



## Housing Chartbook: December 2008

**Mark Vitner, Senior Economist**

[mark.vitner@wachovia.com](mailto:mark.vitner@wachovia.com)

704-383-5635

**Adam G. York, Economic Analyst**

[adam.york@wachovia.com](mailto:adam.york@wachovia.com)

704-715-9660

### Housing Market Still Searching for Stability

Housing firmly remains the weakest link in the economic outlook. Not only is residential construction activity continuing to decline but falling housing prices and rising mortgage delinquency rates also continue to put pressure on the credit markets. A vicious negative feedback loop has been in play for the past several months, with tightening credit conditions dragging sales down further, which leads to additional economic weakness, larger home price declines, higher mortgage delinquency rates and ultimately even tighter lending standards.

We now expect a much deeper and more drawn out housing cycle, but we still believe the floor will be reached in 2009 and or early 2010. New and existing home sales are both expected to bottom by summer. Residential construction should find its trough in the first half of 2009. However, the trough will now be significantly lower than previously thought, as tighter credit conditions for home buyers and builders are sending activity well below recent lows. Overall housing starts are now expected to briefly fall below a 600,000 unit pace before bottoming in the first half of 2009.

Understanding where we are in the housing correction is critical in developing a coherent outlook for the broader economy. The current housing cycle is largely without precedent in timing, depth and breadth. Past housing slumps tended to follow the business cycle. The current housing slump preceded the broader economic slump by about two years, with sales tumbling once easy and inexpensive mortgage credit became harder to come by.

The initial tightening in credit followed a dramatic increase in delinquency rates on sub-prime mortgages, most of which were extremely poorly underwritten and thinly collateralized. As a result, delinquency rates soared well ahead of any noticeable slowing in the broader economy, which is something never seen before. By contrast, the more recent rise in mortgage delinquency rates and defaults is the result of the deteriorating economic environment. Unfortunately the unemployment rate will likely rise for at least another year, which means delinquency and default rates will rise even further.

The peak-to-trough decline in home sales, new construction and prices will also likely exceed anything in the postwar period. New home sales peaked in summer 2005 and have fallen by nearly 70 percent nationwide. Home construction peaked at the end of 2005 and has fallen 65 percent. Housing prices, as measured by the Case-Shiller 10-city composite index, are down nearly 25 percent since their peak in June 2006.

#### Contents

I. Mortgage Applications .....	4
II. Mortgage Rates & Affordability .....	5
III. Housing Starts ...	6
IV. Housing Permits	7
V. New Homes .....	8
VI. Existing Homes .	9
VII. Home Prices .....	10
VIII. Credit Conditions	11

We expect home sales and new home construction to bottom in the first half of 2009. New homes sales are likely to fall below a 400,000 unit pace early next year and sales of existing homes are expected to at least briefly reach a 4.5 million unit pace. This would bring the cumulative peak-to-trough decline to more than 70 percent for new home sales and to almost 40 percent for existing home sales. Home construction will fall even more dramatically, with total housing starts at least briefly falling below a 600,000 unit pace, producing a cumulative peak-to-trough decline of nearly 75 percent.

After bottoming out in the first half of 2009 we expect only minimal improvement in home sales and new home construction. Sluggish economic growth, high unemployment, and tight lending conditions will likely keep home sales well below the growth in households. This should allow even more of the excess supply of new homes to be absorbed and help bring the overall housing market back into balance by the end of the decade. We do not expect to see anything approaching strength in the housing market until 2011 or 2012 at the earliest.

The breadth of this housing slump is also highly unusual. While we have had regional housing booms and busts before, the most recent boom was confined to a handful of states. The biggest booms and biggest busts were largely contained to four states: Florida, California, Arizona, and Nevada. These four states saw the greatest amount of speculative home buying and also saw the largest price gains and declines in the country. Other notable hot spots include the outer suburbs of Washington D.C., greater New York area, greater Boston and some of the coastal metropolitan areas along the Carolina's and Georgia.

There are also a few spots where prices have slumped even though they never enjoyed a housing boom. Most of these areas are in the Midwest, and include the areas in and around Detroit and Cleveland. Housing prices have fallen precipitously in these areas largely due to extremely depressed economic conditions, a disproportionate amount of sub-prime lending, and deteriorating demographics. Home prices in the Detroit area, for example, have been falling since late 2005 and are now down to levels last seen in 1998—a cumulative drop of about 30 percent. Other notable soft spots that did not share the limelight of the housing boom include Atlanta, Minneapolis, Saint Louis and Memphis.

Much of the rest of the country did not really see all that much of boom. Housing prices rose largely in line with their long-run averages and there was relatively little speculative activity to speak of. Sales and construction of new homes is down less in these areas and home values are generally holding up relatively well. Credit conditions are tightening nearly everywhere, however, and sales and construction will remain under pressure next year.

