Neighborhoods go through market cycles, so it's instructive to understand how these cycles work.

- Cycles usually have four elements:
    - Before the fall:
        - Prices are still appreciating but at a slower pace.
    - The fall:
        - Foreclosures and DOM increase
        - Lots of distressed sales
        - Prices fall
    - The bottom:
        - Peak in distressed sales
        - Not much move-in ready properties available
        - Fix and flippers start dipping their toes in the water
        - Buy and hold investors start buying
    - The recovery:
        - The market begins to correct
        - Foreclosures decline
        - Normal owner occupant sales return

What does it mean for the client?

- When working with a client looking to buy or sell a property in a certain neighborhood, show them this chart and discuss where their neighborhood of interest fits on the chart.
- It's fun and instructive to understand neighborhood patterns and walk through the patterns with your clients.
- They'll appreciate your interest.

Source(s): Your Castle Real Estate analysis

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OVERVIEW OF A REAL ESTATE MARKET CYCLE

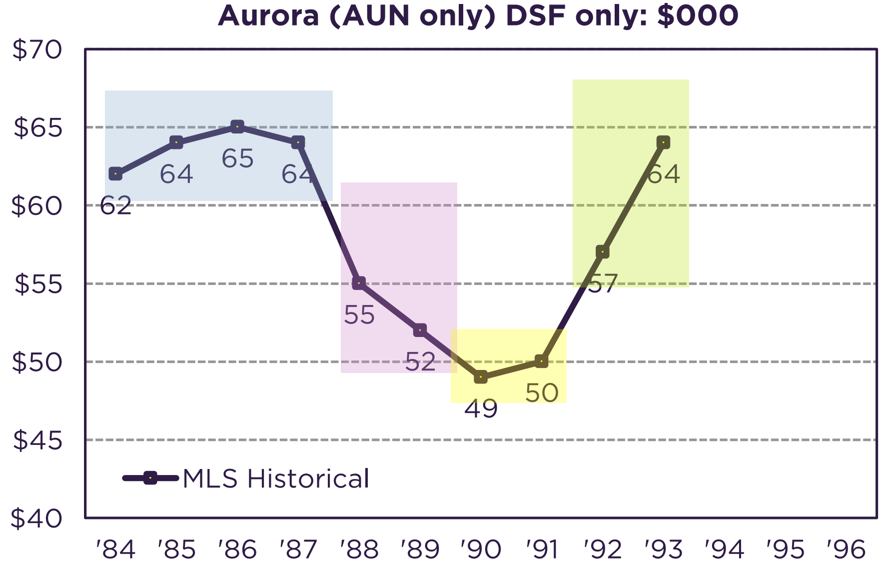
Anatomy of a real estate market cycle. Denver's last two cycles had many common features. This doesn't enable us to predict the future, but it gives insights.

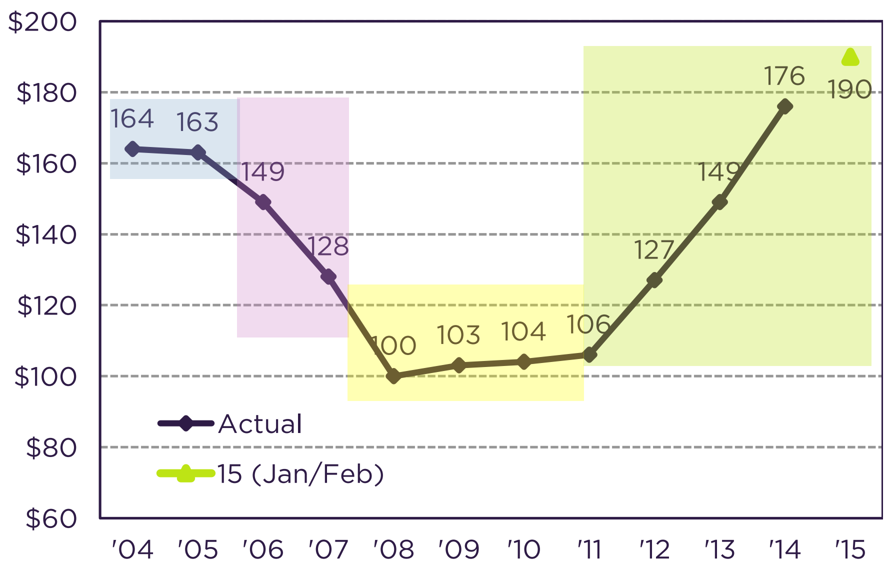
A: Before the Fall

- Prices are appreciating, but at a slowing pace, as the end of the cycle is near.
- Fall is foreshadowed by increasing foreclosure volume (though still at a *relatively* low level).
- Discounts and Days on Market increase as inventory builds.

