3rd Quarter 2009

U.S. Housing Market Conditions

November 2009

Summary

Housing market conditions continued to show signs of stabilizing during the third quarter of 2009, after a downward trend that began in the first quarter of 2006 and just started to ebb in the second quarter of 2009. In the production sector, single-family housing permits and starts increased in the third quarter of 2009, while the number of single-family completions fell. In the marketing sector, sales of new and existing homes rose. The Case-Shiller® repeat-sales house-price index recorded a 1.4-percent seasonally adjusted (SA) increase in the second quarter of 2009, following a 6.8-percent decline in the first quarter of 2009 (the data are reported with a lag), while the less volatile Federal Housing Finance Agency (FHFA) repeat-sales index estimated that home prices fell 0.7 percent (SA) in the second quarter of 2009, following a 0.5-percent decline in the first quarter. Excessive inventories of available homes at the current sales rate maintained their descent in the third quarter of 2009, reaching an average rate of 7.6 months' supply for new homes and 8.8 months' supply for existing homes, compared with rates of 9.4 and 9.8, respectively, in the second quarter. The national homeownership rate rose 20 basis points to 67.6 percent in the third quarter of 2009 but was down from 67.9 in the third quarter of 2008. The percentage of foreclosure starts for all mortgage loans in the second quarter of 2009 was virtually the same as in the first quarter (the data are reported with a lag); the delinquency rate on mortgages continued its ascent, however. The sharp reductions in the multifamily sector persisted in the third quarter of 2009. Housing permits, starts, and completions of properties with five or more units all fell. The rate of apartment absorptions declined in the third quarter, and the multifamily vacancy rate increased sharply. According to the Bureau of Economic Analysis, the advance estimate of overall growth in the national economy in the third quarter of 2009 was an increase of 3.5 percent at a seasonally adjusted annual rate (SAAR), following a 0.7-percent contraction in the second quarter. The housing component of Gross Domestic Product (GDP) rose 23.4 percent in the third quarter of 2009, compared with a decline of 23.3 percent in the second quarter.

Housing Production

Housing production indicators continued to improve in the third quarter of 2009. The numbers of single-family housing permits and starts both rose in the third quarter, while housing completions declined slightly. Multifamily construction (condominiums and apartments), in contrast, is traditionally a volatile market and its fluctuations tend to be less indicative of the market climate. Manufactured housing continued a downward trend that began following the hurricane-induced orders of late 2005.

- During the third quarter of 2009, builders took out permits for new housing at a pace of 573,000 (SAAR) units, 8 percent higher than in the second quarter of 2009 but 34 percent lower than in the third quarter of 2008. Single-family permits were issued for 460,000 (SAAR) housing units in the third quarter of 2009, an increase of 13 percent from the second quarter but 17 percent lower than the third quarter of 2008. This is the second consecutive quarter that single-family permits have increased, after having declined for 14 consecutive quarters.

- Builders started construction on 590,000 (SAAR) new housing units in the third quarter of 2009, up 9 percent from the second quarter but down 32 percent from the third quarter of 2008. Single-family housing starts totaled 496,000 (SAAR) housing units in the

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third quarter of 2009, up 17 percent from the second quarter but down 17 percent from the third quarter of 2008. Single-family starts have risen in the last two quarters, after having fallen for 12 consecutive quarters.

- Builders completed 750,000 (SAAR) new housing units in the third quarter of 2009, down 8 percent from the second quarter and down 31 percent from the third quarter of 2008. Single-family completions totaled 487,000 (SAAR) in the third quarter of 2009, down 5 percent from the second quarter and down 38 percent from the third quarter of 2008. With the one exception of the last quarter, completions have declined for the last 14 quarters.
- Manufactured housing shipments reached a new record low of 48,700 (SAAR) units in the third quarter of 2009, the lowest level since the series began in 1959. Manufacturers' shipments in the third quarter of 2009 were down 1 percent from the second quarter and down 38 percent from the third quarter of 2008.

Housing Marketing

The housing marketing sector showed continued signs of improvement in the third quarter of 2009. The numbers of new and existing homes sold and the median sales price for existing homes all rose in the third quarter, while prices of new homes declined. Sales of new homes increased for the second time, after having declined for 14 quarters. The average months' supply of homes for sale dropped substantially for new homes and also declined for existing homes. The rise in new home sales and the rapidly receding supply of new homes for sale caused builders' confidence, as measured by the National Association of Home Builders (NAHB)/Wells Fargo Housing Market Index, to grow in the third quarter of 2009.

