



Where will real estate bounce back fastest?

Prices have hit bottom in some cities and are heading back up, but recovery rates vary. Here are the places with the best prospects.

By Matt Woolsey, Forbes.com



When it comes to real estate, the questions on everyone's lips are: How low is low, and when's the perfect time to buy back in?

That moment has passed in Seattle and in Charlotte, N.C. Both metro areas hit bottom in the first quarter of 2006 and have since posted price gains of 12.3% and 6.3%, respectively, according to National Association of Realtors (NAR) data.

Ripe for investment? Philadelphia and New Orleans. Based on housing inventory and local economic conditions, both should hit price troughs by year's end and bounce back with moderate gains of around 4% in 2008.

In markets expected to recover more slowly, such as Boston and Denver, low buyer confidence coupled with a surplus of housing stock has lengthened the slump. NAR chief economist Lawrence Yun points out that buyers are looking for clear signs of a market bottom and are content to wait on the sidelines until then.

It's easy to see why. Most of the country's real-estate markets are feeling the effects of overproduction. A strong market hovers near a 1.5% vacancy rate, but the national average currently stands at 2.8%, and in cities such as Miami, Atlanta and Denver, figures hang around 3.5%. In addition, every nugget of good news (like the May Commerce Department report that said new-home sales are at a 14-year high) comes with bad news (median price growth is at a 10-year low).

So which other metro area markets stand the best chance of recovery, and when will that upturn occur?

Behind the numbers

Market corrections follow three basic recovery patterns: a V-shaped recovery where a market experiences a sharp, fast decline but comes out strong once it hits bottom; a U-shaped recovery, where prices decline gradually and recover slowly; and an L-shaped pattern, a hard, fast fall with a paltry price bounce-back after the market trough.

The differences between a V-shaped market and a U-shaped one have to do with barriers to growth. High vacancy rates and high investor share can hurt a market, but if the local economy remains strong and housing stock affordable, it's only a matter of how long it takes to absorb the excess inventory.

Tampa, Fla., is a perfect candidate for a V-shaped recovery, according to research from Moody's Economy.com, an economic analysis, forecasting and credit risk firm in West Chester, Pa. The local economy remains strong, and subprime lending is relatively low. Tampa's problem? A high investor share that led to high vacancy rates. When the market turned sour in 2005, more than 25% of Tampa homes were owned as investment properties. Investors are quicker to flee during a downturn, thus creating a glut of available housing stock. In Tampa's case, vacancy rates now stand at 3.5%.

"As investors exit, the market revives," says Mark Zandi, chief economist at Moody's Economy.com, as fewer speculative buyers result in a more stable market. "Tampa's a pretty affordable market, and first-time buyers can come in once prices fall."

Based on Moody's Economy projections, Tampa should burn off its excess inventory and hit a price trough in the first quarter of 2008, at which point prices are expected to increase by 10.6% the following year.

These projections take into account housing affordability, vacancy rates, the strength of the local economy and job market, investor share in 2005 and the share of subprime mortgages. Data are from Moody's, the Bureau of Labor Statistics and the Federal Reserve.

Predicting the bottom of any asset market, especially real estate, is a difficult thing. While these projections are based on sound data and advanced modeling by Moody's, no one can predict futures markets with absolute certainty.

Other bounces

Like Tampa, Phoenix is afflicted by high investor share (26.1%), and it has a vacancy rate of more than 3%. Good affordability rates and a surging job market suggest that once Phoenix bottoms out, price growth will be strong. Moody's projection model has

Phoenix reaching its price trough in the fourth quarter of 2008 and then growing by 7.7% the following year.

Slower recovery rates are expected in markets such as Minneapolis and Boston, where a slumping local economy, slow job growth and negative migration numbers hamper long-term prospects. Along with other U-shaped markets, like Sacramento, that have double-digit subprime lending share, Zandi says it's going to be harder for these markets to get going again.

That doesn't necessarily mean V-shaped markets are in the clear. The labor markets in cities such as Las Vegas, Phoenix and San Diego, whose future economic success will be critical to recovery, are heavily in housing-related industries, according to Moody's. So long as those economies can weather their respective corrections, they should be all right.

"These markets are going to experience more substantial declines in the coming year," says Zandi. "Gauging the bottom is a very intrepid affair, and the job market is very important to recovery."

Real-estate markets with the best prospects for recovery

Rank	Market	Expected market bottom	Est. price appreciation after bottom
1	Tampa, Fla.	Q1 2008	10.60%
2	Phoenix	Q4 2008	7.70%
3	Las Vegas	Q2 2009	7.20%
4	San Diego	Q2 2008	5.30%
5	New Orleans	Q3 2007	4.30%

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