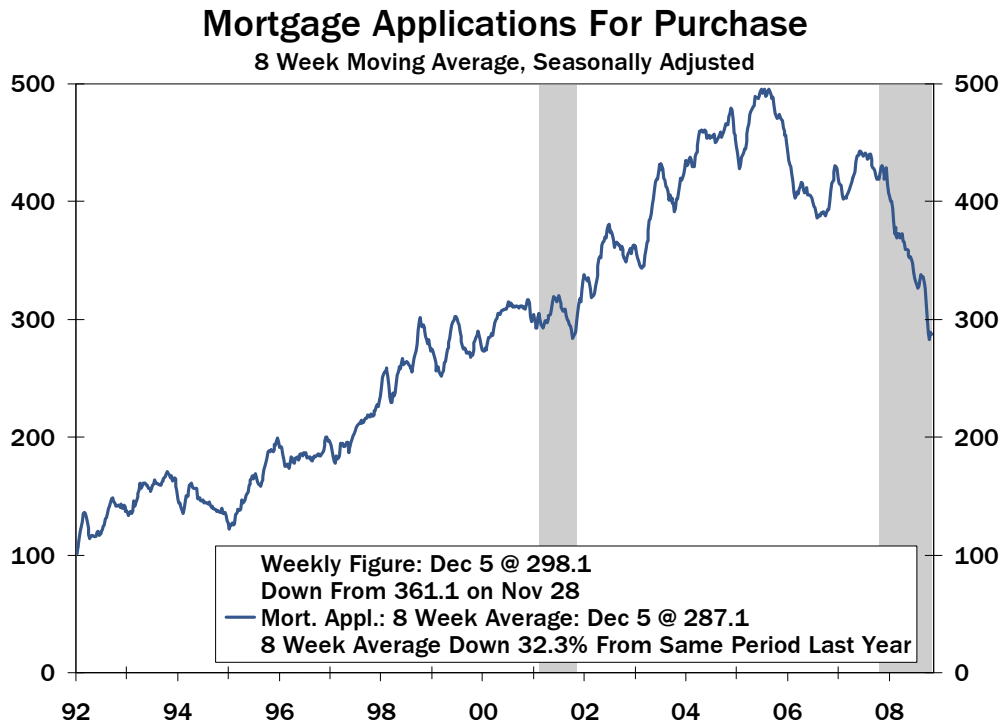
## National Economic &amp; Financial Outlook

	Actual			Forecast		
	2005	2006	2007	2008	2009	2010
Real GDP, percent change	2.9	2.8	2.0	1.1	-2.0	1.4
Nonfarm Employment, percent change	1.7	1.8	1.1	-0.2	-2.0	-0.4
Unemployment Rate	5.1	4.6	4.6	5.7	7.9	8.9
<b>Home Construction</b>						
Total Housing Starts, in thousands	2072.9	1811.9	1340.7	920.0	630.0	800.0
Single-Family Starts, in thousands	1718.5	1473.6	1034.0	630.0	395.0	515.0
Multi-Family Starts, in thousands	354.4	338.3	306.7	290.0	235.0	285.0
<b>Home Sales</b>						
New Home Sales, Single-Family, in thousands	1278.9	1049.3	768.0	495.0	380.0	450.0
Total Existing Home Sales, in thousands	7075.7	6507.6	5670.8	4970.0	4930.0	5150.0
Existing Single-Family Home Sales, in thousands	6180.8	5703.3	4957.5	4400.0	4375.0	4550.0
Existing Condominium & Townhouse Sales, in thousands	894.8	804.3	713.3	570.0	555.0	580.0
<b>Home Prices</b>						
Median New Home, \$ Thousands	234.2	243.1	243.7	227.5	212.5	220.0
Percent Change	7.5	3.8	0.3	-6.7	-6.6	3.5
Median Existing Home, \$ Thousands	217.5	221.9	215.5	195.0	182.5	185.0
Percent Change	12.8	2.0	-2.9	-9.5	-6.4	1.4
FHFA (OFHEO) Home Price Index, Percent Change	11.6	7.8	2.5	-4.4	-8.2	0.6
Case-Shiller C-10 Home Price Index, Percent Change	16.9	7.4	-4.4	-16.2	-7.6	0.5
<b>Interest Rates - Annual Averages</b>						
Prime Rate	6.19	7.96	8.05	5.10	3.25	3.75
Ten-Year Treasury Note	4.29	4.80	4.63	3.65	3.05	3.50
Conventional 30-Year Fixed Rate, Commitment Rate	5.87	6.41	6.34	6.00	5.00	5.25
One-Year ARM, Effective Rate, Commitment Rate	4.49	5.54	5.56	5.15	4.90	5.00

Source: Mortgage Bankers Association, FHFA, National Association of Realtors, U.S. Department of Commerce, U.S. Department of Labor and Wachovia

## I. Mortgage Applications

Figure 1



### Applications Volatile, but Trend is Down

Mortgage applications for purchase have been trending downward since early this year. However, there was a considerable bounce in the weeks following Thanksgiving as the Federal Reserve and Treasury announced programs to add liquidity to the secondary mortgage market and push mortgage rates lower. In response, rates have dropped sharply, almost a percentage point lower in just a few short weeks. Refinance and purchase applications alike responded favorably. If continued efforts are able to return the spread between Treasuries and mortgages to more "normal" levels we may see a sustained pick-up in applications.

