

The Affordable Mortgage Depression

Government policies were designed to increase homeownership. Affordable Mortgages, created to realize this goal, were responsible for the Housing Bubble and distorted the economy. The unwinding of these distortions will result in a Global Depression.

Doomsday Scenarios: Could Condo Prices Fall to Zero?

Why not? Certainly condo prices aren't going to approach \$0 in most markets or on a national basis. But given the right set of local conditions, it is entirely possible that some condo prices could fall to a nominal value functionally equivalent to nothing.

Free condos huh? Does it sound too good to be true? That's because it is. Costless condo purchases would be far from free, which is exactly what creates the possibility that prices could fall so low.

The first myth of homeownership in the United States is that you actually "own" your house or condo. U.S. homeowners have residual rights to their properties as long as the more senior claimants receive their recurring pound of flesh.

This concept is an obvious one for mortgage holders. "Owners" borrow a sum of money from a lender and are allowed to continue to "own" their property as long as the mortgage debt is serviced and repaid according to the terms of the borrowing agreement. We presently see large numbers of people losing houses that they supposedly "owned" because they can't pay their mortgages. The question is why these people with little, no or negative equity actually believed that they "owned" the houses in which they lived?

Now let's assume that a homeowner paid off his mortgage or bought his house with cash. That homeowner would truly "own" his house right? True, except that most houses are subject to property taxes. In such markets, homeowners supposedly own their houses, yet are required to cut a check to the government for the right to stay in it. And unlike a mortgage payment, this is a perpetual liability. Even worse, fickle governments can decide to increase your perpetual homeowner liability at their leisure. (As an aside, how safe is the residual equity value of your home if a government can raise taxes to a confiscatory level at their discretion?)

One of many disadvantages that condo owners have to home owners is that they are also junior in ownership rights to their condo owner associations. Condo owners must pay monthly dues for maintenance, insurance, security, etc... These fees are perpetual and contractually required.

If you don't believe that condo owners have only residual equity rights and are fourth in line in terms of seniority, imagine what would happen if such an individual decided not to pay their mortgage, condo association fees or property taxes? How long would this owner continue to have a legal claim to the property? Not long.

How do you actually own something that can be legally taken away from you if you don't perpetually pay for the right to keep it? In reality, homeowners more closely resemble serfs beholdng to the government, condo associations and lenders who will kick them off of their land if sufficient tribute is not paid.

Additionally, houses generally have a price floor relative to condo values for a variety of reasons. Houses tend to be more heterogeneous than condos. Homeowners have exclusive property rights to their land and thus the opportunity to use the house or land for alternative purposes. A house is a single ownership unit, so if an owner wanted to sell the property to a developer or develop it himself, the process would be relatively simple.

A condo owner has rights only to a few hundred or thousand square feet of space within a building. Condo ownership doesn't come with any claim to land, and all control of the remaining facilities are owned and controlled by the condo association. It is for this reason that, until the Housing Bubble began, condos always traded at relative discounts to equivalent houses.

This brings us to the question at hand. Could condo prices fall to zero? Given the right conditions such

values could indeed fall to nothing. This does not mean that the condos would be free. Owning a condo comes with the laundry list of financial obligations and liabilities which we discussed above.

Imagine a condo with \$1,000 a month in condo fees and \$6,000 in annual property taxes? (these are hypothetical numbers designed to illustrate a point) If you were to purchase such a condo for \$1, ownership of the unit would still be costly. The free unit would cost \$1,500 a month.

Now what happens in markets with the following conditions that may come to exist in places like Miami:

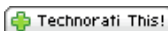
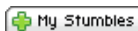
- The supply of condo units dramatically outstrips demand
- A large backlog of units for sale exists
- Credit terms are tight or relatively expensive
- Property values have been falling for years, are presently falling and are expected to continue to fall

In such a market, what would happen if the cost of renting an equivalent unit falls below the \$1,500 a month necessary to service condo ownership expenses? What if real estate prices are expected to continue to fall, people refuse to buy assets or borrow money due to rampant price deflation, or unemployment rises so high that there are insufficient potential buyers to assume ownership of all for sale units? Why would anyone pay for the right to purchase a condo only to be required to pay monthly taxes/maintenance expenses in excess of what it would cost to rent the same unit across the hall?

