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FROM THE MAGAZINE

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America's House Party

Record home prices are inflaming passions--and pocketbooks--as never before. Inside our raucous obsession with real estate

By JAMES PONIEWOZIK

John Williams, a disc jockey from Long Beach, Calif., is available for weddings and birthday parties. He also does real estate closings. Williams, 40, recently decided to hitch his fortunes to the Southern California home market, buying houses, fixing them up and--in the parlance of our times--flipping them for a quick profit. "I saw so many friends and colleagues getting rich," he says. "I wanted to get rich too."

Williams has made some money--he flipped his first two properties for a combined gain of \$27,000--and quickly discovered that he's not alone. "I went to look at some homes in Palmdale- Lancaster [an area of Los Angeles County]," he says, "and the woman showing me and a group of other investors around was a hairdresser who works for Century 21 on the side. We went into Taco Bell for lunch. The girl at the register heard us talking, and she told us she just got her mortgage broker's license."

Ah, the blistering real estate market, where dreams of big bucks come wrapped in aluminum siding, and you can get a three-bedroom ranch house with your hair extensions and a mortgage with your Grilled Stuft Burrito. The stock market may be dragging, but home prices are soaring, fueling a national obsession with real estate. Your house is now your piggy bank, ATM and 401(k). House gawking is a hobby; remodeling, both entertainment and an investment. Folks brag about having bought their home in the '90s the way they used to brag about having bought Microsoft in the '80s. Even if you're not contemplating buying or selling anytime soon, the amazing lift in home values is changing the way we think about the roofs over our heads. Real estate isn't so much about nesting today as it is about nest feathering.

The house has always reflected its occupants' place in society. But now it also determines their place in society. The boom has divided haves from have-nots-- owners from renters, hot markets from cold. The median U.S. home price jumped in April to \$206,000, up a stunning 15% over the past year and 55% over the past five years, according to the National Association of Realtors. The fact that houses are bought for pennies on the dollar magnifies the windfall. Say you put down 20% on a \$150,000 house five years ago. At the average gain of 55%, that's an \$82,500 gain on

a \$30,000 outlay, or a 275% return. In your face, S&P 500!

The biggest markets are much, much hotter. Prices of single-family homes in the Los Angeles area have gone up 135% in five years. Down the coast in San Diego, the figure is 132%. In Las Vegas, 117%. Miami, Washington, San Francisco--128%, 108%, 65%. Fortunes are being made, jealousies are being kindled and the claws are coming out--literally. In Manhattan, where the average apartment costs more than \$1 million, the housing market is so cutthroat that a real estate agent attacked a seller--who had committed the sin of not hiring a broker--at his open house.

The boom has wrought less violent changes too--most likely in your house. Maybe you're like Mike Oakley, 43, who has poured \$100,000 into redecorating his Chicago house, figuring it is already worth \$150,000 more than when he bought it. "Rather than invest in stocks," Oakley says, "invest money in your home." Or maybe you're a renter, paging longingly through listings of ever more unaffordable real estate, praying for a housing-market bust to wipe the smug smile off the face of your brother-in-law, whose house has doubled in value. Or maybe you're counting on refinancing and taking out some cash to put your kids through college. Or maybe you spend an unseemly amount of time looking at classifieds to guess how much your house is worth and surfing websites like domania.com and propertyshark.com to find out what your friends and neighbors paid for theirs. (O.K., that would be, ahem, me.)

Some economists believe that housing lifted the economy after the tech crash. And some, worried that it could take the economy right back down, warn of a bubble in home prices driven by the same psychology of greed as the tech one. Even Federal Reserve Chairman Alan Greenspan--often credited with godfathering the home boom with low interest rates--cautions about "froth" in the market, recalling the "irrational exuberance" of yesteryear.

But who wants to listen to buzz-kill talk? Just as during the 1990s' stock frenzy, the idea that "everybody's getting rich" echoes in a vast media chamber. Joining TV mega-hit Extreme Makeover: Home Edition, HGTV's Designed to Sell and A&E's Sell This House teach you how to unload your home for top dollar. Making its debut this month, TLC's Property Ladder will focus on fixing up houses--not to live in but to flip. Business and personal-finance magazines that once touted tech stocks now promise tips on how to grab land and cash in. Books like the best seller Rich Dad, Poor Dad laud real estate investing as the ticket out of the rat race.

