

February 2012 Housing Notes



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February 2012 Housing Notes

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Executive Summary

This review concerns February's housing data and the intent is to provide a thorough analysis of the existing conditions in the United States housing market. This commentary reports on the housing market and includes data for new home starts and sales, building permits, housing completions, and construction spending – including remodeling. Also included are comments concerning existing home sales, distressed homes, housing trends and projections, new home construction developments, employment, and conclusions.

February's data indicated a small decrease in housing starts. Multi-family housing increased and is still the driver for overall housing starts. New home sales were down slightly from January, permits increased slightly, housing completions decreased, and residential construction spending decreased.

Existing home sales are still “bottom-bouncing,” the quantity of available existing homes increased but remained the least since 2005. United States existing home prices are still declining year-over-year. Private investors are the main purchasers of foreclosures, bank REO homes, existing and new home sales – and they are increasing purchases.

The Eurozone sovereign debt and bank solvency situation may seem quiet at the moment – however, it should be noted that several analysts suggest that things are not as well as they appear.

Have we reached a bottom in housing? Perhaps, but a “bottom” is not a “recovery.” There are still many headwinds confronting the housing industry and it will likely be sometime (i.e., several years) before the winds are calmed and housing markets approach “normal.”

Commentary on Housing

Opening Comments

Economic deterrents to a meaningful recovery are unchanged

- Federal and some State governments' debt → still increasing
- Personal debt → January's revolving debt (mostly credit card debt) fell 4.4% to US \$800.9 billion
- Student loan debt → now over US \$1 trillion
- European sovereign debt crisis → more trouble ahead?
- European bank debt crisis → simmering for now
- China → soft landing still the consensus

New Housing Starts

Commentary

February 2012: Total starts distressed, even with a warm winter:

698,000 starts SAAR: down -1.1% from a
revised January estimate of 706,000

From February 2011 to February 2012 – an increase of 34.7%

Overall Starts:

Multi-family, chiefly 5 or more units, are still the driver
in overall housing starts

New Housing Starts

Commentary

February 2012: Single-family (SF) starts → declining:

457,000 starts (SAAR): down 9.9% from a revised
January estimate of 507,000

From February 2011 to February 2012 – an increase of 17.8%

SF Starts:

Still no relief in sight for hardwood and softwood sales →
fourth consecutive year of historically low-start levels

New Housing Starts

Commentary

February 2012 Multi-family (MF) starts – volatile and increasing:

233,000 starts SAAR: 5+ MF units: up 28.7% from a downwardly revised January estimate of 181,000

From February 2011 to February 2012 – an increase of 108.0%

8,000 starts SAAR: 2-4 MF unit estimate for February ^A

MF housing is critical for overall housing starts

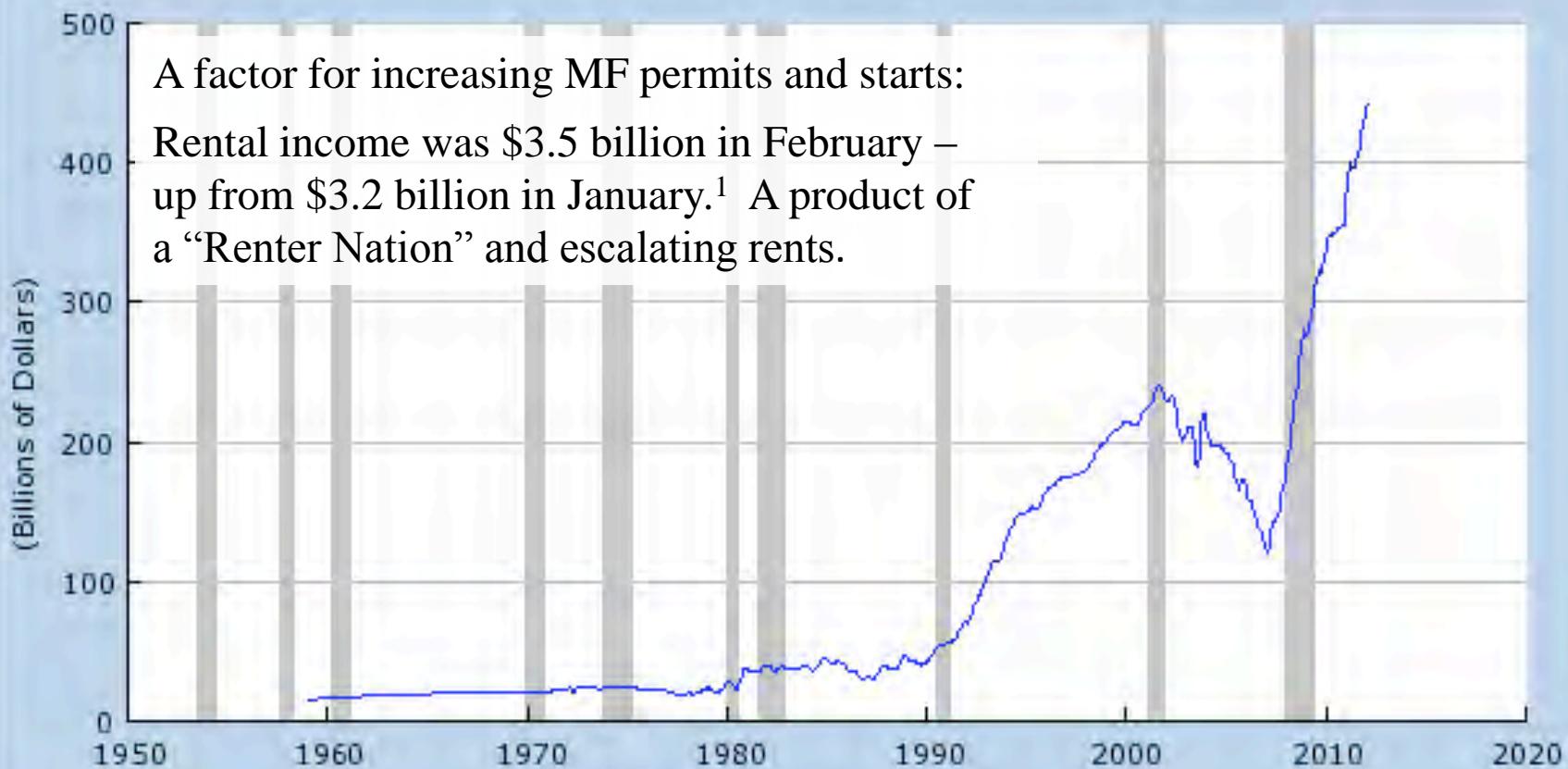
^A The US DOC does not report 2-4units directly, this is an estimation.