Figure 2

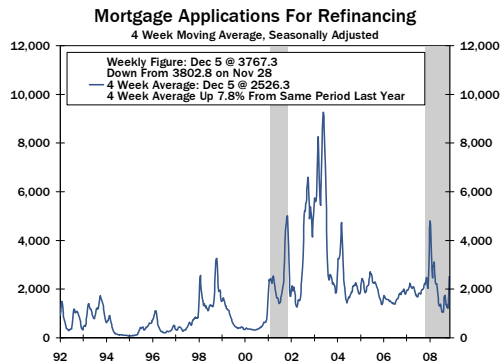
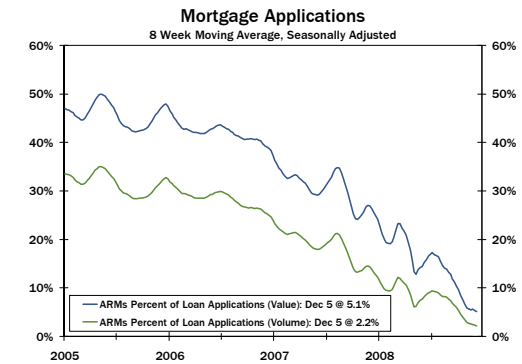


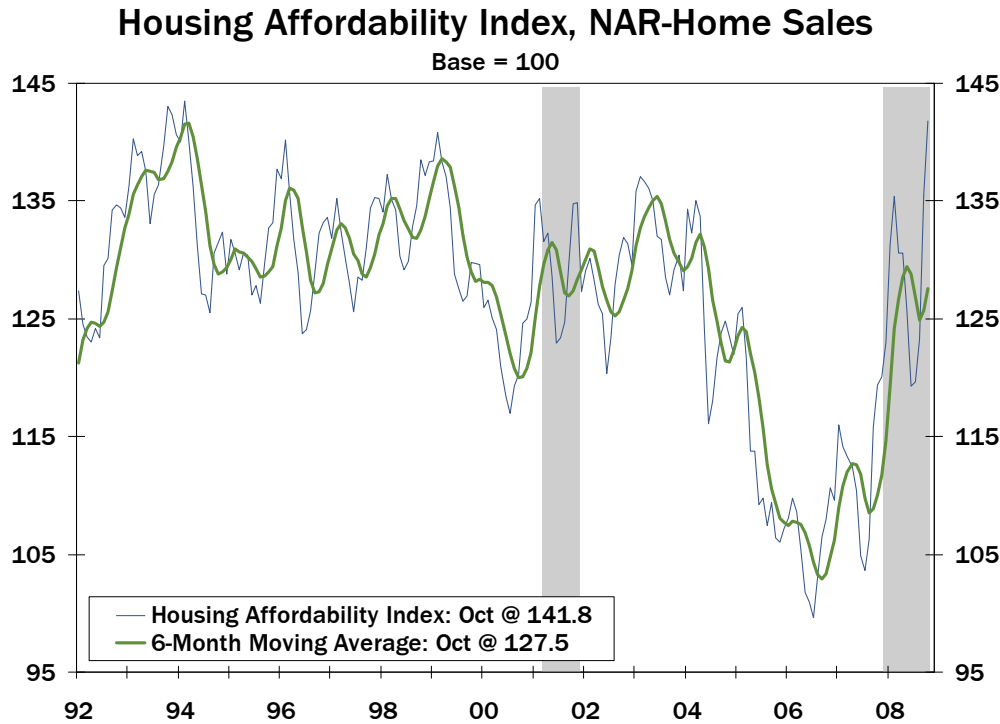
Figure 3



Source: Mortgage Bankers Association and Wachovia

## II. Mortgage Rates & Affordability

Figure 4



### Rates Significantly Lower in Last Few Weeks

We have long discussed the importance of a return to reasonable affordability levels as a precursor to a sustained housing recovery. With prices and rates now moving in the right direction, an important component of a long-term solution in housing markets is now in place. Affordability alone, however, is not the answer. If a large proportion of potential buyers are effectively shut-out of the published mortgage market, then affordability calculations mean far less for the broader market. Credit will need to flow freely again before a sustainable recovery can begin and buyers also must feel more confident about their employment and income prospects.

Figure 5

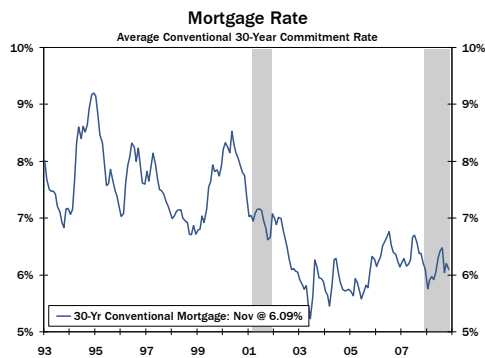
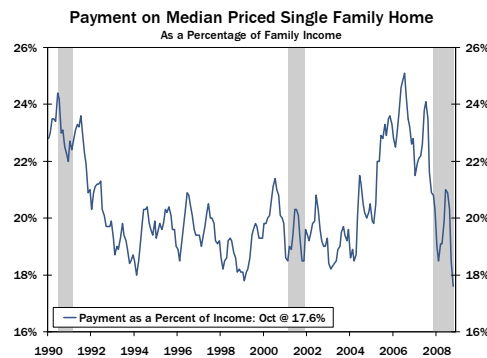


