

Where Are We In The Cycle?

Austin 3Q13 report and forecast

Slides available at www.independencetitle.com/blog

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History of the Financial Crisis

Markets Chart of the Day

History of the Financial Crisis: Mid-2007 to 2010



SOURCE: BLS, BEA, U. MICH.

4

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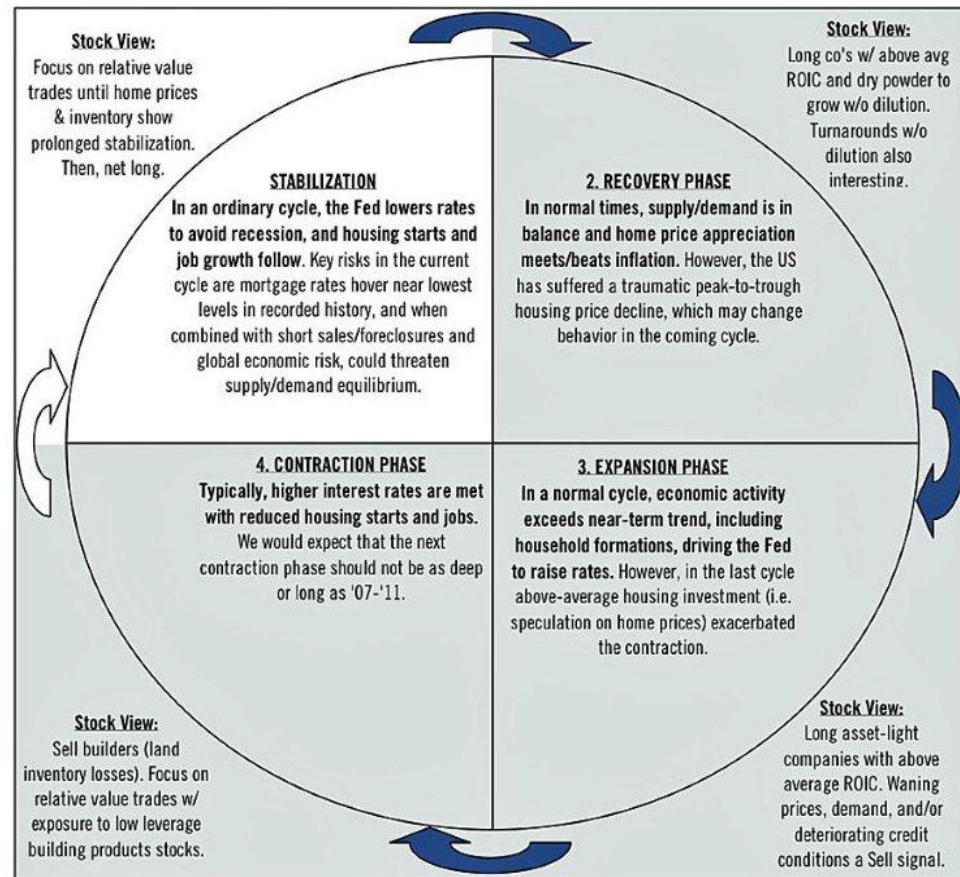


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Where are we in the cycle?

Position in Homebuilding Cycle – Transitioning from Contraction to Stabilization?



Source: Citi Investment Research and Analysis



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Where are we, and where are we going?

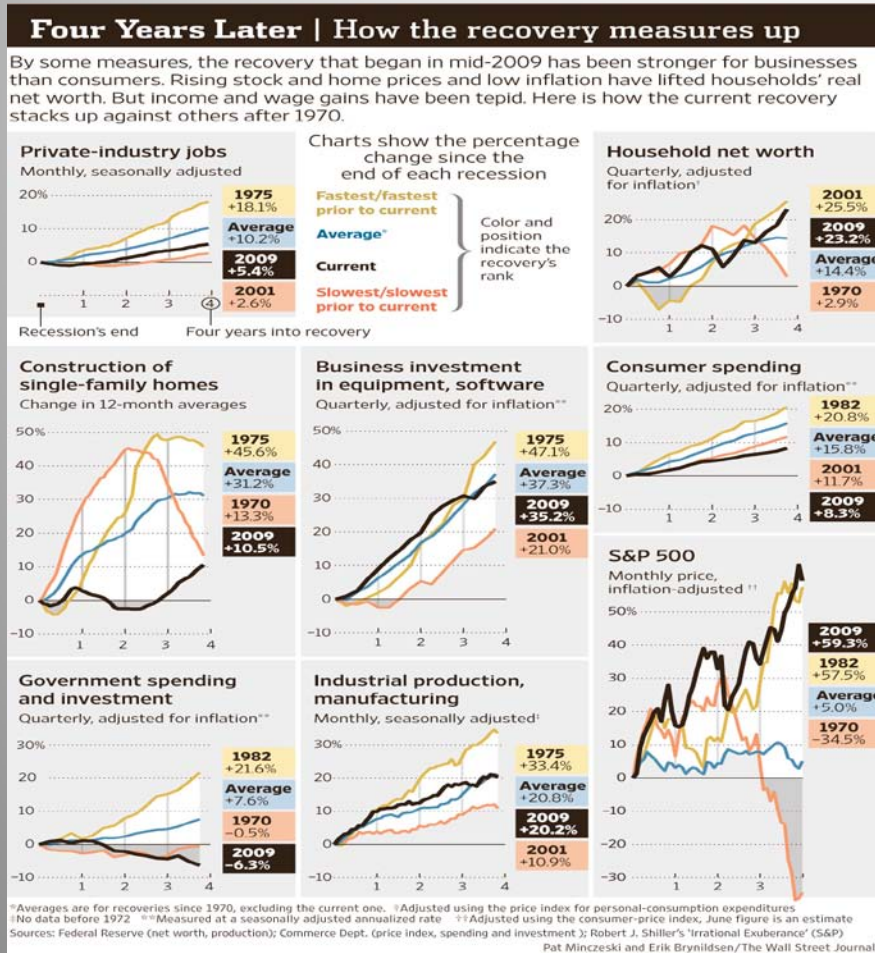
- National rebound started in 2011, slow progress 2012, 1st 8 months 2013
 - Austin and other major Texas metros rebound started in 2Q2010.
 - Slow improvement nationally from worst economy in 60+ years
- Employment – Nationally very slow recovering
 - Unemployment – US 7.4% (U6 13.77) / Texas 6.5% / Austin 5.3%
 - Austin has 4th lowest unemployment of top 50 large US metros (over a million)
 - Austin and Texas have been lower than the national avg. the last 79 months (6+ years)
 - 11.8 million Americans remain unemployed. In Texas there are 833,805 without jobs, in Central Texas with an estimated 52,557 workers looking for work.
- Home, car and retail sales have improved dramatically
- Consumers are spending
- Real estate construction stronger across all channels nationally, Texas leading
- GDP growth improving
- Interest rates have stayed low through most of 2013
- 5+ years of household formation pent up demand
- Corporate earnings continue to improve
- Housing and real estate slowly stabilizing, putting more people to work

Projections for the next couple of years indicate substantive national growth won't occur until late 2013/14 – potentially slower



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Recession recovery: Still slow



- **The last jobs report was disappointing.** At the current rate it will take us 9.5+ years from today to get back to prerecession employment.
- **Yes, the unemployment rate fell to 7.3%,** but that is because labor force participation rate fell to a 35 year low. 3.8 million 'missing workers who have dropped out of reporting. If you include them, unemployment is 9.5%, U6 unemployment is high 13+%.
- As reported by U6, BLS numbers, lots of American workers are underemployed.
- **Corporations are seeing record profits.**
- **Texas workers reached an all-time high of 10.65 million** in December 2011, and has maintained a strong level of employment. 1 out of 2 jobs in US are created in Texas
- The Texas unemployment rate has been **at or below the national rate for 79 consecutive months.**
- **2.6 million fewer jobs,** the U.S. economy lost nearly 8.8 million jobs between January 2008 and February 2010, but has since gained back only about 6.2 million jobs.
- Meanwhile, the population has grown, and some jobseekers have given up. **As of 8/13, 58.6% of the adult U.S. population had a job.** The rate has barely budged in the last three years, and the last time it was that low was in 1983.



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Where are we in the cycle?

- **US – Stabilization** The Federal Reserve lowers rates, then gradually allows increase, as housing and job growth historically follow. When the rates are at zero, the Federal reserve uses other means, such as quantitative easing (QE) to encourage growth. Mildly effective. As Fed reduce stimulus, rates should rise.
- **Texas – Recovery/Expansion** - Supply / demand is in balance, and home / land value appreciation meets or beats inflation.
- **Austin – Expansion** – Economic housing formation as well as other real estate channel demand exceeds supply. Housing and real estate appreciation stronger
- **Houston - Expansion** – Economic housing formation as well as other real estate channel demand exceeds supply. Housing and real estate appreciation stronger
- **San Antonio – Recovery** - Demand has picked up, putting pressure on supply
- **Dallas – Fort Worth – Recovery** - Demand has picked up, putting pressure on supply

All of this is caused by dynamic job growth in Texas.



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Challenges from slow recovery

- National unemployment has improved, but still not recovered; Texas has stabilized and is above pre-recession numbers
- Lending and mortgage rates creeping up
- Real estate prices nationally are slowly improving. National and locally housing and construction is just beginning to recover. It has not lead the recovery as it has in past recessions
- Mortgage lending standards still challenged for another 2-4 years
 - Appraisals a hurdle in purchases
 - Entry level housing challenged
- Commercial real estate regionally has improved, not as big a drain on community and regional banks
- Banks want to lend more, but new regulations are making it difficult
- State and local governments are hiring again slowly. Locally Austin gained about 800 government jobs last year. However debt ceiling / sequester taking \$16+B out of Texas budget and jobs, primarily education and defense.
- Financial regulations put in place by Dodd / Franks, CFRB and Basel III continue to slow lending
 - Many potential buyers can't get a loan if they don't have the higher credit rating, because the above threatens reserves and big fines if the loan goes delinquent
- Homebuilders expanding activity, lack of lots an issue. Locally 60% of prerecession starts
- Lack of **confidence** and **certainty** in the economy slowing recovery. At current national employment growth it will take 9.5 years to recover to pre recession employment



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The welcome surprise of 2013

- **Home price appreciation**
- **Significant change in consumers psychology**
 - Fear of losing job has decreased dramatically, particularly in Texas where
 - 5+ years of pent up demand for a different home. 3 to 5 years of strong employment growth in Austin and other Texas metros. Move up, move out, or move down.
 - Fear of declining home prices largely over across America. Texas received very little of this, and values have improved dramatically the last 8 months.
 - Unbelievable low mortgage / bank rates create 'positive leverage'. Return of positive leverage brings back speculators as well as the consumer.
- **Significant low levels of inventory**
 - Low inventory levels with increased demand = higher prices
 - Increased demand + low inventory + constrained supply = higher prices > Austin
 - Homebuilders / developers constrained to respond
 - 15,000+/- developed lots at end of 2Q13, With 9,000+/- starts this year and only 4,200 delivered, the number of lots will not keep up with demand. The result will be higher land, lot and labor prices.