Source: U.S. Department of Commerce-NAICS 23, Construction.

Commentary on Housing

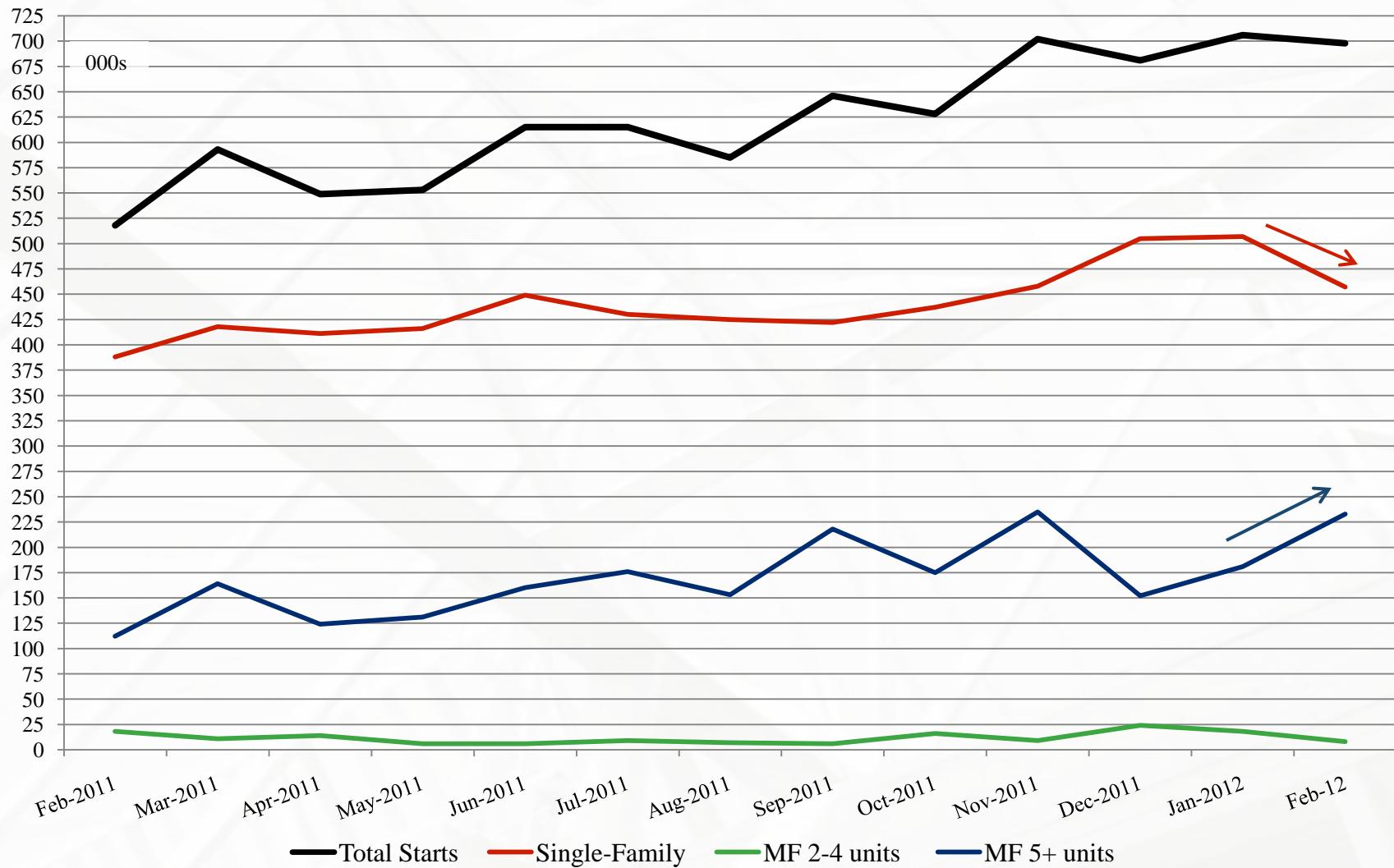
Rental income of persons with capital consumption adjustment (A048RC1)

Source: U.S. Department of Commerce: Bureau of Economic Analysis



FRED

New Housing Starts



Average monthly starts: February 2011 to February 2012

Source: U.S. Department of Commerce-NAICS 23, Construction.

Commentary on Housing

Housing Permits

February building permits – privately-owned housing:
717,000 units (SAAR)

5.1% above the revised January rate of 682,000
34.3% above the February 2011 estimate of 534,000

SF authorizations

472,000 SAAR: 4.9% above the revised January figure of 450,000

MF authorizations

5 units or more – 219,000 SAAR in February: 3.3% above January
2-4 units – 30,000 SAAR in February: 30.0% above January

Commentary on Housing

Housing Completions

February completions – privately-owned:
568,000 units (SAAR)

6.2% above the revised January rate of 535,000
-7.0% below the February 2011 estimate of 611,000

SF completions

421,000: 8.2% above the revised January figure of 389,000

MF completions

144,000: 4.3% above the revised January figure of 138,000

Commentary on Housing

Construction Spending

Private Construction: \$246.45 billion (SAAR) in February

0.03% above the downwardly revised January estimate
of \$246.39 billion (original estimate \$253.64 billion)

February SF construction: \$111,538 billion

January 2011 SF construction: \$113,247 billion

February MF construction: \$16,851 billion

January 2011 MF construction: \$17,194 billion

February Improvement^A construction: \$117,722 billion

January Improvement construction: \$116,288 billion

^A The US DOC does not report improvements directly, this is an estimation.

