for itself. "The place is fabulous," Lert says. "It's exceeded our expectations."

Similar interest is appearing south of the border in Mexico, where activity has been picking up at Cabo's Villa la Estancia, a vacation-home complex along San Lucas Bay, very close to the shops, services and restaurants of Cabo San Lucas. The development registered a 62 percent increase in sales last year, compared to 2012, reports sales manager John Berliner. Two-thirds of the resort's buyers would be considered empty nesters, he adds, and many have used profits from last year's equity markets run-up to buy their vacation homes. But that doesn't mean they come to Cabo alone.

"The majority of our owners are couples with extended families, who choose to balance their stays with family, and by themselves," says Berliner.

The past decade's experiences lead many in the industry to welcome today's moderate growth. And the two groups that are leading it—millennials and baby boomers—hold enough clout that today's market may well represent the new normal. Among millennials, 63 percent say they expect to move in the next five years, compared to 42 percent in the entire adult population. And various surveys show that up to a third of baby boomers are interested in having a second home. "Both generations want increased amenities and lower risk," says Portland real estate agent Terrie Cox. Hopefully, by the end of 2014, the country can comfortably say the real estate market has continued its upward, healthy trend.

Joe Follansbee writes from Seattle.