A Second Home Could Be Your Best Retirement Plan Investment

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The Baby Boomers, approximately 77 million people or 28% of the US population will begin life as retirees over the next few decades. If the past three decades are any indication of the future, these new retirees will flock to resort communities and college towns and pursue their predecessor's passion for ownership of second homes, vacation homes and retirement homes. Most importantly, as the boomers increase the demand for real estate in such towns and communities, the demand for quality residential property will grow and prices will certainly follow suit.

Momentum Investor and Contrarian Investor Opportunities

Despite the often touted recent "national" housing downturn, some parts of the country have been remained largely unaffected, where growth is maintained and boomers continue to purchase second, vacation and retirement homes. Bad news sells, and may be that is why we only here about what is going wrong in the housing market. However, the real experts are quite aware that housing market conditions vary considerably across the country and are by and large a regional phenomenon.

For example, while growth has slowed a little, in general the Carolinas is by no means experiencing a major housing slow down and many cities have continued to experience modest, although consistent, housing appreciation year after year. Because of steady job growth and projected regional economic activity throughout the region, in general, residential real estate is expected to appreciate time and again for the foreseeable future. Investing once an established and predictable trend has been identified is characteristic of "momentum" investors. Likewise, the Carolinas offer an almost sure bet for the "momentum" investor in residential real estate and in particular, second, vacation or retirement homes going forward, where modest and predictable housing value appreciation is almost a given.

On the other hand, some regions of the country have experienced deep declines in housing values over the past few years and in some cases, still in the process of recovery. In many cases, these are the regions of the county that experienced an extraordinary run up in housing values prior to early 2006 only to experience the steep declines that followed. For example, Florida, and Southwest Florida in particular, experienced double digit appreciation as recent as 2005. However now, many properties are at 2001-2002 price levels. Buying at the very lowest perceived price point, as close to the bottom as possible, when everyone else is selling, is characteristic of the "contrarian" investor. We believe Florida, and in particular, Southwest Florida, represents an incredible buying opportunity for the contrarian investor.

History has proven time and again that the real estate market always rebounds and where prices throughout the cycle have declined the most, is where the most opportunity exists. Despite the other players in the retirement destination market, For many reasons Florida will always capture a significant portion of the endless stream of retirees and for the true contrarian investor this is precisely the time when the amazing profits are made by making investments in second, vacation or retirement homes.

Factors Affecting Second Home Growth

It wasn’t long ago that a second home or vacation home was strictly considered a luxury item. However, today a large number of people are realizing it isn't so much a luxury item as it is a sound real estate investment. While recent studies indicate that more than 30 million Americans are expected to enter the second home market in the coming decade, there are potentially 100 million people worldwide that are expected to do the same. The cheap dollar, together with the recent housing downturn and resultant price reductions, have lured many European, Asian and South American buyers to our shores and many of the most popular locations, existing inventories are being reduced and shortages of available homes for sale are quickly developing. Based on projections the trend is likely to continue strong throughout the next decade and for these reasons alone, an investment in a second home or retirement home could be the best investment you and/or your self-directed retirement accounts(s) could possibly make.

Going forward, there are a variety of factors that have and will likely continue driving second home prices to new heights. The following includes just a few of the influential factors include contributing to the next market surge:

- Demographics
- Investment diversification
- Ease of second home mortgage financing
- Growing demand for recreation and quality time
- NIMBY (Not-in-My-Back Yard) movement

Demographics

Demographic changes have in the past contributed to second home demand and will likely continue to do in the future. While there are second home buyers of all kinds, middle-aged heads of households have predominantly made second home purchases in their prime earning years. Over the past decade the number of households headed by 45-54 year olds has increased 46 percent (From 14.4 million in 1990 to 20.7 million currently), and this population segment has significantly contributed to the rise in the number of second homes. Specifically, the Baby Boomers who drove up housing prices during the past two decades are now entering the second home and retirement home market in vast numbers are expected to continue entering the second home market until past the year 2020.

But it’s not just boomer demographics that must be considered. Senior citizens are today experiencing better health and increased longevity and are also stimulating demand for second homes. Moreover, the demand for second homes has been growing and is expected to increase from the post-boomer generation as well. And among this group, second home ownership is quickly emerging as a trend-setting status, an investment that also provides the utility of reducing stress and a setting for family quality time. No doubt, this group will grow in numbers and continue to fuel the demand for second homes and as such, push up housing prices in many desirable locations.

And Americans aren’t the only ones who are increasingly attracted to second homes for investment and otherwise. The dollar’s dwindling value together with an already steeply discounted market have encouraged waves of foreign investors to include the British, Irish, German, French, Japanese, Chinese, Dutch, and Canadians, to jump on the second home bandwagon. The affluent citizens of many countries are busy seeking what their American counterparts are seeking namely, a place to enjoy recreation and retirement as well as a sound investment.

Diversification of Investments

To insure personal financial security, Baby Boomers, like everyone else, must find ways to make their money grow. In this effort, scores have turned to the stock market, but for many, the financial market returns have proved uncertain or have been a grave disappointment. Many are beginning to realize that in order to save for retirement, or for that matter any other purpose, a more active part in the investment process is required and to that end, today’s investors are looking for investment alternatives and real estate and more specifically second homes do represent a sound alternative going forward.

