PANEL *of* EXPERTS

The Manhattanization of Seattle?

BY CYNTHIA FLASH

It's no secret that job growth is golden in the Emerald City. And it's clear to anyone who has driven through or walked around downtown Seattle that most of those workers now live in our urban core. Many are young, well-paid techies who are new to town. Most of these millennials are choosing to rent new, amenity-rich apartments so they can be close to their jobs, peers, and the after-work lifestyle they appreciate.

So what about home ownership in this hot downtown Seattle market? Developers have focused their attention on apartments citywide, which increased by 18,667 units throughout Seattle between 2011 and 2014. Meanwhile, only 1,012 new condominium units were added – meaning that just 5 percent of this new housing stock is for sale.

Recently, four experts representing a real estate brokerage and marketing firm, an appraiser and economist, a mortgage lender and a millennial consumer joined a round table discussion with the *Puget Sound Business Journal* to explore in-city housing trends. After much debate and a review of the market statistics and demographics, they agreed on what the future holds for renters, buyers and

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downtown developers.

"It's the Manhattanization of Seattle," said Dean Jones, principal and owner of Realogics Sotheby's International Realty and Realogics, Inc. "I believe we're going to have one of the most fundamentally dense markets, like New York City, Vancouver and San Francisco. We'll see inflation and appreciation across the board for land, construction costs, rents and condo values. Now consumers need to decide if they want to take an equity stake in all that or watch it from the sidelines."

> **"For consumers, prices will go up so now's a good time to buy."**
> BRIAN O'CONNOR | O'Connor Consulting Group

Jones, along with economist Brian O'Connor of O'Connor Consulting Group, mortgage banker Trevor Bennett of Caliber Home Loans, and millennial digital marketing expert Nelson Yong, concluded that current renters thinking about buying should start getting serious about it now.

Demand for condos in downtown Seattle had been relatively flat since the 2008 downturn, but it's expected to grow once new units open later this year. It's been half a decade since any new condominiums have been delivered and inventory is "like oil in an engine," said Jones. "Without it the market slows down. The in-city condo market is now rebooting because more consumers are buying in and median home prices are increasing."

Added O'Connor: "We need significant appreciation for a strong condo market but that's coming. Developers will be playing catch up given the protracted high-rise construction timelines — demand can rise much quicker than supply."

The last downtown condo boom was 2004 through 2007. Then the credit crunch pinched the development pipeline and buyers retreated amidst the Great Recession. The panel of experts say the in-city condo market fully recovered from the loss in values but prices haven't yet risen as fast as apartment rents. In King County, apartment rents climbed 35 percent since year end 2010, while citywide condo prices rose only 6 percent (higher in the urban core). That value inversion means it can actually be less expensive to own a condominium than it is to rent a similar apartment (especially after income tax deductions). So why haven't more buyers snapped up these condos?

"Most new residents are going to kick the tires downtown for a lease term or two," said Jones. "That's especially the case for young recruits working on contract. They'll want greater security before buying. Many of those apartment units are incubating our future condo buyers."

Apartment demand closely tracks job growth, which O'Connor said may have peaked in 2014, unless of course, more large corporations move in. "We're coming off a record year led by Amazon hiring and there could be another Expedia out there," said O'Connor, referring to the travel giant's announced move from Bellevue to Seattle. Commercial developers are certainly hopeful as they are building millions of square feet of speculative office space.

Although existing condo inventory is anemic, demand has been expanding. Currently there are fewer than 60 resale condos on the market in downtown Seattle and while there are 867 condos currently under construction, Jones estimated that nearly half are already pre-sold. "We see a supply and demand imbalance ahead, especially at moderate price points," he said, adding that he expects more renters to explore the favorable prices and low interest rates while they can. Then there are the discretionary buyers to add to the mix – those moving up to newer units, seeking second homes, fence sitters, students who have paid off their loans and put money into the bank, downsizing empty nesters and investors —the types who typically enter the market every time it rises.

SISTER CITIES — Downtown Seattle and downtown Bellevue operate much like two pistons in the region's high-octane engine and share surprisingly similar characteristics with their distant cousin New York City. As illustrated, their urban growth areas are defined by approximately 10-by-two miles, each featuring a central recreational amenity and a prevailing consumer preference to live, work and play in the city that encourages density. Experts suggest that Manhattan's sky-high property prices will eventually become a reality in Puget Sound's urban markets.

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> DEAN JONES | Realogics Sotheby's International Realty

With historic home ownership levels in the 60th percentile – it seems unlikely that millennials will rent forever. "If even 10 percent of these new renters decide to buy, that's going to be a significant impact on our housing stock," Jones said. "I worry about supply and affordability."