- During the third quarter of 2009, 411,000 (SAAR) new single-family homes were sold, up 10 percent from the 372,000 (SAAR) homes sold in the second quarter of 2009 but down 11 percent from the third quarter of 2008.
- REALTORS® sold 5.3 million (SAAR) existing single-family homes in the third quarter of 2009, up 11 percent from the second quarter of 2009 and up 6 percent from the third quarter of 2008.
- The median price of new homes sold in the third quarter of 2009 was $206,100, down 5 percent from the second quarter and down 9 percent from the third quarter of 2008. The average price of new homes sold in the third quarter of 2009 was $269,200, down 2 percent from the second quarter and down 6 percent from the third quarter of 2008. A constant-quality house would have sold for $279,500 in the third quarter of 2009, down 2 percent from the second quarter and down 6 percent from the third quarter of 2008.
- The NATIONAL ASSOCIATION OF REALTORS® (NAR®) reported that the median price of existing homes sold was $177,900 in the third quarter of 2009, up 2 percent from the second quarter but down 12 percent from the third quarter of 2008. The average price of existing homes sold in the third quarter of 2009 was $223,200, up 2 percent from the second quarter but down 9 percent from the third quarter of 2008. According to an NAR practitioner survey, distressed sales (foreclosures and short sales) accounted for 30 percent of all home sales in the third quarter of 2009 and distressed-sale prices are typically 15 to 20 percent below normal market prices.
- During the third quarter of 2009, the average inventory of new homes for sale was 261,000 units, down 10 percent from the second quarter and down 36 percent from the third quarter of 2008. That inventory would support 7.6 months of sales at the current sales pace, down 1.8 months from the second quarter of 2009 and down 3.1 months from the third quarter of 2008. The average inventory of existing homes for sale in the third quarter of 2009 was 3.87 million units, up slightly from the second quarter but down 12 percent from the third quarter of 2008. That inventory would support 8.8 months of sales at the current sales pace, down 1.0 month from the second quarter of 2009 and down 1.8 months from the third quarter of 2008. The "shadow inventory" of homes from foreclosures and delinquencies has the potential to increase the supply of homes for sale and further depress home prices.
- The Federal Housing Administration's (FHA) share of the mortgage market fell slightly in the second quarter of 2009 (the data are reported with a lag). Based on loan origination data, the FHA's dollar volume share of the mortgage market was 16.4 percent in the second quarter of 2009, down 5 percent from the first quarter but up 32 percent from the second quarter of 2008. Based on the number of loans originated, the FHA's share of the mortgage market was 19.2 percent in the second quarter of 2009, down 6 percent from the first quarter but up 25 percent from the second quarter of 2008.
- The expanding optimism of home builders continued in the third quarter of 2009. The NAHB/Wells Fargo composite Housing Market Index was 18 in the third quarter of 2009, up 3 points from the second quarter of 2009 but down 1 point from the third quarter of 2008. The index is based on three components—

current sales expectations, future sales expectations, and prospective buyer traffic—and ranges from 0 to 100. All three components rose in the third quarter of 2009.

Affordability, Homeownership, and Foreclosures

Housing affordability fell in the third quarter of 2009, according to the NAR® Housing Affordability Index. The composite index for the third quarter suggests that a family earning the median income had 159.2 percent of the income needed to purchase the median-priced, existing single-family home using standard lending guidelines. That value is down 10.0 percentage points from the second quarter of 2009 and down 30.6 percentage points from the third quarter of 2008. The decrease in affordability is attributed to a 2-percent increase in the median price of existing single-family homes sold, a 28-basis-point rise in mortgage interest rates and a 0.6-percent decline in median family income.

The delinquency rate for mortgage loans on one- to four-family homes in the second quarter of 2009 (the data are reported with a lag) was at its highest level since the series began in 1972, according to the Mortgage Bankers Association (MBA). Although the percentage of foreclosure starts (newly initiated foreclosures) was essentially unchanged from last quarter's record high, a major drop in foreclosure starts on subprime adjustable-rate mortgages (ARMs) was offset by an increase on other loans, with prime fixed-rate loans having the biggest increase. Prime fixed-rate loans now account for one in three foreclosure starts; a year ago they accounted for one in five. This change suggests a continuing shift away from mortgage defaults driven by interest rate increases on subprime ARMS to those caused by unemployment and the recession.

The delinquency rate (SA) for all mortgage loans was 9.24 percent in the second quarter of 2009, up from 9.12 percent in the first quarter and 6.41 percent in the second quarter of 2008. The delinquency rate (SA) for subprime mortgage loans was 25.35 percent in the second quarter of 2009, up from 24.95 percent in the first quarter and 18.67 percent in the second quarter of 2008. The delinquency rate (SA) for prime mortgages was 6.41 percent in the second quarter of 2009, up from 6.06 percent in the first quarter and 3.93 percent in the second quarter of 2008. For FHA loans in the MBA survey, the delinquency rate (SA) was 14.42 in the second quarter of 2009, up from 13.84 in the first quarter and 12.63 in the second quarter of 2008.