The boom is as much an emotional story as an economic one. It's about the excitement of potential wealth, the fear of missing out and the envy toward the guy next door who bought for a third of what you paid. It's about the giddy tabulation of how many plasma TVs your house's appreciation could buy and the embarrassment of

feeling too poor for your neighborhood as houses around you are torn down for McMansions. If home is where the heart is, it is now where ever more of your cash is. And when love and money collide, things can get a little crazy.

â€¢ THE GOLD DIGGERS OF '05

You shouldn't get the impression that you can make six figures in real estate by snapping your fingers. Just ask Max Kaiser. It once took him a whole hour. The South Florida real estate investor bought a Miami-area two-bedroom luxury condo--which had not yet been built--for \$425,000 last year. After signing the purchase papers, Kaiser, 32, heard that a couple outside the developer's office was interested in the same apartment. So he sold it to them on the spot for \$525,000. "I heard it's now going for \$570,000, but what can you do?" he says. Don't cry for Kaiser. Four years ago, he was an accountant, stultified by his job. Now he's pricing Porsche Carreras.

A sizable chunk of Miami's condo buyers--as much as 70%, estimates real estate analyst Lewis Goodkin--is made up of investors itching to flip condos like scalpers wanting to unload Orange Bowl tickets. And the story is similar in other highly developed metro areas. **The biggest-paying bets in Las Vegas are being laid on the condos and hotel condos (essentially, hotel suites that you can buy) going up on the Strip. On Valentine's Day morning, Bruce Hiatt, a broker and co-owner of Luxury Realty Group, showed up at the Strip's Four Seasons Hotel with a stack of 14 signed checks. Each of his clients was determined to buy a spot in the Cosmopolitan Resort and Casino, a property that will not exist until late 2007 or 2008 and for which a shovel will not touch the earth until fall. "It's a zoo," says Hiatt. "Buildable land here is running out. We have only one place to go, and that's up." By March 1, the tiniest of the hypothetical condos had risen in price \$100,000 to \$150,000.**

Zealous new investors going into a hot field, chasing market momentum and betting huge sums on the belief that this may be a new era: it sounds disquietingly like the late-'90s day traders who went the way of the [Pets.com](#) sock puppet. Does the parallel bother Keith Weaver, who is contemplating ditching his job as General Mills operations manager for the real estate biz? Nah. "We might be riding that wave," he says. "But the wave is there. So I'm going to get on it." Weaver's plan is to ride south, into the Florida market. Max Kaiser, make room.

â€¢ HOUSE RICH OR HOUSE POOR?

Of course, you don't need a portfolio of condos to have made a pile. Average homeowners who bought in the '90s--not to mention those who have owned for decades--are now, like modern-day Clampetts, sitting atop newly discovered gushers of wealth. Many have borrowed against their fat cushions of equity. Some--like

bettors taking chips off a blackjack table--have sold, trading down to smaller places or swapping a city apartment for a calmer, cheaper life in the country. Still others have stayed put and splurged. Lucky Erganian and her husband, now deceased, bought their Woodland Hills, Calif., home in 1982 for \$260,000. Today she's in the midst of a six-figure renovation. Real estate agents daily slip flyers onto her porch boasting of the windfalls they have won for her neighbors. "The one I have now," says Erganian, 58, "lists three that sold for \$1.2 million, \$1.3 million and \$3.9 million. I love to go look at [the houses] and say, 'They don't have this that my house has, and they don't have that that my house has.'"

Others eyeball the neighbors more wistfully. Lottie Kovarek, 86, could sell her Chicago house for dozens of times the \$10,500 she and her late husband paid in 1952. But as homes she has known for decades are being razed to build million-dollar-plus yuppie warrens, her street--once home to working-class Polish-American families--is losing its tight-knit character. But at least Kovarek owns her home. Writer Michael Glynn, 49, his wife and two kids rent an 850-sq.-ft. apartment in Santa Monica, Calif. There is barely enough space to shoehorn a tree in at Christmas, and Glynn's office doubles as his daughter's bedroom. Glynn and his wife considered buying a house when they married in 1994, but, he says, "I thought houses were overvalued." Now they can't afford their neighborhood, even though their income has grown considerably. So he and his wife are looking--in Oregon and Washington. "I kick myself when I think of places I saw" in the mid-'90s, Glynn says.

Past generations thought of their house as an investment, but a passive one. Burning the mortgage after 30 years promised a debt-free retirement and a little legacy for the next generation. But now people track their home values almost daily. And thanks to home-equity loans and refinancings, the home is an easily tapped source of cash. In 2004, U.S. homeowners took an estimated \$139 billion out of the walls and floorboards through refinancings, compared with \$26 billion in 2000, according to Freddie Mac. They put about 35% of that money into home improvements, spent 16% on consumer purchases, and used 26% to pay off debt (including credit cards for other consumer purchases), according to the Federal Reserve Board.