Source: U.S. Department of Commerce-NAICS 23, Construction

Commentary on Housing

Construction Spending²

Residential building: February rose 3% to \$140.6 billion (SAAR)

Most of the increase was in MF housing, which bounced back 10% after decreasing in January. SF housing increased 1% in February.

Residential building, on an unadjusted basis, rose 20% year-to-date, with MF housing up 23%. SF housing increased 20% from the beginning of 2011.

“While SF housing was able to show some gains towards the end of 2011, the early months of 2012 have seen that hesitant improving trend put on hold.”² - - Robert Murray, McGraw-Hill Construction

Commentary on Housing

FEBRUARY 2012 CONSTRUCTION STARTS²

MONTHLY SUMMARY OF CONSTRUCTION STARTS

Prepared by McGraw-Hill Construction Research & Analytics

MONTHLY CONSTRUCTION STARTS Seasonally Adjusted Annual Rates, In Millions of Dollars

	<u>February 2012</u>	<u>January 2012</u>	<u>% Change</u>
Nonresidential Building	\$127,617	\$137,710	-7
Residential Building	140,575	136,298	+3
Nonbuilding Construction	<u>107,760</u>	<u>128,452</u>	<u>-16</u>
TOTAL Construction	\$375,952	\$402,460	-7

THE DODGE INDEX (Year 2000=100, Seasonally Adjusted)

February 2012.....	80
January 2012.....	85

YEAR-TO-DATE CONSTRUCTION STARTS Unadjusted Totals, In Millions of Dollars

	<u>2 Mos. 2012</u>	<u>2 Mos. 2011</u>	<u>% Change</u>
Nonresidential Building	\$18,075	\$21,751	-17
Residential Building	18,680	15,599	+20
Nonbuilding Construction	<u>16,104</u>	<u>24,076</u>	<u>-33</u>
TOTAL Construction	\$52,859	\$61,426	-14

Commentary on Housing

Residential Remodeling: January 2012

January's residential remodeling permits: 2,998,000 SAAR

13% above December: 2,653,000 and
11% above the January 2011 estimate of 2,705,000³

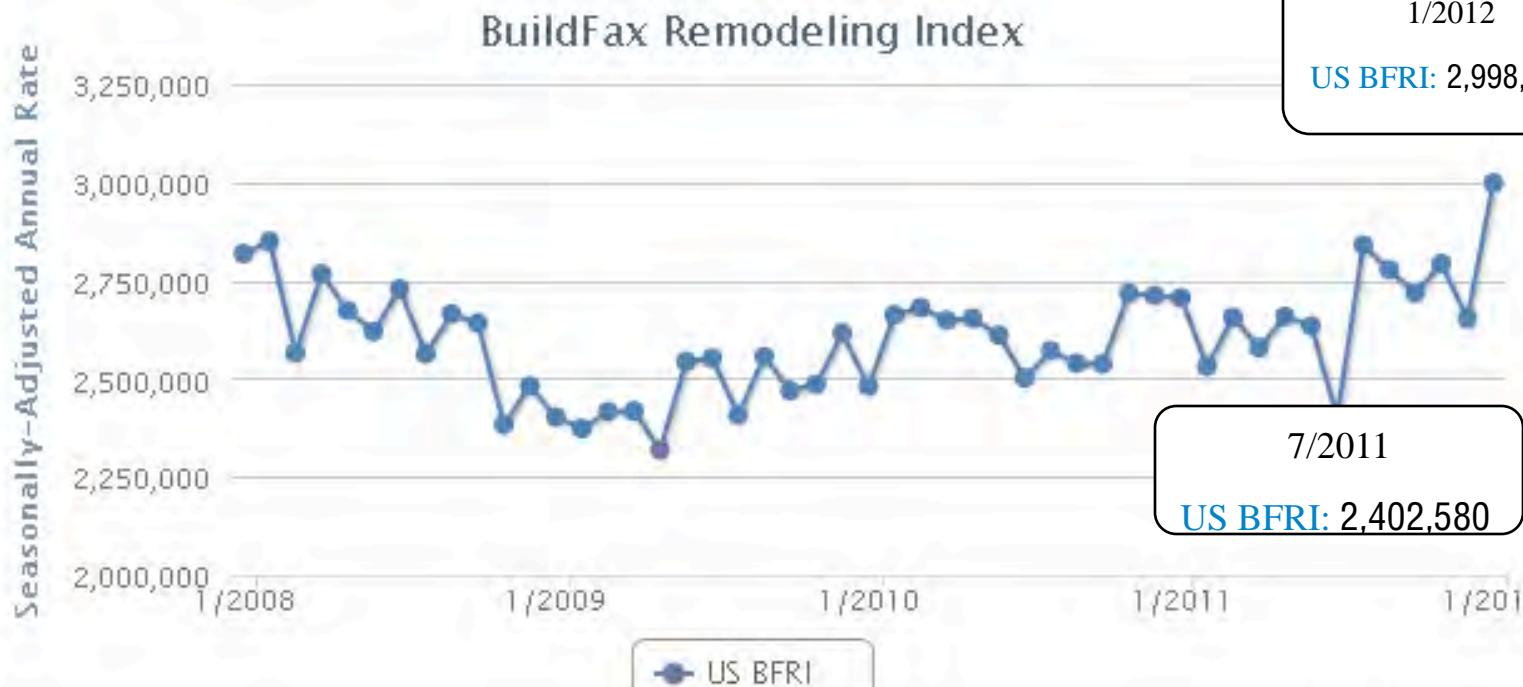
"Residential remodeling this winter is as strong as it has been in more than 5 years. We expect residential remodeling to continue to grow throughout 2012."³ - - Joe Emison, BuildFax, VP - R&D

U.S. Remodeling Rates by Region: January 2012 (SAAR)			
	Permits	From December 2011	From January 2011
Northeast	430,000	down 7%	up 12%
South	1,122,000	up 17%	up 6%
Midwest	595,000	up 9%	up 14%
West	852,000	up 10%	up 14%
Total	2,998,000	up 13%	up 11%

Commentary on Housing

Latest BFRI Release

BuildFax Remodeling Index



Commentary on Housing

New Single-Family Home Sales

February 2012 new SF home sales: 313,000 (SAAR)

-1.6% below the downwardly revised January rate of 318,000

11.4% above the February 2011 estimate of 281,000

New home sales: Still fragile, no increase, and historically weak

Have we reached a bottom in housing?