With this framework of understanding, it becomes hypothetically possible that condo prices could actually fall to less than zero. Negative real estate prices!

A potential buyer may decide that perpetually paying condo fees and taxes that are in excess of the market price of comparable rental units isn't a good idea. Theoretically an owner might be willing to pay a potential "buyer" to take a condo off his hands simply to remove the perpetual liabilities attached to the unit. In such a case, the buyer would require compensation to assume the perpetual liabilities.

This is obviously a highly theoretical potentiality. I am not arguing that it is likely. Furthermore, there are numerous factors, such as the availability of distressed asset investors, which would likely put a floor on condo prices above \$0. But if the economy gets bad enough, house prices continue to collapse, deflation becomes prevalent, unemployment expands and financing for investors dries up, the potential for condo prices to fall to previously unimaginable lows will materialize.



Posted by Whitney Ross at [3/16/2009 2:10 PM](#)

Categories: [Doomsday Scenarios](#)

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[Tran Harry](#) wrote:

[3/20/2009 2:47 AM](#)

That analysis of the \$1,500 a month payment is very eye opening. I know of condo, as well as hoa, fees and of course property taxes. But to see it in writing makes it much more apparent.

\$6,000 in property tax and a monthly condo fee would definitely mean that you are essentially paying to rent forever for a condo which you technically own.

[Reply to this](#)

David wrote:

[4/12/2009 9:00 PM](#)

Nice analysis. Of course, the ostrich mentality that defined that last 10 years of real estate certainly extended to condo associations that often spend like drunken sailors, suffer from cronyism and kickbacks and worse. There are efforts to strength the rights of condo (and HOA) associations to make claims against property owners - Instead, I suggest that owners should have expanded rights to demand transparency and economic efficiency from condo associations.

What happens when the condo association goes bankrupt? It seems likely to me we will see widespread failures of condo associations given the foreclosure/vacancy rates and excessive condo fees prevalent in the boom towns.

Will the condo units lose their occupancy permits?

Will the last remaining owner(s) be held responsible for all the condo costs?

If those costs are passed on to the remaining owners, the exposure to the collective financial liability could drive condo prices far below zero.

[Reply to this](#)

Soeren wrote:

[4/14/2009 3:40 AM](#)

IMO, if you're going to BUY and intend to OWN a home, stay away from Condos, Co-ops, Townhouses, gated communities or anything with a HOA or POA, as the fees and common charges are like paying rent in perpetuity, tend to *increase* over time, may increase dramatically if and when a condo complex starts becoming depopulated and, while on the verge of bankruptcy, fewer and fewer solvent residents remain to pay the maintenance fees, upkeep, taxes and water bills that must still be paid for the entire complex, whether a unit is vacant/abandoned or not.

IMO, these types of properties are not a good investment, and are an easy target to pick on, when trying to imply that renting is better than owning, for the simple reason that renting, in many cases, IS better than owning a condo, co-op, townhouse, ect. Heck, I'm as anti-renting as they come, but even *I* would rent a condo, co-op or Townhouse before I'd EVER buy one.

Could condo prices fall to zero? I would say, yes. IMO, owning these types of properties represents a running and perpetual liability - quite similar in principal to buying a mobile home that's located in a MH park - you may very well

own the MH free and clear, but due to it being in a park, you're obligated to pay lot rent (and possibly water hookup, trash/lawn mowing fees as well), whether you live in it or not, and much like the condo scenario, I can easily envision a situation arising where, due

to circumstances, an owner may want or need to get out of that situation ASAP, and with the market being the way it is,

I can easily imagine a condo owner needing to relocate, be unable to sell and thus, willing to give the condo away for free to anyone willing to sign on the dotted line relieving the seller

of, and officially taking over responsibility for, all the fees, common charges, and property taxes, so that the seller can get on with the next phase of his life, free of those obligations.

