I'm far far from being a financial genius. i try to get partners who run the numbers and deal with details. My business strength is in understanding where technology is going (in the areas I pay attention to), what the business applications of that technology are and most importantly, how to sell them.

Thats a polite way of saying that I'm not a details guy.

I mention this because as they say, "The Devil is in the Details", and I have no idea how to make happen what I'm about to propose. Nor do I know if there are specific laws or common sense "rules of the marketplace" that make this idea just plain stupid. Who knows. What I do know is that I'm curious about whether this would work and there is no better way to open an idea to criticism or support than by posting it on my blog. So here goes.

In the residential real estate world, the concept of buying a house is simple. You pick the house, negotiate a price, then agree to a payment arrangement.

The payment arrangement options are pretty straightforward.

You can pay for it with cash.
You can borrow money to pay for whatever amount that you cant or choose not to pay on the house. The payment terms are then set between you and the lender

This has worked well for a long time. A successful purchase of the house can be quickly defined as being able to make the payments you have committed to make, under the terms you have agreed to, until the house is paid off, all while gaining the utility of living in the house.

The problem with this approach is that when things go wrong and you can't make the payments the "solutions" are very binary.
1. You find a way to make your lender happy.
2. Your house is sold in an effort to satisfy your debt to the lender.

The binary nature of residential real estate financing also lends itself to being an attractive market for "sharks". We dont call the houses we live in "assets", we call them homes. They are very personal and important to us. Which in turn clouds our judgement. People who are at risk of losing their homes get desperate and take measures that aren't necessarily in their best interests just to save their homes and their families from grief.

There has to be a better way to protect homebuyers on the downside.

Lets contrast the financing process of individual homebuyers with funding in the business world. Businesses have any number of ways of raising capital for corporate purposes but they basically can be boiled down to two:

They can raise money via debt.

They can raise money via equity sale.

Debt resolution in the business world is just as binary as it is in residential real estate. If you can't pay the debt, you get foreclosed on and everyone probably goes home unhappy.

Which is exactly why , rather than borrowing money, most startups and growing businesses turn to the equity sale of some percentage of their company to raise capital. Need confirmation of this ? Look at the number of bonds available on national exchanges vs the number of stocks for sale on exchanges . The number of stocks is far greater than bonds and thats on the listed exchanges. Throw in the OTC and Pink Sheet markets and the numbers dwarf debt offerings even more dramatically.

Which leads to the question of…

Why can't home owners sell some percentage of equity in their homes on a listed exchange ? Why can't I
"Take My House Public ?"

Why not create a market or exchange where homeowners can sell equity in their homes ?

The rules could be very eimple
1. The house is appraised by a company approved by the exchange that lists the houses.
2. "Shares" are set with a Par Value of 10pct of the appraised value. For a 100k dollar house, there are 10 shares potentially available. However at no point in time can more than 40pct of the "shares" in a home be sold. We dont want the opportunity for "hostile takeovers"
3. The price of the shares will of course be set by the market. In a hot market it will be set above par, in a tough market like today, it will sell below Par.
4. All Proceeds from the sale of shares MUST be used to pay down any debt on the home.

This is the key element of this approach. By selling equity in a home, the buyer gets an asset based security that will move up and down with the market. If this market is big enough, there should be enough liquidity to move in and out of positions.

The seller receives cash that can be used to pay down the debt and thereby reduce his/her monthly payments. The seller loses a part of the upside if the market for the home improves and prices go up, but thats a small price to pay for not going into foreclosure.

Beyond creating liquidity options for individuals in the housing market, which i think is a good thing, I think this will also reduce the volatility in the market. Despite the best efforts of the residential Real Estate industry, no one ever really knows what their house is worth until you try to sell it. This exchange listing approach will certainly make for better information available for the market, which in turn will also reduce the volatility.

It will also increase the options of homeowners who have paid off their homes to acquire capital for personal uses. If a homeowner has completely paid off his/her home and wants to raise money for whatever purpose, a vacation, a car, education, whatever, rather than taking on debt , they could get their home appraised, have the
option of selling equity in my home that I would not be obligated to pay back. An option that would create a significant flow of capital back into the hands of consumers

How can this actually come together ?

It wouldn’t be easy. It would probably take the country’s biggest banks working together to create an exchange that develops the public market for home equity one city or region at a time. They would have to identify a means to safely set values so that Post IPO price the share pricing was stable. There would have to be provisions set for what happened when a home was sold. Shareholders would have to be paid their share of the salesprice upon closing.

There are thousands of things that i haven’t thought of that would make or break this idea, but I think at its most basic, the concept is sound. However one thing I am sure of, this approach would reduce the Boom Bust cycles of residential real estate and the dramatic impact they have on our economy