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Housing market conditions

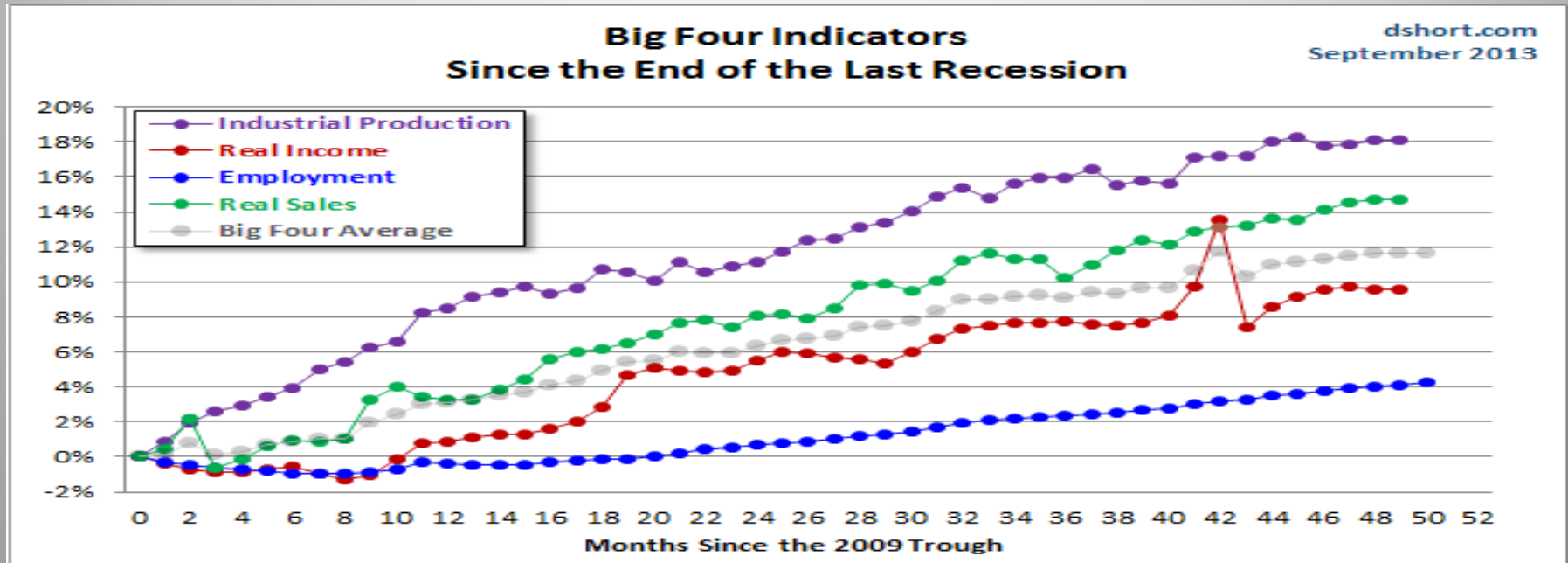
- Affordability – price / payment to income (Rates still at historic lows)
- Pent up demand. Household formations – 1 million+ in 2012, 550K to 600K annually last 5+ years.
- Rising rents (nationally, regionally and locally)
- Fewer distressed sales. Foreclosures on downward spiral (especially in Austin / Texas where they make up less than 1.5% of market)
- Smaller inventory of new and resale homes
- A sellers market locally and regionally
- Nationally improving, but not yet whole. Texas continues to improve
- Mortgage and bank rates creeping up
- Expectations – the market has turned. Set proper expectations.

‘The house or apartment you look at today will be gone tomorrow!’



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Four big national economic indicators continue to be positive



Big Four Indicators Month-over-Month

Indicator	Sep	Oct	Nov	Dec	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug
Industrial Production	0.2%	-0.1%	1.3%	0.0%	0.0%	0.7%	0.2%	-0.4%	0.0%	0.2%	0.0%	
Real Income	0.2%	0.3%	1.5%	3.5%	-5.4%	1.1%	0.5%	0.4%	0.1%	-0.1%	0.0%	
Employment	0.1%	0.1%	0.2%	0.2%	0.1%	0.2%	0.1%	0.1%	0.1%	0.1%	0.1%	0.1%
Real Sales	0.5%	-0.2%	0.6%	0.3%	0.1%	0.4%	-0.1%	0.5%	0.3%	0.1%	0.0%	
Big Four Average*	0.3%	0.0%	0.9%	1.0%	-1.3%	0.6%	0.2%	0.2%	0.2%	0.1%	0.0%	0.0%

Employment is released the first week of the month, Income the last week, Industrial Production and Sales mid-month.

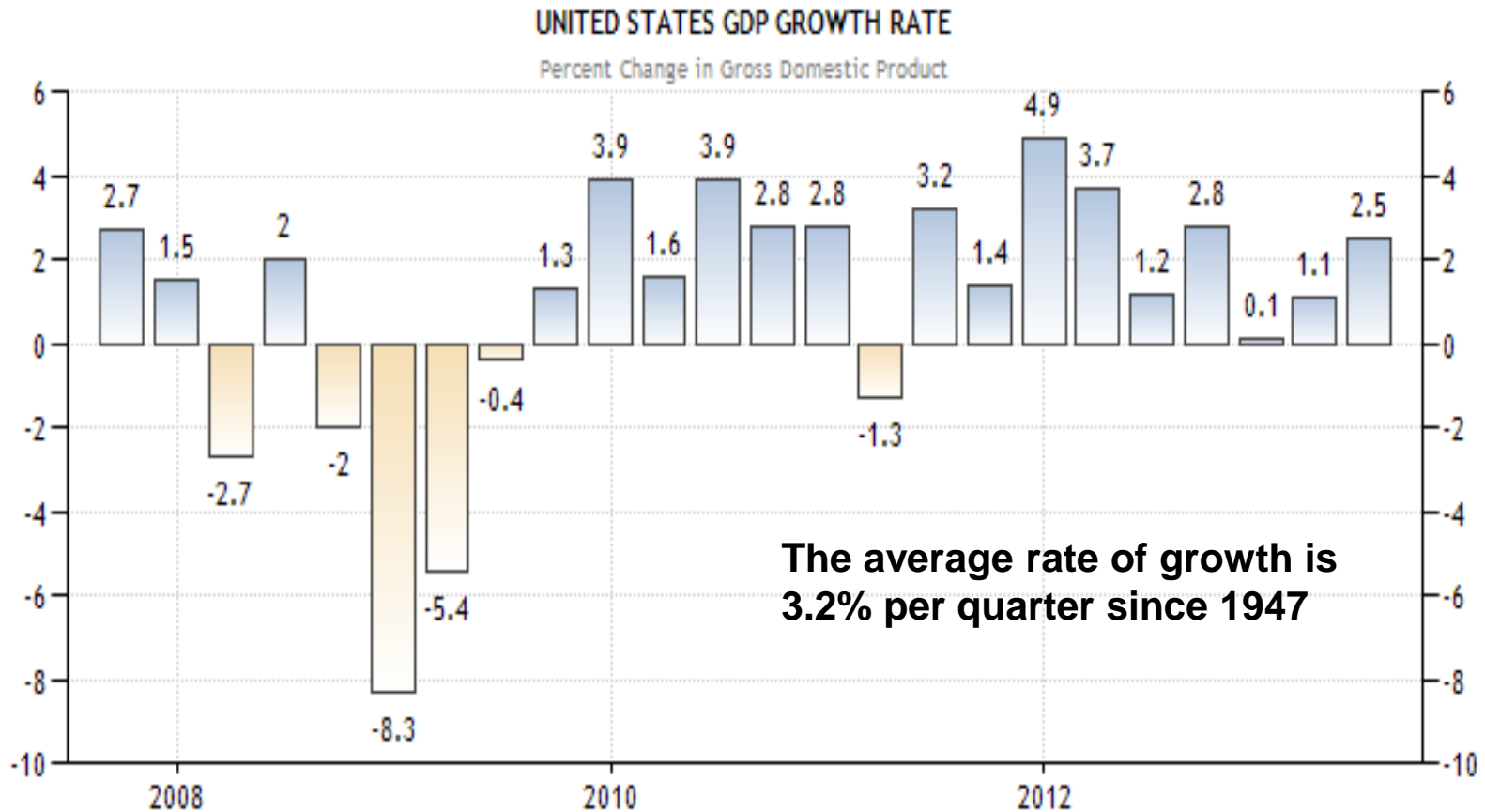
*The Big Four Average is based on four data points, the most recent in each series.



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Change in National GDP



**The average rate of growth is
3.2% per quarter since 1947**

SOURCE: WWW.TRADINGECONOMICS.COM | BUREAU OF ECONOMIC ANALYSIS



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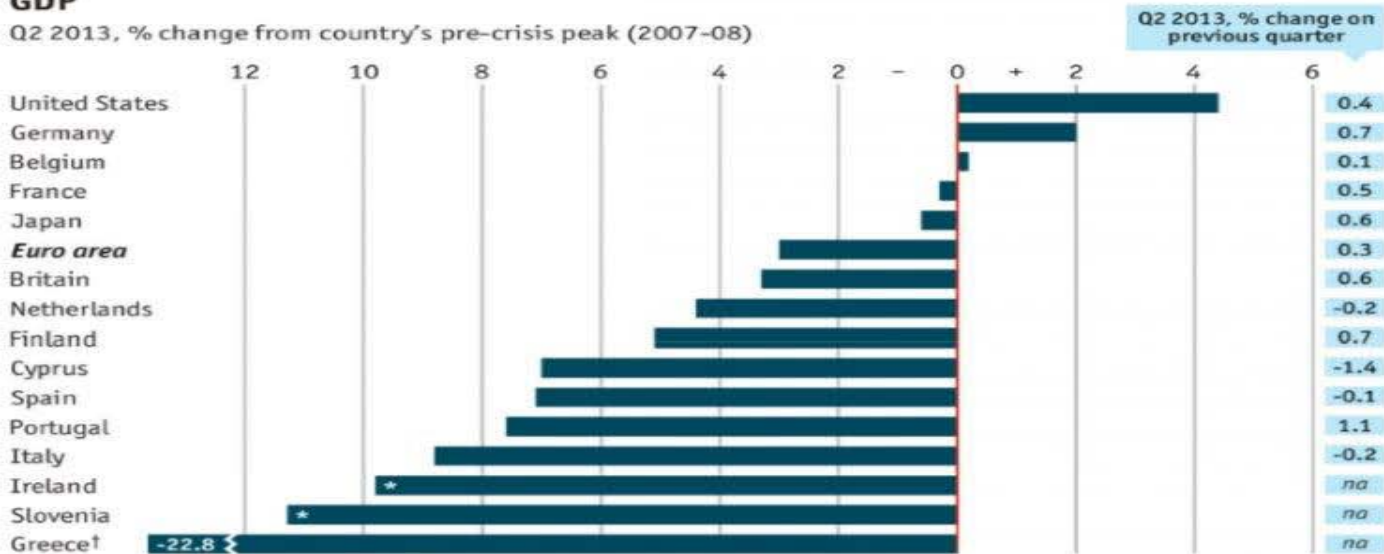
US GDP Comparison

GDP Percentage Change Since Pre-Crisis Peak (2007-2008)



GDP

Q2 2013, % change from country's pre-crisis peak (2007-08)



