



Custom Construction or Buy Existing and Remodel?

In the current market it is much more affordable to buy an existing home than it is to purchase new or custom construction. Why is that?

On San Juan, home prices peaked in 2007 and bottomed out in 2012. During that period, approximately 30% in median home price was lost. More so with the median land prices, they peaked in 2006 and the median price decreased approximately 62% during the recession.

The costs of materials and labor did not change during the recession. As agents we were quoting estimates of \$235 -\$250 per foot for mid-level new home construction costs before the recession, and are quoting that now as well. This price per foot will afford some hardwood floors, custom cabinetry, granite, and a high-end appliance package, if you spend wisely.

Some homes on the island have been built for as high as \$1,000 per square foot. Those sellers that decided to sell after building their dream home at those levels may lose money as the market rarely supports those extra fine improvements and unfortunately, all the receipts in the world do not make a home more valuable than the market is willing to pay. Of course, inventory of similar homes will have an impact on sale as well.

Until such time as the home inventory decreases and the selection becomes a challenge to buyers, custom construction will not be considered the best option as compared to an existing home for far less money. There are numerous advantages to purchasing an existing home and remodeling to a buyer. Those advantages include views, foot print, other amenities such as guest houses and docks that current regulations make difficult or impossible.

To demonstrate existing versus new construction comparison, I've created two hypothetical options for current buyers, loosely based on real properties.

Option A: This week my clients can buy an existing home on a .75 of an acre lot with 100 feet of low bank frontage. The waterfront home offers 3500 square feet with 3 bedrooms, 2.5 baths, a den, a detached 2 car garage with nice landscaping and very good sun exposure and views. The home was originally built in 1974 but has had nice upgrades over the years and currently has very modern interiors and appliances. The home has been on the market for 400 days and is currently offered at \$1,050,000. It needs some cosmetic work; the hardwoods need to be refinished, many of the picture windows have lost their seals, and the deck is showing signs of nearing its life expectancy and will need replacement

boards and full replacement in just a few more years. Oh, did I mention the gutters are growing small maple trees and are full of debris?

I believe my buyer may be able to enter into a contract with this seller at \$1,000,000 or 5% off list price. Sellers on San Juan are negotiating on average 6% off their list price at the time of sale but each property and its situation is unique. If my buyers were to purchase this home they would need to spend the following to improve its condition to satisfy their requirements:

Hardwood floor refinishing	\$15,000
Window glass replacement	\$ 5,000
Deck repairs	\$ 5,000
Total	\$25,000

Based on the improvements itemized above, their basis would be around \$1,025,000. In this market, it is not uncommon for homes to sell well below their replacement costs in all segments of our market, not just homes listed in excess of \$1,000,000.

Option B: If my buyer was unable to find a suitable existing home and decided to build custom construction their costs may be similar to the following:

Waterfront Lot .60 of an acre/100 ft	\$350,000
Main home 3500 sf @ \$250	\$875,000
Garage 600 sf @ \$75	\$ 45,000
Well	\$ 20,000
Septic	\$ 25,000
Power	\$ 5,000
Landscaping, driveway, patios	\$ 40,000+
TOTAL	\$1,360,000

This proforma for new construction also assumes a nice level lot with a typical foundation expense.

The waterfront lot purchased in the example above was on and off the market since 2009. The original list price was \$800,000; it had good sun exposure, a beautiful gravel beach and numerous trees. The price was a bit high at that time, but the owners wanted to test the market, but it failed to sell. Instead, two things happened that dramatically reduced the market value of the lot. First, the recession but even more so was the uncertainty caused by new regulations. The Critical Areas Ordinance process was initially started in 2009 and finalized in 2013. The Shoreline Master Program has been in process for the last several years and is expected to be approved in a few months. Both of these regulations limited the tree removal and the home site locations, therefore affecting the amount of view a new home could potentially have. As you can see, this lot ended up selling for only \$350,000.

As mentioned above, the median lot price decreased in value approximately 62% with waterfront lots incurring the largest negative impact as more factors than the recession were involved. One would think that the decrease in median land prices would have been enough to offset the cost of new construction, but that is not the case.

Under option B my buyers did better building now than if they had built in 2009. This home would have cost them \$1,810,000 to build in 2009 if they purchased the lot for \$800,000. However, they may have

been able to build approximately 50 feet from the shoreline and may have been able to remove a few more trees, brush and limbs.

Once the housing inventory decreases and we have upward pressure on prices and appreciation, then the separation between the cost of an existing home and new construction will be less as the price of an existing home will be more.

The advantage of new construction allowed my buyer to construct exactly what they were looking for in a floor plan and use of materials. Unfortunately they were not able to finish the home for 1.5 years and during that time, they had what seemed like a body cavity search by their lender, interviewed two general contractors and architects prior to finding one they felt was compatible and then they incurred numerous cost overruns, change orders and delays in the process due to their building decisions.

Further, they had to hire a consultant to argue with the County over the storm water management plan and due to an Indian Midden, an archaeologist had to be retained. In addition, their property required a pre-treatment septic system so now they are looking at an annual expense to maintain the technically advanced septic system for the rest of their ownership.

There were only two dead or dying trees on their lot that could be removed so their view is filtered. Below is a photograph of their view from their deck which is approximately 110 feet back from high tide mark with the first 35 feet being a "no touch" buffer. They are able to trim up to 4% per year and maintain a trail to their beautiful gravel beach. They have yet to figure out how to measure the 4% and may have to hire an arborist to process the calculation and do the work.

As they used a federally insured lender, they had to pay \$2,500 in survey costs to prove to the lender and Corps of Engineers that the flood determination maps are faulty and that they were eligible for a Letter of Map Amendment and waiver of flood insurance.

For some, the new construction process can be very stressful and in fact many therapists rate it comparable to a death in the family or a divorce. Others enjoy it very much. Fortunately, my clients made it through even though their well tested with high sodium levels and now they must monitor that, as after this entire process, they now have high blood pressure.

Of course I have exaggerated all of the problems my hypothetical clients dealt with during the course of their construction and I admit that if all of these items actually happened during their project, they most likely would be divorced.

View from Custom Construction Home



View from Existing Home on the market for \$1050,000



The lower amount of buyers currently interested in custom construction has not had an impact on the general contractors and related service providers; they are all very busy. There are always people that are willing to pay for getting the exact home that they want for their lives. For many others, they are still able to find existing homes that meet their criteria at great prices.

Evidence in support of custom construction is Roche Harbor Resort; we expect 5 homes to be under construction in 2016. Roche Harbor is a good example of a destination that people are willing to pay for to create the type of home that meets their needs and their rental pool is attractive as well.

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