Housing Collapse

Keith Jurow | May 30, 2012, 8:31 AM | 26,869

Editor's Note: Keith Jurow has been posting articles regularly for the past two years on BUSINESS INSIDER. He is the author of Minyanville.com's Housing Market Report.

After being one of the few analysts who was correct in stating for the past two years that there is no housing bottom in sight, it's time for me to tell you what I see ahead.

Housing pundits are nearly unanimous in declaring that housing markets are showing signs of bottoming. This is nonsense!

What is Really Happening Now

We hear that California markets are showing signs of revival and that prices are rising in certain markets. Let's see. Here are the latest figures from trulia.com.

In Los Angeles, trulia reports that the average price-per square foot for homes sold in February through April was down 9.3 percent year-over-year for 3-bedroom homes and down 8.7 percent for 2-bedroom homes.

In San Francisco, allegedly one of the hottest areas in the nation, the 3-bedroom average price-per-square-foot was down 4.7 percent year-over-year and 1-bedroom price-per-square foot was down 8.1 percent.

Price-per-square-foot statistics are the best way to compare prices because it does not matter how large the house is. Median prices are skewed by square footage as well as by the percentage of distressed properties sold.

Here in Connecticut where I live, double-digit price declines are commonplace:

Fairfield County – down 10.7 percent year-over-year
Darien – down 13.5 percent New Canaan – down 15.7 percent Norwalk – down 13.8 percent New Britain – down 15.3 percent Branford – down 15.9 percent City of New Britain – down 15.3 percent City of Hartford – down 14.4 percent

These statistics come from Wm. Raveis & Co.'s website – raveis.com. They are the largest family-owned brokerage firm in the northeast with offices in 7 states.

Their reputation for integrity is excellent. Try it. You can search any town/city in six states in the northeast plus Westchester County in New York. No indices here, just the raw data.

The figures above are for all single-family homes sold in the period February through April of 2012 compared to the year earlier time frame. You can also find price comparisons for different time periods to give you a broader perspective. My latest BUSINESS INSIDER article showed prices for several northeast states.

Serious Mortgage Delinquencies – The Real Story

We have been told that the rate of mortgage delinquencies has been declining over the last year. Let's see.

In the NYC metro area, the banks drastically cut back foreclosing on properties in the spring of 2009 and have never changed their policy. This has nothing to do with the robo-signing scandal which occurred 18 months later.

Through sheer persistence, I obtained accurate statistics on serious delinquencies from the New York State Division of Banking. Let me explain.

In late 2009, the NYS legislature passed a law requiring all servicing banks in the state to send a "pre-foreclosure" notice to all delinquent owner occupants. It warned them of possible foreclosure and explained steps they could take to prevent this. These servicing banks were also required to report to the Banking Division all notices that were sent.

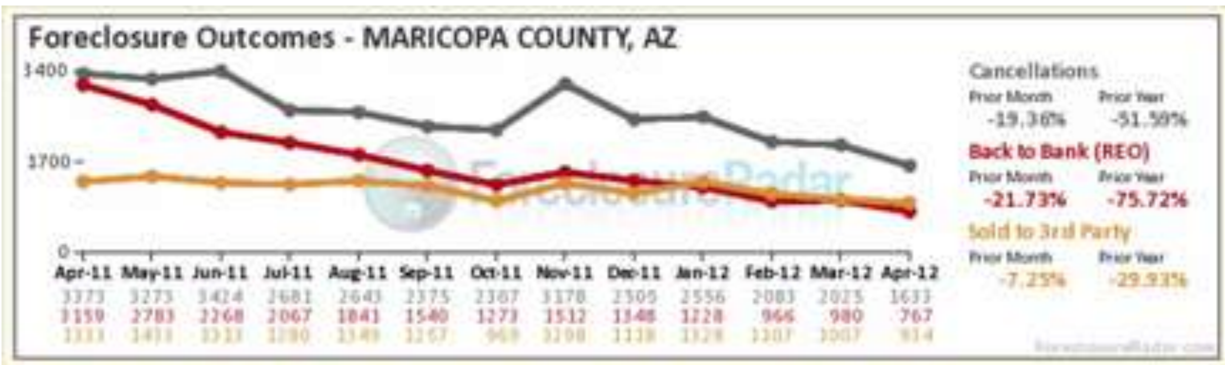
The Division published preliminary figures in October 2010 but has never updated these numbers. Here is what I learned.

Through the end of March 2012, a total of 192,000+ pre-foreclosure notices had been sent to delinquent owners in NYC. This does not include delinquent investor-owned properties because the law did not require servicers to send notices to them. There are lots of 2-3 family homes in the four outer boroughs of
NYC. I estimate that there are roughly 75,000+ delinquent investor-owners.

This means there are roughly 265,000 seriously delinquent homeowners in NYC who have not yet been foreclosed. Why so many? The banks do not foreclose in NYC. As of May 24, foreclosure.com reported a total of 301 foreclosed properties on the active MLS and 103 in Brooklyn. Together, these two boroughs have a total of 4.7 million residents. That is more people than live in Maricopa County where Phoenix is situated.

