Michael Spottiswoode's Albuquerque Real Estate Newsletter Summer - 2010

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Real Estate Recovery by 2013

Economists speaking at the annual meeting of the National Association of Real Estate Editors earlier in the year agreed that the housing market likely will not recover until 2013. Stan Humphries, Zillow chief economist, said home prices continue to decrease, and he sees the "tremendous amount of shadow inventory" delaying recovery so that "the market will be flat in nominal terms for three to five years".

Fannie Mae chief economist Doug Duncan thought it would be another three years before new household formation and housing starts pick up. He believed home prices would fall 1-3% before bottoming out in the third quarter of 2010.

Analysts at investment bank Goldman Sachs came out with a report indicating that 2009's recovery in values had stalled and that U.S. housing values would fall 3% in 2010.

Driven largely by the high foreclosure rate, which translates into some 300,000 to 400,000 fewer new housing starts than there otherwise would be, Zandi, chief economist of Moody's Analytics, expected home prices to continue to fall modestly in 2010, down about 5% on a national average. He calculated the difference between supply and demand at approximately 750,000 units annually, and that the excess inventory wouldn't be worked off until the end of 2011. He was expecting GDP to rise 3% this year, approximately 4% in 2011 and closer to 5% in 2012, thinking that this would translate into improved employment statistics which would then work their way through to improved home sales. His expectation has been for an average monthly job gain of 125,000 this year (-below the 150,000 needed just to account for the increase in the workforce due to population growth -), 250,000 in 2011 and 300,000 in 2012.

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According to RealtyTrac foreclosures are plateauing, will hit about 1 million in 2010, and won't drop off dramatically any time soon. One positive glimmer of good news is that, compared to a year ago, slightly fewer homeowners (21.5% compared to 23%) now owe more on their house that it's worth. However, the present emphasis on loan modifications may simply be delaying the inevitable for many delinquent home-owners and may thus merely be providing some short term price stability for the market that is but a prelude to further price declines. If these materialize, the number of homeowners who owe more on their home than it's worth will increase once more. Suttmeier, of Zillow.com, says that there are waves of foreclosures coming because very few of the HAMP modifications are becoming permanent.

Although default notices have dropped, repossession rates are at a record level, indicating that banks are working through their backlogs, which are considerable. For example, the average borrower presently in foreclosure is unlikely to be evicted for 438 days (says LPS Applied Analytics) and more than 650,000 households haven't paid their mortgage in 18 months. In addition, in 19% of these situations the lenders are already so overwhelmed with the volume of foreclosures on their books that haven't yet made any effort to repossess the property at all. Additionally, in preference to resorting to the relatively expensive and time consuming foreclosure process (which can be especially slow in states requiring court approval prior to foreclosure & eviction) most banks are now opting for the short-sale process wherever they can. Under this scenario, in return for the forgiveness of their debt upon sale, homeowners delinquent on their mortgage payments cooperate with the bank to get their homes sold. The homeowner usually gets to live in his/her house for many a month at no expense but for utilities, and the bank is happy that the house is occupied rather than sitting vacant acting as a magnet for vandals.

It is perhaps not so surprising that with so many households now living in their homes mortgage payment free, or at lower loan-modified rates, the number of consumers behind on their credit card payments has fallen to an eight-year low - according to the American Bankers Association. [About 3.88% of bank credit card accounts were past due by 30 days or more in the first quarter of the year -- the first time since 2002 that the rate has fallen below 4%.]

The American consumer is, however, still in a very precarious position, even if Wall St. has shown signs of recovery.

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The CredAbility Consumer Distress Index (published by CredAbility, the leading national nonprofit credit counseling and education agency previously known as Consumer Credit Counseling Service of Greater Atlanta) is the first index to provide a regular and comprehensive snapshot of the American consumer's total financial picture over time. The new index, based on a 100-point scale where a score of 70 or less indicates consumer financial distress, draws upon the multiple data sets that CredAbility collects, such as employment, housing, credit, house- hold budget, and net worth. [Financial distress is defined as the condition where the situation is acute enough to require an immediate remedial response (if at all possible)].