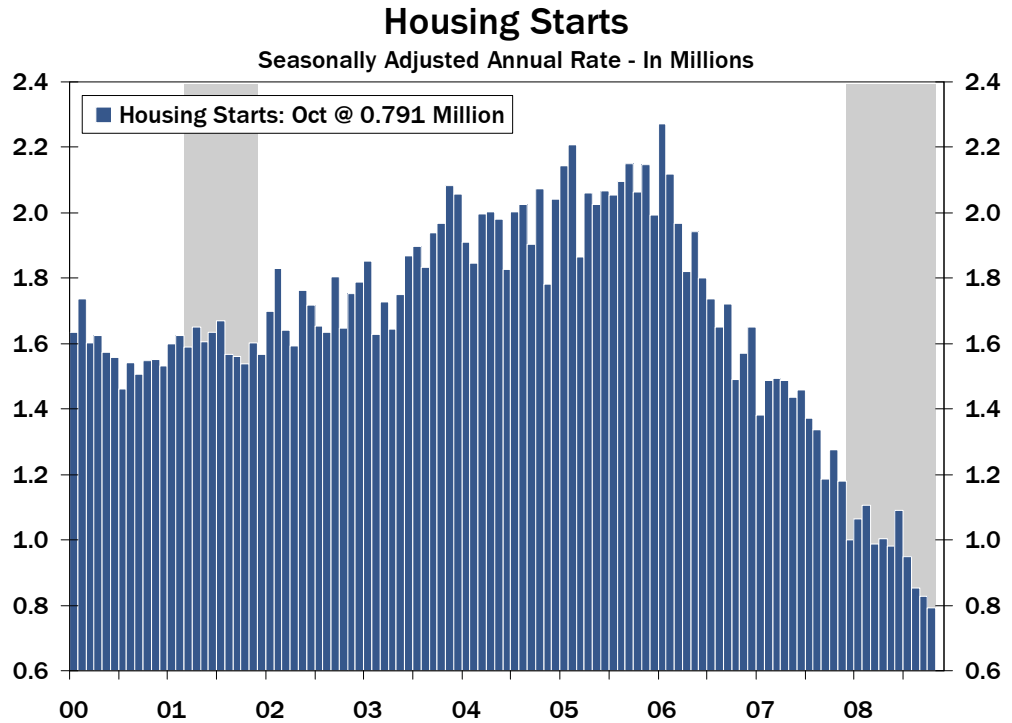
Figure 6



Source: Freddie Mac, National Association of Realtors, and Wachovia

### III. Housing Starts

Figure 7



**Starts Reached New All-Time Low**

Starts continued their long-running slide to a new low since the post World War II housing boom, when records began. The continued slides are consistent with our expectations for construction activity to continue to struggle into the first half of next year. Starts may fall another 20 to 30 percent, briefly slipping below a 600,000 unit pace in the spring. The specific bottom will largely depend on the weather, which induces volatility almost every year. Single-family starts may fail to average a mere 400,000 unit pace in the coming year as credit constraints continue to hamper builders and buyers alike.

Figure 8

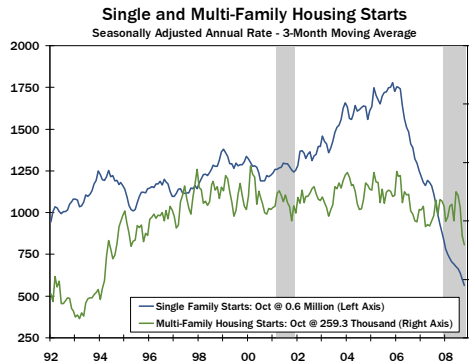
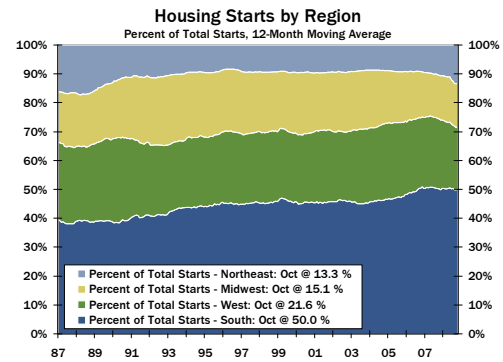