Source: Eurostat

*Q1 data †Data not seasonally adjusted: change from Q2 2007

Economist.com/graphicdetail

Source: The Economist; Eurostat

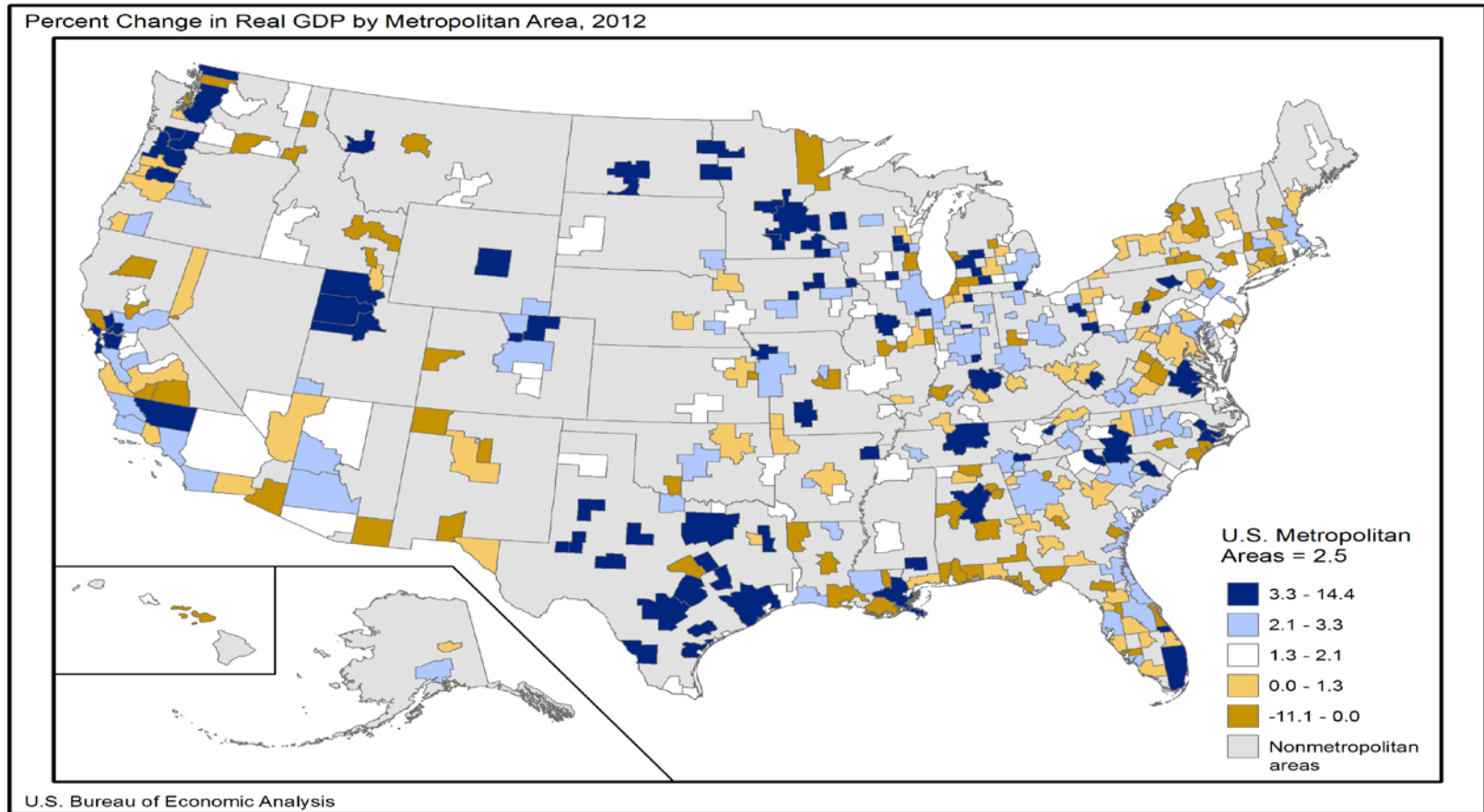
Euro area includes: All other EU countries not already represented in the chart. Includes: Austria, Bulgaria, Croatia, Czech Republic, Denmark, Estonia, Hungary, Latvia, Lithuania, Luxembourg, Malta, Poland, Romania, Slovakia, Sweden and the United Kingdom.

Gross Domestic Product (GDP) = The monetary value of all the finished goods and services produced within a country's borders in a specific time period, though GDP is usually calculated on an annual basis. It includes all of private and public consumption, government outlays, investments and exports less imports that occur within a defined territory.



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Texas Region Led Nation in GDP growth



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And they want to own homes in Texas!

Top 10 Healthiest Housing Markets in 2013

Among the 100 largest U.S. metropolitan areas



Note: Peabody, MA refers to the Essex County metropolitan division, which includes the suburbs north of Boston, with a population of 740,000.



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Consumer Confidence Level

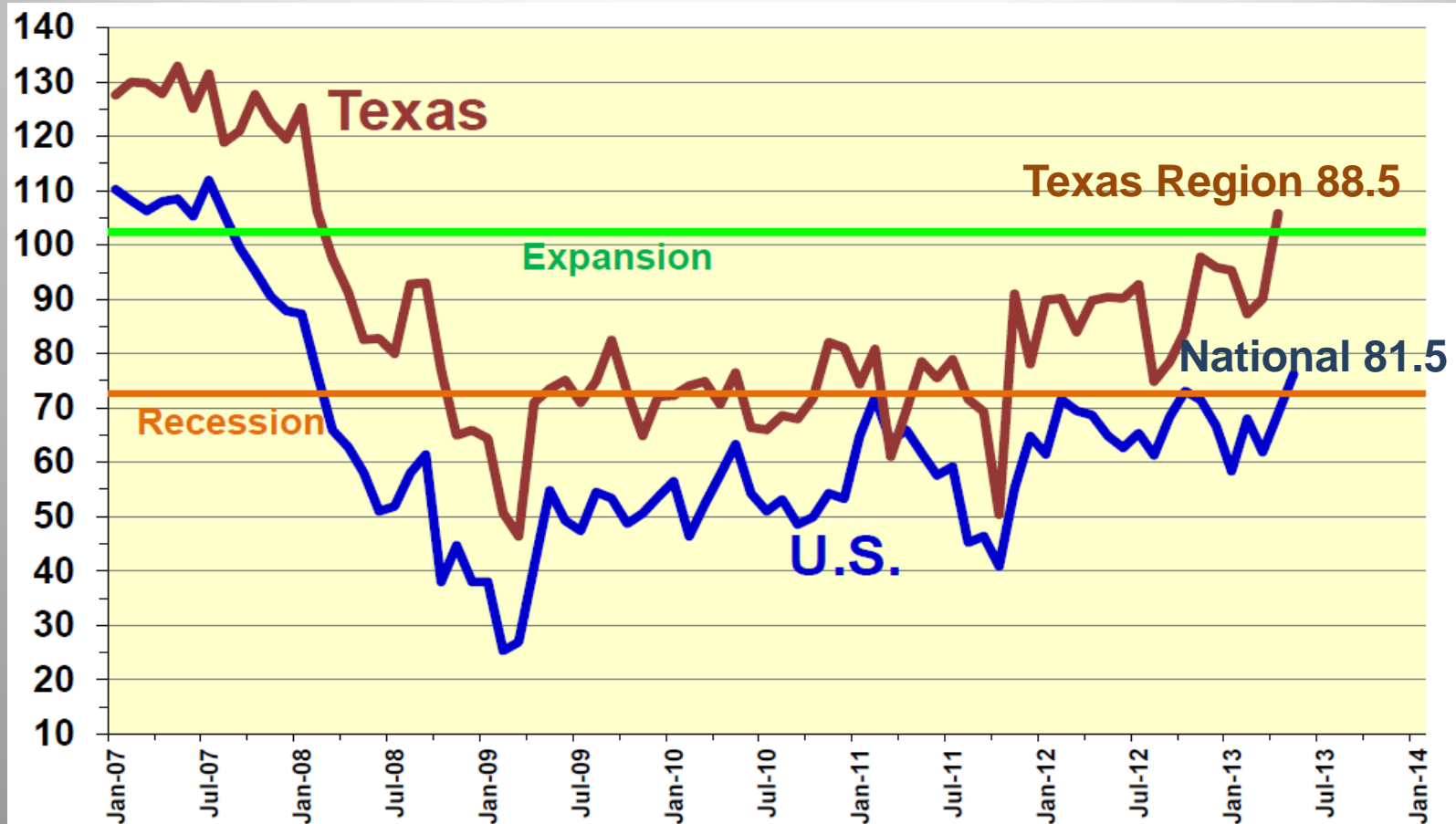
Consumer Confidence

— Consumer Confidence Index — Present Situation — Expectations



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Consumer Confidence Level



Source: The Conference Board (1985=100); Texas is the West-South-Central Region including Texas, Arkansas, Louisiana and Oklahoma (per source's data groups)

12



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Traditional economic indicators in Texas remain strong

- Texas and Austin indicators continue to show strength:
 - Total debt balance per capita 2nd lowest in US
 - Debt balance 90+days late, 2nd lowest in US
 - Percent of new bankruptcies lowest in US
 - Job creation still strong, 1 out of 2 every jobs in US created in Texas
 - Austin, 1st in US metros economic rankings
- Demand greater than supply
- Real Estate and Land values continue improvement
 - Central Texas area leading the state with a 6+% increase in rural values sold over the previous year, 2012. Texas leads the nation in number of farms and ranches, with 247,500 farms and ranches covering 130.4 million acres as well as the highest average value of farm and ranch real estate in any state.



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Americans still want to own homes

In Today's Strong U.S. Housing Market, Purchases Almost As Common As Refinances



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As a hard asset, home prices vs. gold – Undervalued!

Negative Correlation: New Home Sales Average Price vs. Price of Gold Bullion



July 1, 2005 through July 31, 2013



Source: DoubleLine Capital, St. Louis Federal Reserve, U.S. Commerce Department
Correlation = Statistics: The simultaneous change in value of two numerically valued random variables:



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National comparison of price rebound

Austin comes out strong!



Price Rebound or Construction Rebound



Source: Trulia 9 2013

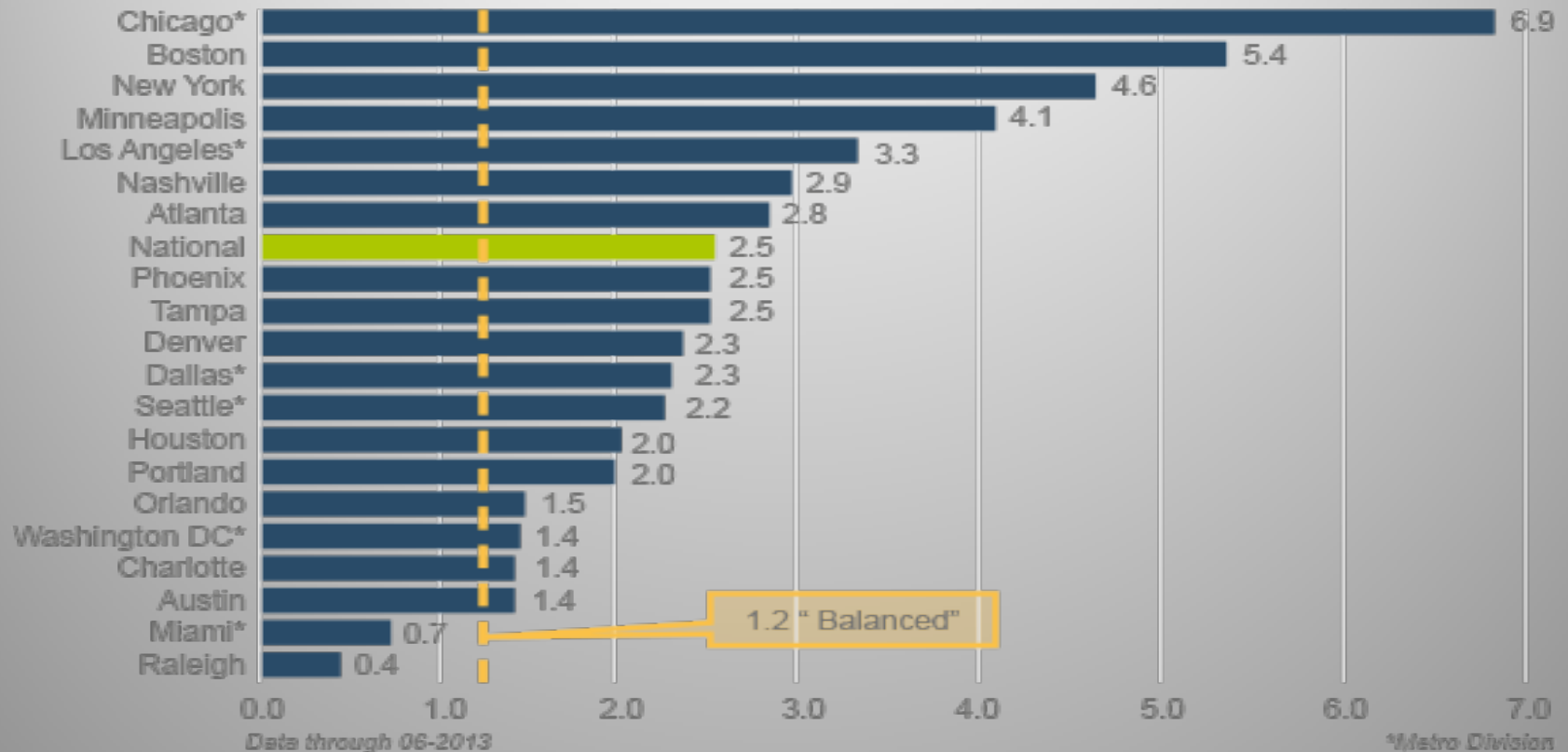


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Austin playing catch up on housing

Employment Growth/Permit Ratio
Top 20 US Markets



Source: John Burns 8 13



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Now is the time to buy!

- Austin area resale home inventory is at 2.8 months (can you say sellers market....)
 - 6104 single family listings. 20% less than a year ago. Slight increase in listings (+22% since 8/12)
- New and resale home inventory levels extremely tight
 - Values appreciating in most Austin sub markets
- Austin home values remained positive during recession and continue to gain value
- Record affordability, 2nd lowest mortgage rates in 60+ years
- 1 out of 2769 properties in Travis County, 1 in 3629 in Austin are in foreclosure
- Residential, rental and office entitlements at lowest levels in 6+ years
- Lending requirements still tight, causing fewer opportunities
- Rentals – 95.1% occupancy / less than 13,605 units left in five county area
- 60,000+ people annually moving to Austin annually
- Lower Supply + Higher Demand = Value improvement



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The numbers...