Perhaps, but there are analysts who state that until foreclosures clear the market, a bottom cannot be called.

We also know that a “housing bottom” and “housing recovery” are completely different entities.

Commentary on Housing

New Home Sales

Median new home price in February: \$233,700

Average February sale price: \$267,700

Estimate of new homes for sale at February's end:
150,000 (SAAR)

- 5.8 months inventory (median) at current sales rate –
an increase of 2 months from January

Again, the lowest number of new homes on the market in 47 years. Obviously, new starts are impacted by demand, the glut of existing homes on the market, - - and Jobs.

Commentary on Housing

February Existing Sales

National Association of Realtors (NAR) February 2012 sales data:

4.59 million (SAAR): A decrease of 0.9% from
an upwardly revised 4.63 million in January

Existing housing inventory rose 4.3% to 2.43 million homes →
a 6.4-month supply at the current sales pace (6.0 in January)

Contract cancellations:

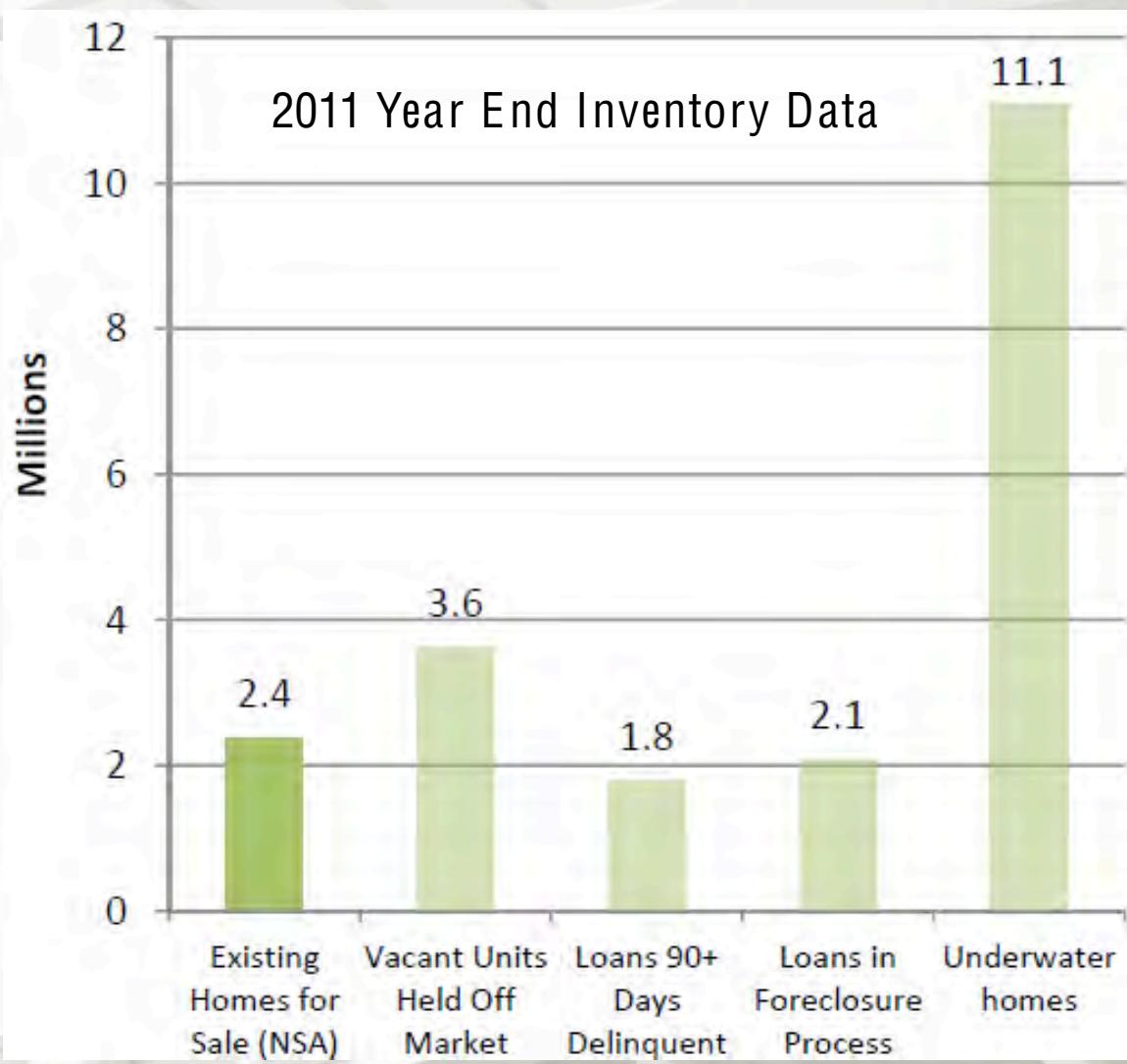
31% in January 2012 vs. 9% in February 2011⁴

“Home sales appears to be driven by the willingness-of-sellers to lower their prices rather than a broad-based increase in demand and buyer confidence. Unfortunately, difficulty in accessing financing and concerns over inventory are preventing buyers from entering the market in force.”⁵ - - Radar Logic

Commentary on Housing

“...Given the number of homes in each of these categories of potential inventory, the figure of 2+ million existing homes for sale probably understates the current supply overhang by millions of homes.

