

Your condo, your money pit?

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Though condo values have been rising, they historically have been much more volatile than single-family home values. Worse, living in a condo can be maddeningly complex -- and costly.

Something weird is happening with condominiums across the country. They're not only gaining value, but they're appreciating faster than single-family homes.

Condo values rose more than 27% between 2000 and 2002, double the increase for regular housing. Incredibly, the median value of condos in the second quarter of 2003 (\$163,500) -- is now just slightly below that of single-family homes (\$168,400).

This is a big deal. Condos have long been the unloved stepchild of the real-estate world. Typically, they've gained value more slowly in good times and lost value more quickly in recessions than other homes.

Median values of houses vs. condos

Year	Single Family	% Changes	Condo	% Change
1990	\$ 92,000	2,8 %	\$ 85,200	- 1 %
1991	\$ 97,100	5,5 %	\$ 85,800	0,7 %
1992	\$ 99,700	2,7 %	\$ 86,000	0,2 %
1993	\$ 103,100	3,4 %	\$ 84,400	- 1,9 %
1994	\$ 197,200	4,0 %	\$ 87,200	3,3 %
1995	\$ 110,500	3,1 %	\$ 87,400	0,2 %
1996	\$ 115,800	4,8 %	\$ 90,900	4,0 %
1997	\$ 121,800	5,2 %	\$ 95,500	5,1 %
1998	\$ 128,400	5,4 %	\$ 100,600	5,3 %
1999	\$ 133,300	3,8 %	\$ 108,000	7,4 %
2000	\$ 139,000	4,3 %	\$ 111,800	3,5 %
2001	\$ 147,800	6,3 %	\$ 123,200	10,2 %
2002	\$ 158,200	7,0 %	\$ 142,200	15,4 %

Source: National Association of Realtors

Does this mean that condos suddenly have become a great value? Hardly.

Condos can make sense for some buyers, but they'll never replace single-family homes as the best way to invest your home-owning dollars. Condos simply have too many drawbacks, and too limited appeal, ever to be more than a second choice for most buyers.

Here's what is behind condos' recent run-up in value, according to National Association of Realtors Senior Economist Lawrence Yun, and why I don't think the trend will last.

Low rates brought out first-time buyers in droves

Cheap mortgage rates brought home-owning within the grasp of many renters, who happily traded up to what they could afford. The homeownership rate in the second quarter of this year -- 68% -- was the highest recorded since the Census Bureau started keeping track in 1965.

In the middle of the country, where real estate is relatively cheap and condos few and far between, first-time buyers bought single-family homes. On the coasts, where real estate is expensive, many bought what they could afford -- condos. (Perhaps not surprisingly, the homeownership rate is highest in the Midwest and lowest in the Northeast and the West.)

What interest rates giveth, though, interest rates can taketh away. Rates can't stay low forever, and every up tick from now on will exclude more potential purchasers. With fewer entry-level buyers, the market will cool for the typical condominium.

The supply of condos is expanding

A rash of construction-defect lawsuits in the 1990s drove some builders out of business and made others leery of this market. Add to that the fact that the highest condo demand is concentrated in cities like Los Angeles, New York and Boston, where buildable land is at a premium, and you have a limited market.

Condo construction is picking up, though. While building condos is still expensive and risky, the hot real-estate market is making it worth more builders' while. Combine that growing supply with cooler demand, and you'll see less appreciation in condo values in the future.

The price numbers are skewed

The fact that the median price of a condo is now a hair's breadth away from that of a single-family home doesn't mean you'll soon be able to buy a house for less than a condo in the same market.

As I've noted, most condos are located in the expensive real-estate markets along the coasts, while the single-family home data reflects prices throughout the entire country. Result: The numerical averages skew sharply upward.

The condo median is further tilted by one phenomenon that is likely to persist: luxury down-sizing.

More wealthy older folks are trading in high-end homes for equally high-end condos, economist Yu said. These upscale condos offer quiet, exclusive luxury with none of the maintenance hassles that come with owning a stand-alone house. A rising number of better-off Baby Boomers likely will continue this trend, keeping the upper end of the condo market strong.

It's harder to imagine a similar trend among middle-class Boomers, though. If the choice is between the single-family house you've lived in for years and a middle-class condo -- thin walls, questionable neighbors and all -- you'll probably stay put or opt for assisted living when the time comes.

All this leads to the crux of the condo problem: Many of them just aren't very nice. Shoddy construction did, indeed, plague the industry in the boom years of the 1980s. But even when condos are decently built, residents still have to deal with the people who live there and maintain the place. To wit:

Condo associations can be the pits

These associations typically are run by residents, not professionals. So, all kinds of nightmares can ensue. Petty personal spats can turn into fines that turn into liens or lawsuits that can even turn into seizures and auctions. Even seemingly innocuous issues can become full-fledged battles.

Here's a small sample of condo-association controversies:

- A Northern Virginia condo association has twice ordered residents to take down American flags that went up after Sept. 11. The first time, the association backed off after protests, but it renewed its demands this year saying the flags are tattered and worn.
- A Houston condo association mounted a four-year legal battle against a resident who complied with his doctor's advice to install a window-mounted air conditioner. (The complex's central AC didn't filter out the dust and mold that aggravated the resident's breathing difficulties.) The association won the first round when a judge ordered the resident to remove the unit and pay \$100,000 in legal fees and costs, but it dropped the fight when the resident won a new trial.
- A Laguna Hills, Calif., condo association is threatening to kick out any residents who don't pay their shares of an \$8.36 million special assessment to repair water and mold damage. The residents say they wouldn't be facing the \$9,000-per-unit assessments if the association had done its job and properly maintained the property.

Those shared maintenance costs, by the way, are a real bugaboo.

It's nice not to have to mow the lawn yourself and to have someone else clean the pool. But many condo associations do a poor job of keeping up with maintenance and repairs. One out of three associations, according to Association Reserves of Calabasas, Calif., doesn't have enough money in the bank to pay for needed upkeep.

And that affects your bottom line. If your fellow residents let the complex go to pot, your unit's resale value will suffer.

Your investment is in your neighbors' hands in another way, as well. If enough of them become landlords, you could have trouble selling your unit. Lenders often balk when renters make up more than a third of a condo complex's occupancy.

Condo owners in hard-hit Southern California learned about this potentially vicious cycle during the last recession in the early 1990s. As real estate values started to drop, those who couldn't sell their units for what they owed on their mortgages often decided to rent them out instead. That made it harder for those who remained and wanted to sell. The more values dropped, the more renters appeared, and the more lenders refused to offer

mortgages to potential buyers.

If you're still determined to buy a condo, take the following steps to protect yourself:

- **Read the codes and covenants.**

These outline what's allowed and what's not. Many restrictions are designed to preserve the complex's value, but you may find the lack of freedom stifling. Make sure you know what you're in for.

- **Talk to other occupants in any complex you're considering.**

A high number of renters or complaints about the condo association should be a red flag.

- **Ask about the association's operating budget and reserve fund.**

Bad signs: More than 10% of owners are late paying their condo-association fees, and more than 50% of maintenance liabilities aren't funded

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