- **145,0099 total rental units Austin**
 - 95% occupancy = 7,105 units available + 6500 units under construction to be completed 2013

Total of 13,605 rental units available in the next 12 months.
- **7,800 to 9,000 home starts this year**
 - For every 2 jobs / one home start
- **6,104 listings presently**
- **Total shelter 27,805 units available**
- **Total annual immigration 60,000+**



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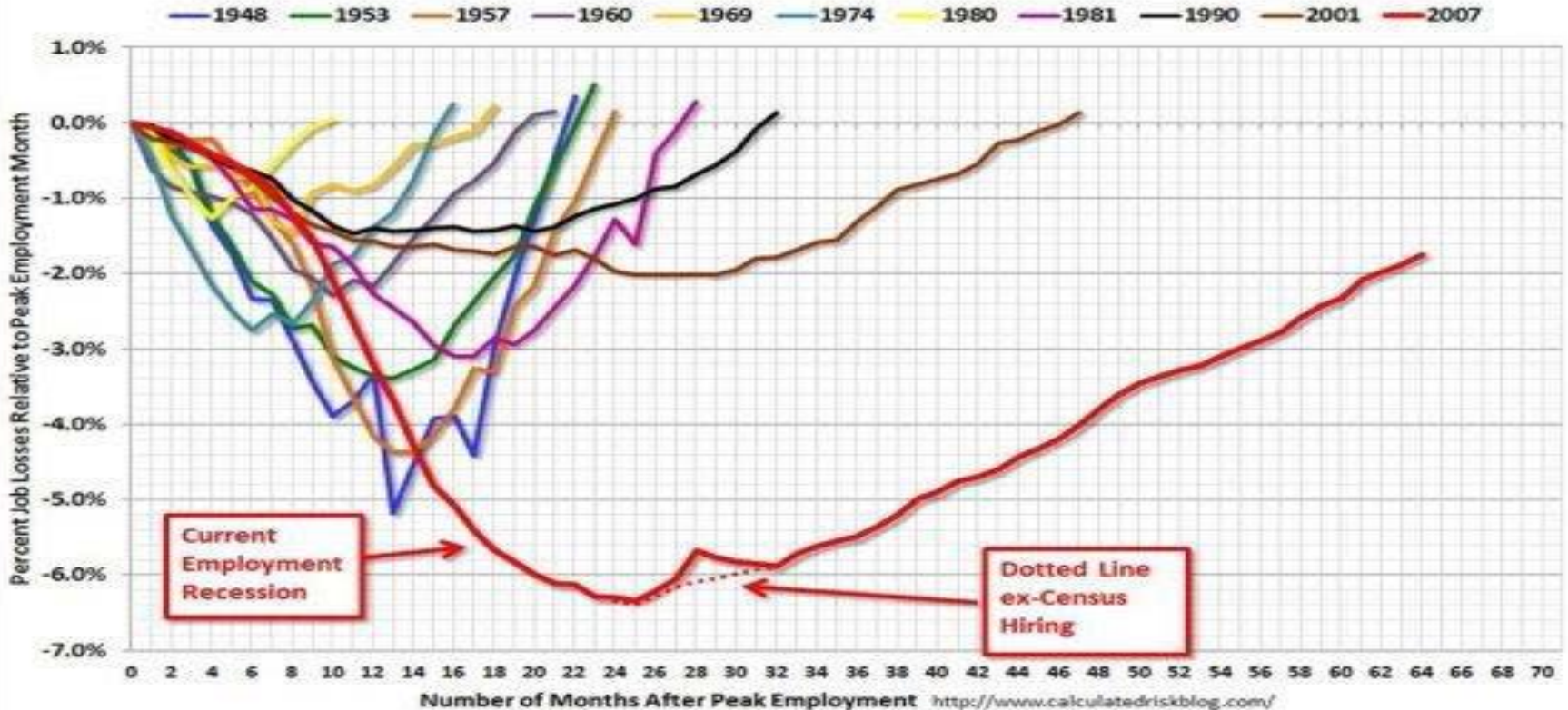
Unemployment has persisted longer than in previous recessions

MoneyGame



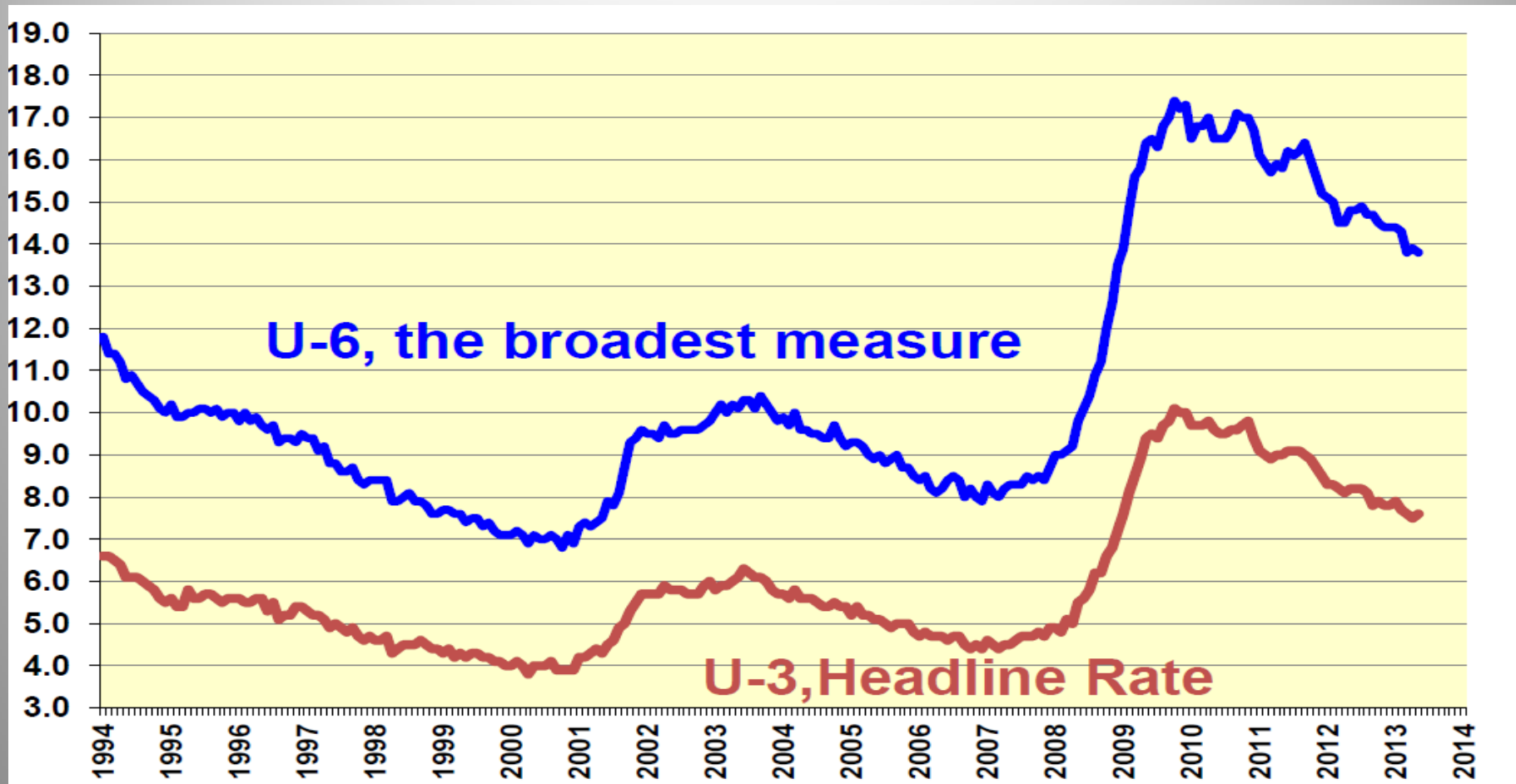
Chart of the Day

Percent Job Losses in Post WWII Recessions



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True National Unemployment vs. Headline



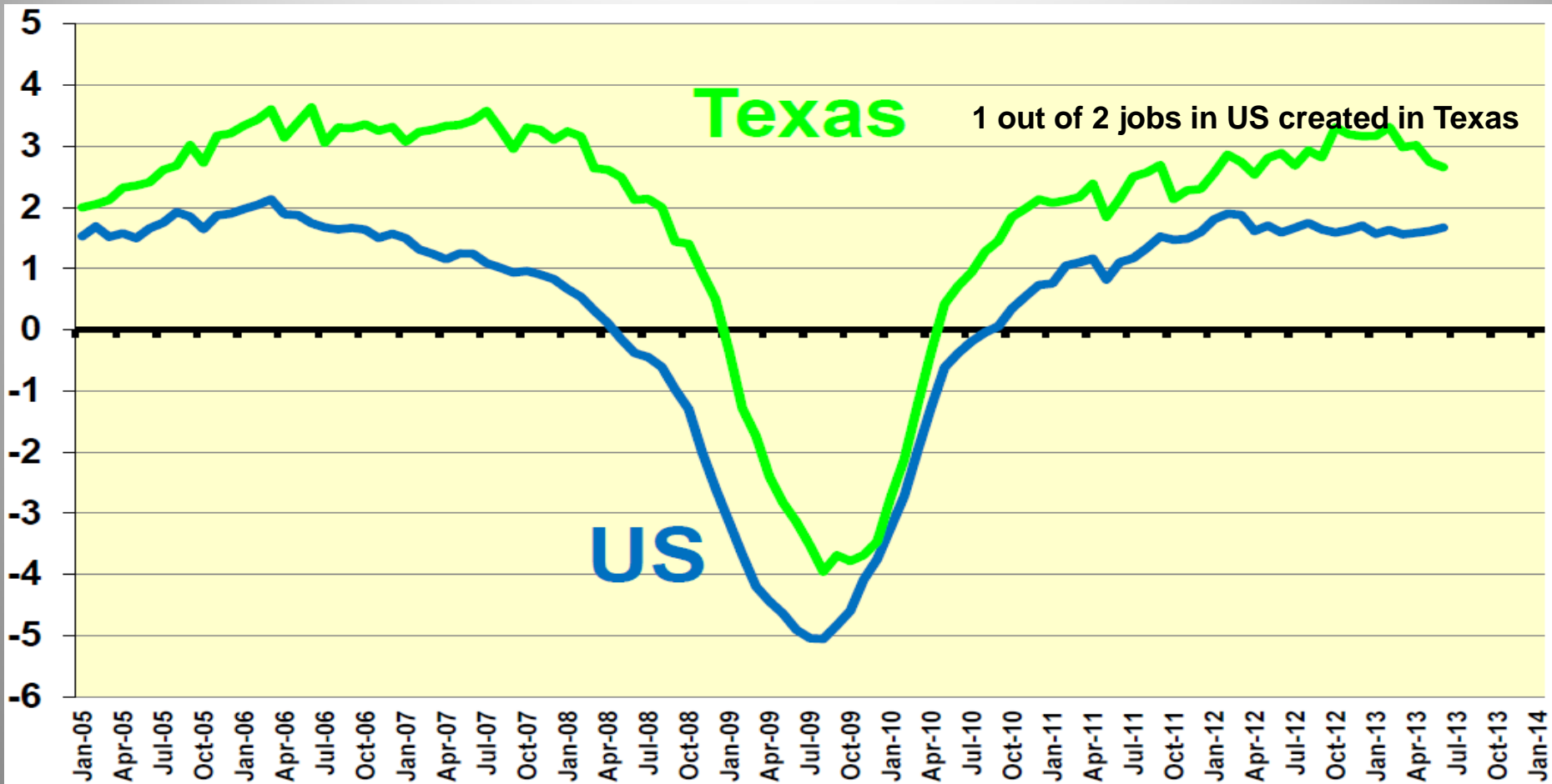
Source: BLS 8 2013



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Annual Employment Growth Texas and US



