THE REAL ESTATE SECTOR IN GREATER LOS ANGELES IN AN INTERNATIONAL CONTEXT: AN EXPLORATORY STUDY

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EXECUTIVE SUMMARY

This report provides a unique perspective on international real estate investments, trends, and effects on the Greater Los Angeles (GLA) market. The information within this report was gathered from a diverse spectrum of sources within the real estate industry. This report aims to examine present day global economics, policies, and the influx of international investment trends. Moreover, this report discusses the effects that international buyers have on the domestic real estate market, and the pros and cons of foreign investment growth. In the 2014 report ‘Winning in Growth Cities,’ the global real estate investment market is valued at $788 billion, and Los Angeles ranks fourth as a top investment city with $33.1 billion in Q2 2014 (Cushman & Wakefield). To better understand the real estate investment industry, this report will analyze major foreign players, domestic supply and demand, and economic trends. Moreover, the findings will unveil the main drivers and dynamics as well as statistics influencing the GLA real estate market.
INTRODUCTION

The real estate industry consists of purchasing, owning, leasing, and renting of commercial, residential, and industrial properties. The real estate industry (NAICS code 531) is powered by business development, which creates employment opportunities. This motivates population increase, economic conditions, and demand (Hoovers). According to Cushman & Wakefield, America and Europe currently lead the way in the global real estate market, with $1.34 trillion for 2015. Particularly, international investors have been scooping up available real estate in Southern California while American soil is regarded as relatively inexpensive. In 2014, this growing trend boosted GLA into fourth place with $23.2 billion in real estate investment.

SCOPE

This report unfolds historical events that marked GLA as a prime real estate investment location. Additionally, an overview of national and local economic conditions, which ultimately led to the real estate bubble burst, are revealed, including current market trends, contributing international players, and growth rates in the GLA real estate playground. Moreover, the report takes a closer look at the top five countries that exercise purchasing powers in the GLA real estate market and their drivers, trends, and growth rates.

METHODOLOGY & RESEARCH

This report aims to answer the following questions: “What are the current real estate market trends and dynamics in GLA and how do international buyers affect the domestic economy?” The research method consisted of analyzing statistics, reports, and real estate articles published by industry professionals. This report takes a look at the
global real estate market as a whole, followed by international investments in California, with a specific focus on the GLA area. This method assists in understanding the market, and future impact on the domestic real estate sector.

REAL ESTATE SECTOR IN THE GREATER LOS ANGELES AREA

Many envy Southern California living, and who can blame them? With undeniably perfect weather, access to hundreds of miles of coastline and beaches, and home to the entertainment industry, Los Angeles truly embodies unique experiences and opportunities for its residents and visitors. Historically, individuals flocked to California beginning with the 1848-1855 Gold Rush, and gained momentum when the Santa Fe railroad connected Chicago to Los Angeles in 1885. Post World War I, the real estate market significantly grew in Los Angeles, as Hollywood film studios and manufacturing businesses set up shop, creating thousands of new jobs in GLA (Dirks, 2015). This grew demand for the construction of single-family homes. By the late 1960s vacant land was extremely hard to find, real estate prices escalated, and the market continued to top the charts as one of the most populated cities (Barnes, p. 5). The United States Census Bureau noted that GLA was home to over 10 million residents in 2015; this number is multiplying at an average of .75 percent annually. In addition, the Southland ranks as the second fastest growing urban territory in America (Census Bureau) and median home prices are on the rise.

BACKGROUND

To understand the emergent interest of why international investors pursue GLA real estate warrants a glance at the economic circumstance in the United States between the years 2007–2009. America underwent a financial crisis beginning in 2007, causing
the stock market to plummet. Large commercial institutions were on the brink of collapse while national banks pleaded for a government bailout to dodge an irreparable tragedy. Financial experts acknowledged this impasse resembling the Great Depression in the 1930s. Stirring up an international frenzy as stocks continued to fall, leaving 8.8 million Americans out of work, with a deficit of $19.2 trillion in household wealth by 2011 (Department of Treasury).

