

Real Estate Market Review

Last Updated Saturday, 30 May 2009

We Were Warned 3-Years Ago - Isn't Hindsight Great!

One of the many dire predictions done these past few months by many [Profile.market] ‘bubbleologists’ out there -

that is all those who indulge in the contemplation of bubbles in the [Profile.market] real estate market of all sizes and colors, whether real or imaginary, coming our way - was that by now real estate markets everywhere would be inundated and swept away by a tsunami of foreclosures of apocalyptic proportions.

The general rationale among those specializing in the fine art of staring at crystal balls (or perhaps at several empty bottles of rum) was that the steady increase in interest rates, the consequence of a tightening monetary policy implemented by the Fed since mid-2004, would have led by now to a collapse of the adjustable-rate mortgages (ARMs) market, since consumers could not possibly cope with the increased monthly payments. This, in turn, would dramatically increase mortgage defaults and foreclosures, with the end result that real estate markets everywhere would be flooded with excess inventory at deflated prices, thus causing markets to crash - the tsunami I was talking about.

The Mortgage Bankers Association of America (<http://www.mbaa.org>) does not seem to share this particular vision of the end of the world. In its Economic Outlook update released in May 2006, the Mortgage Bankers Association of America (MBAA) pegs the ARMs share at 27 percent, down from the 36 percent peak of early 2005, an indication that many prudent consumers have locked in already. Likewise, the inventory of mortgages held by banks is virtually unchanged at 1,500 billions (aggregate nominal face value of mortgages, by dollars), the same level of 2005, suggesting that, rather than defaulting, consumers are ‘holding on’. And, finally, the rate of delinquency is at 4.38 percent, down from 4.70 percent in the final quarter of 2005, clearly another measure of consumers financial stamina, and an indication that banks were actually faring worse when real estate markets were doing better.

But that’s not all!

In the Mortgage Finance Forecast released also in May 2006, MBAA highlights that the rate of housing starts nationwide has increased nationwide, up to 2,131,000 units (annualized) for the first quarter of 2006 from 2,059,000 units in the last quarter of 2005 – an increase of 72,000 units representing a robust +3.496 percent overall, although this rate is forecasted to slow down as the softening trend in real estate markets continues throughout the year. Home sales overall are forecasted to decrease by 501,000 units nationwide to 6,574,000 units by December, 2006 from the 7,075,000 of December, 2005. Although this represents an annualized drop in sales of 7.08 percent compared to last year, it can hardly be called a bubble burst!

And here is the most surprising figures of them all – surprising for the bubbleologists, that is. Notwithstanding the increase in interest rates and the toll that many think ARMs will take on defenceless consumers, MBAA forecasts that the average market share of ARMs will remain constant at 27 percent of institutional mortgages for 2006, down only 3% from the 2005 average. The significance of this forecast is twofold: 1) MBAA does not anticipate that interest rates will increase significantly higher for the remainder of the year and 2) MBAA mirrors a Gallup survey conducted in May 2006, which found that only 11 percent of Americans worry about ARMs, down from 20 percent in 2005.

And why should they worry? In the latest release, the Bureau of Labor Statistics, has pegged the Consumer Confidence Index at 109.6 in April, up from 107.5 in March and higher than the 103.8 of December, 2005. The Consumer Confidence Index is now at the highest level since March, 2002, with the average family income up 0.8 percent in March, 2006.

To finish, I would like to spend a few words on how politics are filtering into economics, especially in times of elections. It is a shame that an increasing number of Bloggers and even journalists out there are twisting and interpreting economic data to fit their own political agenda. Although November, 2006 is pretty much around the corner and the battle is on to take control of Congress, the manipulation of economic and statistical data for political ends and means is a great disservice to consumers, no matter the political colors.

For example it is not true, like some Bloggers assert out there, that the recent appreciation in [Profile.market] real property values is the direct result of President Bush’s domestic economic policies. Real estate capital growth was largely due to the correlation between capital and employment or, if you will, between income and labor. An increase in levels of consumption has set forth an increase in prices caused by a corresponding increase in demand, in itself generated by a commensurate increase in the income-employment factor. So growth was derived by the equilibrium of capital and investment with labor and employment. And since, furthermore, production is in direct function of consumers spending which increases as unemployment falls, capital accumulation has increased as employment rose steadily. It is as simple as that!

Likewise, it is not true that President Bush is the main culprit for the real estate bubble burst – like many Democratic sources imply and some actually cry out loud. Poor President Bush has absolutely nothing at all to do with real estate bubbles and their bursts, essentially for two reasons: 1) because there are no bubbles in real estate and 2) because there are no bursts either. Like Prof. Bernanke has repeated now several times, far from being a bubble burst the present cooling-off trend through higher interest rates will have the beneficial effect of consolidating market wealth achieved thus far, by allowing the economy to get an even footing through a slowdown of capital appreciation and, at the same time, allowing real wages to catch up, thus reducing the affordability crisis and rejuvenating the pool of buyers.

And, finally, it is not the President of Iran, Mahmoud Ahmadinejad, that is trying to promote his country’s nuclear programme by putting a stranglehold on North America’s real estate markets through higher crude prices, while attempting to get rid of Secretary Rice at the same time (I know, this is laughable, but I read it in the commentary of a political blog – TIME Magazine should make this particular blogger ‘Man of the Year’).

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