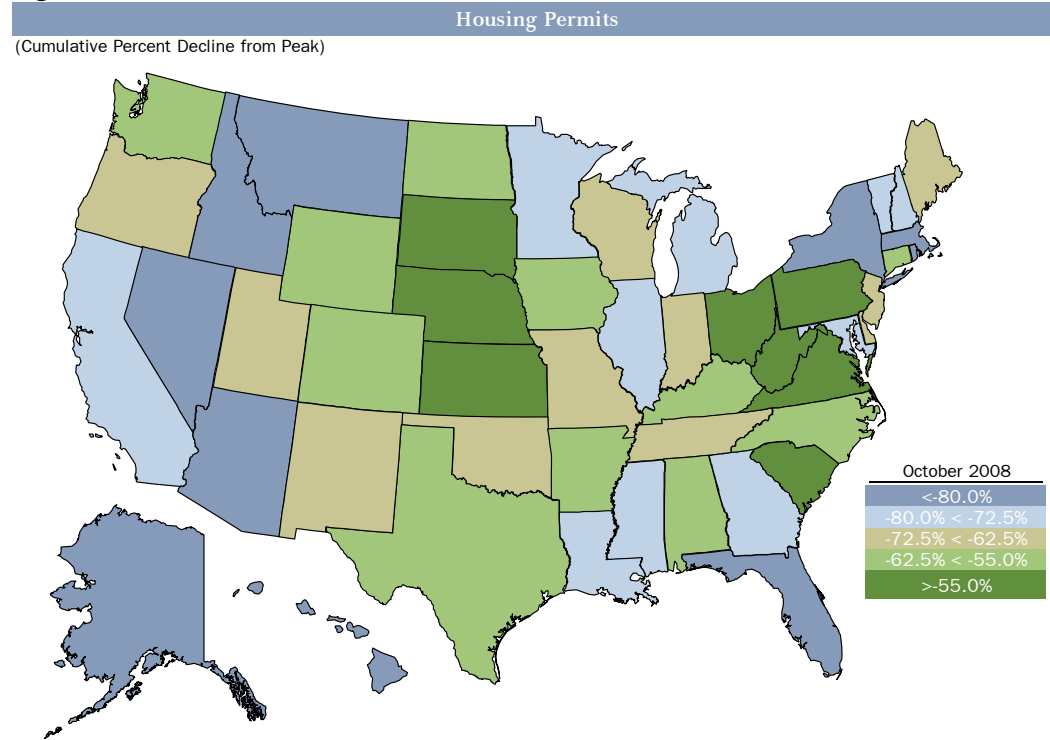
Figure 9



Source: U.S. Department of Commerce and Wachovia

## IV. Housing Permits

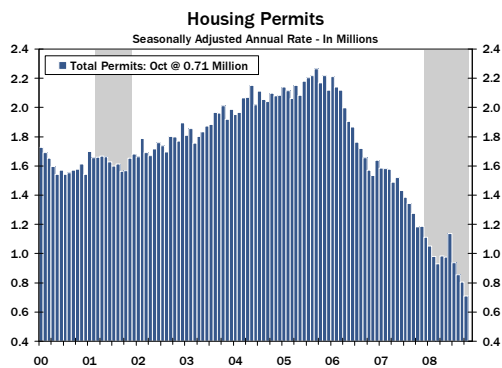
**Figure 10**



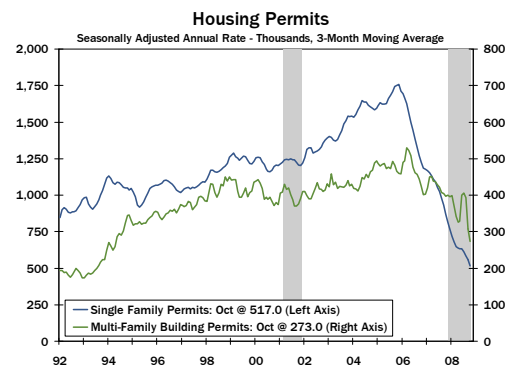
### Permits Hit Hard by Market Troubles

Permits have continued to tumble despite reaching virtually zero in many of the formerly hot markets. In states such as Florida, Nevada and Arizona permits have declined more than 80 percent from their respective peaks in 2005. While this effectively limits the downside risk in some of the hardest hit markets, permits still have room to fall in the rest of the country. As credit has dried up for new building and completed inventories remain bloated, builders have little ability or desire to start new projects in much of the country. Permits should continue to slide into the first half of 2009, in concert with our forecast for housing starts.