Heck, you can BUY a *house* NOW, for \$50 and up in the Detroit area, because the banks know, and are pragmatic enough to realize that they're better off taking a \$10k or \$20k loss and getting rid of the property, than being stuck paying property taxes on it, potentially for years, with the value of the property only going down as it deteriorates.

That same pragmatism and rationality will surely see free condos up for grabs. Heck, if things get bad enough,

I can see "sellers" offering incentives

for "buyers" to take their condos off their hands for free - free closing costs, perhaps.

[Reply to this](#)

Eric wrote:

[4/14/2009 11:27 AM](#)

Re: your comment on Mobile Homes -- I have a friend who just paid \$6000 cash for a very nice mobile home in a pleasant, clean and quiet mobile home park. I was shocked such a deal existed. But, even though she owns the mobile home outright, there will always be the lot rent, the yearly state tax, and insurance. So, minus upkeep, she pays \$575/mo and that amount will probably eventually go up.

[Reply to this](#)

Soeren wrote:

[4/14/2009 3:32 PM](#)

I bought a MH on it's own land last year in a very nice little town in upstate SC - average home price in this town at the time was \$175k - for slightly over \$6k, including closing costs, title insurance et al, and my "rent"(Property taxes) are about \$150 a year for both the MH and the land, or about \$13 a month. I would NEVER buy a MH in a park because you are no closer to home ownership than you were renting an apt. I am on a foreclosure mailing list, and a 1993 double-wide on it's own land in the same general area just came in the other day - a 4 bdrm, 2 bath home that sold for \$58k in 2008, is now up for the taking at \$9900, land included.

<http://www.emailforeclosures.com/searchresults.cgi?caller=details&idnum=762724>

IMHO, as the market continues to dive, and better and better homes become available for less and less money, only a fool would continue to pay rent - but that's just my opinion.

[Reply to this](#)

Glenn Peters wrote:

[4/14/2009 4:45 AM](#)

Taxes for municipal services and maintenance costs are fair enough if you want society to collectively pay for such services. If you rent, you 'pay' for these services anyway.

The true cost of ownership of a fully paid property is the total of these costs per annum' there's no 'serfdom' aspect to it at all.

[Reply to this](#)

Whitney Ross wrote:

[4/14/2009 7:56 AM](#)

Well said. Obviously necessary government services need to be paid for and it is up to each society to decide how to fund them.

I do challenge the notion that by definition "if you rent you pay for these services anyway".

Insanely, there are "owners" of investment properties who receive rent insufficient or barely sufficient to offset their maintenance, insurance and tax costs. This is particularly prevalent in Florida where insurance costs and taxes have risen dramatically. These people either counted on capital gains to make their investment worthwhile or have been caught by declining rental rates or unexpectedly rising costs. As property values fall and rental receipts continue to decrease, this phenomenon is likely to proliferate.

New Condo owners are another example. Rental rates in overbuilt markets are rapidly approaching or have fallen below the relatively high HOA, insurance and tax expenses. (This is an unsubstantiated assertion but I believe provable and would make for an excellent analysis)

I assume by your email address that you are either from or presently reside in Australia. Hopefully your real estate market and taxes are more rational than ours. If the costs of providing municipal services and maintenance were directly offset by the property tax receipts of individuals consuming those services the system would be rational. But the states rely upon property taxes as a general source of revenue to fund unnecessary and dramatically expanding Government expense.

This is illustrated by the extraordinary expansion of state government spending nationwide during the Housing Bubble. As property values rose states received windfall tax receipts. One would rationally expect those states to have run huge budget surpluses from the unexpected and unsustainable windfall. Especially since the vast majority of municipal services had already

been established and incremental increases in maintenance expenses were minimal.

Instead, these states spent all of the windfall revenue and then some! Today, despite the fact that in many cases property tax receipts continue to rise, the states are in terrible financial trouble with massive budget deficits.

Florida provides a clean example of this phenomenon as the state has no supplemental source of revenue from income tax. People's property taxes continue to rise annually even as their housing values collapse. Yet the state's budget deficit is unsustainable and only persists due to the overwhelming kindness of the Federal Government.