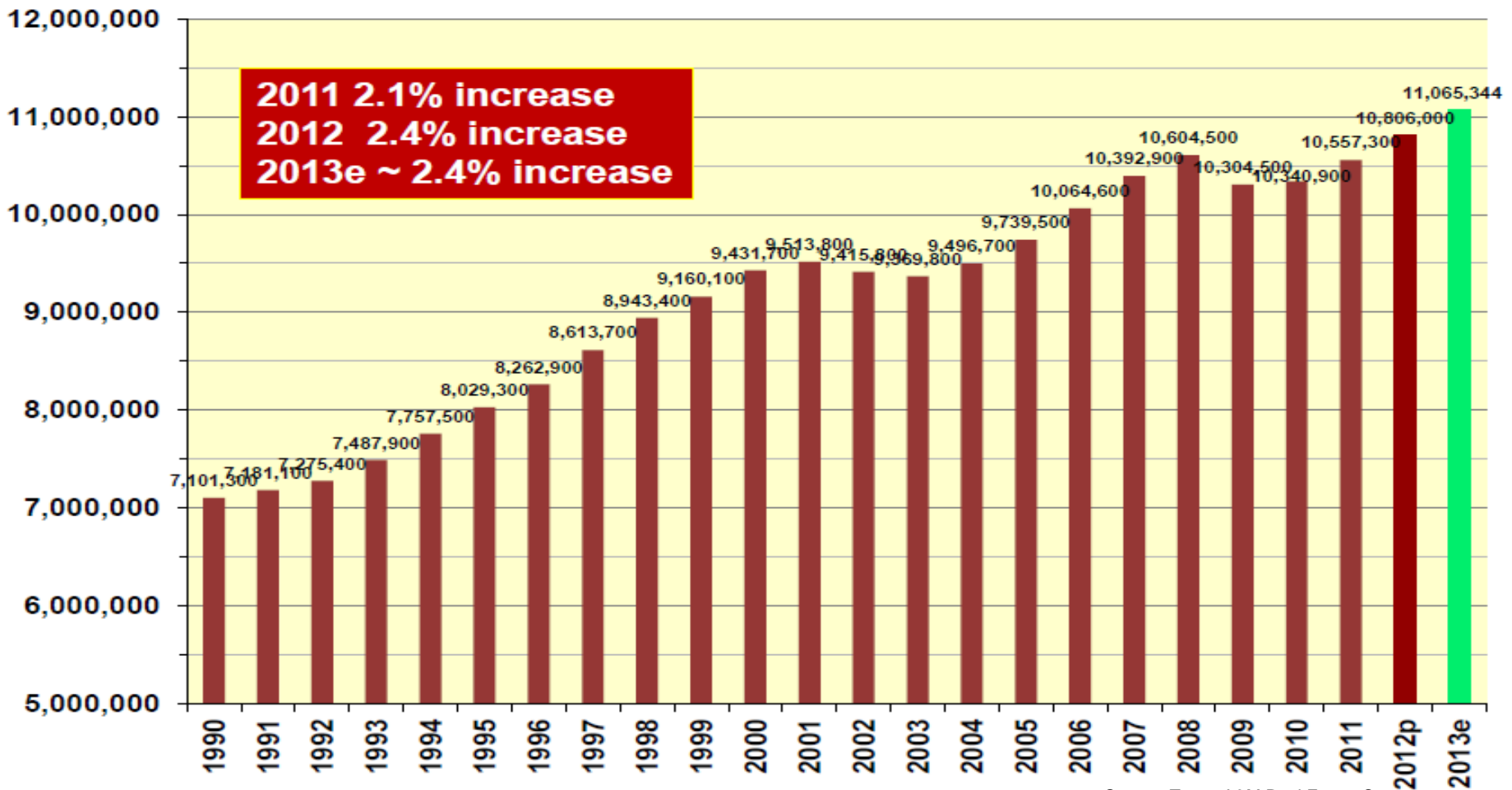
Source: TWC, Real Estate Center at Texas A&M University



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Texas Annual Job Growth



Source: Texas A&M Real Estate Center



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Texas economic outlook

2013-14

- **Downside risks:**
 - National (global) recession
 - National slow economic growth and recovery
 - Energy sector slower growth
 - Tech decline and new technology
- **Texas job growth continues to outpace national rate**
- **Energy industry slowing expansion**
- **State and local budget deficits and level spending**
- **Federal furloughs – defense, education, etc.**
- **Population growth continues even stronger with continued job creation**
 - The need for ‘tech’ workers in all metros, across the state
 - Continued immigration from California due to ‘business friendly’ / less tax burden environment
- **New construction rebound continues, but far from ‘recovered’**
- **Pent up demand for all channels of real estate driven by investment, affordability, low interest rates**



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National and local housing is improving

- **Nationally the housing market is improving**
 - National 2013 –914,000 projected starts (off 49%)
 - Austin SMSA - forecast 2013 – 8400 to 9200 (Austin could do 15,000+ if desirable lots were available.)
- **Nationally, lack of inventory and appraisals are still a challenge to values**
- **Housing inventory back to more balanced levels**
 - Resale listing inventory
 - US avg. 5.1 months / 2.16 Million
 - Austin SMSA 2.8 months / 6,104 listings
 - **Inner Core Neighborhoods:** tight
 - **Close in Neighborhoods:** tight
 - **Suburban Neighborhoods:** Improved. Most have become ‘sellers’ market
- **House price trends** (annual basis / median value)
 - US 4 to 6% / Texas 8% / Austin 10+% SMSA



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National economic outlook 2013-2014

- **Most indicators positive, but not robust**
 - Job formations & employment slow nationally
 - Real income not increasing
 - Local example: last 10 years / home appreciation 58% / rent appreciation 38% / wages flat
 - Personal consumption / economic activity (GDP) slow
 - Inflation dangerously low
- **Sluggish growth thru end of the year**
- **Interest rates stay low thru 2014**
- **Bank and mortgage credit attractive, but still tight**
 - Still dependent on major government support: interest rates, MBS purchases by Fed, FHA and GSES
- **Housing challenged with lack of inventory as well as appraisals nationally thru 2015**
- **Construction Recovery mostly in MF as rental markets remain strong**
- **Only 7 states are at prerecession employment**
- **International and national economy uncertainty**
- **Good news – you live in Texas! You live in Austin!**



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Where are we comparatively?

Nationally

- Home prices down 35+% since 2006 peak
- \$6.5 Trillion, over 49% lost equity in housing meltdown
- Defaults, delinquencies, and foreclosures improving
- New home starts improved for last 12 months, 34.5 % annually. 50+% less than 2006 starts.
- New household formation 25% of historic annual rate
- Federal government mortgage programs have had little impact to national economy.
- Federal Reserve policies have helped.
- CFRB continues to affect mortgage / bank lending

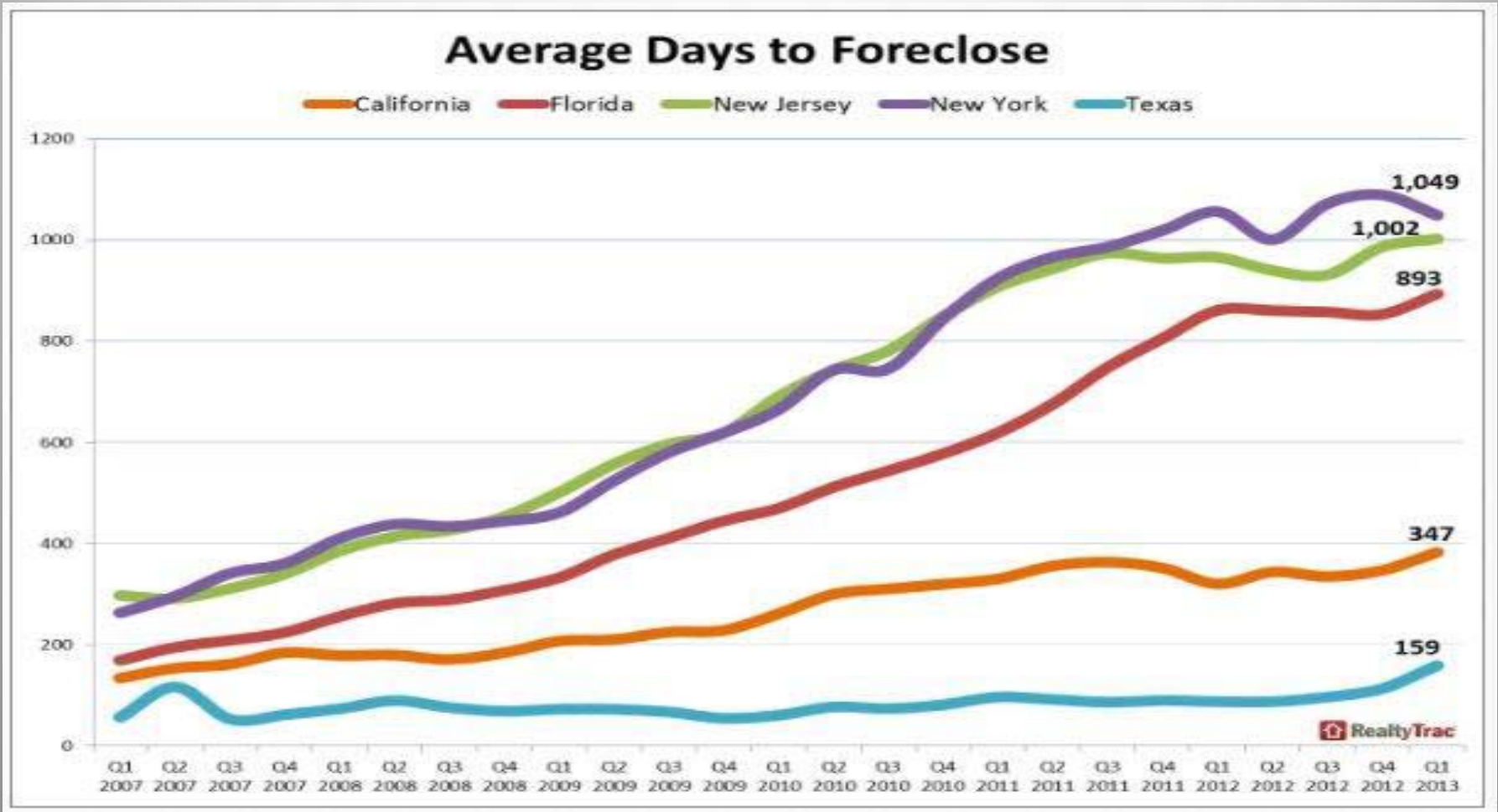
Texas

- Home prices improving statewide. Austin double digit appreciation
- All major Texas metros have turned positive
- Labor and materials costs dramatically up
- Texas foreclosures minimal, small impact
- Austin foreclosures minimal
- Texas and metros doubling in population next 20 years
- Not enough inventory in most real estate channels in Texas metros
- State Job Creation 50+% of national growth
- Regional banks are healthy



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Foreclosure Process and its Challenges

