



Miami Confidential

By NAR Chief Economist Lawrence Yun

Miami has a glut of homes for sale. Skylines are dotted with cranes and construction of high-rise condominiums just keeps continuing - guaranteeing an even a bigger glut. In five years, do not be surprised if home prices in Miami are 20 to 30 percent higher than the current levels.

Current homes priced at \$200,000 could sell for \$250,000; a current million dollar home for \$1.2 to \$1.3 million, in five years. If a buyer is successful in price negotiation - which can be done in the current buyer's market - the return on price purchase will be much higher.

The median home price in Miami was \$80,500 in 1985 and \$105,800 in 1995 and \$363,900 in 2005 at the peak of the market. Since then, prices have come down a bit. Prices fell by 5.7% for single-family homes and 6.0% for condos over a one-year period to the 4th quarter of 2007 according to NAR data. Prices grew 0.3% for single-family homes over the same period according to the government agency OFHEO. In some neighborhoods, the price declines are no doubt much more significant.

Even with recent price declines, home prices have grown much faster than income. Some, therefore, surmise that home prices will fall or perhaps even crash. I conjecture that this fear is the principal reason why there is excessively low sales activity in Miami. Soft sales makes months' supply ridiculously high and therefore pressures home prices to fall.

There are a few key factors not being accounted for in the simple analysis using home price in relation to income or rent. First, low interest rates, as any person with a mortgage calculator will be able to show, permit a lower monthly payment. In early 1980s, mortgage rates averaged in excess of 15%. In early 1990s, it was hovering at 10%. In 2000, the average rate was 8%. Today, a 30-year fixed rate can be locked at 5.5%.

What is more important in a home price analysis is not the home price to income measurement, but rather the mortgage obligation to income measurement, because the latter accounts for the positive impact of lower interest rates. In Miami, mortgage obligation to income is currently at about 30%, if a middle-income person was to buy a median priced home. That 30% obligation is above the historic norm for Miami, but is much lower than the 40% conditions of San Diego and San Francisco, or that of New York. (Many were shouting in the early 1990s that home prices in San Francisco were way over valued because of "out-of-whack" conditions based on simple price to income or rent ratios. In 1990, San Francisco prices were trading at near \$200,000. Today, prices are touching \$800,000)

Another factor not considered in the simple home price to income ratio is wealth accumulation. There is no reliable wealth or life time savings information at the local metro level. A financially stable retiree may have a rather low yearly income from social security checks and pension income, but that same person may have a cool million dollars or two sitting in the bank. Yet, because there is no reliable published wealth data, many analysts just use the income measure and totally ignore wealth info. Trust me, New Yorkers and other snowbirds who are moving to Florida will have a thicker bank account than others.

If Miami was a sleepy southern city as it had been considered as recently as 1990s, then home prices in Miami could be considered as being "out-of-whack." However, if Miami is transitioning itself into a major global cosmopolitan city, then a comparison should be made to markets like Honolulu and Los Angeles. Then, prices in Miami suddenly look attractive.

In five years, Miami's housing market will be doing quite fine. What are the factors that will drive the Miami market?

- U.S. Baby Boomers. This massive group of people is just turning 60 and the more financially successful ones are on the verge of retirement. Over the next 20 years, a steady flow of wealthy retirees will be flowing into sunny warm weather destinations. Ocean views will be particularly sought after and people will be willing to pay high premiums for that privilege.
- Foreign Baby Boomers. The Second World War finished at the same time for Japan and Europe as in America. Peace brought a spike in baby births. The financially successful baby boomers from abroad will demand a piece of the American Dream. It is a status symbol.
- Nouveau Rich. There is no one who likes to show off more than the people who lived through equality in income and consumption. Former communist countries like Russia and Kazakhstan are creating newly minted oil barons. Entrepreneurs are springing up en masse in Eastern European countries. Business probability says a few of them will be wildly successful. A property in London and Miami is the ultimate conspicuous consumption.
- Improving Insurance. Miami is artificially being harmed because of high property insurance rates. After the unprecedented number of destructive hurricanes (those with category 3 and higher wind speeds) in 2004 and 2005, the insurers jacked up insurance rates. I foresee some retreat in regards to insurance rates in upcoming years because insurance companies have been getting fat profits over the past two years. Profits draw new entry and competition will lower rates. Several legislative measures will further help on insurance rates. The high insurance premium, in my estimate, knocked about \$30,000 off housing values in Miami. An improvement in insurance will mean a boost to home prices.
- Improvement in Property Tax. The very high property tax on second homes that is placed on non-residents of Florida has hurt this important housing segment. A good bet is that the populace will demand of legislators some measure to alleviate this tax, which appears to hurt non-residents, and has also harmed home values of primary homeowners in the state.

As I've mentioned before, Warren Buffet's investment philosophy is to be scared when everyone is greedy and be brave when everyone is scared. The current high inventory conditions may be that perfect window of opportunity for some astute homebuyers to take advantage. Though it is difficult to call the precise bottom because of so much interplay between confidence and fear factors in today's housing market, one can be comfortable in predicting a measurably higher price prices in Miami five years from now.

I used Miami as an example. Interchanging Miami with other similar warm weather "internationally" well-known cities would follow the same logic. Flashing signs are beginning to appear in Las Vegas and San Diego as well.

This is one in a series of commentaries by the Research staff of the National Association of REALTORS®.

NAR Chief Economist Named Among Top Forecasters for Accuracy

The National Association of Realtors® Chief Economist Lawrence Yun has been named among the top 10 economic forecasters by USA Today. Yun is ranked fifth on the list and is responsible for NAR's real estate statistics and economic forecasting. The annual list recognizes accuracy in forecasting. [Read more. . .](#)