

If Homes are Like Stocks, Maybe the Risks are Too

Wayne Faulkner, Real Estate editor

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Investing in real estate is all the rage. And, if you think it's just those with \$1 million lying around who are buying property to rent out or to use for vacations or retirement, figures from the National Association of Realtors might surprise you. The typical vacation-home buyer is 55 years old and earned \$71,000 in 2003 while investment property buyers had a median age of 47 and earned \$85,700. That's according to a study by the Realtors reported last week by the Tribune's Mary Umberger and detailed in her column on the cover of Real Estate today. Most importantly, it said that nearly one-third of all home sales transactions in 2004 were by investors or by second-home buyers.

So, if you have savings, or even lots of home equity, how much should you invest in real estate? Is there some percentage of your investment portfolio that should go to buying housing? "What I'm used to seeing is that a home for an average individual is frequently 30 to 50 percent of their investment," says Diane Maloney, a certified financial planner with Beacon Financial Planning Services Ltd., in Plainfield. But the home is a relatively larger portion of total investments for those who have less expensive homes, she says. "We have had more clients who were saying: 'What would you think if I picked up a piece of rental real estate or commercial property?'" Maloney says. But money isn't the only issue, she says. "A lot of people don't want to be bothered with a renter."

Cindy Menker, a financial planner with Contour Financial in Orland Park, takes a different view: "We don't really view your residence or a second home as an investment property" because of the costs involved -- the mortgage, taxes, etc. Above and beyond a principal and second residence, Menker would suggest that 5 to 10 percent of a portfolio be in real estate mutual funds "depending on the type of investor." But the rule of thumb for monthly outlay for all real estate owned outright is still 28 percent of gross income, she says. That means that the mortgage, taxes and insurance on a first and/or second home should not exceed 28 percent of gross monthly income.

"When you're younger, a home is a huge asset relative to your portfolio," says Armond Dinverno, co-president of Balasa Dinverno & Foltz LLC in Itasca. "When they get older, it gets smaller. "When you get older you don't want to be real estate-rich and cash-poor." "People generally buy a second home in a warm climate, then it becomes a valuable investment. It starts out as a personal preference, and then it's a good value." It's been his experience that "people who have a lot of real estate, they just like owning real estate. They are comfortable as an investor owning hard assets like property."

Menker acknowledges the popularity of real estate. "People are going into third homes" now, she says. "My only concern is that [real estate] might be like Internet stocks," which saw huge appreciation in the 1990s before the bubble burst in 2001. The Realtors' chief economist, David Lereah, says the real estate market has become more like the stock market, more liquid and available to more people.

But Dinverno doesn't see that the real estate market has changed fundamentally. Boom and bust cycles will continue, he says. "Properties on the coasts are appreciating at great rates, but somebody's going to end up holding the property and taking the loss on it. Appreciation doesn't continue forever in any marketplace." Think of it this way: While homes may have become more liquid, you can't unload \$500,000 worth of real estate while you're on the phone with a broker like you can stocks. Perhaps, if we think of trading houses like stocks we should remember the phrase in every stock or mutual-fund prospectus: "Past performance is no guarantee of future returns."