B: The Fall

- Number of foreclosures increases dramatically.
- Low cost distress sales replace regular full price sales; so blended average price decreases quickly.
- Elective sellers in good condition decide to wait or rent their homes, further reducing non-distress sales.
- DOM reaches peak; then inventories fall as owner occupant sellers pull out.





C: The Bottom

- Distress volume peaks and distress pricing hits bottom.
- First time buyers frustrated with lack of move-in ready inventory: pent-up demand.
- F&F'ers start to re-enter.
- Buy and hold investor (land lord) demand outstrips supply; multiple bidding gives a floor to prices.

D: The Recovery

- Foreclosure volume declines.
- Non-distress sellers waiting on sidelines finally re-enter.
- Mix shifts from beat-up to nice homes; prices increase.
- "Show me investors" on sidelines rush in to market, increase market frenzy.
- Number of true "deals" shrinks but newbie investors buy anyway, driving up prices
- F&F activity increases; increasing quality and price of inventory.
- First time buyers finally buy; using up pent-up demand.

Source(s): Your Castle Real Estate analysis. From REcolorado®, Inc.,

Home prices and MOI

- The top graph shows metro Denver home prices as well as average yearly appreciation from ‘71 to present.
- The bottom graph shows the Months of Inventory for homes in metro Denver from ‘75 to present.
- Seeing home appreciation and MOI lined up one above the other shows the inverse relationship between the two.
  - Prices rise when demand outstrips supply so MOI falls.
  - Put another way, during periods of high home price increases, MOI is low.
  - Prices fall when supply outstrips demand so MOI rises.
  - Put another way, during periods of low price increases or price drops, MOI is high.
- For example, look at ‘87 – ’90. You see that MOI fell dramatically. As the inventory (supply of homes) fell, it set up the market for home price increases starting about ‘90 when demand overcame supply, forcing prices upwards.

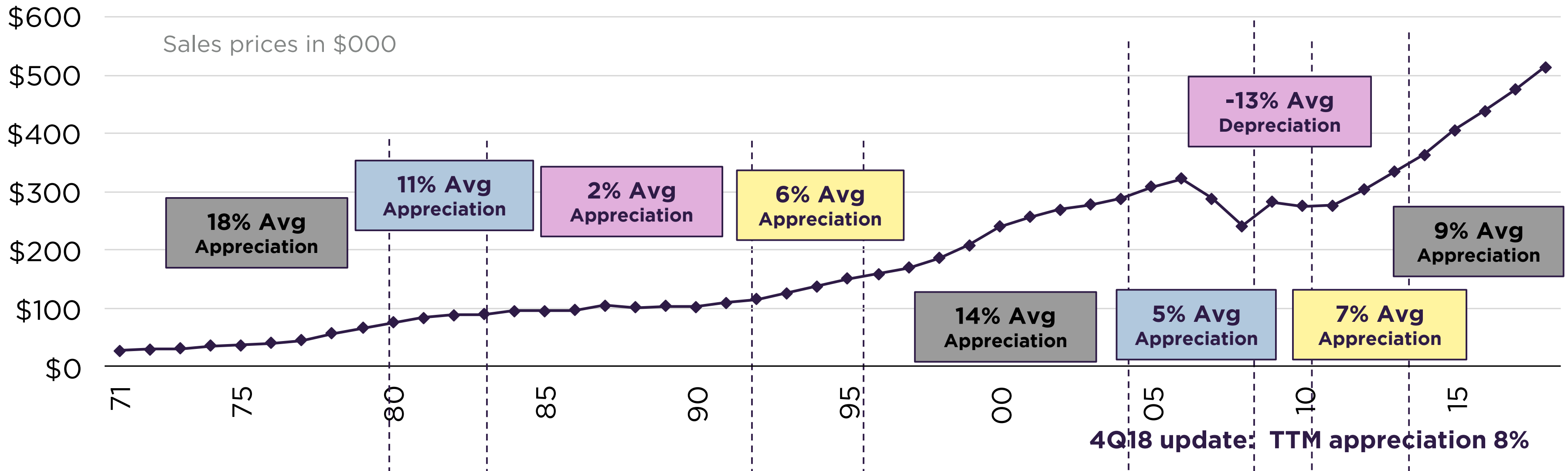
What does it mean for the client?