O'Connor said he also fears the cost of new construction will only rise as many labor union contracts will reset this year – five years after they corrected with the recession. The city wants to charge additional fees as well. Developers will have to charge more for new projects or defer building more condos until prices cover the added costs.

"It's a good time to buy as we're early in this condo cycle," said O'Connor, who predicts that new towers will soon need to average more than $900 per square foot to pencil out. Because of high rents and even higher demand for income property investments (evidenced by low capitalization rates), apartments have been more profitable, leaving few projects in the condo pipeline. With that lack of supply, we'll experience upward pressure up on prices.

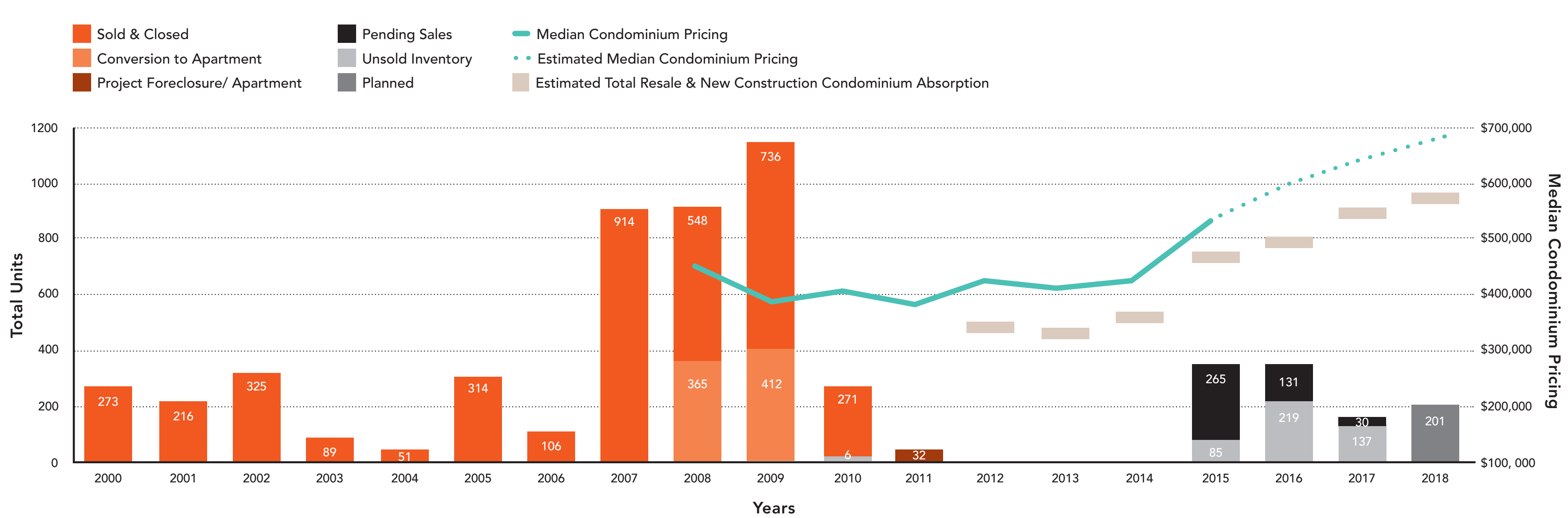
Will rent control be a residential safe harbor? Seattle city leaders have been discussing it just like San Francisco did decades ago. Most business leaders oppose government intervention. Jones said he believes the better solution is to encourage more density to create additional supply, which will slow the increases in rents. "I feel that the market should decide the price of housing," he said.

Bottom line? These experts have a strong message for those young tech workers who may be afraid to commit to a purchase: If you are secure in your job and you love Seattle, now's the time to own a piece of it. Waiting will only cost more in the future.

SALE

New Construction Condominium Deliveries & Sales Status

(Downtown Seattle Submarket - Supply & Demand Shown in Year of Unit Completion)



CONDO COMEBACK — Following a dearth of new supply after the 2008 economic recession and credit crunch, a new cycle of in-city condominiums will begin becoming available in 2015 as both homebuyer interest and median home prices rise. As illustrated, the resale market is also expected to expand significantly as new product allows move-up buyers to introduce more resale inventory to the marketplace and more renters are expected to purchase that supply. | **Graph by Realogics, Inc.**

FROM LEFT TO RIGHT — Brian O'Connor, Trevor Bennett, Dean Jones, and Nelson Yong.

Mortgage Restrictions Easing Up

Qualifying for a home loan has become much easier over the past five years – especially for first-time buyers — at the same time that consumer purchasing power may be peaking.

That's the word from Trevor Bennett, mortgage loan officer with Caliber Home Loans, the region's largest private mortgage banker. It's good news for millennials and other renters who are considering buying a home or condominium.

