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Housing Affairs Letter

THE INDEPENDENT WASHINGTON REPORT ON HOUSING SINCE 1961

Analysis: Housing Market Dysphoria Deepens

With the nation's housing market analysts coalescing around the prospect that the market is and will no longer be the lynchpin of the U.S. economy, they are going even further to portray a market that could be a bellwether of a new financial crisis.

Bank of America just noted that the most important segment of the housing market -- existing home sales which make up 90% of home transactions -- has peaked and worsening affordability, coupled with higher mortgage rates make, it unlikely the market will revive any time soon.

The Standard & Poor's Supercomposite Homebuilding Index in down 21% and is on track for the biggest annual drop since the 2008 housing market collapse.

With financial giant Nationwide leading the pack -- its Leading Index of Healthy Housing Markets is considered a bible of the market's long-term outlook -- and the real estate industry along with the even more reluctant homebuilders chiming in, the outlook for the market is at a worrisome low going into the normally bleak winter season.

Nationwide's Health of Housing Markets Report forecasts a neutral outlook for the housing market for the second quarter in a row -- that despite a handful of somewhat healthy market pockets the report sees as sustainable for a year or two.

Noting a mixed outlook for the national market's health, the LIHHM says, "Historically low inventories are holding back sales while pushing prices upward. Combined with rising mortgage rates, the resulting hit to housing affordability could begin to weigh on demand soon."

The Federal Reserve's third benchmark interest rate hike this week portends a continuing rise in mortgage interest rates, reflected in the burst of mortgage loan applications last week from prospective homebuyers seeking to lock in an interest rate in anticipation of the Fed increase (*see corresponding story in this issue*).

"Housing health in many regional markets is also being pressured by rising prices," the LIHHM continues. "While still half of MSAs (Metropolitan Statistical Areas) are ranked positive, more markets have fallen into neutral or negative rankings, mainly due to unsustainably rapid price growth."
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Moreover, the imbalance between supply and demand is causing home prices in more local markets to heat up," the LIHHM observes. "Price gains have accelerated in two-thirds of the country's 400 metro areas over the past year -- further challenging the search for affordable housing for homebuyers."

Nationwide puts some of the blame on its neutral outlook on higher mortgage delinqu3ency rates recovering from last fall's hurricanes along with stronger household formations.

"Without the temporary negative from last years' hurricanes on serious delinquency rates, the national LIHHM would be rated as positive, although barely." the report says.

The Nationwide report was compiled before the devastation of Hurricane Florence on several Mid-Atlantic States which is expected to compound the negative outlook.

The ultra low mortgage interest rates that helped fuel the brief revival of the housing market following the market's collapse in 2008 quickly evaporated as mortgage lenders pulled back in the wake of new, strict mortgage regulations crafted by the Consumer Financial Protection Bureau, the super housing finance regulator created out of the 2010 Wall Street Reform & Consumer Protection Act.

The new regulations all but wiped out the subprime mortgage market, the abuse of which helped fuel the 2008 financial crisis and resulting four-year recession from which the housing market struggled unsuccessfully for years to recover.

With mortgage rates on a steady rise since the beginning of the year -- the most sustained increase in the 40 years since Freddie Mac began tracking such statistics -- the increases are certain to put a great drag on an already shaky market.

That market is beset by homeowners reluctant to sell despite the increasing values of existing homes, escalating prices of homebuilding materials exacerbated by new tariffs adding thousands to the cost of new homes, and the cornering of single-family homes for rentals by real estate investors reaping profits on an overheated national rental market.

The housing market has been struggling to reignite what had been its central role in the nation's economy. But a solution so far, considering the numerous roadblocks to market sustainability -- new, complex regulations, home price inflation among them -- has made that effort difficult. And the easing of mortgage obtainability for risky borrowers poses the prospect of a new financial threat.

The Federal Housing Administration is already worried whether the many loans it is insuring could withstand a price collapse in which mortgages exceed the market value of the homes they insure, much like what occurred during the 2008 home-price bubble burst triggering the market collapse.

But FHA and mortgage giants Fannie Mae and Freddie Mac are making mortgage loans more attractive to low- to middle-income homebuyers to help generate a new subprime loan market. Fannie Mae's Home Ready and Freddie Mac's Home Possible programs are now offering mortgages for a little as 3% down to buyers who can't afford the customary 20% downpayment.

Fannie and Freddie's regulator, the Federal Housing Finance Agency that has controlled their activities for the past 10 years under the Treasury Department's conservatorship -- initiated in 2008 to prevent their default, has just introduced its plan for a new "affordability metric" to allow lower-income families to meet loan requirements under a new set of loan guidelines.

While there are now more checks in place to ensure the 2008 market collapse doesn't repeat itself, those restraints are untested on a large and mostly unwieldy market.

Homeowners are reluctant to sell in order to cash in on the increased values of their properties because there are scant affordable replacement properties available. At he same time, even with a booming economy in place, there are few prospects available for homebuyers other than in a handful of markets nationwide where construction is booming, such as Houston, TX.

All that portends a bleak housing market much like what the Nationwide report portrays and many market economists fret over.

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