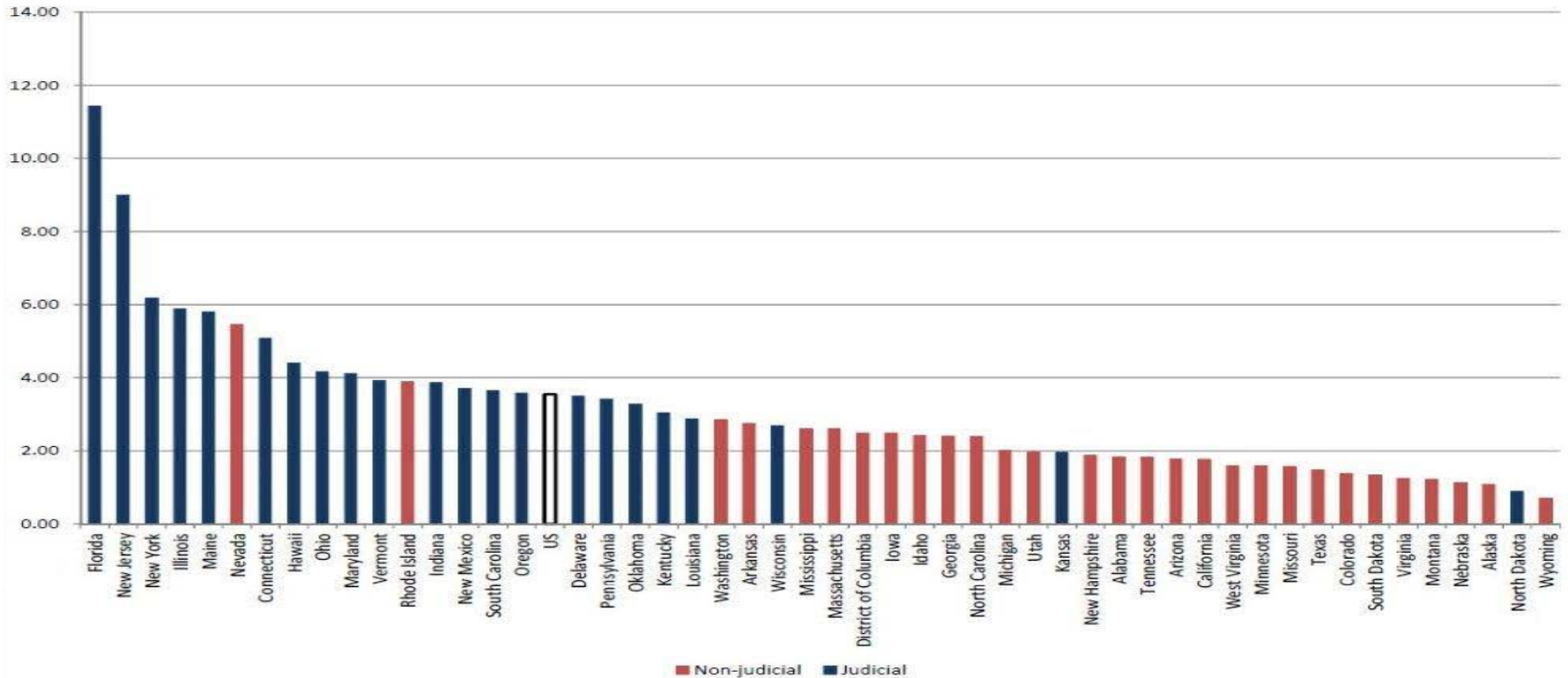


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Percent of loans in foreclosure 3Q13

Percentage of Loans in Foreclosure by State (NSA)

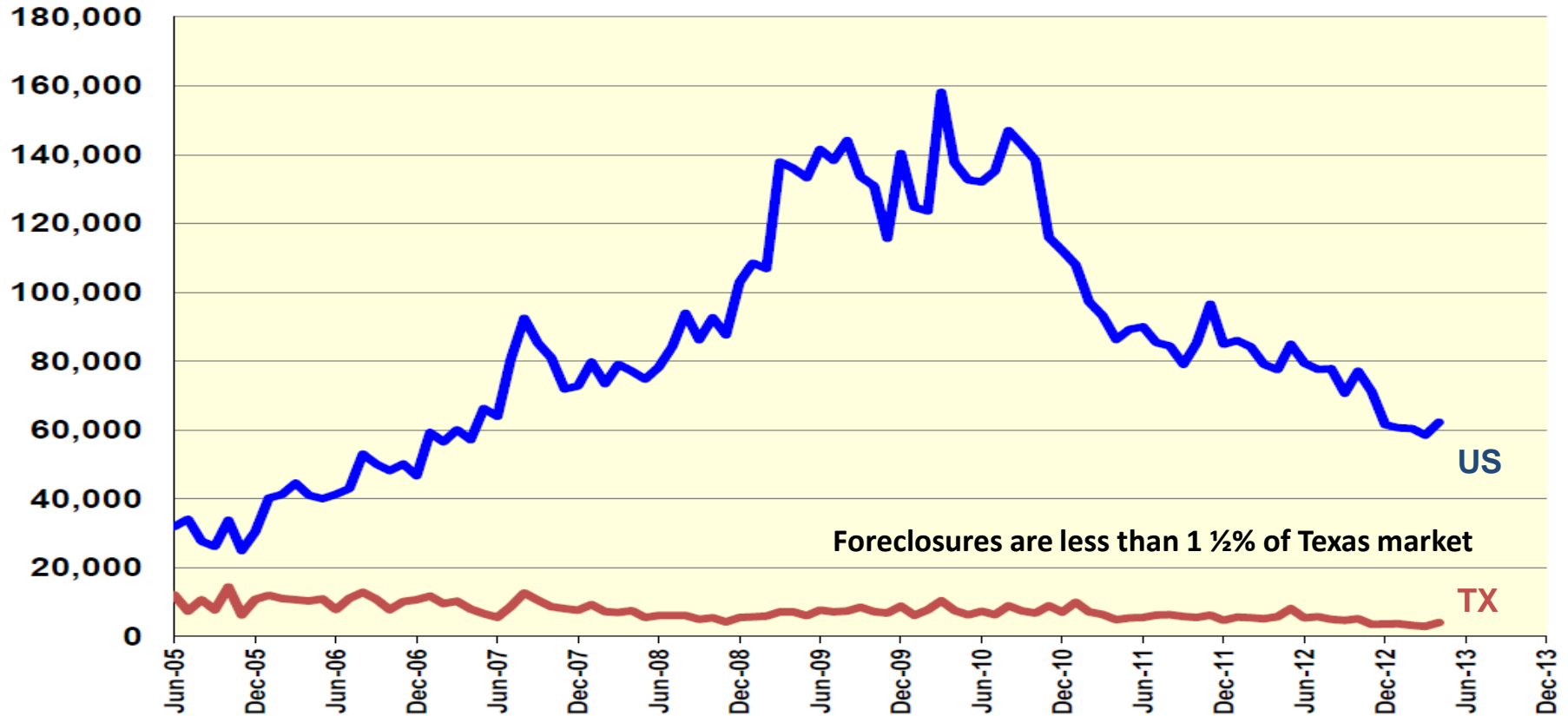


Over 55% of all foreclosures are in 32 counties



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Monthly Foreclosure Listings



Source: RealtyTrac, Inc.; Real Estate Center at Texas A&M University (Notice of Trustee/Foreclosure Sale)

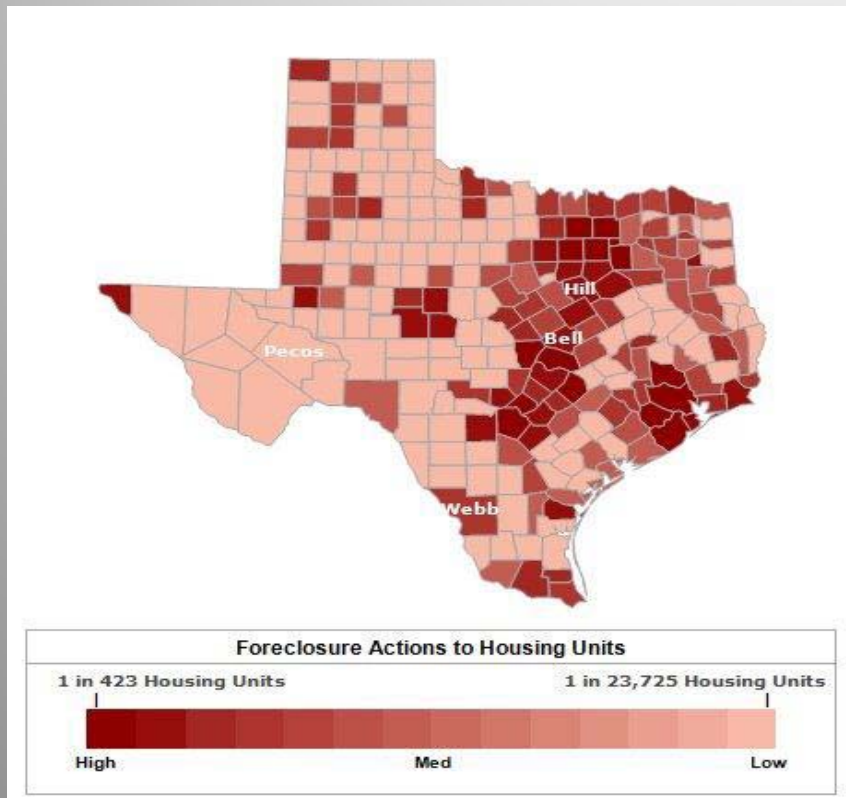
Source: RealtyTrac 5/13



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Texas foreclosures



- Travis – 1/3375
- Williamson – 1/1239
- Hays – 1/1611
- Bexar – 1 /1305
- Dallas -1/1276
- Harris – 1/1684

Texas –1/2008

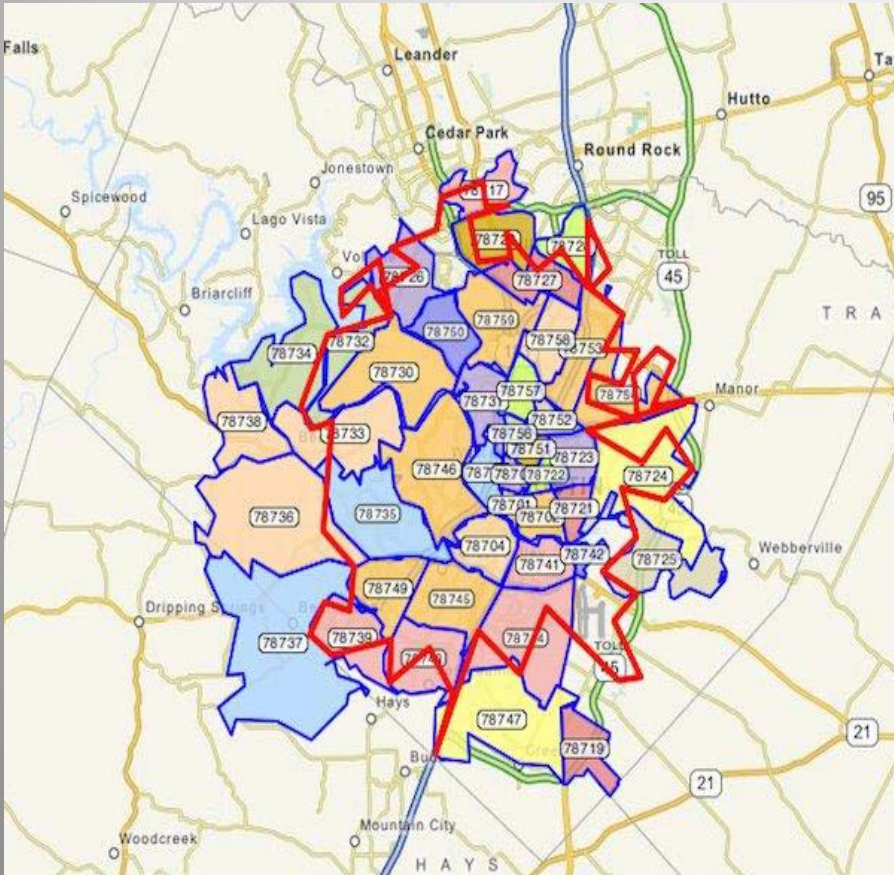
Source: Realtytrac 9/13



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Foreclosures



Top 5 Zips

78725 1 in every 362

78724 1 in every 554

78754 1 in every 1560

78744 1 in every 1566

78747 1 in every 608

Austin 1 in 3620

Source: Realtytrac 9/13



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Housing markets are changing



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Conclusions

- **Austin and Texas Metros continue to grow in jobs and population**
 - How much more can it grow with constrained supply?
- **Years of pent up demand – 5+ years**
 - We are 2+ years into local recovery
- **Interest rates stay low through 2014, great time to buy**
 - Affordability; prices and interest rates. Rate increase will slow sales temporarily
 - QE3 and monetary policy changing. In healthy economy, rates should go up.
- **Real estate to get stronger and hotter**
 - Under supply of homes. less downward price pressure
 - Not many 'A' opportunities left; housing, land, commercial. Where is the opportunity?
 - Rents are up, as are values. Bottom of market was 2 years ago.
 - For qualified buyers, an ideal time to buy, selection and inventory a problem
 - Housing inventory looks like it bottomed in 2013
- **National housing market will remain slow and steady, local and regional continue to strengthen through 2014**
 - Homebuilding and Realtors more optimistic than previous 5+ years
 - Homebuilders constrained to respond
- **National and regional rental market will strengthen through mid 2014**
- **National economy slow improvement, Regionally and locally the economy could be surprisingly strong 2013/14**
- **In Austin the market is more like the early 80's**



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Overcoming buyers objections



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Overcoming Buyers Objections

**“Is now the right
time to buy a
home?”**



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If not now, when?