Moreover, the predominant instigators in the crisis are considered to be the following complexities; banking institutions estimated a prolonged market increase, offering relaxed mortgage access to borrowers. Through securitization, a method of remodeling a liquid asset into cash flow “asset-backed” security banks had greater capital, better interest rates, while lending to an even greater extent (Department of Treasury). Furthermore, in commitment to the Housing and Community Development Act of 1992, a tremendous 56% of affordable home loans were approved to accommodate
minorities and low-income families with 84% of the mortgages from private lenders. In an article by Goldstein & Hall titled “Private sector loans, not Fannie or Freddie, triggered crisis,” they defended the Federal National Mortgage Association “Fannie Mae” and Federal Home Loan Mortgage Corporation “Freddie Mac” when stating, “they purchase loans from the private lenders who actually underwrite the loans” and those institutions avoided appropriately considering the long-term capital responsibility when dominating the mortgage market. Therefore, real estate prices ballooned, resulting in $5 trillion owed in mortgages by 2008 (Federal Reserve Board).

Many housing markets in America suffered, leading to foreclosures, evictions, and construction came to a halt indefinitely. The country’s economic circumstances initiated further agony for California as the state tried to climb out of an $11.2 billion budget deficit in 2008 (BBC News). At the time, President Obama reassured residents of California “we intend ... to start making a down payment on the critical investments that are going to be necessary to sustain long-term economic growth as well as pull us out of the current slump.” The combination of these historical events had an enormous impact on GLA businesses, residents, and the real estate market (BBC News).

According to the Bureau of Labor Statistics, in 2010 California ranked second highest in the nation with a 12.2% unemployment rate (BLS). Rick Sharga, vice president of RealtyTrac, confirmed that 546,669 or 4.08% of home owners in the Golden State received default fillings. Los Angeles County experienced a 12.5% unemployment rate with a 16.6% rate in foreclosure fillings, forcing many to move from Southland. In 2012, the Department of Treasury released a budget summary for the Troubled Asset
Relief Program (TARP) acknowledging that the real estate market “remains weak” while the “overhang from the crisis continues to weigh on prices” (DOT).

**CURRENT PROFILE**

Even though the value of the dollar has not fully recovered, it is beginning to show significant growth. The changes made in lender and mortgage policies have assisted in healthier business practices, and the local economy is in a state of rehabilitation. GLA welcomed stabilization of the economic climate with excitement and the Bureau of Labor Statistics reports that unemployment rates are at 6.6% (BLS). The current market average in GLA for a single-family dwelling is priced at $1,719,268 and median sales price is $624,000 - this is a 10.9% increase while the amount of home sales has slowed down by 9.9%. Even though there are 3,545 active foreclosures, this is a huge recovery from 2010. The California data analysis company DataQuick reports that the most recent real estate purchases have been by investors, holding 23% of the market, which is the lowest rate since 2001 (CNBC).

Experts closely monitored 2014 trends, as property sales were highest in transactions with limited availability. These negotiations elevated the median price in the GLA housing and office real estate market and drew hundreds of startup tech companies to Wes Los Angeles to an area known as Silicon Beach. Moreover, as international investors make all cash offers, domestic frustration arises as prices escalate, inventory dwindles, and mortgages are difficult to obtain. Foreclosures for Los Angeles County are 11% higher than the previous month with over 28,000 homes listed (RealtyTrac).
FUTURE OUTLOOK

Property ownership is considered a smart and safe investment in a financial portfolio. Los Angeles County has access to highly respected universities, business opportunities and career growth – making it an ideal real estate investment. Therefore, real estate prices will continue to grow, while availability becomes scarce. According to DataQuick, real estate sales slumped 7.1% and the median price leaped 2% from 2014 to present. This serves as a trigger for Southland residents as “absentee buyers bought a full quarter of the housing sold in January in Southern California” (Barragan, B. 2015). As the desperation seizes, fewer properties are in despair as the housing market reaches for equilibrium. However, DataQuick reports that in 2013 close to 32% of purchasers were solid investors not wishful home buyers (DataQuick). Furthermore, Cushman & Wakefield are in agreement with the above statistics and foresee that as financial agencies fizzle out, an additional 400,000 square feet of office space will become available by 2016 (Cushman et. al., 2014).

