THE Independence Voice

From: MARK SPRAGUE, ITC State Director of Information Capital

By now it is apparent that the real estate recovery is in full effect in most areas, and that means more of you are hopping off the fence to buy or list a home. To say that the housing market is a different place than it was just six months ago is an understatement.

So what has changed?

Homes and real estate in most channels are more expensive

If you have not been paying attention to real estate trends, then you may not be aware of the dramatic gains in real estate and housing over the last six months. The improving national and regional economy and low interest rates have boosted buyer demand in most markets, decreasing supply and raising prices. Case-Shiller and many housing indices have show a remarkable increase of values from 10 to 12%. The national median home price was $214,200 in June, up 13.5% from June 12, the sixteenth consecutive month of home price increase.

Not only has limited supply forced values up, but land, materials and labor continue to see strains on supply due to the new demand, again particularly in Texas where we see competition from the oil shale plays for labor and materials.

With present pressures on inventory on resales in Austin, San Antonio, and Houston we are looking at 6-12% annual appreciation for the next couple of years due to lack of inventory. Before you get all excited remember a lot of this appreciation is catch up to the recessionary years.

This can be challenging for consumers as incomes are not keeping up with that appreciation. Consumer wages have not increased in line with values and they traditionally do not in a strong real estate markets.

Rents are rising as more consumers enter the market

There is shadow demand in the rental market—the 3 to 5 million people, mostly in their twenties and thirties, who have been riding out the shaky economy by moving back in with their parents or staying with friends. Household creation has been very low over the past several years. There is a backlog of at least 500,000 consumers who would love to buy or rent on their own. That is a lot of demand, with little to no supply available.

We here in Austin are familiar with the term ‘doubling up’, where more than one couple may be sharing a home as their friends move here looking for employment. Other Texas metros have not seen as much of this. Now, as they start to get jobs, they’re looking for their own apartments. Housing analysts forecast that they represent a pent-up demand for rentals that’s twice as big in percentage terms as the country has ever seen.

This year, average rents have been rising nationally at about 4% a year and in many metro areas by 7-9%. A recent Zillow analysis also found that buying beats renting in close to 60% of markets after three years or less.

Reports from FNMA and FHA predict that growth in demand for single-family homes next year will likely be driven by first-time home buyers. That trend is visible in an NAR survey of buyers and sellers released in

November. 39% of borrowers were first-timers, up from 37 percent in the 2011 survey. So the 'myth' of young people not wanting to own is just that…..there is a need for an offering for entry level buyers.

The cost of loans is getting higher

After bouncing along at record lows in 2012 (the lowest in over sixty years), interest rates are beginning to rise in 2013. Just how much is really anyone's guess. But the Federal Reserve (who sets borrowing rates) has said that they will begin to ease rates higher as the market strengthens. Most analysts wouldn't be surprised if rates hovered between 3.5% to 4% for much of the year, barring any big changes in the overall economy.

The costs associated with securing some loans are rising, as well. The Federal Housing Administration (FHA) last spring once again increased its one-time upfront mortgage insurance premium for minimum down-payment loans (less than 5% down) to 1.75% of the loan, while raising its annual monthly premiums to 1.25%. This year, the discussion is to raise those premiums again. The Federal Housing Administration Fiscal Solvency Act of 2012 gave the FHA authority to raise premiums to as high as 2.05% annually to build and maintain its reserves, which are at record low levels. If that happens, the increase would tack an additional $133 onto the monthly payout for a $200,000 loan. Again most analysts don't expect small increases to deter many buyers from the FHA's low down-payment loans. Many people just don't have enough cash tucked away for a conventional loan. If you are looking at making less than a 10% down payment, your options are limited to the government backed loans.

Supply is bottoming out

Rates are great, but there are a lot of houses for sale in most price points. Nationally, the inventory of existing homes for sale at the end of November was down 3.8% from the previous month to 2.03 million. Nationally that represents a 4.8-month supply at the current sales pace and is the lowest supply since the go-go market of fall 2005. Listed inventory is down 22.5% from a year ago, when there was a 7.1-month supply.

In Texas it is a tighter market with Austin at 2.9 months, San Antonio with 5.1 months, Houston at 3.3 months and DFW just over 3 months supply. All are considered 'seller's markets' (the dividing line between a buyer's or seller's market is six months of supply). The problem is, prices haven't gone up enough to enable many homeowners to sell and recoup enough to put down on a move-up home. Also, the banks are funneling more of their distressed sales to investors as rental properties. The lack of listings should begin to change sometime this year as pent-up demand, historically low interest rates, and slightly higher home prices prompt more move-up buyers to list their home and move up or down. However, for the foreseeable future, if home shoppers see a desirable property, they should move quickly, because in this tight market they can be sure that someone else will.

New mortgage and banking rules will protect buyers from shady lenders

Many laws have been passed to head off another financial crisis, including Basel III and the Dodd-Franks Act. Through Dodd-Franks, the government set up a consumer watchdog, the Consumer Financial Protection Bureau (CFRB), which recently announced a new rule to ensure that prospective buyers are actually able to repay their mortgage. The Ability to Repay Rule, which officially takes effect in January 2014 but will be put into place by most lenders sometime this year, protects consumers from risky practices such as "no doc" and "interest only" features that contributed to so many people losing their home in recent years. "When consumers sit down at the closing table, they shouldn't be set up to fail with mortgages they can't afford," said CFPB Director Richard Cordray.