Of course, that's not free money. It's more debt, albeit at low interest. But you have to excuse homeowners for getting a little giddy. When they look at the rest of the economy, they see little else to be excited about. Employment has picked up, but wages haven't. Inflation has risen from the grave. The stock market is crawling to get back to where it was five years ago. Savings accounts throw off barely enough interest to feed a parking meter. Companies are cutting pensions, and politicians are making dire noises about Social Security. It's a scary message people are getting: We are heading toward a future in which we will need more money than ever to avert disaster, and there are fewer opportunities to get it. So people see their homes as their last, best hope for prosperity--as not just houses but also lifeboats.

FROM HOME TO PIGGY BANK

When people feel rich, they spend--whether their wealth is actual or merely on paper. We saw that phenomenon at work during the stock run-up of the '90s. It's called the wealth effect, and it's even more potent with housing. Over the past three years, the wealth effect from rising home values accounted for a third of all growth in consumer spending, according to Eric Belsky, executive director of the Joint Center for Housing Studies at Harvard University. He says consumer spending was single-handedly responsible for keeping us out of recession for two years.

Home-improvement retailers like Home Depot and Lowe's have particularly benefited. If the housing market is a gold rush, they're selling pickaxes. Greg Bridgeford, executive vice president of business development at Lowe's, says his outfit has been able to sell not just more items but also pricier ones: "In something as mundane as gas grills, our average price was \$149. We started bringing in some very, very high-quality grills that priced from \$497 to \$697 to \$997." Says Home Depot's John Costello, executive vice president of merchandising and marketing: "America's love affair with their homes has had a dramatic impact on our success."

As it has generally on the economy. "When people's house value increases," says Belsky, "they feel freer to spend from the wealth they have. You may decide to buy a bigger car, to eat out more at restaurants." And, he adds, people spend those hypothetical riches faster when their houses go up in value than when their stocks do because they believe housing gains are more stable. But that's all well and good, because housing gains are more stable, right? Ahem, right?

â€¢ TROUBLE ON THE HOME FRONT?

This is the \$64 billion question of the 21st century's first boom: Are today's real estate revelers partying like it's 1999--just before the stock-market bubble burst? To Edward Leamer, economist and director of the UCLA Anderson Forecast, the housing market, especially in hot coastal areas, is a bubble just as ripe for popping. "We've had a more than doubling of housing prices in the past three years here in Southern California, for instance, and there's no fundamental driving it," he says. "There isn't some big crush of people coming to California. That's ridiculous."

Instead, say Leamer and other bubbleologists, what's driving the market is low interest rates, herd psychology, speculation and the expectation of unending price increases. (One study found that Los Angeles homeowners expect their home values to grow 22% every year for a decade.) Meanwhile, promiscuous lenders are throwing money at buyers like beads during Mardi Gras. "Anybody who can crawl in off the

street can get a loan with 0% down at three or four times their income," Leamer says.

It's tempting to call real estate NASDAQ 2.0, but there are key differences. David Lereah, chief economist for the National Association of Realtors, predicts another record year for real estate in 2005, with a 9% jump in prices nationwide. Lereah says the run-up in house prices is not built on the kind of hot air that promised that theglobe.com would be the next General Electric. Rather, he says, it is based on fundamentals that include tight housing supply--especially in places where it is tough or expensive to build, like New York City and San Francisco--such population factors as immigration, foreign buyers (snapping up properties cheap because of a weak dollar) and baby boomers' demand for second homes. "It's the demographics, stupid," he says.

Stocks, he adds, are more readily sold and thus more volatile. "Stocks are pieces of paper," Lereah says. "People can get in and out very quickly. Real estate is different. It's tangible. It's secure. So even if the price of the home next door may go down, it doesn't always mean yours will go down too. It doesn't mean you're going to sell. You're not going to react the way IBM's shares would react if there's a big sell-off."

But there are troubling aspects to the real estate boom. At the stock market's peak, 1% of investors controlled about 33.5% of stock wealth; the top 1% of home-equity holders have only 13% of housing wealth. In other words, a broad drop in home values, should it happen, would affect a far larger cross section of Americans than did the NASDAQ bust.