I think serfdom is an appropriate term given Government's demonstrated willingness to arbitrarily increase the perpetual liability of property ownership in order to fund its excessive, unnecessary and wasteful programs.

[Reply to this](#)

Richard wrote:

[4/14/2009 5:43 AM](#)

Excellent post. This is exactly what happened with timeshares. You "own" a week or two and pay thousands a year in fees/taxes etc. You can buy these on e-bay for anywhere from a dollar on up. Some timeshare operators actually charge the owner to return the unit week (!)

[Reply to this](#)

John wrote:

[4/14/2009 7:22 AM](#)

Exactly David! The article is great, but leaves out the risks associated with HOA failures due to high foreclosures/vacancies.

I see this happening in Wildwood NJ, a market I've been following since last fall. Lots and lots of condos on the market, many built in 2005-2007, so many "owners" are underwater and walking away. They are now typically listed as short sales for a big discount over their original sale price. But, the condos are just not selling and banks won't finance a purchase without a strong HOA and high occupancy. So, entire buildings are sitting, mostly vacant, and deteriorating due to lack of maintenance. Prices continue to drop, but as the article above illustrates, the purchase price is only the beginning of your liability of ownership. Of course, these can be considered "investment" properties, but the strength of the vacation rental market is in question with 8.5% unemployment and rising.

So, how does this all end? Will Wildood and other places like it become ghost towns?

[Reply to this](#)

Grizz wrote:

[4/14/2009 7:42 AM](#)

In NH some people are dumping their timeshares for free to avoid the fees, so your theory (although may not happen in some markets) is entirely possible.

Its probably a fantasy the Boston Metro area, but I can dream.

[Reply to this](#)

SoCal wrote:

[4/14/2009 9:04 AM](#)

One tactic to fight this scenario is to demolish vacant or 'blighted' properties. Jim Cramer actually proposed the idea of bulldozing entire housing tracts in the Inland Empire of CA. I think this is a completely disgusting idea, but one that the govt may resort to.

The govt can make the claim that by demolishing vacant properties, it is protecting property values. Or that the govt cannot support the utility infrastructure for these properties.

The real motive, of course, is to destroy supply and to protect the banks and developers.

[Reply to this](#)

Soeren wrote:

[4/14/2009 9:24 AM](#)

I wanted to add(in response to the original question) this: My elderly mother lives alone in a 3brm, 2 bath, 2 story, 2 car garage, oceanfront condo on an island in S Fla. At peak, it was probably worth \$300-350k. It probably wouldn't fetch \$100k in this market, and the taxes, common charges, fees and special assesments are brutal(2 hurricanes did a lot of damage and now the insurance has skyrocketed. My brother and I would be the sole heirs if/when

she passes away. The place is such a money-sucking pit(nice as it is, that in the event of my mother's death, I would try and urge my brother to agree to immediately put it up on ebay with a starting bid of \$1 and no reserve, and take whatever it fetched, and count our blessings we no longer owned it.

[Reply to this](#)

surferdude wrote:

4/14/2009 12:28 PM

this is an absurd example:

"Imagine a condo with \$1,000 a month in condo fees and \$6,000 in annual property taxes? (these are hypothetical numbers designed to illustrate a point) If you were to purchase such a condo for \$1, ownership of the unit would still be costly. The free unit would cost \$1,500 a month."

there are not that many condos with a monthly hoa fee of \$1k. if so, that pays for a number of items such as exterior maintenance, capital repairs, etc. all of these things an owner in a detached house face as well. who do you think pays to the landscaping, replace a roof, or paint the exterior in a single detached home?

your example is absurd as owners of detached properties face the same costs of ownership. if pricing is rational, the operating costs of condos and detached generally becomes equivalent.

the issue or big risk with condos today is a mismanaged or underfunded association because of foreclosures. this is where someone could be a disadvantage versus a detached owner. but all property owners have their value influenced by the neighbors. there are many detached owners that lament the junk yard of car parts or the uncontrolled yard of the next door neighbor.

all forms of residential real estate have risks. best advice is to do a ton of research, do not buy anything that is more than 3x your income, try to pay \$150 per square foot or less, do not let your residence become more than 25% of your net worth, expect to break-even at best during ownership.