INTERNATIONAL ACTORS IN THE REAL ESTATE MARKET: TRENDS & DRIVERS

As the overall international economy slows down, investors scout for new and exciting ways to initiate their capital growth; traveling from Canada, China and Singapore, foreigners “view gateway cities in the US, such as Los Angeles, as safe havens for investment” (Blosfield, 2015). As early as 2011, these international entities have been courageous in obtaining real estate in the Southland; therefore GLA is naturally gaining popularity and intriguing overseas and neighboring border investors.
These foreign entities are typically searching for a “trophy” house; this is not their main residence, but rather a vacation home.

The National Association of REALTORS® (NAR) issues a yearly report that discloses market analysis, opportunities, and challenges by the real estate industry. In the 2014 report by Lawrence Yun, Jed Smith and Gay Cororaton, NAR concluded that Canada became the biggest international real estate buyer at 19%, with China not far behind at 16% followed by Mexico at 9%, India and England tied at 5% with a grand total of $92.2 billion entering the American real estate and economical market through international property buyers (Yun, et. al., 2014). Therefore, with already limited available inventory, international buyers have yet another trump card—all cash purchasing power. Meanwhile realtors appease their foreign clients in any way they can, strongly supporting the notion of “foreign capital into LA’s market, pricing has risen across all
sectors” as it motivates the economy and creates a healthy competitive environment (Doler, 2014).

Although various foreign states are attracted to invest in GLA, there are five countries that have made their mark on the industry: Canada, China, Mexico, India, and the United Kingdom make up about 54% of all international transactions. Even though Canada ranks as the top client in volume, China has attributed to the highest sales (NAR, 2014). Canadians tend to buy in lower-priced markets in comparison to the Chinese who buy in higher-priced markets. NAR reports that international sales by the Chinese in 2014 amounted to $22 billion, this is a stupendous jump from $12.8 billion from 2013. Chinese buyers have been responsible for 24% of all international sales in dollars, and according to industry professional Dolly Lenz “many foreign buyers now see luxury U.S. real estate as a store of value, it's like a safety deposit box with gorgeous views. NAR discovered that 69% of international “buying preferences” are all cash deals in comparison to one third of national transactions payment, a huge advantage over those who don’t have capacity to bypass banks loans, escrow, credit approval (Doler, 2014). Rick Sharga, who holds a vice president position at Auction.com, feels “cash buyers can move fast, so competition for hot properties is stiff” leaving national buyers in the dust (Doler, 2014).
In addition, the majority of purchasing activity has been influenced by the rise of Chinese and British currency making Los Angeles real estate reasonably priced for international buyers. “Sometimes they slightly overpay for a property versus what a lender believes is the value” said Rick Sharga, and they don’t mind feeling that this is still a huge bang for their buck (Doler, 2014). Dolly Lenz is convinced these business transactions are “boosting U.S. property sales and competition” without hesitation on ways this economic stimulation may reflect on local residents and chances of owning a home (Doler, 2014).

INVESTMENT DRIVERS & CONSTRAINTS

A primary driver for international investors occurred when Congress passed the “Jobs Originated Through Launching Travel” (JOLT) Act, which facilitates visa approval rates, making it easier for foreigners to travel at their leisure as long as they stay under 90
days (Times Editorial Board). Moreover, the EB-5 program supports investors who desire to live in the United States, there are only 10,000 visas granted to individuals who bring forth $500,000 and upward to America’s playground in development, which in turn creates more jobs and stimulates the local economy (Doler, 2014).

