Six Basic Real Estate Market Combinations and Their Implications

Real Estate Tech, April 1998.

By Stephen Chung BS BBldg(HKU) MS in Real Estate Development(MIT) ARICS AHKIS MAACE PQS RPS
Zeppelin Property Consultants Ltd – Phone(852)24016388 / 6619 Fax(852)2401 3084
Real Estate Development, Investment, Asset Management, Marketing, and Operational Analysis

---

In terms of long term real estate asset appreciation, there are 3 possibilities:
a) Increase = i.e. actual real estate prices generally go up
b) Stable = i.e. actual real estate prices remain the same
c) Decrease = i.e. actual real estate prices generally go down

In terms of cyclical behavior, there are broadly 2 possibilities:
1) Volatile Pattern = i.e. the fluctuations between peaks and bottoms are large
2) Gentle Pattern = i.e. the fluctuations between peaks and bottoms are small

Combined the above together, there will be 6 combinations of market:
a+1) Increase & Volatile = favours speculative real estate development and big gains (and losses) are possible. A high risk high return combination.
a+2) Increase & Gentle = favours steady real estate development. A medium risk medium return combination.
b+1) Stable and Volatile = NOT sure if such a combination exists in the real world. Favours speculative real estate investment. A very high risk yet high return combination.
b+2) Stable and Gentle = favours steady real estate investment. A low risk and low return combination.
c+1) Decrease and Volatile = favours speculative real estate investment. Extremely high risk yet perhaps giving only medium-high return. Not recommendable for most.
c+2) Decrease and Gentle = not favourable for either real estate development or investment. Better rent real estate required and in short leases only.

In general, growth economies are likely to demonstrate (a+1), (a+2), or (c+1) at different stages while mature economies generally show (b+2) or (c+2).

The above is meant to provide a very simple and quick classification of real estate markets though individual markets may have characteristics of more than one of the above as they transform or evolve. For markets which favour real estate development, investment is also viable though in terms of return development would generally be somewhat higher as there is a "value-creation" process. Moreover, even in less favourable market conditions, real estate development or investment may be necessary due to other considerations beyond the scope of this article. Development here implies building new or redevelopment while investment means acquisition of existing properties and keeping them largely as they are.