**A Crystal Ball**

by Jane Garvey

I have been asked several times since the recent election what I expect to happen in the real estate market. Some of these questions come from other investors or industry professionals and some from curious friends and neighbors who are more than likely looking to strike up a conversation. It seems to me that this is a question worth addressing on many fronts. The answer is complicated by many factors.

Let's start off recognizing that real estate is local, very local. And real estate markets are both seasonal and cyclical. Our property values are affected by the push and pull of politics, taxes, population change, jobs, regulations, crime, neighbors, weather and many other things. Some of the things that affect our values and our rents are things we can control and other things we have no control over. We also need to recognize that change is a given. There will always be changes that affect values.

I am located in suburban Chicago. Even within this one city there are neighborhoods that are popular and others that aren't. Prices in some areas are being driven up by demand, others are holding, and others are going down. So, huge sweeping generic statements about how one factor is going to affect the real estate market are misleading at best, and about as accurate as I can be consulting a crystal ball.

What I can tell you, safely and accurately, is that you should be paying attention and prepared for change. This is one constant of investing.

Two of the biggest hits to the values in the national real estate market that I have seen have had their underpinnings in changes in national tax laws. Our tax laws provide incentives, sometimes known as loopholes. These incentivize certain actions or investments. When the incentives change, the game changes.

The "savings and loan crisis" in the late 1980's was rooted in a change in the tax laws. Prior to the Tax Reform Act of 1986, which was signed by President Reagan in October 1986, high-income earners could write off unlimited negative cash flows against other income without playing an active role in the investments. Syndicators bought up properties for long-term growth with current negative cash flow. To do this, they found partners who would pay the negative cash flow in exchange for the tax write-offs. Lenders provided loans to help them buy the properties. When the write-offs went away, the high-income partners quit paying for the negative cash flows and the loans went bad. Of course, the huge volume of foreclosed properties had a cascade effect bringing down values throughout the market. The savings and loan industry was blamed for making bad loans and regulated out of existence. As a real estate investor at the time, the root of the problem was very evident. Politicians and the press never really seemed to get, or else they didn't want to admit what happened.

The second round of legislative tinkering that had a devastating effect on the markets came about because of attempts by the Clinton and Bush II administrations to bring the rate of homeownership up so that more families could experience the American Dream. This was achieved through the mass extension of low or no down payment home loans without adequate underwriting, much of which was backed with government guarantees. A buying frenzy followed with the added demand and easy credit pushing prices up. The stated goals of increased homeownership were met, but we all know the disaster that was to follow as the slightest problem in the economy had a cascade effect. Values fell as the huge volume of foreclosures devastated the market.

The pendulum has now swung in the opposite direction. The Homeownership Rate is at the lowest it has been since they began tracking it in 1965. This is great for landlords, but it will likely shift over time.

Going from the national stage to the hyper-local stage, we often see a problem home making it nearly impossible for neighbors to sell without significantly decreasing their prices. We have also seen whole neighborhoods turned around by a few urban pioneers taking their rehabbing skills and capital into a troubled neighborhood. This sort of growth is the result of someone accepting risk and taking action rather than waiting for the tide to lift all boats.

All we know at this point is that things will change. New administrations always promise to change things. And, anytime there is change, there is increased risk. If you can position your investments in a way that minimizes your risk while still offering you the opportunity to profit on the change, you will do well. Using options to buy will offer you the potential for capitalizing on the growth without as much risk of loss. Adding some extra margin in your purchase formula for the added risk is a good idea when you expect change. Plan more than one exit strategy when you buy property. For instance, when buying properties to rehab, make sure that they would make sense as a rental as well, just in case you have to change the game plan.

In any market you can actively change your outcome by improving property. There are always at least a few buyers and renters looking. Offering your property at a price that is cheaper and better than the competition will bring them to you. You can still benefit locally, even if the market is not helping you with growth.

Most importantly, stay informed. Join your local investors association and go to the meetings. Read the articles that National REIA offers in realestateinvestingtoday.com. Watch legislation that will affect your industry at the local, state, and federal level. And, talk to your team of industry professionals - accountant, attorney, title professionals, contractors, lenders, real estate agents, etc about what they are seeing in the marketplace. Change will be noticeable first to those in the trenches, so make sure you stay connected.