- The market is not going to improve for buyers. Waiting will be easily a 12+% annual cost. Just because they couldn't buy at the bottom, no reason to wait.
- The supply of U/C inventory is dropping; won't be able to replace at values sold. Resale has picked up in all neighborhoods this year, showing strength of market.
- Rates are inching up.....(These are the lowest rates in 60+ years)
 - 12% rule
- Owning is cheaper than renting!
- Finished vacant housing and real estate inventory is a thing of the past! Its either sold or leased, creating a limited purchasing opportunity.
- Builders aggressive on land, concerned about enough capacity in 2015, driving values up
- Labor and materials increasing in cost
- There is not many deals in the market today. If on the market more than 45 days, value or product needs to be 'reviewed'.
- Discounted housing is a thing of the past.



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Overcoming Buyers Objections

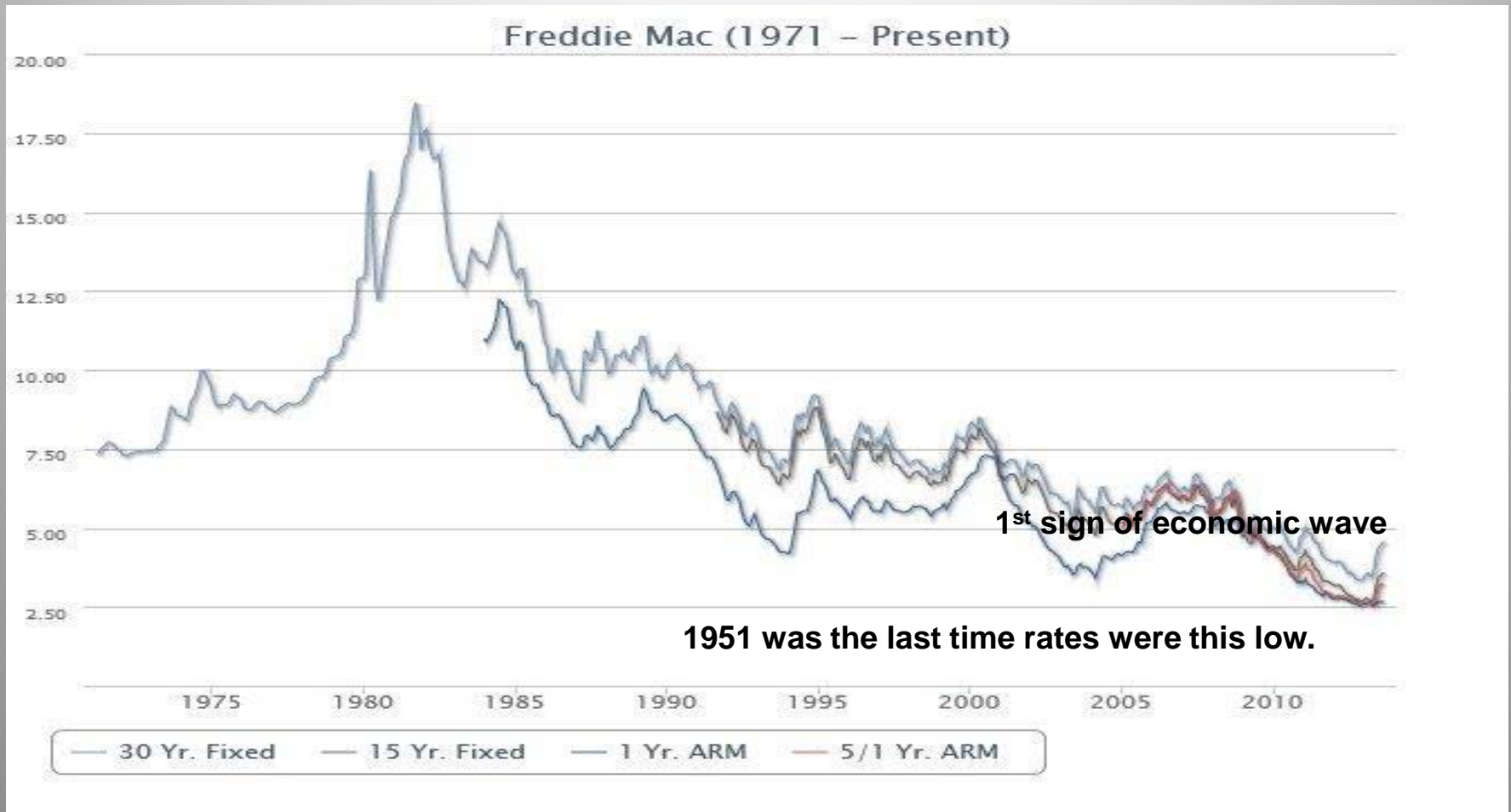
**“Are we really out of
the recession?”**



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Mortgage Rates

Why wait?



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Signs of economic recovery

- Housing prices stabilized and improving
- Rates are rising ahead of the Fed
- Growth (slow), no recession
- Most hard asset values improving
- National and state GDP growth
 - Growth isn't booming but momentum is gaining
 - the U.S. economy will post GDP growth near 2% for all of 2013 and improve on that performance in 2014.
 - State wide all economic indicators lead nation
- Auto, home, retail, major purchases improving
- Cities and states are spending again
- Employment is slowly improving
 - One bright spot: Manufacturing businesses increased payrolls in August 2013
- Layoffs at low levels
- Small business is optimistic and growing



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Overcoming Buyer Objections

**“Are housing prices
stable yet?”**



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Local numbers show strength

July 2013 Statistics

- **3,135** – Single-family homes sold, 35 %more than July 2012.
- **\$228,250** – Median price for single-family homes, 8% more than July 2012.
- **3,523** – New single-family home listings on the market, 22% more than July 2012.
- **2,773** – Pending sales for single-family homes, 20 percent more than July 2012.
- **41** – Average number of days single-family homes spent on the market, 23 days fewer than July 2012.
- **2.8** – Months of inventory* of single-family homes, 1.5 months less than July 2012.
- **\$933,242,475** – Total dollar volume of single-family properties sold, 43% more than July 2012.

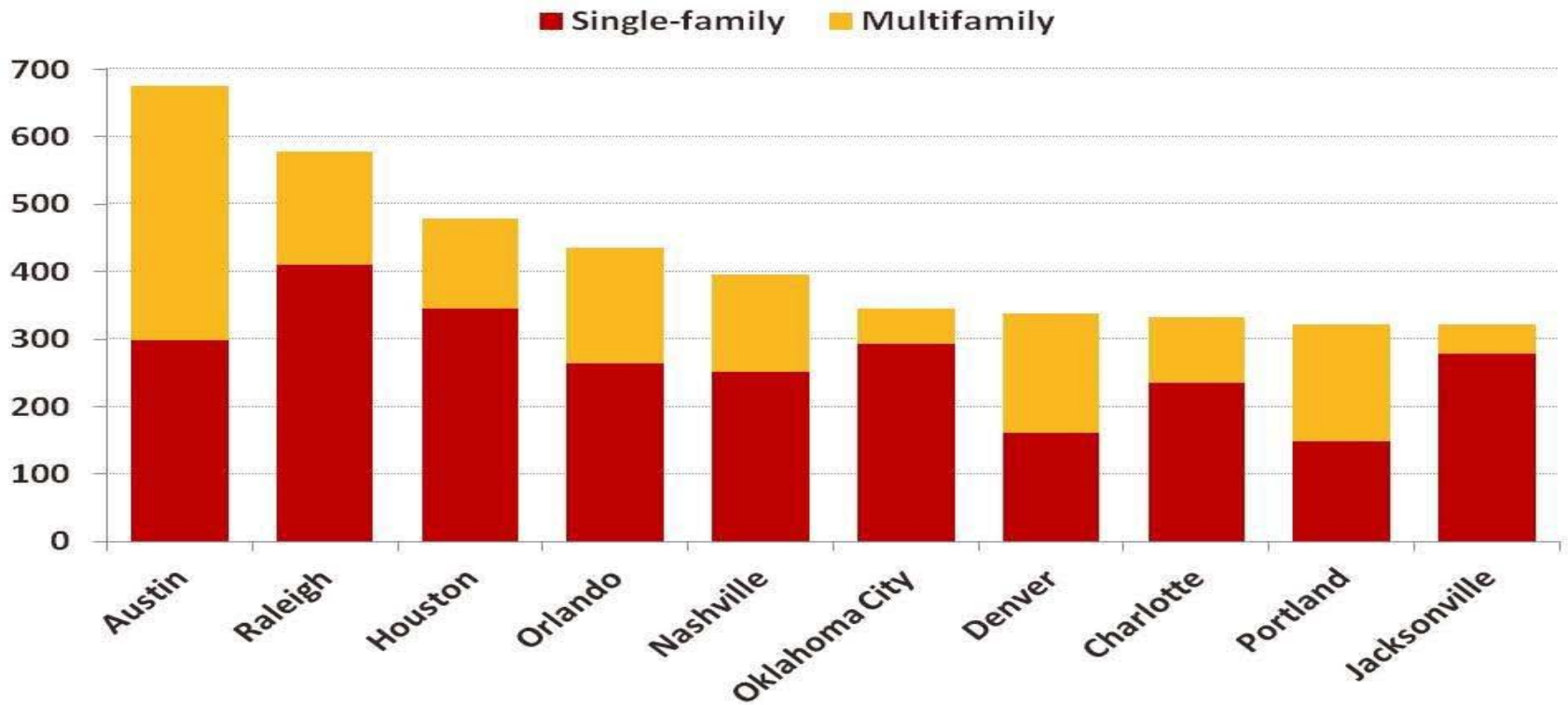
There is not enough product for demand!



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Metro Comparison

2013 Residential Permits per 100,000 Population
Best Performing Major Housing Markets by Per Capita Permitting Activity



Source: U.S. Census Bureau.