It is important to note that the large potential housing inventory does not need to be put up for sale in order to weigh on home prices. The mere perception of a large supply overhang reduces buyer confidence that home values will rise in the near future, and feeds fears of further declines.”⁵



Commentary on Housing

February Existing Sales

\$156,600 median existing-home price, up 1.3% from January 2012

Distressed homes: 34% of sales --
(20% foreclosures and 14% short-sales)
down from 35% in January and 39% in February 2011

All-cash sales: Unchanged at 33% (31% in January)
Investors account for the majority of purchases:
Cash purchases 23%; no change from 1/12 -- 20% in 2/11

First-time buyers: a decrease to 32% from 33% in January
and 34% from February 2011

Commentary on Housing

Second Homes Sales: Highest Level Since 2005

Investor purchases of second home sales rose 64.5% in 2011:

1.23 million from 749,000 in 2010

Sales of vacation homes rose 7% to 502,000 from 469,000 in 2010

Second home sales: 38% of 2011 house sales
(27% investment homes and 11% vacation homes)

Region of Home Purchase	Primary Residences	Vacation Properties	Investment Properties
Northeast	20%	15%	15%
Midwest	23%	12%	17%
South	35%	42%	44%
West	22%	30%	23%
Outside the US	0%	1%	0%

Commentary on Housing

Standard & Poor's/Case-Shiller Home Price Indices

“2012 Home Prices Off to a Rocky Start”

Annual declines of 3.9% & 3.8% for the 10- & 20-City Composites

Both composites saw price declines of 0.8% in January

In 16 of 19 Metropolitan Statistical Areas: Home prices decreased over the month⁶

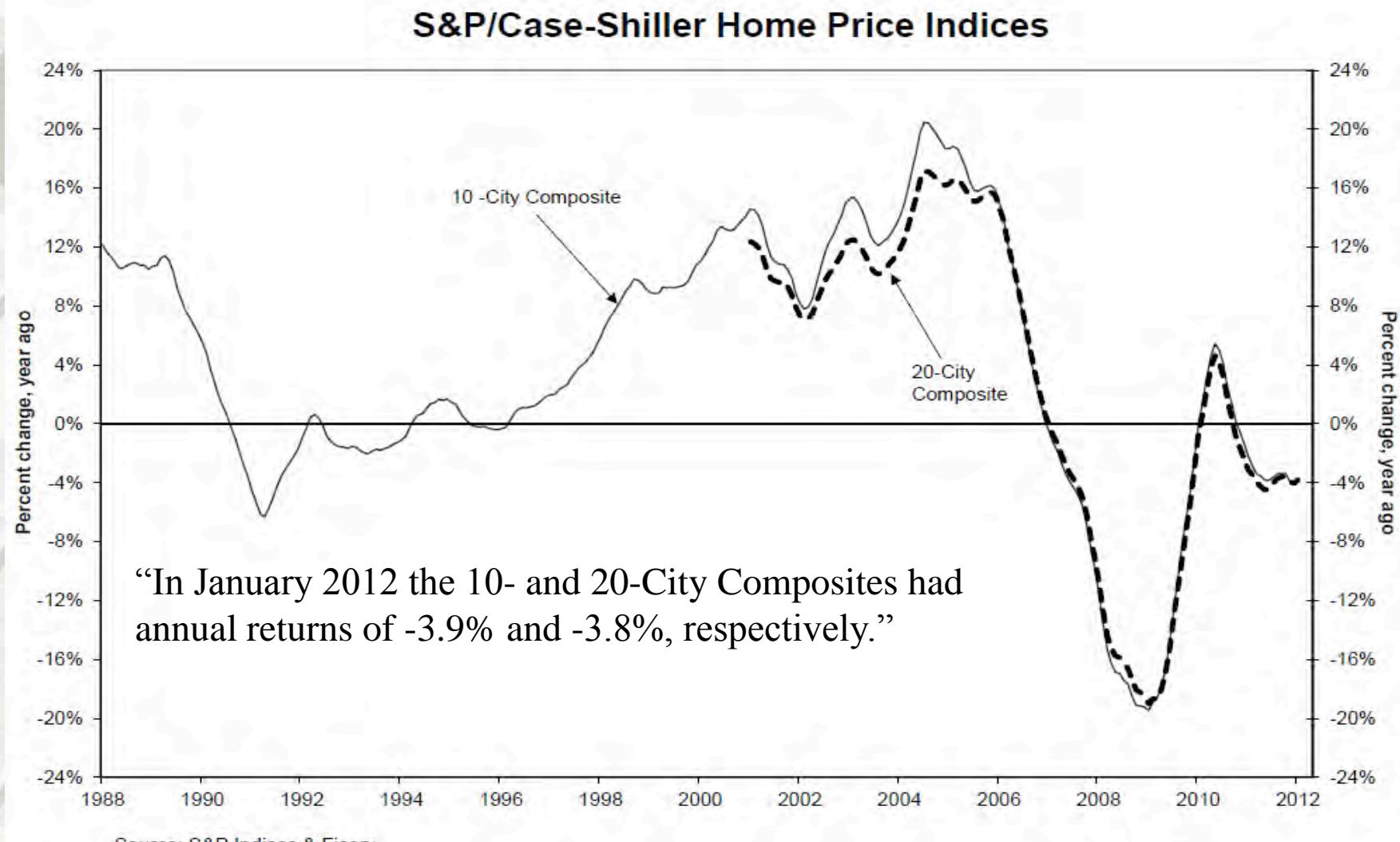
“FHFA House Price Index Unchanged in January”