[Reply to this](#)

Whitney Ross wrote:

4/14/2009 1:46 PM

Absurdity is my specialty!

It is indeed a hypothetical example with round numbers.

That said a large and material percentage of the condos constructed in Miami, New York, Los Angeles, Las Vegas, San Diego, San Francisco, Washington D.C., Boston and Tampa that were built in the past several years have HOA monthly fees in excess of \$1,000 a month. My assumptions are not unreasonable for the markets with which I am familiar.

That said, each market is distinct and I am advancing a general hypothesis. But I believe the logic of the argument to be reasonable.

Please see my other responses for perspective on maintenance costs and relative valuations.

You provide excellent advice.

[Reply to this](#)

dog-walker wrote:

4/14/2009 12:32 PM

Yes, but...

HOA fees go to maintenance, which is NOT the same thing as tribute or rent...

property taxes go to provide services used by the "owners" (water, power, roads, fire & police depts, etc.) without which life as we enjoy it would not be possible (especially in the urban centers where such fees tend to be highest.)

Which is not to say such "ownership" is not an essentially absurd swindle... but this is true of ALL "permanent" and "secure" notions of possession. In truth everyTHING is borrowed, shared, trespassed upon.

[Reply to this](#)

Whitney Ross wrote:

4/14/2009 1:31 PM

I agree with your every word.

Condo owners MUST pay HOA maintenance fees though. Home owners have the option value not to, which becomes increasingly valuable during times of economic distress. If you can't afford to fix your roof now you can wait until next year. If you don't pay your HOA every month you enter foreclosure. This is one of many reasons condos have historically been cheaper than houses and will be so again in the future.

Please see my response to Glenn Peters above with respect to municipal services and maintenance expenses.

[Reply to this](#)

BrassServices wrote:

4/14/2009 3:59 PM

Property taxes only go to "provide services" like water, power, roads, police and fire because we have a captive (socialized / nationalized) system which is anti-competitive in nature. Private water and power companies exist in many jurisdictions quite successfully employing the subscriber model for pay. Private roads have long been a part of American society, more out East than in the West, but in existence none-the-less. Private security, personal alarm companies, private investigators, citizen patrols, bodyguards, gun permits and self defense courses do far more to protect people than police who arrive after the shooting to find out why you or your wife is already dead. The markets will respond to the demand if given the chance to do so. Remember, there was a time in America when caveat emptor reigned supreme and we didn't have government watching us at every turn. A bit more of that Libertarian ethos would do us all well.

[Reply to this](#)

Somalia wrote:

4/14/2009 8:39 PM

Hi,

the Cato institute had a paper about how Somalia was a great model. With the lack of government, the private warlords provided security (to those in their clan.)

For me I prefer the US, but those who prefer no taxes might like Somalia better.

[Reply to this](#)

Whitney Ross wrote:

4/15/2009 1:59 PM

Brilliant insight.

Obviously reality dictates that there are only two options from which we may choose.

- High taxes and a large, rapidly growing, wasteful, confiscatory Government which accounts for 25%+ of GDP

or

- No taxes, no government and a lawless, failed-state like Somalia

My resistance to high and arbitrary taxes obviously means that I am against all Government spending including providing security, military, police, roads, municipal infrastructure, clean water and the other public goods for which the Federal entity was originally created.

Happy tax day!

[Reply to this](#)

BrassServices wrote:

4/15/2009 2:08 PM

LOL!

Yep, I can't wait to take upon myself the mantle of Warlord of Northern California. I will be like the Governor, dark and brooding upon my mighty sword.

The rallying cry of the tax-lover has been heard. I'm surprised that he didn't invoke

the security of our children like most good Nationalist Socialists prefer to do.

Lets settle on this. Everyone who does not want to pay taxes stops doing so and those who love taxes continue to do so at a higher rate in proportion to the loss of the rest of us. You get your government / state services and we'll put our money where our mouths are and make due with the commercial market.