Hard as it may be to believe, the situation is even worse on Long Island. With fewer than 3 million occupants, Nassau and Suffolk Counties showed a total of 175,000 pre-foreclosure notices sent out as of the end of March.

Banks Gamble Again By Closing the Foreclosure Spigot



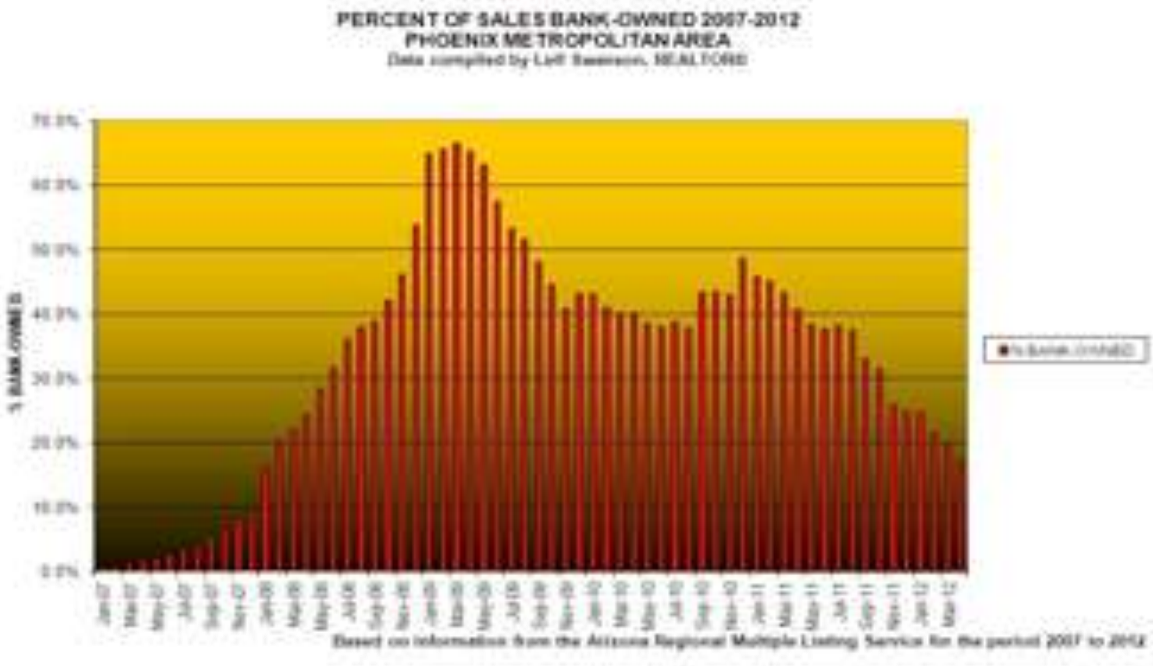
If you think the reduction in foreclosing is limited to the NYC metro markets, you’re mistaken. Take a good look at this revealing chart for Phoenix from foreclosureradar.com.

Bank repossessions in Maricopa County plunged from 3,159 in April 2011 to a mere 767 a year later. Clearly, the banks are gambling that this will help to stem the decline of home prices.

Or let’s take a look at Miami -- a market that suffered one of the largest price collapses since the bubble popped. In 2010, the banks repossessed 23,000 properties just in Miami-Dade County. They foreclosed on 54,000 properties in the 3 south Florida counties of Dade, Broward, and Palm Beach. Although they sharply curtailed repossessions in 2011, that number still totaled roughly 35,000.

I spoke with the head of data for the Miami Association of Realtors on May 18 and was amazed to learn that there were only 282 repossessed properties on the active MLS.

A similar tactic has been occurring in Phoenix. During the height of the credit crisis in early 2009, 2/3 of all homes sold in Maricopa County were repossessed properties. That percentage was down to 40 percent a year ago. Take a look at this chart from Phoenix broker Leif Swanson.



In April, only 17 percent of all homes sold in the Phoenix metro were REOs on the active MLS. Banks are hoping that this cutback of foreclosed properties for sale will steady home prices.

Why the Collapse is Coming

Despite all the mortgage modifications, refinancings, and cutbacks in REOs for sale that have taken place in the past 2 ½ years, prices continue to decline. Will this change anytime soon?

Let’s take a look at potential buyers. It’s an undeniable fact that the trade-up buyer is gone in every major metro market. Most of those who would like to sell and buy another house are unable to do so. Their house is underwater and their equity is gone.

I talk to Phoenix broker Leif Swanson on a regular basis. He has explained that the few normal sales he closes are for sellers over 70 years old. Because they have owned the property for decades, they have equity. The trade-up buyer of the past – ages 30-60 -- has disappeared.