**Figure 11**



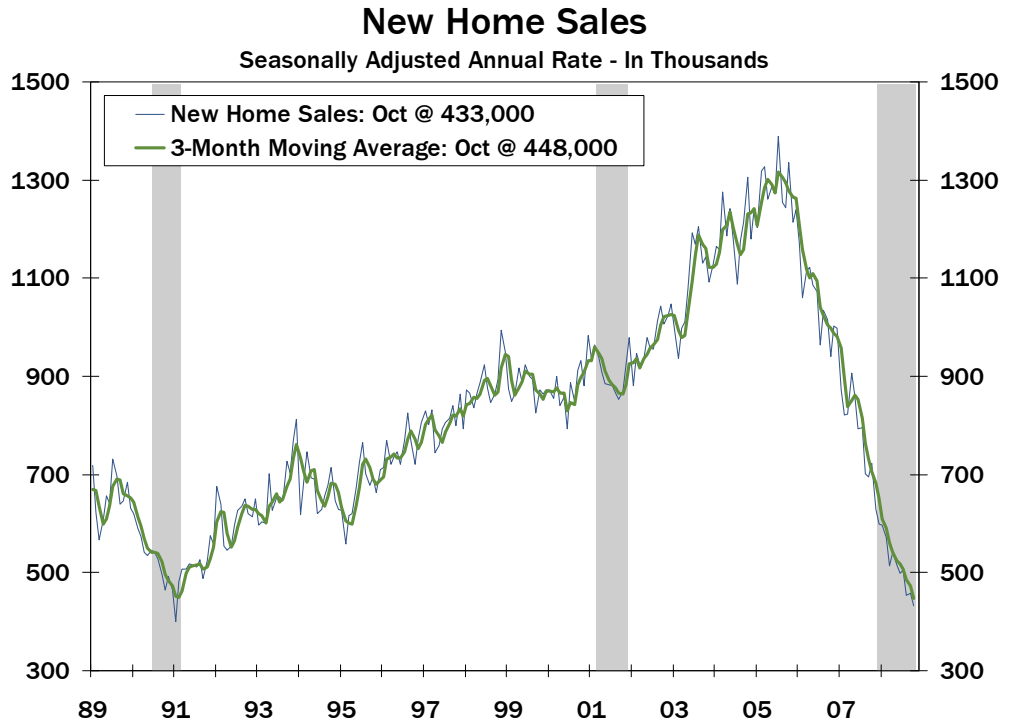
**Figure 12**



Source: U.S. Department of Commerce and Wachovia

**V. New Homes**

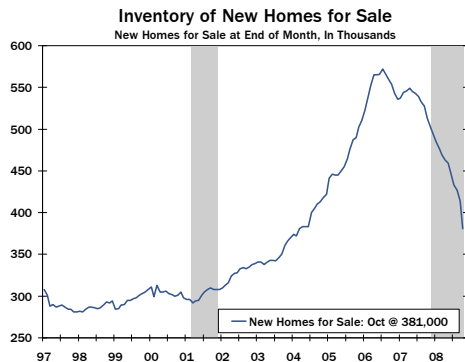
**Figure 13**



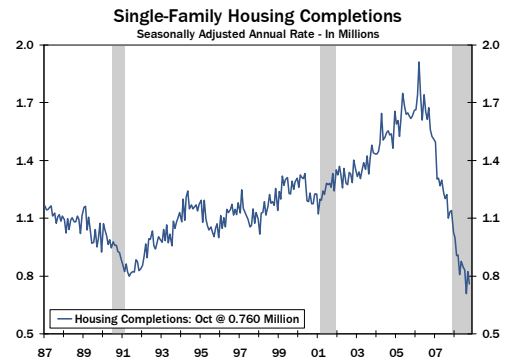
**Slide in New Home Sales Continues**

New home sales have been on a downward trend for close to three years, and we expect declines to persist into the new year. Sales may fail to average even a 400,000 unit pace next year. Inventories of new homes continue to decline at a rapid pace, however, having declined by 52,000 units in the last three months alone. With continued improvement, inventories may reach equilibrium by late spring. Low inventories will set the stage for an eventual recovery in home construction, but foreclosure-bloated inventories of existing homes, many of which are essentially new, will need to be reduced as well.

**Figure 14**



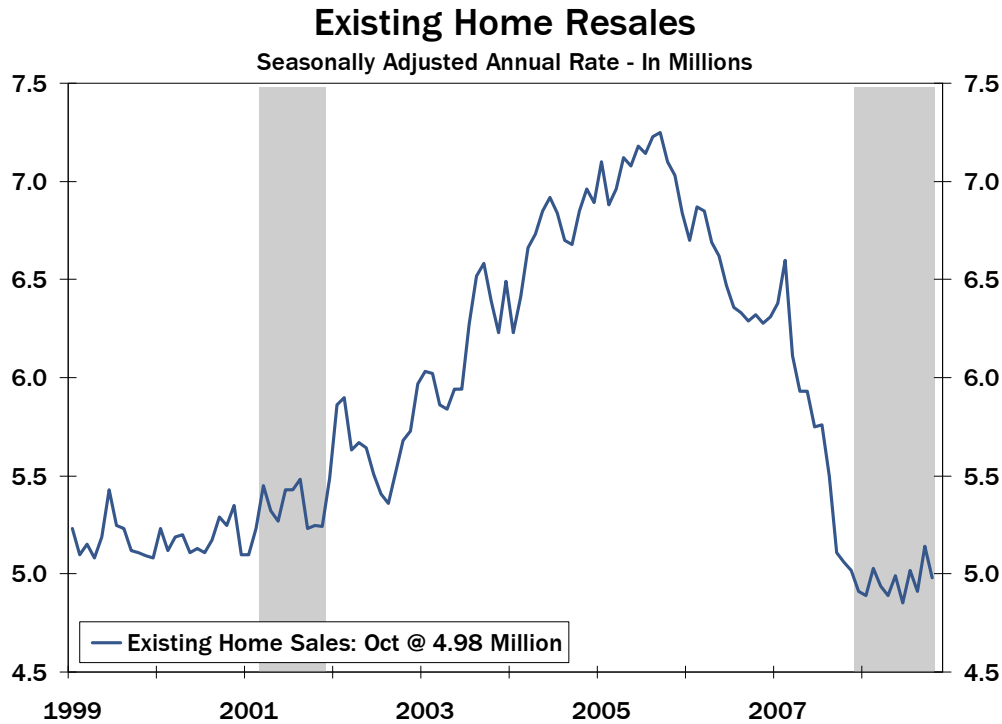
**Figure 15**



Source: U.S. Department of Commerce and Wachovia

## VI. Existing Homes

Figure 16



### Existing Home Sales Supported by Foreclosures

Existing home sales have been range bound for the past 14 months. Because sales have been supported largely by foreclosures, significant downside risk remains to this apparent bottom. An estimated 45 percent of existing homes sold nationwide in October were distressed sales, exerting significant price pressure, especially in boom/bust areas. Inventories remain elevated, which will keep pressure on housing prices. Further inventory declines are a prerequisite for a bottom. Pending home sales are roughly flat, reflecting tight credit conditions and possibly some weakening in foreclosure sales due to temporary foreclosure moratoriums.