- It’s important for clients to understand that there is long term logic to the market and the law of supply and demand works in real estate.
- It is instructive to realize the connection between the amount of inventory in a market (described in this example by MOI) and prices.
- This doesn’t mean you can perfectly predict the real estate market or future home prices. Don’t think understanding the economics of real estate makes you (or especially your client) a soothsayer!
- Many speculators have made this mistake much to their disadvantage. But it is helpful and comforting to see that, long term, the real estate market is driven by identifiable market conditions.

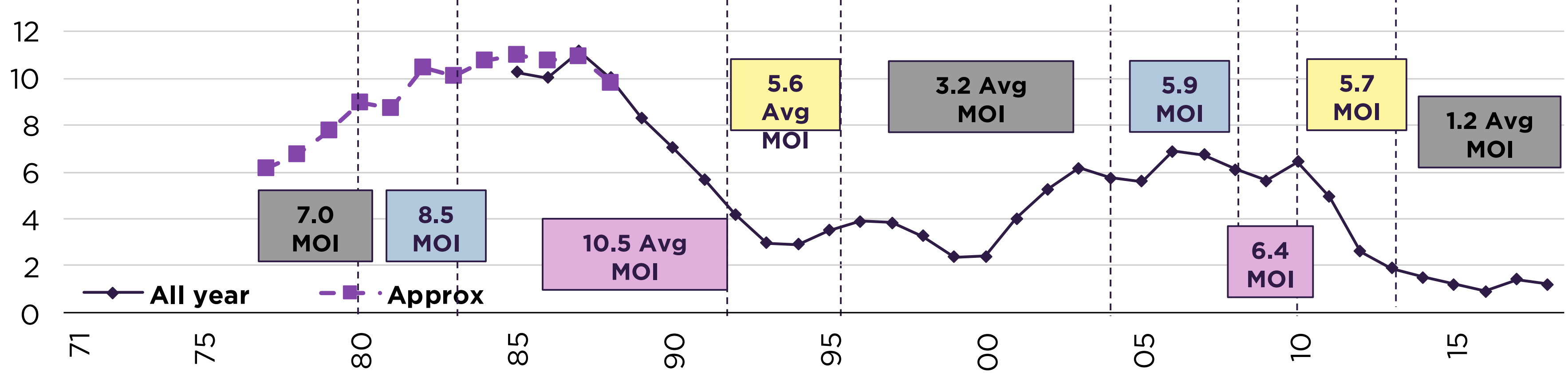
Source(s): Your Castle Real Estate analysis

Home price appreciation vs. MOI. During times of high appreciation, MOI is low. MOI grows for ~3 years (highlighted in blue) before a real estate recession starts (highlighted in red).

DENVER METRO (DSF ONLY, NOT CONDOS OR TOWNHOMES)



MONTHS OF INVENTORY (MOI)



Source(s): Your Castle Real Estate analysis. REcolorado®, Inc.,

4Q18 update: MOI 1.2

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Home prices and DOM

- The top graph shows metro Denver home prices as well as average yearly appreciation from ‘71 to present.
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  - Prices rise when demand outstrips supply so DOM falls. Put another way, during periods of high home prices DOM are low.
  - Prices fall when supply outstrips demand so DOM rises. Put another way, during periods of low prices increases or price drops, DOM are high.
- For example, look at ‘93 – ’03. You see that DOM fell dramatically. As the DOM fell, it set up the market for home price increases during this decade when demand overcame supply, forcing prices upwards

.

What does it mean for the client?

- Just as in the previous slide, it’s helpful to understand that the basic tenants of supply and demand rule the real estate market.