December's 0.7% increase revised downward; a 0.1% increase

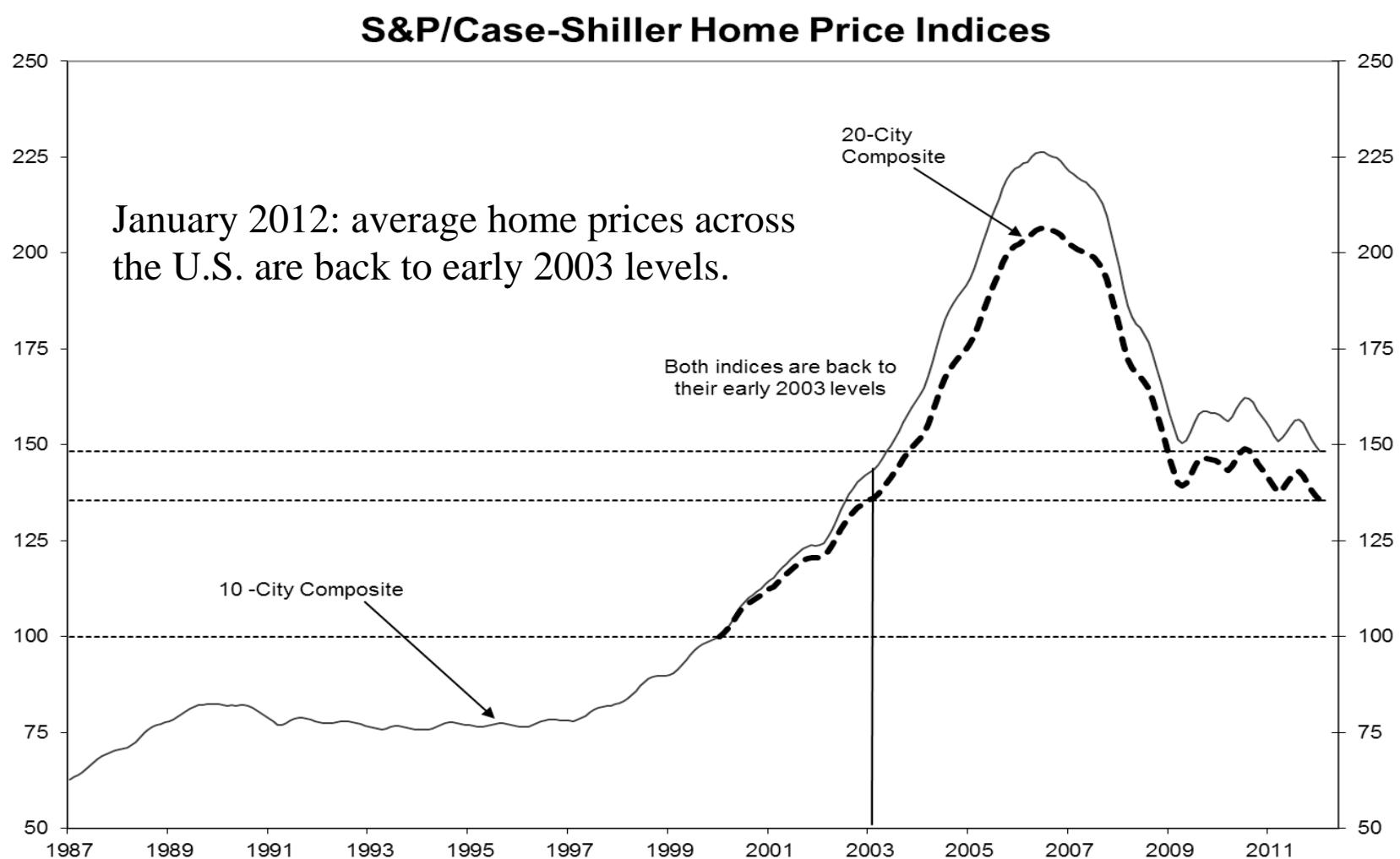
For the 12 months ending in January, U.S. prices fell 0.8%

FHFA index: 19.2% < April 2007 peak; near February 2004 level⁷

Commentary on Housing



Commentary on Housing



Commentary on Housing

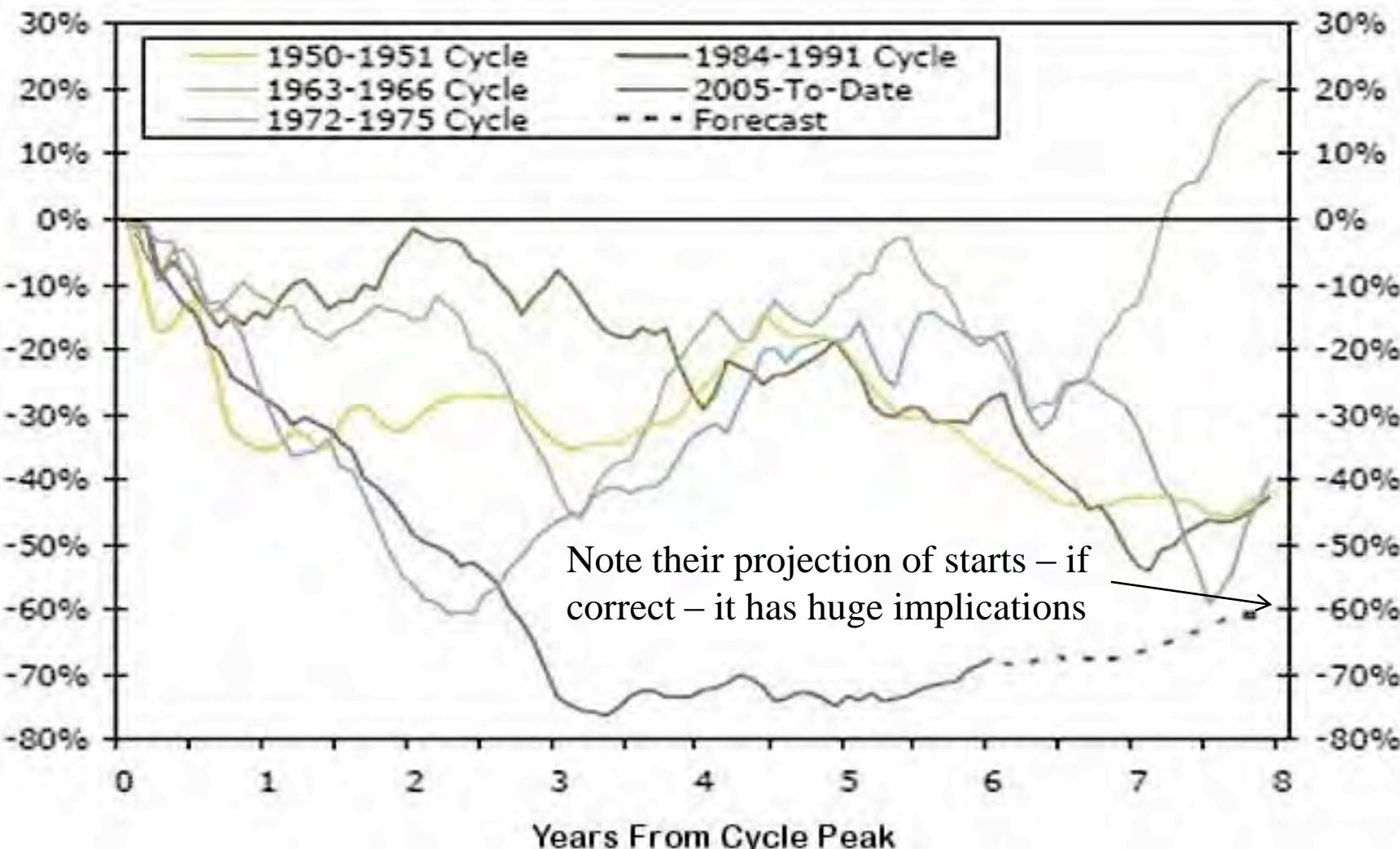
“For the past 40 years, the eligibility of homeownership has been supported by increasing leverage of the household balance sheet as well as significant federal sponsorship of financing that leverage. This approach worked as long as the value of the underlying asset -- the house -- rose consistently in price. However, that crucial assumption no longer can be taken with a probability of one.

