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The emotional side of real estate professionals

March 13, 2008 - Appraisal & Consulting

Where can we real estate professionals put our money these days? Or more importantly, where can we get money!

The financial news is dominated by problems with credit availability. We all know about the housing crisis, which was both brought on by and continues to worsen the mortgage market. It is a vicious cycle, spiraling downward, of loans going bad, fire sales lowering housing prices, creating more bad loans and a credit crunch.

We then learned that these loans were held in funds, institutions and even our own stock portfolios. Since no one knows the extent of exposure, it causes doubt about other investments, and credit further tightens. Even the surety of bonds developed issues. Short-term bonds, which behave like money markets, have failed to attractive investors at auction. There have been more failed auctions of these types of bonds in the last two years than in the previous twenty. Why, because people cannot quantify the risk and are wary to make the investment. Fear has set in.

Other credit markets have also dried up including commercial mortgage back securities, a previous source for funding of commercial projects. This has led to some slow down in the purchase of commercial properties, and the pundits are beginning to say that prices are coming down in this market as well.

So where does one go? I was fascinated to learn that the only area of increased value, at least in the housing market, has been the island of Nantucket. With all other residential markets slipping by 20% to 30% over the last two years, Nantucket, and occasionally Martha's Vineyard, improves. It seems impossible, but when you peel it all away, the fundamentals are there: low supply of product (an island), international demand, trophy status, and well-heeled emotional buyers. Similar to bond auctions, but on the other end of the scale, no one knows where the price of the real estate actually is. In the bond auctions, no one buys because they can't really understand what the price is, and they can't adjust for the risk. In the Nantucket housing market, they don't understand what the price is, but they don't care. If they have the resources, they pay whatever it takes to buy the asset. Thus, that little island is where you still hear about people doubling asking prices for no apparent reason.

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I use this example not to suggest that everyone go buy Nantucket real estate as a hedge against all of the problems in the financial world. Rather, it's an example of the many emotions that play in the real estate market. A careful business person will analyze stocks and bonds, other credit sensitive investments, and may decide to stay on the sidelines because they cannot price the risk. Where it might be perfectly reasonable to buy small positions, despite the fact the market may be still going down, they hesitate because they don't want to lose money. On the other extreme, people throw careful analysis out the window when it comes to buying trophy properties on Nantucket. The other end of the emotional spectrum takes over. Ego, the worry that someone else may beat them out, all cause people to jump into that market if there have the wherewithal.

There is no lesson learned from these examples other than to perhaps temper one's emotional extremes. Rather it is just an observation of what we hoped were perfect markets, responding perfectly to accurate information, actually being imperfect. There is plenty of information in this internet age, but people still behave with emotion. After all, we are all human.