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April 1, 2013

Investors and Foreigners Pushing the Recovery

I read a piece from Dr. Housing Bubble, and it helped to bring some clarity to the unfolding housing recovery story. Interestingly, the number of houses exiting the available-for-sale inventory exceeds the number of loan origination, which implies an increase of cash transactions. Who is buying the houses for cash? Investors, foreigners and even banks, since they are now allowed to collect rent on the houses. If these investors can collect $2,000/month in rent, then an 8% yield would imply a home market price of $300,000. So, all these investors are fetching for these houses right now, while home prices are low, on the cusp of a ramp up, as we have seen across the 20 metro cities in the Schiller Index over the past 12 months.

This could bring down rental prices while depleting the inventory which is already low, as more of these owner occupied homes become rental properties. Once the investors hold for about 5 years and recoup their investment, while earning a healthy yield, housing prices may collapse again, should they all run for the exit.

We mentioned earlier how large asset management firms are creating REITs where they collect rent from the single-family residential properties. They have been buying thousands of properties, which is a contributor to the upward price movement, that was never a factor during the 20 year bull cycle leading up to 2006, as that was more of a frenzy amongst retail investors and first time home owners.

So the commonly quoted metrics, which imply we are in a recovery, such as Schiller Index, is seriously skewed by 1) institutional investor involvement, 2) QE money, 3) shadow inventory. Said simply, the market is ripe for institutional investors, not retail. We are still uneasy over the housing recovery as it doesn't seem to be supported by a healthy fundamental. Retail investors and individual homebuyers may fall prey to a trap set by the smart money.