For the first quarter of 2010, American households' scored 64.2 on the 100-point scale, marking the seventh consecutive quarter of financial distress for the average American. This was just a slight improvement from the prior quarter's 63.9 score, which was the lowest score since 2006, the first year for which CredAbility has calculated an index score.

The highest score since then was 78.7, registered in March 2007. It first dipped below 70 in September 2008 and it has remained in the mid-60s region ever since.

So, it is against this backdrop that upbeat news like "the national median existing single-family home price was $176,900 in the second quarter, up 1.5 percent from $174,200 in the same period of 2009", must be measured. Despite record low mortgage rates, more than 76% of people say they would prefer to rent a home rather than buy one – up 5% from 2009, (according to the National Apartment Association). And 33% of renters say they are definitely shying away from the unpredictability of the real estate market &/or the possible threat of foreclosure. This negative consumer psychology is heavily impacting the market and is part of the reason why the national inventory of homes for sale increased in July for the seventh straight month (according to ZipRealty Inc.), even though July is a month when inventory levels typically decline.

Meanwhile, rents have gone up as rental demand has increased and rental vacancies have declined. Rents rose 0.7% from April to June. That's the largest quarterly gain in two years.

Of course, property price declines in the US have been attracting more Buyers from overseas (18% of Realtors were estimated to have completed a sale with at least one international client this year, compared to 12% last year), but this can hardly be expected to offset declines in demand here at home.

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In the Greater Albuquerque Metropolitan Region the median sale price for a single-family detached house rose to $186,000 in July, up 0.54% from the previous year and up 2.76% from the previous month. However, the number of houses under contract declined by 14.06% and the number of homes actually sold and closed decreased by 24.22% compared to a year ago.

This indicates that demand has weakened significantly now that the home buyer tax credit is no longer available. And although prices may have increased slightly, due to the lower mortgage interest rates presently available it is actually costing today's Buyers less, in monthly payment terms, to buy these slightly higher priced properties than it cost Buyers a year ago to buy their slightly less expensive homes at the higher interest rates then prevailing. If we were in a healthy market and Buyers were feeling confident enough to spend as much in monthly payment terms as they did last year, sales prices would have risen far more dramatically.

We are now about to enter what is typically the back-to-school, end-of-year period when housing demand dwindles and prices can tend to soften alongside. This softening is especially likely to occur this year since inventory levels are elevated. Almost inevitably, facing stiff competition from so many other Sellers, and with relatively few Buyers around, those Sellers who are absolutely desperate to sell will lower their asking prices if they can possibly afford to do so. The questions we might ask then are 1) will prices decline by very much?; and 2) if they do, will they rebound early next year as can happen when demand revives after the seasonal lull?

At this point, overall global economic demand appears to be languishing, bringing down interest rates to even more attractive levels. Added to this, the Federal Reserve and Treasury will probably continue to support the market the best they can. So, real estate just might muddle along through, though the risk right now is definitely to the downside.

There is little doubt that, with mortgage rates so low, it can be far cheaper to buy than to rent. However, new entrants into the market must discern for themselves just how confident they are about their job security and their ability to settle in one place for at least five years. Because, if the market truly doesn't begin to recover until 2013, it probably won't be until around 2015 before today's Buyers will be in a position to sell and break even (after all sale fees & expenses).