On the other hand, as Rick Sharga puts it “the global reach of the Internet made the U.S. real estate market global…they call it the Worldwide Web for a reason” suggesting that easy access allows for accommodation, and a quick turnaround especially when paying with hard cash (Doler, 2014). Lastly, the American economy has not yet completely recovered from the recession; however, experts admit that the bounce back has been one of the fastest in global history.

Chief economist for the Los Angeles County of Economic Development Corp Jack Kyser believes “one reason the United States is a popular destination for investors is
that the country has a relatively stable political and economic climate and real estate is a low-risk investment.” The security and overall national stability plays a big part of why international buyers choose Los Angeles as their second home (Wilcox, 2014).

This type of news prompts mixed emotions as loyal Angelinos realize that foreign competition is a threat. GLA residents can’t compete as these investors are looking for gorgeous properties that many can’t afford with only 42% of purchased homes to be considered as primary residence for new immigrants, business professionals and international students. While the other 58% of purchases by foreign investors are acquired for the purpose of a vacation, rental, or “trophy assets” (PR Newswire, 2014).

Brian Fielding, president of his own firm and an industry veteran of 40 years, indicates that “we see this activity as a prudent diversification strategy by well-heeled investors who recognize the stability of the U.S. real estate market” (PR Newswire,
The wealth in information can be attributed to the spread of information by word-of-mouth about buying, and living in already established communities. NAR reports that many international buyers take into consideration the location, family, friends, work opportunities, education and climate and the fact that foreigners tend to congregate in one area of a city.

With sunny weather and a kaleidoscope of entertainment, amusement parks, and the glitz and glamour of Hollywood, Los Angeles ranks seventeenth on the Business Insider’s list of most cultural cities in America (Willett, 2014). For these property sharks, the Los Angeles real estate market is considered very inexpensive; therefore domestic properties are viewed as a steal deal.
MAJOR PLAYERS & THEIR MARKET SHARES

CANADA

Canadians who hold the majority of international real estate purchases in Southern California prefer to get away in order to avoid their brutal winters. In 2014, Canadians were responsible for nearly $13.8 billion in real estate transactions; this is roughly 15% of all international real estate dealings. The average per purchase is around $212,500. Estimated 86% of transactions are all-cash. Reports suggest that the majority of properties acquired are used for rentals, and vacations with less than six months of stay in America. NAR 2014 report analyzed that about 50% of Canadians tend to buy houses and the other third is interested in condominiums or apartments in less expensive neighborhoods (Yun, et. al., 2014).

CHINA

The Chinese buyer is interested in various real estate investments. Most recently beyond the marketplace for residential properties, Chinese international investment firms seek commercial real estate space that ranges from $10 million to $25 million. China’s wealthy citizens have invested an estimated $22 billion in real estate in 2014. Average purchase price was $523,148. Estimated 76 % of transactions are all-cash. Moreover, Chinese buyers are attracted to suburban and developed areas. NAR 2014 survey reports that 50% of transactions are mostly for vacation and rental purposes and 5% are intended for commercial use. Chinese international investors are interested in purchasing single-family homes with the intention to use the property for longer than six months (Yun, et. al., 2014). These transactions include private residences, commercial office space, with a major focus on Downtown Los Angeles. Top destinations for Chinese investors include
upscale, lavish cities such as Irvine, Los Angeles, and the San Gabriel Valley. A local real estate broker mentions that buying such properties assists wealthy Chinese international students while they attend American universities. Furthermore, the Chinese purchase these immaculate homes while their children are young and integrate into the community over time (Doler, 2014).

**INDIA**

India is reported to have invested $5.8 billion in total real estate value, about 6% of international sales. The average purchase price is $342,857. However, only 23% of international buyers were all-cash sales. Majority of purchases are single-family detached dwellings, and out of this approximately 6% are commercial use, or rentals with the intention of long-term residence (Yun, et. al., 2014). As the online real estate market continues to grow, India’s businessmen and women now have access to make purchases on the Internet without the need to travel.