That leaves first-time buyers and investors. According to Inside Mortgage Finance, their survey of roughly 2,500 brokers nationwide finds that roughly 30 percent of all purchases nationwide are by investors, many paying all-cash. Some analysts have argued that this is a good thing for housing markets. This is rubbish. There aren’t enough potential all-cash investors to make-up for the collapse of the trade-up market.

Furthermore, investors are concentrating in the sand states where prices have collapsed more than anywhere else – Arizona, Nevada, and Florida. Prices have plunged so much in the past year here in Connecticut because there are not many investors.

That leaves first-time buyers. Do you really think there are enough potential first-time buyers out there to keep prices from declining further? I've written extensively about renters and the changing attitude toward buying a home.

Had it not been for the FHA's program of mortgage insurance, buying by first- timers would have collapsed. The latest FHA Single-Family Outlook revealed that 78 percent of all purchase mortgages went to first-time buyers.

When you look at securitized mortgages bought or guaranteed by Fannie Mae and Freddie Mac, the picture is very grim. In the fourth quarter of 2011, 80 percent of all Fannie/Freddie mortgage originations were refinancings. The average down payment was 30 percent. How many first-time buyers can put that much down?

More recently, an April 2012 Federal Reserve Board survey of bank loan officers found that fewer than 4 percent of those surveyed said that their bank had eased mortgage lending standards for prime mortgages.

Worst of all is what I've been saying for more than a year. A growing number of prospective first-time buyers are reluctant to buy even though they can afford to. Their attitude is this: What's the rush? I think prices are headed lower. And I like the flexibility that renting gives me.

As prices continue to decline, this new attitude feeds on itself – it becomes a vicious circle.

What About the Potential Sellers?

Over the past two years, I have written extensively about the so-called "shadow inventory." It's real, growing and very scary in what it says about where things are heading.

You need to keep in mind that the total number of underwater homeowners is far larger than just those who purchased during the bubble years 2004-2007. Millions of homeowners took out what became known as "cashout" refis. Banks were only too willing to shovel out cash to owners whose homes were rising at double-digit rates.

What has been almost completely overlooked by the media is the enormous number of properties with second liens. There are still nearly 12 million home equity lines of credit (HELOC) outstanding. It's safe to say that 98 percent or more of these properties are underwater. Roughly 30 percent of all HELOCs were originated in California. There are millions of owners there with HELOC balances in excess of $100,000.

The HELOC boom began in 2003. Most of these revolving lines of credit were interest-only loans for the first ten years. After that, they convert into 15-year fully amortizing loans. This means that beginning next year, these loans start to transform into a fully-amortizing loan. The number of HELOCs which do this increases in 2014 and even more in 2015 and 2016.

What will these homeowners do when their HELOC payment soars from a few hundred dollars per month to more than $1,000. The monthly payments that will go into effect in California are mind-boggling.

Finally, let's not forget all those homeowners who have pulled their home off the market in the past year. A recent survey published by ProTeck Valuation Services showed that MLS listings had dropped more than 35 percent over the last year in metros such as Phoenix, Miami, Atlanta, Orlando, Tampa and Riverside,
CA. Dozens of others saw reductions of more than 15 percent.

Many are frustrated homeowners who were unwilling to take the hit and do a short sale. Nearly all are simply hoping that the pundits are right that housing markets are bottoming this year. Sooner or later, some of these homes will be put back on the market.

Conclusion

Let's put this housing credit bubble and collapse in historical perspective. Prior to this disaster, the largest bubble and collapse in American history was the U.S. stock market from 1927 to 1932. Most of you probably don't know that during that stock market boom, you could buy stocks with only 10 percent down. Brokers would lend you up to 90 percent of the price. Sounds like the housing bubble, doesn't it?

The Dow Jones Industrials peaked at nearly 400 in October 1929. When it finally hit bottom, the DJI had collapsed to 34. Now that's a true collapse. Every few months, pundits would claim that the worst was over. Sound familiar? Then the stock market would plunge lower.

Do I see anything on the horizon that could turn things around and correct the growing imbalance between potential homebuyers and sellers. No. Nothing whatsoever. Wishful thinking won't do it.

My advice to homeowners in nearly all major metros is quite simple. Get an appraisal from a professional appraiser to find out what the market value of your home is. Seriously consider putting your home on the market within the next six months. You will have a chance of selling it.

Within a year, I expect many of the weakest markets to show signs of unraveling. Perhaps the most vulnerable market is the entire NYC metro area. Sooner or later, the banks will have to start foreclosing or even doing short sales. When these properties hit the market in significant numbers, I have no doubt that prices in the entire region – where 19 million people reside – will collapse.

For other major metros, the plunge will depend on how crazy the bubble was during 2004-2007 and how large the total number of underwater owners becomes.

Predictions are always iffy. But I am convinced that things will get ugly from here and that there is no solution that can prevent this collapse. The wisest thing is for you to do is prepare for the worst. Is there anything wrong with renting a nice house or condo to ride out this perfect storm?