[Reply to this](#)

BrassServices wrote:

4/15/2009 2:13 PM

The Cato Institute paper addressed the issue of chaos, NOT anarchy as a governing system. The two are defined differently and you obviously cannot distinguish between the two. Even the esteemed tower of intellectual superiority of the Cato Institute had trouble understanding the difference and addressed the issue by casting an overly broad net. Nice try applying this, but allow me to refer you to Rand. Rand will save you.

[Reply to this](#)

mikke wrote:

4/14/2009 3:10 PM

Dog-walker wrote that property taxes go to services that property owners use.

That simply isn't true everywhere. In our area, we pay exhorbitant property taxes that go 95% to the public schools. Everything else--all those other services?

We pay for them out of pocket. EVERYTHING is privatized...but we still have to pay crushing, and constantly exploding (doubling in 6 years!) property taxes.

I have no kids, never wanted them, and don't see how I'm profiting by having to pay this extortion to people who breed, then, regardless of what is affordable, continue to demand of the minority of homeowners an escalating series of luxury accoutrements (pools, orchestra camps, trainers, "life coaches") and full-service state day care centers. Their kids come out increasingly unable to do anything but sit in a room and whine their demands. They can't work, they're too sensitive/stupid/"special" to live with, and they have not skills and nothing to offer.

Meanwhile the constant demand for socialized private academies for all creates incentives to gentrify the housing base, and apply unreasonable and vaporous tax assessments.

This article is a very good one, and cuts to the point. The only reason I can think of to "own" (ha ha ha) a house is to have a land or building base for productive creative work, like growing food, performing services for barter, etc. These enterprises have been taxed and regulated so heavily that it's no longer possible to do them at reasonable small scale. And each time the hard-working homeowner finds a way to, say, sell cut flowers to help pay the taxes, or offer sewing/tailoring services to the neighbors, in comes the city, the county, the state, the feds, demanding a cut.

We need to tax the things we want to discourage--pollution, stupidity, speculation--not the things we want to foster, like responsibility, hard work, sacrifice, attention, and prudence. It's no wonder that we've got a nation of slackers and scammers.

[Reply to this](#)

BrassServices wrote:

4/14/2009 3:50 PM

I would encourage any holder of title on real estate that bears secured property taxes to pay off any and all bonds issued on that property in advance. Contact the bond administrators on your tax bill and figure out the pay-off amount. This will lower the annual tax bill. Secondly, if you are in a state that allows it (like Calif.), make sure that you have your value reassessed by the Assessors Office of your county in order to lower your tax burden. Also, make sure you have any tax exemptions that you are entitled to, like a HOE (homeowner occupancy exemption) which will serve to lower the tax basis. Some states offer other exemptions for seniors, so ask about these too. Ultimately, the Land Patent process whereby a person acquires "higher" or "Alloidal" title from the State and Feds might be worthwhile process to consider in order to get out of the property tax system.

[Reply to this](#)

George wrote:

4/14/2009 6:18 PM

This happened to single family houses in Detriot in the '90s (and may have again for all I know).

Changes in building codes that required owners to bring a house up to code before selling it resulted in houses being worth less than \$0. It doesn't pay to spend \$30k to fix a house that will only fetch \$20k.

[Reply to this](#)

Robert wrote:

4/15/2009 3:54 AM

I bought a condo at foreclosure auction in NH in 1989 for \$13,000. This Unit had previously sold for \$140,000. it was not zero but close.

[Reply to this](#)

Eric wrote:

4/15/2009 12:22 PM

Article assumes that you only pay maintenance/HOA and property taxes on condo. You have the same if not bigger expenses if you own a house. How much a new roof will cost for the house that you OWN will cost you?

[Reply to this](#)

Soeren wrote:

4/15/2009 3:09 PM

"How much a new roof will cost for the house that you OWN will cost you?"

About the equivalent of 10 months rent, but a new roof is good for many years, and I'd *much* rather lay out \$5-6k for a new roof, and, after the equivalent of "paying rent" for 10 months, go the next 120 months rent-free, than pay rent every month just so I don't have to worry about the roof.

[Reply to this](#)