"Now, first-time buyers can buy restricted stock unit (RSU) income now, which is great for tech workers who receive a significant portion of their compensation that way instead of through a salary.

Buyers should not be afraid to take out mortgage insurance. Rather than put down 20 percent to avoid this insurance, they can get into a home with less down, and take the tax deductible insurance, which avoids taking out a more volatile adjustable rate second mortgage or higher interest rate fixed second

> **"Now, first-time buyers can buy a home without any contribution of their own and 100 percent of the down payment can be gifted."**
> TREVOR BENNETT | Caliber Home Loans

a home without any contribution of their own and 100 percent of the down payment can be gifted," Bennett said as one of four industry experts who met recently to discuss the region's apartment v. condo real estate market.

He's also seeing higher loan-to-value jumbo loans with as little as 5 percent down today. Lenders believe home prices are rising, making them feel more secure in making such large loans. In addition, mortgage underwriting also takes into consideration mortgage, Bennett said. He also thinks appreciation is rising much faster than most consumers can save up for larger down payments.

"I meet many first time buyers that are misinformed and we simply want to be a resource at this pivotal time in the market," said Bennett. "Buyers need to be prepared and recognize an opportunity when it surfaces. And first time buyers should remember —just get in. This isn't your final house."

www.NoPlaceLikeOwn.com

Apartment Conversion Déjà Vu?

With demand for ownership increasing, will it translate to increased conversions of rental housing to for-sale properties? It happened last cycle and it's happening again. Carbon 56, a condominium project in the Denny Triangle, sold 36 of 56 units before converting the remaining 20 units to apartment rentals in 2007 to straddle the economic downturn. Recently, those homes reverted back to condominiums and the development is now sold out, according to Realogics Sotheby's International Realty. Likewise, the firm will bring to market 26 landmark homes at Fort Lawton in Discovery Park, which had been rented and will soon be fully restored and offered for individual ownership. "We'll see fewer [apartment] conversions this round because buildings are simply worth more as income properties right now," said Brian O'Connor of O'Connor Consulting Group. "The for-sale economics simply won't win, especially considering onerous tenant relocation requirements, rising renovation costs and declarant risks. Don't count on conversions delivering a flood of entry-level housing for-sale like last cycle." I seriously doubt we will see many apartments convert to condo, the math does not work and the risks are too great.

Coming of Age - Anticipating the Millennial Market

What is it about those fence-sitting, immediate gratification, fear of commitment millennials anyway? They come to Seattle with the newest skills, are wooed by the best tech companies, and rent themselves trendy apartments in the city's urban core.

And there they wait. They wait to marry. And they wait to buy. In fact, according to a recent report in the *Puget Sound Business Journal* and *Seattle Times*, the rate of people ages 25 to 34, (those generally considered millennials), who own homes in King County is the lowest it's been since the Gold Rush era.

That's a history lesson. Some 93 percent of millennials who currently rent want to and eventually plan to own a home, Wells Fargo Home Mortgage senior vice president Carmen Bell said in a recent interview with *Mortgage Servicing News*. So it seems both consumers and industry leaders should anticipate some changes ahead. Lead-or-follow?

"Millennials are the largest and most important consumer group on our radar," said Trevor Bennett, mortgage loan officer and Kirkland branch manager with Caliber Home Loans. He is one of four industry experts who met recently to discuss the region's real estate market, which is flooded with this demographic.

Nelson Yong, a 30-year-old digital marketing expert with SILK is not only is a millennial renter, but markets to that group, and explains the mentality of his peers: "Millennials are hit by conspicuous consumption with the media. They see a snapshot of people's lives via Twitter and Instagram, which looks great, but may not be." That makes them believe they should be wealthy, but instead they come out of college with significant debt, are pressured to go to grad school, and then face rising rent or home ownership costs. A burgeoning career and a focus on lifestyle over savings will have many deferring their desire to buy a home.