Figure 17

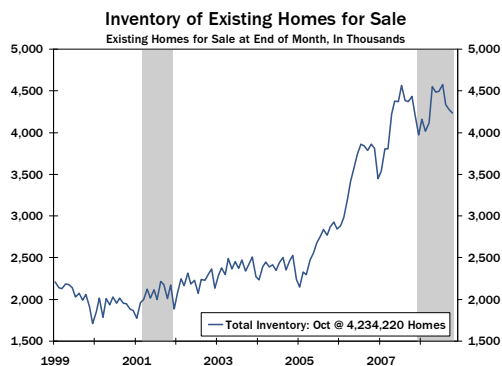
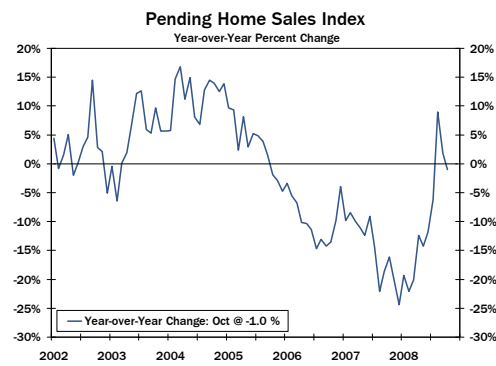


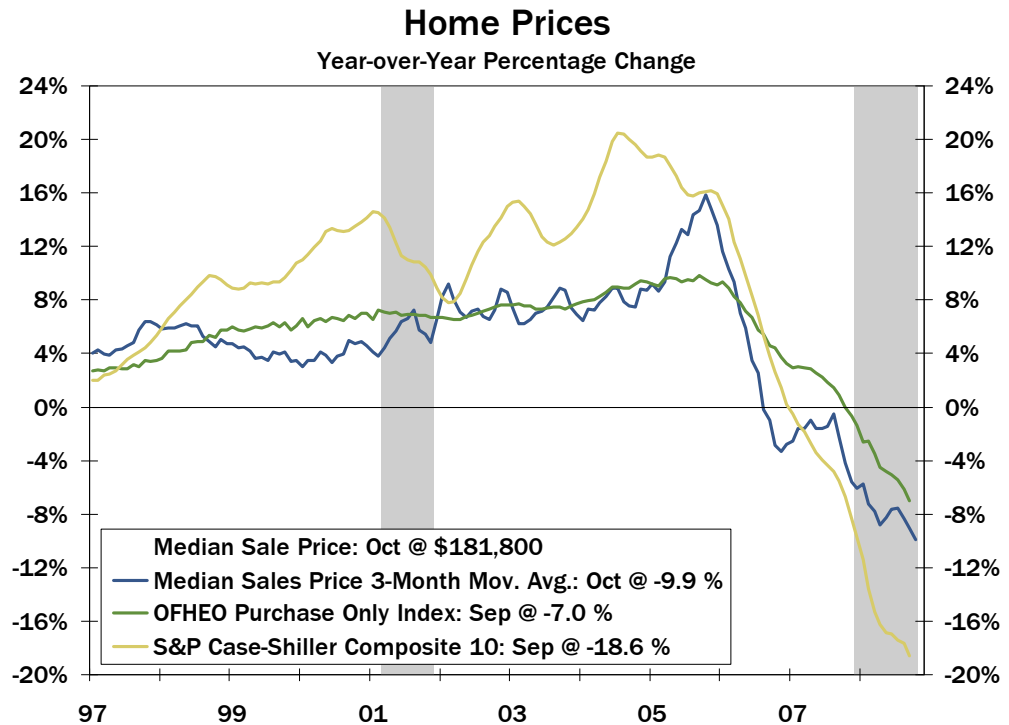
Figure 18



Source: National Association of Realtors and Wachovia

## VII. Home Prices

Figure 19



### Price Slide Reaccelerates

Price declines had shown some signs of easing this past summer, but declines appear to have reaccelerated as foreclosure sales have ramped up and credit has tightened further. The FHFA (OFHEO) home price index is starting to catch up with the declines the other indices have already shown, with some metro areas now showing declines in excess of 40 and 50 percent from peak to trough. Foreclosure activity and other distressed sales will continue to put considerable pressure on prices until credit and mortgage markets stabilize. We expect that prices nationwide will continue to fall through next year and perhaps as far as 2010.

Figure 20

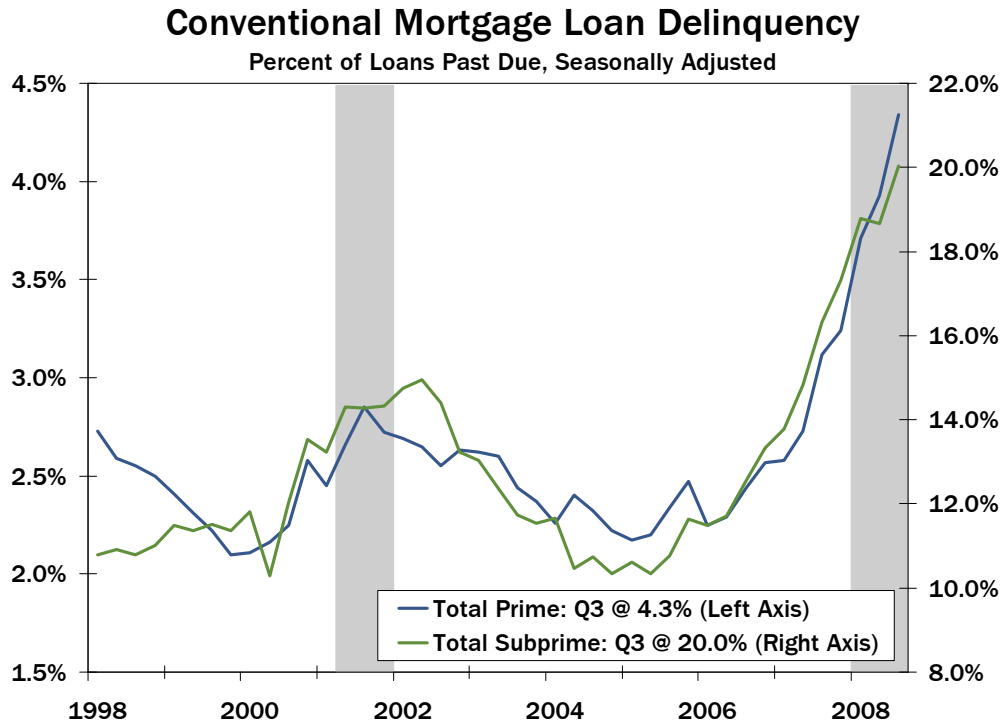
**S&P/Case-Shiller Single Family Home Resale Value**  
(September 2008)