Source(s): Your Castle Real Estate analysis

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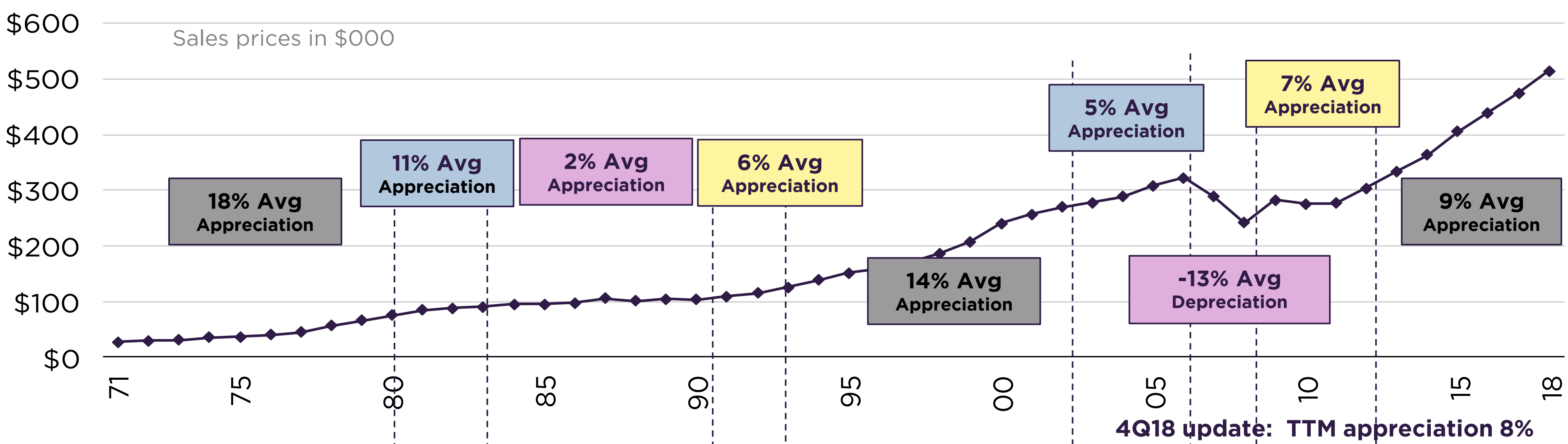
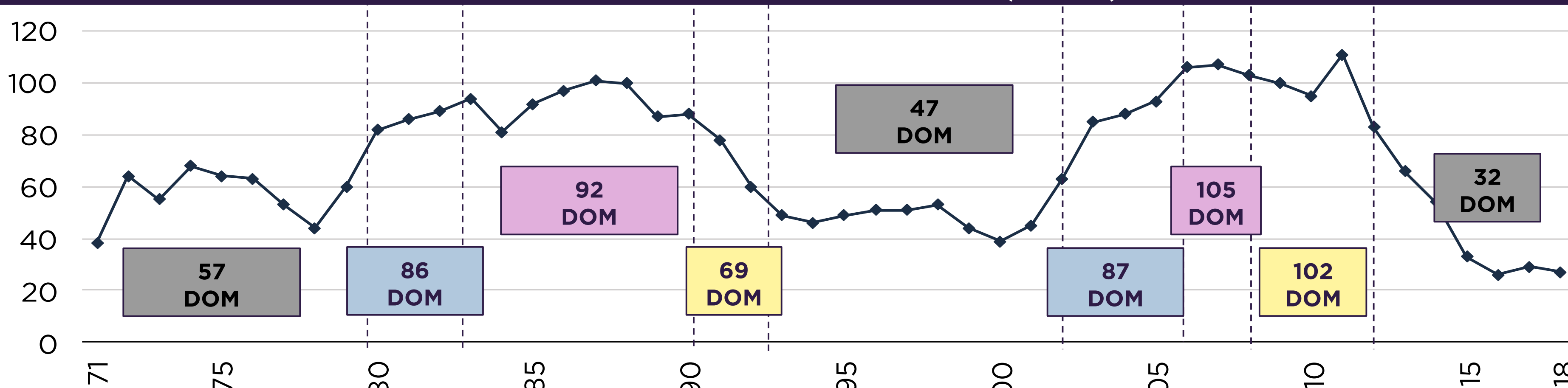
Home price appreciation vs. DOM. As inventories build (as measured by MOI), marketing times (as measured by DOM) increase. The transition from growth to recession is highlighted with blue.

DENVER METRO (DSF ONLY, NOT CONDOS OR TOWNHOMES)



AVERAGE MARKETING TIME (DOM)



Source(s): Your Castle Real Estate analysis. REcolorado®, Inc.