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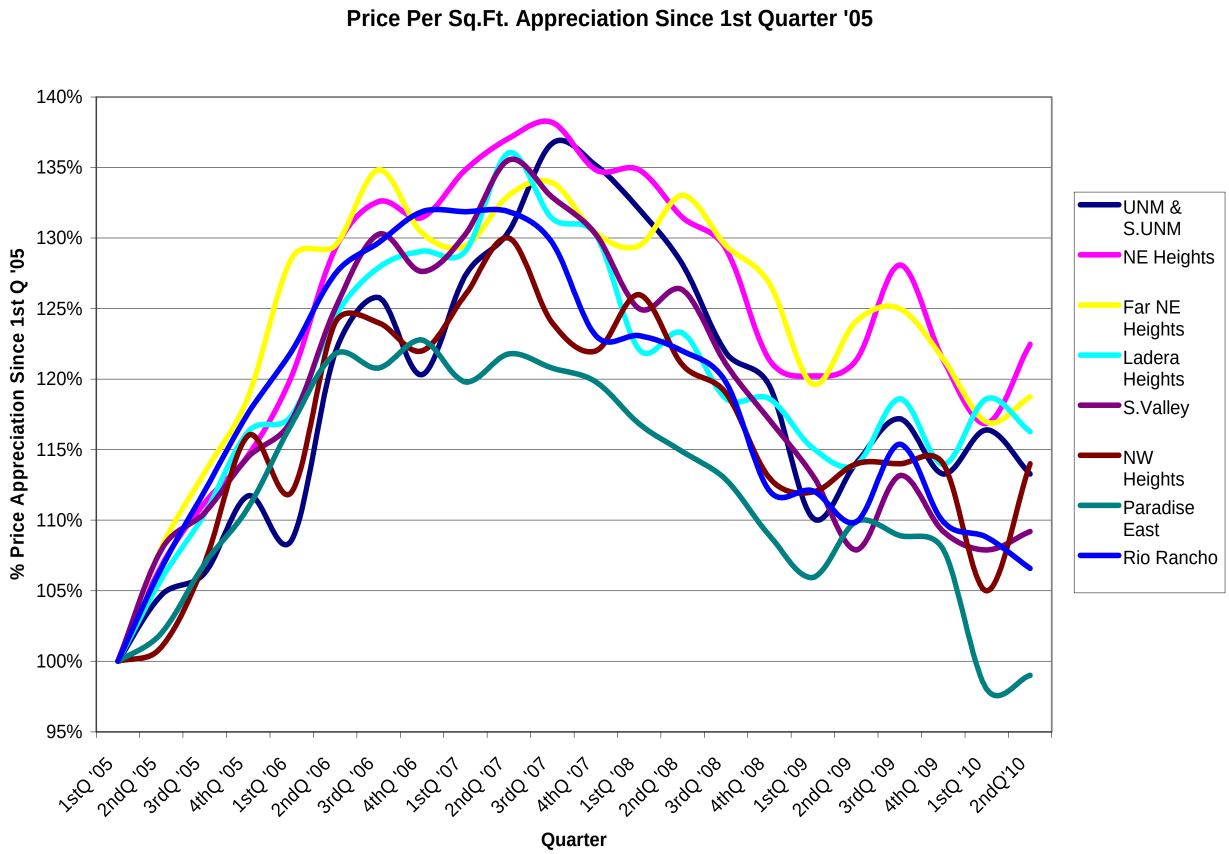
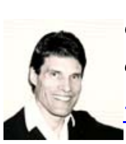
Here is a graph of price per square foot appreciation/depreciation that has occurred in various regions within our community since the first quarter of 2005:



Property Owners Beware! - EPA Toughens Lead Rule

Back in April 2008, the EPA issued its Lead Renovation, Repair and Painting (RRP) Rule, which requires the use of lead-safe work practices (including dust control, site clean up and work area containment) **and** associated recordkeeping **whenever** contractors paint, repair, or renovate residential buildings or child-care facilities built before 1978. At the time, there was an opt-out provision available so that contractors would not have to follow these lead-safe work practices if there were no pregnant women or children under six years of age occupying the building. Last month the EPA eliminated this opt-out provision.



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However, although they are encouraged not to do so, home-owners are still allowed to perform renovations themselves without having to adhere to this Rule. Tenants are also allowed to perform renovations as long as they are not compensated by their landlords for doing so.

As contractors in some areas have not obtained the required lead-safe work training, the EPA is giving them until October 1, 2010, to become adequately certified. Individual renovation workers need to be enrolled in certified renovator classes by September 30, 2010 and complete the training by December 31, 2010.

Either when submitting the final invoice or within 30 days of completing the renovations, whichever occurs earlier, the contractor performing renovations must provide the home-owner and occupants, or the operator of the child-care facility, with information demonstrating compliance with the training and work-practice requirements of the Rule. In multi-family dwelling situations where renovations have been made to common areas, the firm must provide the occupants instructions on how they can review or obtain this information from the firm at no charge. Likewise, parents and guardians of children at child-care facilities must also be provided with instructions on how to review such documentation.