Complicating that danger, home buyers have turned to some risky strategies to afford their purchases. Nothing-down, interest-only and "negative amortization" (in which you wind up paying so little each month that your loan amount grows larger, though hopefully your house's value rises faster) mortgages are on the rise. Such loans can pay off--if you sell within a few years at a profit. But if interest rates rise and home values stall or--gasp!fall, those borrowers may become overwhelmed by steadily rising payments. (Household monthly debt costs are already at an all-time high.) Even the bullish Lereah is concerned about the loose lending practices. Such trouble would have repercussions for the whole economy. If enough homeowners become swamped by their debts and have to sell, prices would drop, creating a reverse wealth effect and fueling a slowdown.

California's \$186 billion state pension fund is worried enough to have begun unloading some of its real estate holdings. Phyllis Rockower, who started the Real Estate Investor's Club of Los Angeles in 1996, is worried too. Membership in her club has soared. "Most people who come to my meetings sold their high-tech stocks after 2000," she says. "We had to move to a bigger room. It's either a sign of the times or a

market top." What's her bet? Rockower has six houses on the market--nearly every investment property she owns.

AFTER THE PARTY'S OVER

Whether the market rises, plummets or flattens, whether it happens over one year or five, it will not undo changes that the boom has wrought in the relationship between homeowner and home. The tech crash and the market slump didn't erase the culture of stocks. Even after day-trading mania disappeared, there remained a broad class of people buying stocks and mutual funds who were more knowledgeable than they used to be about the market and more closely attuned to business news.

Likewise, the deeper changes of the real estate boom are likely to stick, particularly the notion that the house is no longer just a home. By tapping their built-up home profits through refinancings and home-equity loans, owners have ensured that the home-as-piggy-bank will be with us for some time, and that may have wide implications for tomorrow's economy.

The American home now occupies a place somewhere between the humble family hearth of old and the cold numbers in our bank and broker statements. It is like a family gem, to be displayed, enjoyed for itself and continually polished and cared for--but one that you might just hock or sell off to pursue gaudier baubles. It is a statement of aesthetics and values and financial acumen. "It is a way to express your good taste," says Atlanta Realtor Heather Steiner, "and to show how much smarter you were than your peers."

It can be hard to remember that a house, boom or bust, remains the place where you kick off your shoes at the end of the day. Carol Connelly, 53, and husband Mike, 52, live in a 4,000-sq.-ft. house in the small central Michigan town of Gobles. The Connellys used to live in Chicago, where they sold their Lincoln Park house for \$450,000--having paid \$208,000--giving them enough money to buy their place in Gobles outright, leave their high-pay, high-pressure jobs and spend more time with their kids, now 14 and 18.

Yet that was in 1996, before the boom. A coldhearted investor could say the Connellys, for all their success, screwed up. Little Gobles is not exactly the white-hot center of the real estate inferno. If they had continued trading up for nine years--buy, fix, sell, buy, fix, sell--there's no telling how much profit they could have made. (Their Chicago house, they say, would now sell for more than \$750,000.) And if they had plowed that profit into a second investment property ... and a third ...

But today, ensconced on a forested lot overlooking a private lake and running a free-

lance asset-management business from her basement, Carol Connelly has no regrets. "We did things at the right time, and now we have the life we wanted," she says. Besides, she adds, "my kids would kill me if we ever sold this house."

It happens like that sometimes. You make an investment, and along the way, it ends up turning into a home. --Reported by Sonja Steptoe and Jeffrey Ressler/Los Angeles, Anne Berryman and Amy Bonesteel/Atlanta, Jeanne DeQuine/Miami, Eric Ferkenhoff and Leslie Whitaker/Chicago, Wendy Grossman/ Houston and Barbara Kiviat and Coco Masters/New York

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BY THE NUMBERS

HOT AND NOT-SO-HOT MARKETS

Where house prices have gone up most

% change over

five years one year

District of Columbia 108.1% 22.2%

California 103.0% 25.4%

Rhode Island 97.6% 17.1%

Nevada 84.7% 31.2%

Hawaii 82.9% 24.4%

Florida 80.5% 21.4%

Maryland 77.9% 21.0%

New Jersey 76.5% 15.8%

New Hampshire 72.3% 12.1%

Massachusetts 71.8% 11.6%

U.S. 50.5% 12.5%

Where prices have lagged

Utah 17.5% 6.3%

Indiana 19.9% 4.1%

Nebraska 21.8% 5.4%

Mississippi 21.8% 4.9%

Tennessee 22.4% 5.5%

Source: Office of Federal Housing Enterprise Oversight

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