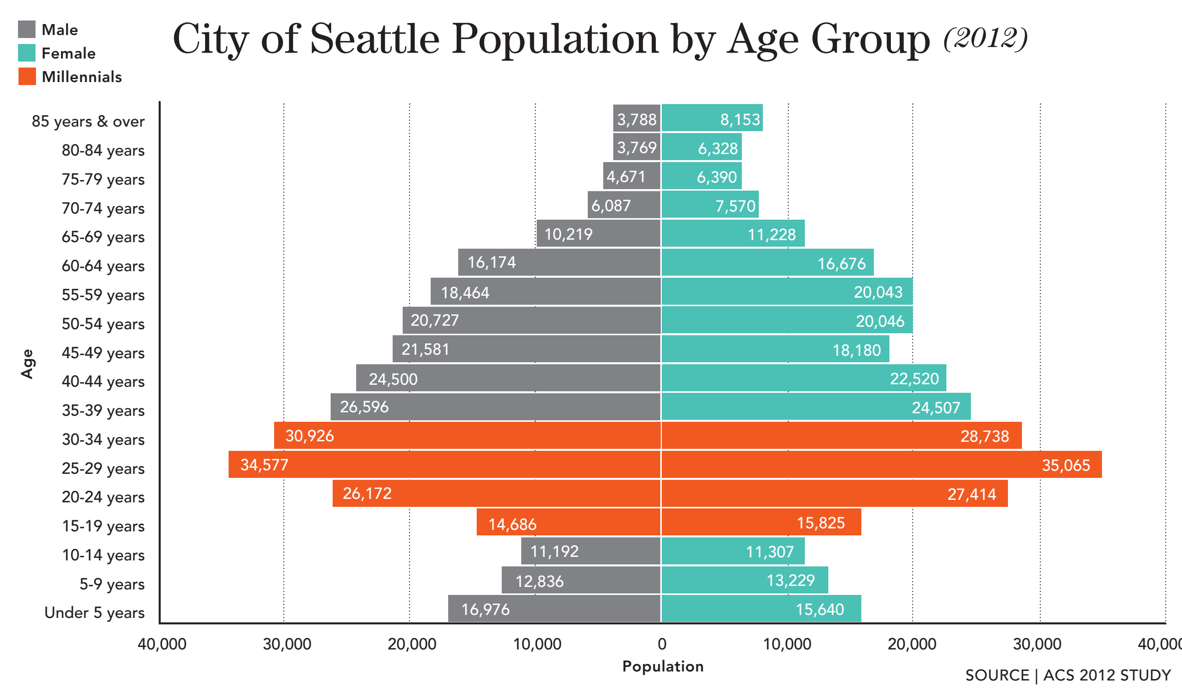
> ***"Make events experiential, factual and social — then you'll have your audience."*** NELSON YONG | SILK

Couple that with little financial literacy, fear of another economic downturn, and a propensity against commitment (the average millennial in Seattle is 25, and many won't marry until their 30s) makes them a tough demographic to sell to, let alone communicate with.

Yong, who has lived in China and the United States, suggests that millennials be taught the benefits of real estate ownership. "Bring information in consumable ways that's not scary. Show the pressure that there will be decreasing inventory – especially in Seattle," he said. "Make events experiential, factual and social – then you'll have your audience."

To Bennett, the future is clear: The longer millennials wait to buy, the longer they'll be missing out on appreciation, tax benefits and purchasing power. And he's not worried about another market correction either. "Except for some global event triggering another downturn, we have a fundamentally strong market in the region and long-term home equity has proven to be the most secure asset class."

Yong is listening and admits he's likely to buy before he competes with more of his peers. "I realize it's time for me to stop treading water and start building equity," he said. "I'm not alone."



Panel of Experts

TREVOR BENNETT

Trevor Bennett is a branch manager and loan officer for Caliber Home Loans. Trevor and his team have been assisting Puget Sound home buyers with real estate financing since 2001. His clients include many of the region's leading home builders and real estate agents. He is a board member of the New Home Council and consistently recognized as a top producer in the greater Seattle market. Trevor and his wife live in the Madison Park neighborhood of Seattle with their new baby daughter.

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DEAN JONES

Dean Jones is the recognized market strategist behind many of the Pacific Northwest's most respected real estate projects over the past 20 years. He was named "Marketing Director of the Year" in 2003 by the National Association of Home Builders and as an advisor to third-party developers and lenders his firm Realogics, Inc. drove more than $1 billion in project sales. He also owns and manages the region's global real estate brokerage Realogics Sotheby's International Realty, a top-selling office in downtown Seattle.

BRIAN O'CONNOR

Brian R. O'Connor, MAI, CRE received his MAI designation in May 1996 and is certified as a General Real Estate Appraiser for the State of Washington. He is also a State Certified General Appraiser for the State of Oregon and a Certified General Appraiser for the State of Idaho.

Brian R. O'Connor has been inducted into the membership of The Counselors of Real Estate and has been awarded the CRE designation as of November 2014.

NELSON YONG

Nelson Yong is a Seattle-based marketing and branding thought leader. He leads business development and marketing for SILK, a digital marketing agency with a focus on bridging the U.S. and Chinese markets. He has over 10 years of online and offline marketing experience managing interactive projects for small business to global brands like Microsoft, XBOX, Dell, Kodak, and Lionsgate Studios. Nelson often travels between China, Hong Kong and the U.S. while remaining heavily involved in the Seattle technology, investment and real estate communities.