Without the certainty of home price appreciation, the extensive leverage of the past decades does not work (see next slide). Supply and demand has also shifted as lenders are more stringent with credit and potential buyers worry about the asset’s value and how it may affect future mobility. Furthermore, the oversized ex-urban home has lost some of its allure with the rise in gas prices over time.”⁸ - - John Silvia – Chief Economist, Wells Fargo Securities Economics Group

Commentary on Housing

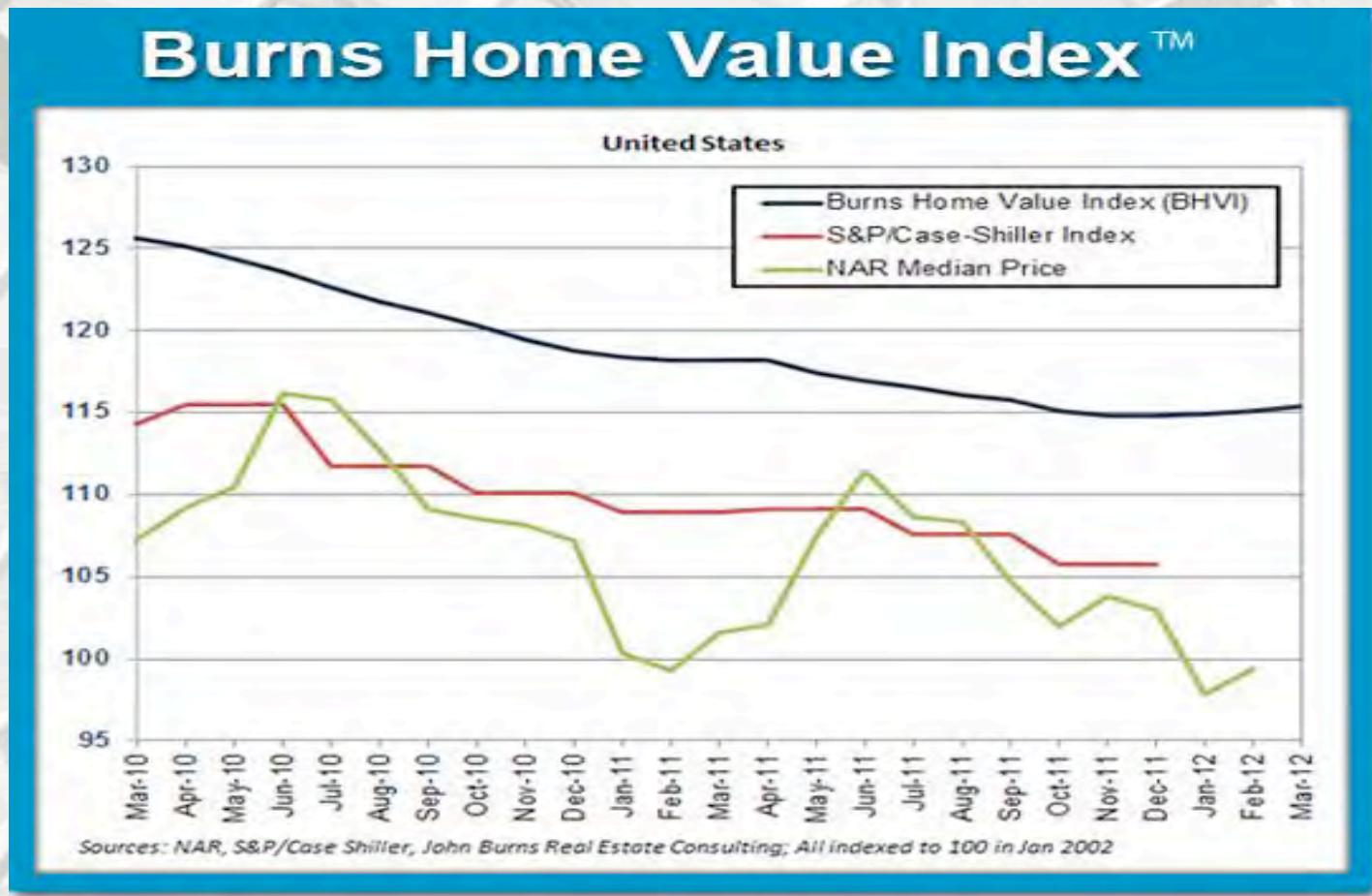
Housing Starts Cycles

Percent Change from Cycle Peak



Contrarian View of the Housing Market

In the past 3 months, prices increased in 90 of the 97 markets analyzed; the average price increase was 1.1% or a 4.5% annual rate.
93 of 97 markets analyzed showed appreciation in February⁹.



