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Market Report: Pricing Premiums

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Although sales of newly built condos have fallen sharply throughout Southern California, the fact that builders adjusted prices quickly after the market peaked, postponed new projects or converted them into rentals has actually meant some small increases in median asking prices for the year ending November 2007 (the latest data available). In some counties, such as Los Angeles and Orange, median asking prices for new condos rose by over 30 percent, although that's likely due to the relatively low volume of sales skewed towards higher-priced urban infill communities or mid- to high-rise units.

For existing condos, closed sales during December 2007 in various regional counties were 25 to 50 percent below levels of last year. Although median condo prices remain below the conforming loan limit of $417,000, a combination of tightened lending requirements, higher down payments, a market segment more prone to troublesome subprime loans—and, thus, potential foreclosures—plus newly competitive detached home prices continue to exert downward pricing pressure in Southern California.

And, while some urban infill areas such as downtown Los Angeles and Long Beach remain popular, the softening market has forced several developers in these areas to postpone the construction of mid- and high-rise multifamily projects—including, most recently, work at the $3-billion Grand Avenue project—until sales rebound, credit loosens up and building costs decline to allow for healthier profit margins.

In the rental market, the high cost of buying homes continues to keep vacancy rates in low single digits for Los Angeles, Orange County and San Diego but slightly higher in the Inland Empire, which saw its own apartment boom over the past few years and now must contend with excess inventory.

Rental supply of all types is also expected to increase in Southern California as long-time homeowners, speculators and even owners of foreclosed properties choose to lease out unsold homes rather than sell at a steep discount, putting pricing pressure on existing apartment communities.

Consequently, according to Marcus & Millichap, rents in the region are projected to rise by 3 to 5 percent in 2008 while vacancy rates skew upwards to 3.7 percent in Los Angeles, 3.5 percent in Orange County and a potentially troublesome 6.6 percent in the Inland Empire. But in a revitalizing downtown LA, rentals continue to demand a pricing premium of over 30 percent versus the overall county.

Managing Principal Patrick S. Duffy consulted for nearly 20 years on various projects across the U.S. before launching MetroIntelligence (www.metrointel.com) in 2007.