Housing – 25 February 2010

Housing upturn proves elusive

WASHINGTON – Feb. 25, 2010 – The rest of the U.S. economy may be bouncing back, but for the battered housing sector, the hopes of economists and real estate experts are still modest.

“Recovery is probably too strong a word,” First American Funds Chief Economist Keith Hembre says of recent housing data. Call it “stabilization at a lower level.”

Home prices and buying activity are coming back, but only from a disastrous 2009. In the first quarter of 2009, for example, the Standard & Poor’s Case-Shiller National Home Price index dropped 19 percent from the year before. In the last quarter of 2009 – for which data were released on Feb. 23 – the index was down just 2.5 percent from the year before.

“We’re showing signs of the housing market bottoming,” says Michael Strauss, chief economist at Commonfund. “The bad news is we still have a long way to go.” The widely watched S&P Case-Shiller 20-City Composite Home Price index rose 0.3 percent from November to December. But the figure only increased when adjusted for the winter slowdown. Without a seasonal adjustment, home prices fell 0.2 percent from month to month.

Government support to end

Improvements have occurred only after extraordinary efforts by the U.S. government to prop up the housing market. To lower mortgage rates and heal financial markets, the U.S. Federal Reserve has been buying up to $1.25 trillion in mortgage-backed securities. To bring more buyers to market, Congress approved, and then extended, an $8,000 first-time homebuyer tax credit.

“Even with these dramatic efforts to bolster home sales, they’re still languishing at recessionary levels,” says David Rosenberg, chief global economist at investment manager Gluskin Sheff & Associates.

And now comes 2010’s big test for the housing market: The Fed’s mortgage buying will end at the end of March, and the homebuyer tax credit expires at the end of April. What happens without government support?

“I see no evidence that this is a sector that has the capacity to stand on its own two legs,” Rosenberg says. Real estate professionals are worried, too.

Earl Lee is president of Prudential (PRU) Real Estate, which has 2,000 franchised real estate offices in North America and employs 62,000 real estate agents. “The first half of the year will be strong,” Lee says. “The question is what will [the second half] look like.” Without government support, he adds, “the economy is still not strong enough.”

Bright spots

There are bright spots in the housing market, and they're often in places hardest hit by the bursting of the real estate bubble. In December's Case-Shiller data, only five cities did not see prices decline before adjusting for the season: San Diego, Las Vegas, Los Angeles, Phoenix, and Detroit. In the upscale Detroit suburb of Birmingham, M. Michael Cotter, a real estate broker at SKBK Sotheby's International Realty, says he has seen a "rather substantial improvement" in the housing market in the last three months. After local giants General Motors and Chrysler declared bankruptcy last year, Detroit's already weak real estate market fell into the doldrums.

Now, "there is optimism that we didn't have a year ago," Cotter says. Though conditions could be much better, he says, "the economy is starting to right itself."

Crucial for the housing market in 2010 is the jobs picture and the amount of homes coming onto the market. "At 10 percent unemployment, it's difficult to think Americans are going to be out there on the market for homes," says Brian Levitt, an economist at OppenheimerFunds. The U.S. unemployment rate was 9.7 percent in January, and economists expect it to edge up to 9.8 percent in February.

Foreclosure supply

Another concern is how many foreclosed houses will be pushed onto the market in 2010, flooding markets with unwanted supply. "There is a fair amount of shadow supply waiting in the wings," Hembre warns.

A Feb. 16 analysis by Standard & Poor's estimated the number of troubled mortgages "will likely take about 33 months – or nearly three years – to clear at the current rate of liquidations."

A recent slowdown in foreclosed homes is temporary, the report said. The state of the housing market has large ramifications for the rest of the economy. Home Depot (HD) Chairman and Chief Executive Francis Blake often notes the impact of residential real estate spending on his company's business. After the No. 1 home-improvement retailer reported earnings on Feb. 23, Blake told analysts such spending "has stopped its dramatic and historic decline." However, he added, "the housing industry remains at distress levels, mortgage defaults continue to increase, unemployment remains high, and our pro customers" – contractors who buy supplies at Home Depot – "are still under pressure."

Sales of furniture, appliances, and electronics all are linked to housing, economists note. And home prices can weigh on consumer confidence, which unexpectedly fell on Feb. 23 to its lowest level since April.

"It will be very difficult to have a strong economy without housing kicking into gear," Rosenberg says.

Action Economics Chief Economist Michael Englund is not so gloomy. He says housing is "on a slow but steady recovery," driven in part by the natural life cycle as people form families, move up, and retire and downsize their homes. After the rough conditions of 2009, "my assumption is we have nowhere to go but up from here," he says.