Foreclosures started represented 1.36 percent of all mortgage loans in the second quarter of 2009, virtually the same as 1.37 percent in the first quarter but up 28 basis points from 1.08 percent in the second quarter of 2008. Foreclosures started on subprime loans fell to 4.13 percent in the second quarter of 2009, from 4.65 percent in the first quarter and 4.26 percent in the second quarter of 2008. In contrast, foreclosures started on prime loans rose to 1.01 percent in the second quarter 2009, from 0.94 percent in the first quarter and 0.61 percent in the second quarter of 2008. Not all newly initiated foreclosures end in foreclosure. The lag between a foreclosure start and a completed foreclosure ranges between 2 and 15 months, with an average lag period of approximately 6 months.

The national homeownership rate was 67.6 percent in the third quarter of 2009, up from 67.4 percent in the second quarter but down from 67.9 in the third quarter of 2008. The homeownership rate for minority households increased from 49.7 percent in the second quarter of 2009 to 49.9 percent in the third quarter but was lower than the third-quarter-2008 rate of 50.1 percent. The increase in homeownership reflects the recent upturn in home purchases and servicer emphasis on home retention actions, including those under the "Making Home Affordable" program, which helped keep the number of newly initiated foreclosures flat despite rising serious delinquencies.

Multifamily Housing

Performance in the multifamily (five or more units) housing sector continued to be weak in the third quarter of 2009. In the production sector, building permits, starts, and completions all declined. The absorption rate of new rental units fell during the third quarter, and the rental vacancy rate increased sharply.

- In the third quarter of 2009, builders took out permits for 95,000 (SAAR) new multifamily units, down 8 percent from 103,000 in the second quarter and down 66 percent from 276,000 in the third quarter of 2008.
- Construction was started on 84,000 (SAAR) new multifamily units in the third quarter of 2009, down 20 percent from 105,000 units in the second quarter and down 67 percent from 254,000 units in the third quarter of 2008.
- Builders completed 247,000 (SAAR) multifamily units in the third quarter of 2009, down 16 percent from 293,000 in the second quarter and down 10 percent from 274,000 in the third quarter of 2008.
- Market absorption of new rental apartments decreased in the third quarter of 2009. Of the total number of new apartments completed in the second quarter, 48 percent were leased in the first 3 months following completion. That absorption rate is down 9 percent from the second quarter of 2009 but is the same as the third quarter of 2008.

- The multifamily rental vacancy rate in the third quarter of 2009 was 13.1 percent, up from 12.1 percent in the previous quarter and 11.0 percent in the third quarter of 2008. In contrast, the rental vacancy rate for single-family units was 9.9 percent in the third quarter of 2009, the same as in the second quarter but up from 9.4 percent in the third quarter of 2008. The vacancy rate for all rental units in the third quarter of 2009 was 11.1 percent, up from 10.6 percent in the second quarter and 9.9 percent in the third quarter of 2008.

Eye on Multifamily Housing Finance

Throughout what is likely to be known as the recession of 2007–09, much attention has been focused on the single-family housing market. This focus on single-family housing, in large part, is due to the economic distress that followed the rapid rise of subprime mortgage defaults to unprecedented levels, precipitating a loss of confidence in the nation's credit and finance markets that brought on declines in economic activity, wealth, and home prices, eventually increasing prime mortgage defaults and foreclosures to generational highs. Although the second and third quarters of 2009 have shown signs of recovery in single-family housing and the economy as a whole, it might surprise some to know that the multifamily housing sector has been subject to many of the same stresses that could bring on comparable difficulties in the coming quarters.

The 2007 American Housing Survey estimates the U.S. occupied housing stock to be 110.7 million units, composed of 78 percent single-family, 16 percent multifamily, and 6 percent manufactured or mobile homes.[1] Of the 110.7 million U.S. housing units, 68 percent are owner occupied, while 32 percent are renter occupied, with renters occupying primarily multifamily units (43 percent) followed by one- to four-family attached units (27 percent), single-family detached units (25 percent), and manufactured or mobile units (4 percent). Policymakers are concerned about the multifamily housing finance market because, among other reasons, a disproportionate share of people occupying multifamily housing units are households living below the poverty line, minority populations, and people with disabilities; thus, if multifamily housing conditions deteriorate, these populations may suffer disproportionately.[2]

During the years of rapid home price appreciation from 2004 through 2006 (and possibly into 2008 for multifamily housing), the aggressive underwriting standards that characterized the subprime home mortgage market were mirrored in the multifamily mortgage market. While subprime lenders used hybrid adjustable-rate mortgages (ARMs) and option ARMs to increase the ability of borrowers to afford higher priced single-family homes, some multifamily lenders employed pro -forma underwriting based on aggressive estimates of future earnings and 5- to 10-year, interest-only balloon and other short-term mortgages to support rising property prices in similarly overheated multifamily housing markets.[3]

U.S. multifamily mortgage debt totaled $914.3 billion and U.S. home mortgage debt totaled $10,951.1 billion at the end of the second quarter of 2009.[4] In the 3 years at the height of the subprime boom and home price bubble, 2004 through 2006, the dollar value of single-