

THE REAL ESTATE REPORT

March 2007

Market Roundup for 2006

Top line: For a year and a half the nation and our region has been in a real estate market characterized by dramatically increased numbers of new and existing houses for sale, fewer buyers, fewer sales, longer periods of time to sell the average house, but a remarkable resistance to lower selling prices despite these other negatives.

Middle line: The market has reached bottom just about now and will slowly advance during 2007 and 2008, supported by increasing economic activity, increasing average incomes, decreasing inventory of houses for sale, and continued low mortgage rates. Caveat: a major international incident (a bigger 9/11) or trend change (Japan, China and others deciding not to absorb all our debt bonds) would change this prognostication.

Bottom line: For all those owners who rushed to sell their homes and have not been able to since April 2005, don't panic, the sky is not falling. For all those would-be buyers who put off buying because prices had gone up so much in recent years that they now anticipate a market implosion, observe that prices have not gone down, and likely will begin to increase in 2007. These conclusions are based on national market figures. Regional, statewide and especially county performance varies more widely, read on.

The national market

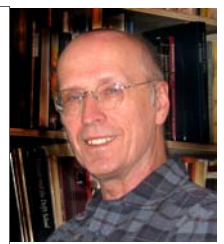
Now the details. In parts of the country where there has been speculative new construction which, unsold, overhangs the market, the adjustment will take longer. If you see a lot of empty new houses in your neighborhood, be patient about a recovery, give it another year to work off this large inventory.

Sale prices of existing houses have been remarkably resistant to this soft market. Nationally they actually increased in 2006 (1.1%) and should again in 2007 (1.9%) and 2008 (3.2%) according to the National Association of Realtor's current forecast. Their Pending Home Sale Index (based on contracts signed but not yet closed and thus a leading indicator) showed a change in trend upwards in sale numbers (+4.9%) in December, the biggest increase in monthly sales since March 2004, after nearly constant decreasing activity since July 2005. NAR's chief economists concluded from this that "...buyers are becoming more comfortable, sensing the timing is good and that their local market has bottomed out..."

Even though the national level of sales of single family homes dropped 8.1% in 2006, median prices stayed the same. How come? If sales are off shouldn't prices accommodate this change in supply and demand by decreasing? Buyers have certainly expected this as many of them just sat on the sidelines hoping for bargains. Since early 2005 sellers had rushed to the starting post in great numbers, boosting inventories of houses for sale as much as 50%.

Used to heady annual increases in many regions (ours included) resulting in a doubling of prices over a five years period, they over price their houses, backing off some when they did not sell. Those that did sell sold for prices similar to the

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prior year. It looks like the sellers had a better sense for what this market was doing than the buyers.

Mortgage rates (and availability of lending money) are a prime determiner of real estate sales. With low inflation continuing the Federal Reserve's Open Market Committee has not boosted rates since last summer and appears to be willing to continue this policy, keeping bond rates and thus mortgage rates steady at historically low levels -- 6.31% for the 30 year fixed rate, down from 6.93% last summer.

The regional markets

Despite the national market figures, regional differences are pronounced.

NAR statistics on existing house sales and median prices by region, December 2005 to December 2006, highlight these differences.

Midwest	sales	-5.8%	Prices	-2.9%
South		-7.1%		0%
Northeast		-5.5%		+3.7%
West		-15.5%		+1.5%

Our region declined in sales less than other regions and had the best increase in prices, a healthy resistance to negative market factors, boding well for a recovery.

The New York State market

The more locally you look at market performance the more volatile it appears, especially at the county level. The New York State Association of Realtors (NYSAR) reported that in 2006 single family house sales dropped 6.3% from the prior year and the median selling price, \$248,500, was up 6.4% (NYSAR reported -2.8% in error), higher than the Northeast as a whole. But on a county level and month-to-month comparisons the figures can be dramatically different. For example, comparing 2006 to 2005. Sales gains were realized in only 16 of 59 counties. Some were down 15 to 25%. There was even wide disparity between some adjacent counties, such as Rensselaer County +14.7% vs Columbia -15.9%. Despite drops in sale numbers, nearly all other counties had increased median house prices year on year. Generally counties which had the greatest increases in recent years had the biggest decreases in number of sales this last year. Under priced counties did the best as buyers sought out these relative bargains. Several counties with low median prices had sale numbers and prices this last year up by 20% or more. Those are now hot markets after years of being neglected. Go west (and north) young man, there are still plenty of bargains.

Looking back over the last year, the northern part of Berkshire (MA) county experienced a healthy 4.9% increase in single family house sales (third quarter 2006 from a year earlier, the latest available) in a state which was off 20%. The Capital District was up 2.5% in the same period while the state as a whole was off 7%. Both regions did surprisingly well according to National Association of Realtors statistics. Adjacent Hudson Valley counties, however, experienced significant declines in num-

ber of houses sold in the same year period to September 30, 2006 yet still maintained nearly even median prices (NYSAR data): Columbia County down 27.3%, Greene County down 10.9%, Dutchess County down 9.6%, Saratoga County down 7%. Weak sales performance is also characteristics of the remainder of the lower Hudson Valley in that period.

The Massachusetts Association of Realtors recently reported “It is hard to ignore speculation concerning a housing bubble in the local real estate market, but are those concerns warranted? Recent research conducted by the National Association of REALTORS® for six metropolitan housing markets in Massachusetts suggests that the housing price bubble does not and never did exist in the local markets throughout the Commonwealth. In most areas of the state, sound economic and housing market fundamentals are in place, which should ensure that no significant price declines in home values are anticipated in regional housing markets in Massachusetts over the coming months.”

More considerations

Harvard’s annual *State of the Nation’s Housing* confirms that present market conditions point to a resumption of a positive real estate market this year and into the future. It points out that in past housing recessions one or both of two conditions need to be present: increasing unemployment and/or overbuilding. In most of the nation neither is present and where there is overbuilding the market is adjusting with lower prices. Historically major unemployment episodes have resulted in housing price declines of 4.5% . For overbuilding, the average declines have been 8.3%. This is not the case nationally nor in our immediate region (Berkshires to Capitol District) which would indicate that we will likely see a slow resumption of a positive market this year.

The report draws attention to a dark cloud on affordability of housing, especially for lower and middle income families. For house ownership, this has become more acute because of the dramatic increase in housing costs in so many regions. Zoning regulations have contributed to the cost of building affordable houses by specifying larger minimum lot sizes, increased infrastructure costs, and more time and expense in getting permits.

For those who can no longer afford to buy a house, the alternative is to rent, an option which is also suffering from an increasing lack of affordability. The combination of property taxes increasing at twice the rate – or more – of average income increases plus the recent strong increase in heating fuel adds further to the housing unaffordability. We are likely to see increased government subsidies to lower and middle income families to cope with housing cost inflation.

Recent publications (try James Howard Kunstler’s *The Long Emergency*, for an eye opener to our new century) are pointing to a new world order based on the supply of oil not keeping up with increased demand, especially with China and India expanding their energy needs so rapidly. Conservation and new fuel types are unlikely to fill the gap, at least in the near future. This will result in ever increasing fuel cost, which means living closer to work, not in far flung suburbia. To help compensate for this we are likely to see a lot more “green” construction (better insulation, passive solar, photovoltaic arrays, etc), and – reversing a long trend -- smaller houses. Manufactured houses by modular or panel construction likely will become more popular for good reasons: increased quality of construction, better fuel efficiency and lower construction cost. Will those suburban mega-mansions become white elephants as they did in the Depression?