

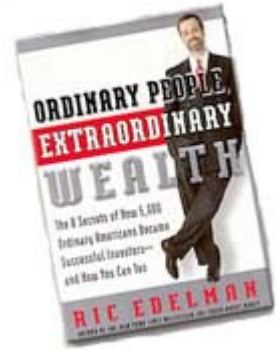
Forget About Buying a Condo

By Ric Edelman From *The Truth About Money*.

Thinking about buying a new home, or investing in real estate? Forget about buying a condominium, and if you already own one, you have my condolences.

Most condos are small, and their tiny size allows for very low prices, which makes them attractive to college graduates, newlyweds, and others just starting out in life.

It's a very attractive sales pitch - builders require very small down payments, and after factoring in the tax deduction, the mortgage is often as low as a rent payment. So (as you can read in every newspaper's weekend real estate section), why rent when you can own your own home? This is a tremendous tug on your desire to live The American Dream.



But that dream can turn into a nightmare.

First, consider the condo association fee. As the owner of one of the building's units, you're required to pay this fee, which covers the building's common areas and grounds. But unlike a mortgage, you never pay it off! (So much for the dream of owning your home with no payments.)

Second, the association fee is guaranteed to rise over time - simply due to inflation. Worse, many of those "common areas" are expensive to maintain, such as elevators, swimming pools and heating systems. As any long-time condo owner can attest, condo fees can rise dramatically. Thus, your condo fee actually can be more than your mortgage payment - and guess what: It's not tax-deductible!

Third, many condo buyers are first-time buyers, and they fully expect to "move up," perhaps after marrying and having kids. If that describes you, you're in for a big surprise: When you're ready to move, you probably won't be able to sell the condo for what you paid (and you almost certainly can forget about selling for more than you paid, despite promises from the builder or real estate agent). Why will the condo fall in price?

Because condo builders are continuing to build - so why should a prospective buyer choose your (old) condo in an even older building instead of a brand new condo in a brand new building? To find a buyer, you'll have to lower your price.

Even if new condos do not pose much of a competitive threat, two other problems do. For one, only Generation Xers, divorcees and retirees, are potential buyers (because of their often limited income). Therefore, unless there's dramatic salary growth among these demographic groups, your property cannot grow in value, or it'll exceed their ability to buy. After all, those who can afford to buy a town house or single family home almost certainly will (just like you would if you could afford to).

The second threat to your condo's value is, simply, all the other condo owners. Check out any building, and look at all the condos for sale or rent. With so many from which to choose, why would a buyer select yours? Since the floor plans are all identical, the only way to attract a buyer is to lower the price. This makes it hard for condos to maintain their value.

And it gets worse. For a buyer to qualify for a mortgage, your condo must be appraised. Since all the units are the same, the appraiser will simply compare your unit to other recent sales in the building. Say another tenant needs to sell in a hurry and therefore sells his condo for \$15,000 less than what he paid. Guess what? This "comparable" will serve as the basis for the appraisal - and it could serve as the new pricing standard for the building, to the consternation of the other owners in the building.

Have you ever noticed that a lot of condo units in a given building are available for rent? Ask around, and you'll discover that many (even most) of the owners used to live there themselves - until they wanted to "move up" as you'll want to do. Why are they renting? Because they couldn't find a buyer, yet they needed to move and couldn't afford to let the condo sit vacant. Thus, they've become landlords, which leads us to the next problem

If you plan to rent your condo, beware of several things. For one, you'll be competing with the builder. To beat him, you must give the renter a better deal (after taxes) than the builder is offering. This means you probably will find yourself receiving less in rental income than what you spend on the mortgage and association fee. I'm assuming that you do indeed find a tenant - I won't even talk about the costs you'll incur by renting to The Tenant From Hell. You know him. He's the guy who fails to pay the rent or who trashes the place - or both. When your tenant moves out, you'll spend several months finding a replacement - with you paying the mortgage and condo fee in the meantime.

Having many investors and former owners trying to rent their condo units leads to another problem: You might not be able to sell your condo - even if you have a buyer! This is because most mortgage lenders will reject your buyer's application unless two-thirds of the building is owner-occupied. You see, lenders realize that renter-filled buildings usually are not maintained as well as buildings whose owners live in them. When a building isn't maintained well, it falls into disrepair. Tenants begin to move out faster than new tenants move in, and property values fall - placing the lender's loan at risk. (In the worst cases, the buildings become slums, and many well-intentioned investors and owners find that they've become slumlords. If you think this can't happen to your building, think about it: Nobody ever builds a slum.)

Therefore, if you were planning to buy a condo, STOP. DON'T DO IT.

If you're looking for a real estate investment, look elsewhere. If you're looking for a place to live, rent the condo instead (because, as a renter, you can walk away anytime). And never buy a home that you aren't willing to own or live in for a long, long time.

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