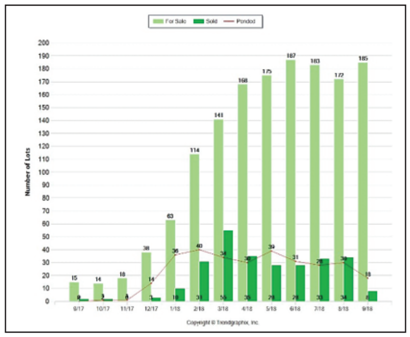
Getting the Dirty on Lot Sales

By Jeff Schween, Pacific Union International

Land is valued in many different capacities for not only its location, but its composition. The proximity of land to a desired place creates value while the underlying component or natural resource that exists below it may bring even greater worth: water, oil, gold, diamonds and so forth. The scale of a property impacts its' use and capabilities as does the maltreatment of it by man-made deposits of toxins being left behind thereby rendering it not only temporarily unusable but also creating a costly liability. Some say the basis of all wealth is land, but the creativity brought to any particular plot will truly unlock its greatest potential.

According to BAREIS MLS, as September concluded, Sonoma County had exactly 504 non-commercial parcels on the open market - 71 of which were newly exposed to the market during the month. Sonoma County saw 46 lots receive accepted offers during the period while another 22 parcels formally traded hands – at a median value of $298,000 – now tracking closely to the fifteen-year running average of 20 sales per month. This shows waning strength in this sector of the market from where it has been since last December and with supply currently outweighing demand we may see values for dirt come into a range more palatable with buyer's interests over the next six months.

Specifically, within Sonoma County, Santa Rosa's Northeast quadrant (see graph) has been the primary catalyst for the increased activity levels. Due entirely to what transpired last October, the Tubbs fire has reshaped the landscape and the marketplace as we know it. The region was showcasing 185 non-commercial parcels on the open market as we wrapped up September – 1,133 percent more than last year as well as the historical average of 14 lots at any given time. New offerings from sellers accounted for 42 of those during this month. September buyers captured 18 new contracts on parcels – well above the historical average of two per month - while sellers concluded just eight sales during the period – a tremendous fall in purchase activity from the prior 10 months rate.



As the volume of offerings and transactions stack up we see measurable data points appear. In Northeast Santa Rosa, the average price paid for a lot in September was $283,000 while the median price hovered at $298,000 – median is the midpoint of all sold properties where by half sold for more while the other half sold for less. In a market as liquid as we are encountering, even though the average number of days to sell a parcel has climbed to 80, the only thing keeping the dirt from transacting is the price being asked by the seller. This is a common theme in basic economics – a seller sets a price, but a buyer establishes the market value.

Less buoyant activity can be seen in Northwest Santa Rosa – the second most impacted by the fires where there are many fewer sellers than across town in Northeast Santa Rosa. September witnessed sellers adding only five new offerings while buyers in waiting placed an additional three lots into contract leaving 25 properties available to open with in October. The average price paid for dirt in this region during the month was $235,000 while the median value rested near its seven-month static point of $210,000 – albeit on a sample size of only three sales being completed there is not much value in these current metrics.

Along with this, as more parcels make their way to market, another metric comes into play – the elasticity of demand. This is the measure of the change in the quantity demanded or purchased in a product – vacant land in this case - in relation to its price, or required adjustment of such, so that it finds a willing and capable buyer.

As this new paradigm evolves we anticipate values on lots to be more closely associated with the effective cost of the newly built home that rises in its place. A rule of thumb typically used by investors is that no more than 15-20 percent of the value of the total combined asset can be assigned to the underlying cost of the dirt. This means for a $1,000,000 home a builder or investor should be reluctant to pay more than $150,000 - $200,000 for the lot the home will sit on unless there cost to build is below market costs. With the rising costs of construction, these market forces may diminish the value a willing buyer may place on the parcel they are seeking – expect lot prices for most lots to fall in line with market requirements before being transacted on.