MSA	Yr/Yr % Change	MSA	Yr/Yr % Change	MSA	Yr/Yr % Change
Dallas	-2.7%	Atlanta	-9.5%	San Diego	-26.3%
Charlotte	-3.5%	Seattle	-9.8%	Los Angeles	-27.6%
Denver	-5.4%	Chicago	-10.1%	Miami	-28.4%
Boston	-5.7%	Minneapolis	-14.4%	San Francisco	-29.5%
Cleveland	-6.4%	Washington, DC	-17.2%	Las Vegas	-31.3%
New York City	-7.3%	Tampa	-18.5%	Phoenix	-31.9%
Portland	-8.6%	Detroit	-18.6%		
U.S. - 10	-18.6%	U.S. - 20	-17.4%		

Source: FHFA, S&P Corp. and Wachovia

### VIII. Credit Conditions

Figure 21



#### Credit Conditions Continue to Deteriorate

Mortgage delinquencies and foreclosures continue to accelerate as we add the fundamental challenges of a deep recession to an already struggling housing market. As consumers continue to lose jobs and incomes decline in the first half of 2009, delinquencies will most likely continue to accelerate. Foreclosure activity will continue to have some dependency on the myriad of policy responses being considered in Washington. As loans are modified and foreclosure moratoriums are considered, the foreclosure data could become difficult to follow in the coming year.

Figure 22

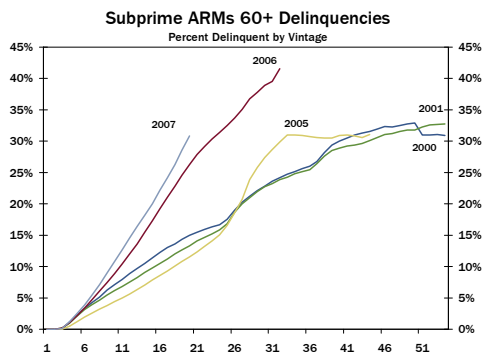
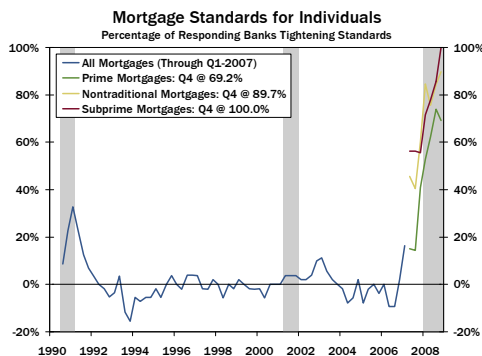


Figure 23



Source: Mortgage Bankers Association, Wachovia Securities and Wachovia

## Wachovia Economics Group

---

John E. Silvia, Ph.D.	Chief Economist	(704) 374-7034	john.silvia@wachovia.com
Mark Vitner	Senior Economist	(704) 383-5635	mark.vitner@wachovia.com
Jay H. Bryson, Ph.D.	Global Economist	(704) 383-3518	jay.bryson@wachovia.com
Sam Bullard	Economist	(704) 383-7372	sam.bullard@wachovia.com
Anika Khan	Economist	(704) 715-0575	anika.khan@wachovia.com
Azhar Iqbal	Econometrician	(704) 383-6805	azhar.iqbal@wachovia.com
Adam G. York	Economic Analyst	(704) 715-9660	adam.york@wachovia.com
Tim Quinlan	Economic Analyst	(704) 374-4407	tim.quinlan@wachovia.com
Kim Whelan	Economic Analyst	(704) 715-8457	kim.whelan@wachovia.com
Yasmine Kamaruddin	Economic Analyst	(704) 374-2992	yasmine.kamaruddin@wachovia.com

Wachovia Corporation Economics Group publications are distributed by Wachovia Corporation directly and through subsidiaries including, but not limited to, Wachovia Capital Markets, LLC, Wachovia Securities, LLC and Wachovia Securities International Limited.

The information and opinions herein are for general information use only. Wachovia does not guarantee their accuracy or completeness, nor does Wachovia assume any liability for any loss that may result from the reliance by any person upon any such information or opinions. Such information and opinions are subject to change without notice, are for general information only and are not intended as an offer or solicitation with respect to the purchase or sales of any security or as personalized investment advice. © 2008 Wachovia Corp.



**WACHOVIA**