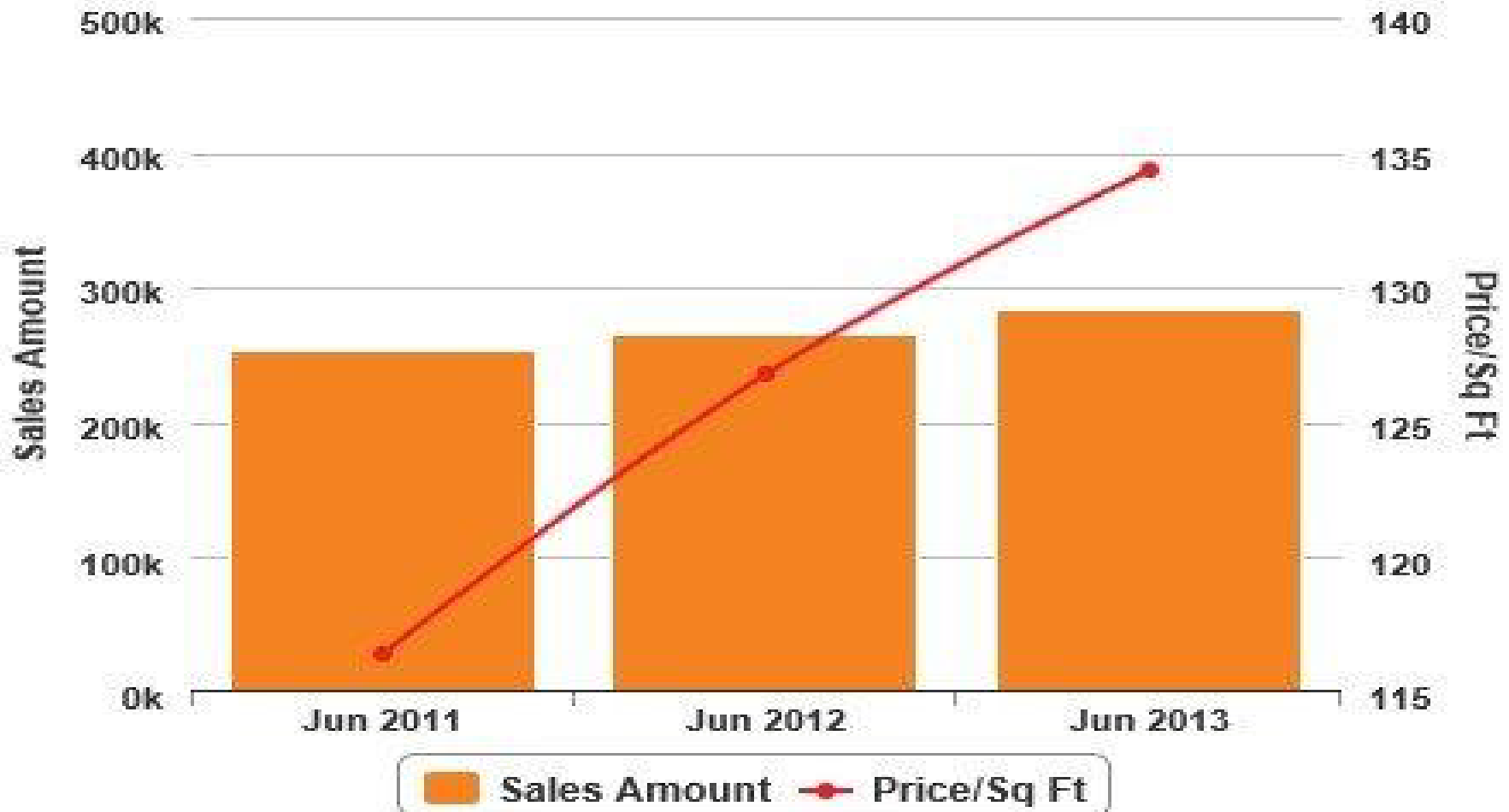


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Austin Values Improve

Year over Year Change in Price and Price/Sq Ft

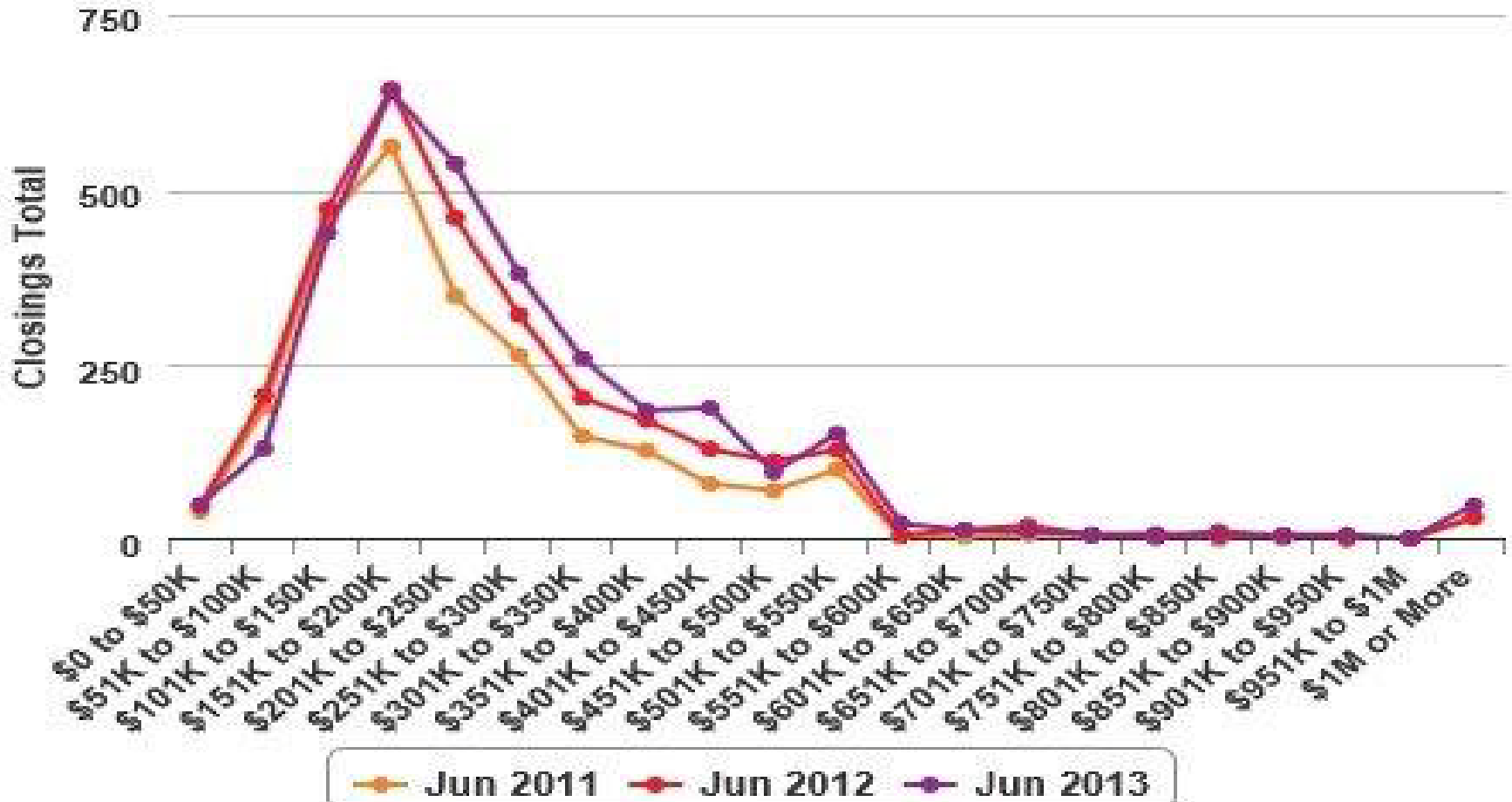


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Austin Consumers Needs Similar

Inventory is the challenge

Shift in Home Sales by Price Range



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Texas and Austin are different from the rest of the country!

- Home and real estate prices continue to appreciate in Austin
- The wide value swings of the rest of the country were never present here
- Austin is still an affordable metro market in comparison to the nation
- Texas has one of the lowest tax burdens in the country (46th)
- Continued positive job growth
- Over 50% of all jobs created last two years were in Texas
- Limited supply of Inventory / rental homes / apartments
 - Rent values increasing
 - Rental occupancy has been steady at 93%
 - Not enough developed land and lots
- More Fortune 500 corporate headquarters are located in Texas than any other state.



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Overcoming Buyer Objections

**“I’ve heard you can’t
get a loan right
now—it’s really
gotten hard!”**



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Mortgage qualification changes

- Yes, it is harder to qualify.
- Sub – prime is non existent. Jumbo has eased up and rates are better.
 - No down payment loans with FICO scores <740 very difficult to obtain.
 - Modest down payment loans will not work without documentation.
- American Mortgage Bankers Association research indicates that latest changes in mortgage qualification standards will increase percentage of buyers unable to qualify.
 - Previously thought that 10% of buyers that purchased in 2006 would not qualify today.
- Entry level will continue to be challenged.



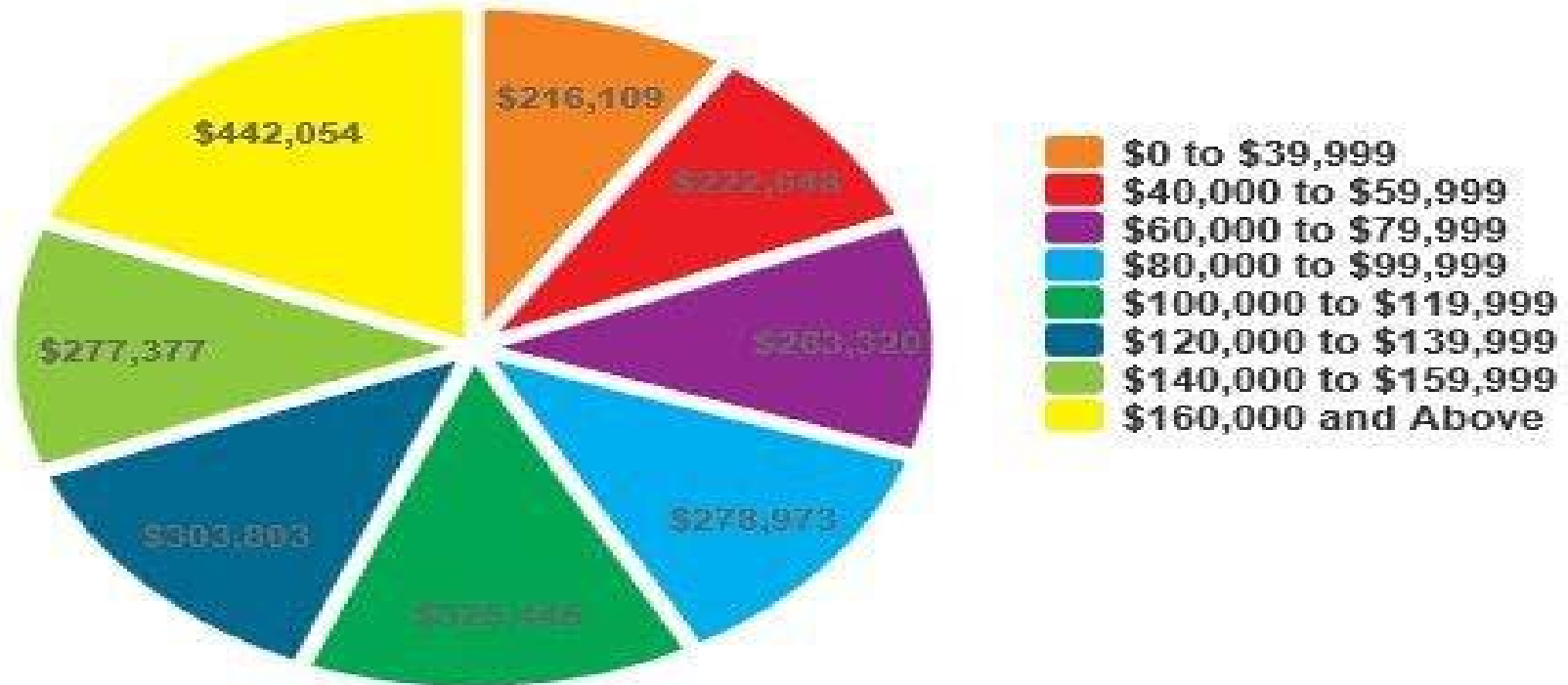
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Local perspective

Who is buying what?

Buyers Report

Sales Price by Income Level for June 2013



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Reasons mortgage rates will continue to rise

- **No more cheap money. Fed has announced the move to higher borrowing costs**
- **The End of Freddie and Fannie;**
 - Don't know what it will be, but every one wants a change
 - 95% of all loans are done by the government presently, 60% prerecession. Hard to replace or compete against.
- **Inflation is on the march**
 - Mortgage rates have a direct correlation to demand.
 - As the economy improves, inflation will begin to set in naturally. To offset the risk of drastic rising inflation, the federal government (Federal Reserve) will be forced to raise their interest rates.
 - Supply and demand
 - Something's go to give and it doesn't look like it will be inflation.
- **History**
 - Interest rates have risen....however they are still at near 60 year lows
 - **30 year mortgage rates have averaged 8.88 percent over time.** They have been under 5 percent in just 41 of the 524 months on record or about 4+/-% of the time. Just a return to the lower 25th percentile of all time mortgage rates would see rates rise to 6.92%.
 - Interest rates are expected to go up! Not down!
 - For every point increase, there is a loss of 12% buying power



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How do you build confidence in the housing market?

- Realtors / mortgage professionals need to explain to buyers why the market has changed and why now is the time to buy.
- It would be helpful to see what the months inventory number looks like in their community and the city as a whole. Explain why prices are firm when supply drops below six months.
- It would be helpful to show buyers the mortgage interest rate chart to help buyers to get a perspective of the current rates and affordability. Be sure to use more than 5 years of history.
- Purpose of this is to **show them there never will be a better time to buy!**



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Why buy Austin today?

- Of all the markets, Austin has seen little to no price erosion over the past few years
- Hard costs for development and housing continue to rise at about 18% to 22%
- Austin and Texas are strong short and long term investments
- Barring a catastrophic event, values will continue to improve in Austin and other Texas Metros
- Investment income has continued to rise in Austin, and they have stabilized in the Texas Metros. As the national economy improves, Austin, etc. is at the top of most lists for relocation, corporate and personal.



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**There is not a better time to
buy a home in Austin or
Texas!**

If not now, when?



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Thank you



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