So, please take note!: Owners of residential properties built before 1978 should ensure that, if they don't perform renovations themselves, they hire contractors trained and certified to adhere to the EPA Rule. Otherwise, not only will they be in violation of that rule but, when they are ready to sell, they won't have the required disclosure documentation for their Buyers, which may undermine the sale.

For more information on the lead RRP program, see: **http://www.epa.gov/lead**

Formaldehyde-free Fiberglass Insulation Available

The U.S. Environmental Protection Agency has recommended minimizing exposure to formaldehyde and the California Air Resources Board recommends using building materials that are free of the colorless gas. Responding to these growing concerns, Johns Manville has introduced the only formaldehyde-free line of fiber glass building insulation available - selling at Lowe's. Carpets and furniture rank amongst the other most common sources of formaldehyde gas in the home.

Albuquerque improves in weak national commercial real estate market

Office vacancy rates nationwide continued to climb in the second quarter, reaching 17.4%, according to research firm Reis Inc. This is the highest vacancy rate since 1993.

Also, only $34.2 billion worth of commercial real estate sales were completed through June – about 26% of the usual volume during the first half of the year since 2004, according to Real Capital Analytics.

Moody's overall average score for the commercial real estate market across the country sits at 53 out of 100 – well within its yellow zone of "caution" for investors. This zone spans scores from 34 to 66 out of 100. Scores below this level fall into the red zone for investors to avoid. Scores above this level fall into its investment-grade green zone. Somewhat promisingly, Albuquerque's commercial real estate market ranked as the seventh healthiest in the country (out of the 56 metro areas covered) with a score of 57, showing significant improvement from its year-ago score of 34, but still in the zone for caution. In Albuquerque, three property types -- industrial buildings like warehouses and assembly plants, limited-service hotels and full-service hotels -- were singled out by Moody's for showing significant improvement from the first-to-second quarter of 2010. Albuquerque's apartment market was one of the strongest in the country in the second quarter with a healthy green investment grade score of 89, slightly higher than the nationwide average of 85. After apartments, retail is the second-healthiest commercial property type across the country with an average score of 60 in the second quarter. This is largely because, nationwide, the construction of new retail space is virtually non-existent. Demand thus quickly absorbs the limited supply. Moody's reported that Albuquerque had the second-biggest drop in retail vacancy rates in the country from the first-to-second quarter, scoring an upbeat 75, the third-highest score of any of the 56 metro areas tracked by Moody's. The office market in Albuquerque is still registering substantial distress, though. Moody's divides this market into two: the central business district, or CBD, and the suburban region. Albuquerque's Downtown had the fourth lowest score of any CBD tracked by Moody's at a red 14, showing extremely poor demand for the available space. Nationwide, CBD office markets have shown signs of improvement, with an average national score that has increased from 52 in the first quarter to 55 in the second. Albuquerque's suburban office market also scored in the red, at 30 - slightly lower

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than the national average of 35. Contrary to Moody's bearish analysis, some other statistics suggest that Albuquerque's local office market is performing somewhat better than the national average. Nevertheless, it is far from turning the corner. (Source: Richard Metcalf; Albuquerque Journal)

Putting a value on trees:

According to the U.S. Department of Energy, three properly placed trees can save home owners between $100 and $250 a year in energy costs. Their shade cuts cooling costs in the summer. In winter, they serve as windbreak and help hold down heating costs.

The National Tree Calculator (http://www.treebenefits.com/calculator/) estimates that a 12-inch diameter elm in an Omaha yard can save $32.43 a year on homeowners' energy bills; the same tree in Atlanta would save them $11.89 annually. The 12-inch elm adds an estimated $40.23 to the Omaha home's value and $57.33 to the Atlanta home. As trees grow larger, they can add even more value.

I hope this newsletter has been of interest &/or value. If I can help you or one of your friends in any real estate venture, please do let me know.

Blessings to One & All!

- Michael

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