Ease of Second Home Mortgage Financing

It wasn't long ago that most mortgage lenders showed little or no interest in financing second homes. Fearful of defaults, disinterested lenders either refused to make such loans or applied such stringent requirements that would be buyers were quickly discouraged. Today, primarily due to very stiff competition between lenders, things are quite different and the financing conditions for second homes have changed for the better. Although some limitations still exist, especially if you plan to treat your second home as a rental, securing a mortgage on a second home is far easier and less costly than ever before. As competition increases between lending institutions for borrowers, there is no doubt that the ability to finance a second home purchase will be even easier in the future, further fueling the second home trend.

Growing Demand for Recreation and Quality Time

With all the stress modern life brings, people need their quality time. More than ever before, Americans are working harder and longer and all with added stress and anxiety. The facts are that the lifestyles, attitudes and need for quality time of many Americans as well as many worldwide, are pulling them toward the purchase of second homes for rest and relaxation. It isn’t likely that the stresses of everyday life will not subside any time soon and the incentive to own a second home to provide a needed getaway to provide rest and relaxation should be with us for the foreseeable future.

Not-in-My-Back Yard Movement

In many communities throughout the country today, taxpayers and homeowners are committed in their refusal to pay the costs of growth. In response to this community outcry, civic, environmental and the assortment of special interest groups have sprung up to organize, raise money and ultimately defend the wishes of their supporters to transform “stop growth” policies into law. The “not in my back yard movement” use catchwords words like “green space,” and “managed growth, but what is really sought is a complete halt on development. If the past is any indication of the future, real estate development faces an uphill battle from here on out. This will especially be the case in many popular and desirable areas. Inexpensive land is quickly becoming a thing of the past and higher development costs will further fueling the price of real estate and the second home trend.

Second Homes and Retirement Plan Investments

Given how the current trend is expected to continue, if you have thought about buying a second home or retirement home, it may not be wise to wait much longer before acting, as many desirable properties, especially in communities largely unaffected by the housing downturn of late, are being snapped up quickly at bargain prices. This means that your piece of paradise may no longer be available be so exorbitantly priced by the time you retire. Now is the time to buy.

Of course, the decision to invest in a second home is be followed by how to fund the purchase. Certainly, if you can afford to buy a second home by simply writing out a check for the full price, that’s great. But, for the vast majority, paying the full price out discretionary funds is not an option.

One of the first funding methods to consider is to tap into the equity of an existing primary home. This method of funding a second home purchase could take the form of refinancing an existing home loan or taking out a home equity line of credit. This method works very well if you are able to handle the higher payments that would result. Even if you expect to rent the second home out on a seasonal or full time basis, for those working with a tight budget there may be no room for periods of vacancy if you expect to make loan payments based on the expectation of rental income. If this option is not for you, don’t let a lack of capital dissuade you from making the investment because thanks self-directed retirement accounts, you can use retirement funds today to purchase your retirement home. And you don’t have to take a distribution or pay any taxes or penalties to do so.

Use of your self-directed retirement plan as a funding source, in part or in full, could be just what the doctor ordered. A self-directed IRA, SEP, 401(k) or collective self-directed retirement accounts may already have the funds needed in full to make the investment. Moreover, partnering in property investments can be accomplished quite easily. Second home ownership interests can be accomplished between you and other individuals (friends, family, partners, associates, etc.) as well as other people's retirement accounts. In a "partnered" arrangement with other individuals and/or other people's retirement accounts, each investor entity would own an interest in the property. Self-directed retirement account(s) offer a lot of flexibility in structuring the investment. The mix-and-match of retirement accounts and personal funds from multiple entities in such ownership arrangements are typical when there are budgetary concerns. While the law permits such arrangements, it is important to discuss this possibility with your selected self-directed retirement plan custodian up front, since each custodian does not offer the same account flexibility. Fortunately, the custodians we work with do permit and are very experienced with the facilitation of such ownership arrangements.

Self-directed accounts offer considerable flexibility in purchasing a second home. But remember, in order to stay within the IRS rules, if your retirement account holds title to the home, owners of the account(s) can not occupy it until the property is distributed to from the account(s) to the respective account owners. However, in the interim, the property can be leased to qualified parties and rental income can be earned. Your self-directed retirement plan custodian is well versed on the rules that need to be followed and will in part them to you before the purchase is made.

In this regard, all income is distributed according to the proportional ownership interests in the property. Specifically, all income attributed to self-directed retirement account ownership interests is invested right back into the respective retirement account to grow tax-deferred or tax-free, depending on the account type. Moreover, all income attributed to personal ownership interests, would be directly distributed to the respective individual owners. Likewise, all expenses are paid according to the proportional ownership interests in the property. Specifically, all property expenses attributable to the ownership interests of the retirement accounts are paid directly by such retirement accounts according to their respective proportionate ownership interest and all expenses attributable to the ownership interests of individuals are paid by such individuals according to their respective proportionate ownership interest.

A second home investment in a desirable location could benefit greatly from price appreciation over time and depending on the retirement account(s) type, could be available completely tax-free when you retire. Moreover, once the property has been distributed, it essentially remains a viable long-term investment together with added utility of the ability to be occupied for your own personal use.