**MEXICO**

Reports reveal that in 2014 $4.5 billion worth of real estate transactions were from Mexico. This is about 5% of total international real estate sales. Between California and Texas NAR reports an average of 70% being from Mexican border. Purchases of an average price $141,071, with an even cash and financing process of buying. These buyers are interested in single-family homes for rent or commercial use intended for long-term use (Yun, et. al., 2014).

**UNITED KINGDOM**

United Kingdom investors are responsible for $5.8 billion, an estimated 6% of purchases in America with an average price point of $350,000. Main purpose was to
reside in a single-family home with a mix of all cash and financial loans as a process of buying. This is exciting for the Brits, considering that all land in England belongs to the Royal family, giving them bragging rights to ownership of prime real estate (Yun, et. al., 2014).

**ECONOMIC IMPACTS OF FOREIGN INVESTMENT & PARTICIPATION ON THE GREATER LOS ANGELES REGION**

As of 2014, Los Angeles reached new heights when LAX accounted for 18.9 million global visitors (based on international flights), a 6% jump from 2013 with 17.8 million foreign travelers. President and CEO of LA Tourism Ernest Wooden Jr. could hardly hold back the joy, as he announced the Southland’s “fourth consecutive record-breaking year for tourism and strong growth in international visitation underscores that Los Angeles has emerged as a leading global tourist destination” with approximate spending of $9.96 billion (lamayor.org).
The increase in tourism supports nearly 464,600 jobs in GLA, giving Angelenos a healthy economic arena (laedc.org). Enthusiastically, Mayor Eric Garcetti admits, “this is a competition, and if we’re not out there hustling, people will go someplace else” as he collaborates with others on attracting 50 million visitors yearly, by 2020 (lamayor.org). Trulia.com recently reported that the median home price in GLA is $619,000 and requires an individual to make over six figures to sustain a mortgage. Given that the median household income is $55,909 according to census reports for the years 2009-2013, it seems unlikely for most to live the American dream in GLA with the present minimum wage of $9 an hour. While most GLA residents dream of buying a house, most can’t afford one according to the Redfin 2014 discovery that only 8.7% of Los Angeles teachers can purchase a home with a standard salary of $69,400. These calculations are in respect to the median price of a home marked at $417,333 and an average of 28% as a
rule of thumb of the gross monthly income suggested when calculating mortgage payments (Unger, 2014). RealtyTrac recently estimated that the cost of owning a house in GLA is greater than renting, based on 2013’s Q4 and the median price of properties “including principal, interest, property taxes, and maintenance and insurance costs would run you $1,987—$100 more than it would cost to rent” a comparable apartment (LA Curbed).

CONCLUSION

In conclusion, it is safe to say that Southern California real estate is highly sought after as an attractive investment. Even with the fluctuating global financial market, foreign buyers are confident in GLA and future developments within the area for personal or commercial use. A couple of factors to take into consideration: even though the influx of cash supports the local economy, it is important to evaluate where this leaves domestic players when it comes to buying real estate. As of right now, the recent real estate market invasion leaves Angelinos at a huge disadvantage among those dreaming of buying their home.

Moreover, international real state buying habits have increased the median home price in GLA making it nearly impossible for an average income family to own real estate property as a primary residence. These changes drove many folks to the rental market, causing an immediate increase in cost of renting apartments. Reports confirm that GLA rental market reached 52% in 2012 and increased in 2014 to 47% of average income applied to meet mean rent (Kidler, 2014). Even with the minimum wage at $15 an hour, it would still be less than half of what an individual needs to earn to afford an average apartment.
When an average American resident in the GLA area can barely afford a rental unit, there is a need for dialogue beyond the statistics of inbound international investors in the real estate market. With the economy on the rise and the dollar stabilizing, Los Angeles needs to utilize its major resources to grow average incomes, and create a healthy work-life balance, generating demand and raising incoming profits while creating export opportunities for Los Angeles. This would result in a continuous surplus and raise the median of salaries, giving people a genuine chance of being a proud homeowner in Southern California.
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