The new rule, part of the 2010 Dodd-Frank financial-reform law, requires that borrower's financial information — employment status, income, assets and debt – be supplied and verified by lenders, thereby eliminating no- or low-doc loans. That information, including debt-to-income ratio, must be used to prove that the borrower has the ability to pay back a loan. In addition, the aforementioned acts and laws will force conventional loans to require more down payment and the banks to have more capital on hand as well as require the borrowers to but larger down payments down on conventional loans.

There are fewer distressed home bargains

While the number of distressed homes is still fairly high at 2.3 million units, according to CoreLogic, fewer of these homes are coming to the market. One reason is that almost half of those 2.3 million homes are still seriously delinquent but haven't been taken back by the bank because of a backlog in processing. Many of the states where you are seeing foreclosures are judicial states where the foreclosures of three years ago are just now coming to the market.

Many realtors, investors, and consumers thought the trend of short sales would stay around for a while. But with an improving national economy, many lenders are giving new opportunities to distressed homeowners to stay in their properties. They are even offering principal reductions to their loan balances as opposed to going the short-sale route. Here in Texas foreclosures and short sales have been a small portion of our regional marketplace, historically less than 2%. That said, foreclosures in you neighborhood are never a positive thing. And they usually happen in clusters, affecting specific neighborhoods more than others.

Most of the large banks and lenders have sold the majority of their REO's. 2011-12 saw a large number of foreclosures sold en-masse to investors, rather than listed for sale to individual buyers. When they make it back onto the market with a little face lift, they aren't such a bargain anymore. Many of those portfolios of single-family bank-owned homes are being brought back to the market as rental properties. These big portfolios of homes are attracting the big guns, including national real-estate investment trusts (or REITs) that are expected to buy tens of thousands of properties over the next few years. Most are driven by discounted and truly distressed markets. That just has not been the case here.

The chance to snap up a bargain-basement foreclosure has faded. Sales of those homes fell to about 11 percent of all sales in June 2012, down from about 30% of the national market in March 2011. Helped In part, because the Federal Housing Finance Agency (FHFA), the Federal Deposit Insurance Corporation, and banks have been selling off hundreds of distressed home loans in bulk to purchasers who agreed to work out new terms with borrowers rather than simply foreclosing. Foreclosures have also dropped because the equity position of thousands of borrowers has improved with rising home prices, righting many upside-down loans.

That's great news for sellers, who have seen their neighborhood property values hammered by bargain-basement bank sales. But it's meant rising prices for buyers as inventory has dwindled.

More new home construction is coming

With existing homes in short supply, there is an opportunity for builders. They are desperately trying to address the market by putting as many new homes as they can. However a lack of desirable lots and short speculative lines at banks is holding them back. New housing starts have risen a whopping 27% from the same time last year. Record-low interest rates and an uptick in hiring spurred the increased activity by builders. New-home sales are up 15.3% over the past year, hitting an annual rate of 377,000 in November, according to Census Bureau data. After years of building inactivity and a lack of turn-key homes on the market, many buyers are welcoming the chance to buy new and have it their way.

New-home prices, however, are being forced to move up faster than prices for existing homes. The median price of a new home in the US rose to $246,200 in November, a 15% increase from the previous year. Greater supply in the months ahead, however, could ease the pace of future price increases, but don't count on it. Higher home construction costs will continue. Building materials like sheet rock, lumber, and copper are at high prices even though levels of home construction remain low. The same is true for construction labor costs—after the crash, many qualified construction workers migrated out of the country or into other industries. As a result, you've got the possibility of some pretty potent price increases in the cost of constructing new homes, again with competition for that labor from the energy sector here in Texas.

The luxury market continues to be slower

Nationally, regionally, and locally sales of homes over $1 million surged 51% in November 2012, as high net worth owners rushed to list their existing homes and buy new ones to avoid the capital-gains tax hikes in January that were part of the fiscal-cliff deal. Under these changes, high income earners would pay $88,000 less in taxes if they made a $1 million profit on their home in 2012 rather than in 2013. So, out went the for-sale signs, and down came the inventory of luxury homes in the last quarter of 2012.

We have seen this in our own Texas metros, where luxury listings are slower. Think about it, most of these consumers do not have an urgency to sell if they cannot get the values wanted or needed. And there is the issue of a much smaller demand market for these opportunities (not everyone can live the million dollar lifestyle).

Publicly traded Toll Brothers, which specializes in the luxury-home market, saw its sales contracts jump 60% in the fourth quarter from the same period last year — the highest level since the red-hot market of 2005. However, due to the dwindling supply of luxury homes in many markets and the huge number of buyers who took the plunge last year, analysts have seen and predict a bit of a slowdown in luxury-home sales during the rest of this year.

For those shopping for a high-end custom home, it means less to choose from, but also a lot less competition. Of course, the drop-off in demand probably won't last long. More and more big-budget international buyers are continuing to invest in U.S. real estate, particularly here in Texas.

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