Commentary on Housing

Shadow Inventory, Delinquencies, and Foreclosures

+/- 65,000 completed foreclosures in February 2012

8% decline from January's 71,000

66,000 in February 2011

Completed foreclosures year-over-year at February's end: 862,000¹⁰

In January, 8.4 out of every 10,000 homes were being liquidated, up from 8.1 per 10,000 in December.

Reason: banks increasing foreclosures after the
“Robo-signing” settlement.¹¹

Commentary on Housing

Shadow Inventory, Delinquencies, and Foreclosures

Foreclosure filings fell 8% year-over-year in February, with 206,900 properties receiving some form of filing.

Foreclosure activity is expected to increase 15% in 2012 vs. 2011¹²

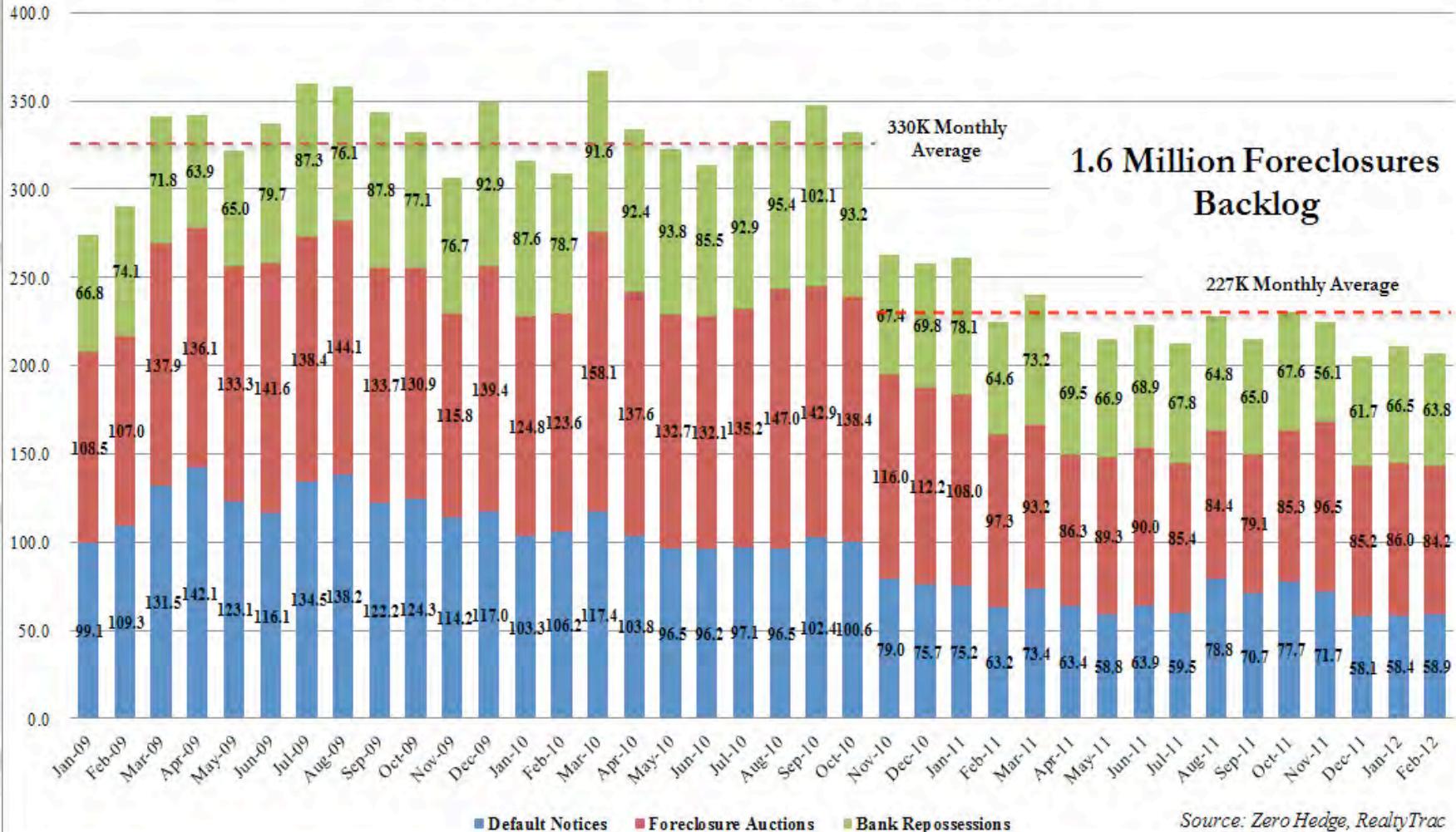
Shadow inventory: January '12 - 1.4 million units (6-months' supply).

On a year-over-year basis, Shadow Inventory decreased from January 2011 to 1.5 million units.

New seriously delinquent loans (90 days or more) are going into Shadow Inventory -- offset by an approximately equal flow of distressed sales (short-sales and REO sales (real estate owned))¹³.

Commentary on Housing

RealtyTrac Monthly Foreclosure Activity ('000)



Source: RealtyTrac and Zero Hedge April 4 2012

Commentary on Housing

Shadow Inventory, Delinquencies, and Foreclosures

“Nonprime lending during the housing boom was concentrated in what were called “exotic” mortgages with little down payment, initial “teaser” rates and, in some cases, negative amortization. However, since 2010, 65% of foreclosure starts have been associated with borrowers who took out 30-year fixed-rate amortizing mortgages (viewed by consumer advocates as the “safest” mortgage product) — up from 40% early in the crisis.

Similarly, the prime borrowers who have entered foreclosure in the past several years have on average made a meaningful down payment of 20%.

A large foreclosure pipeline hangs over U.S. housing markets, creating headwinds for housing market recovery. What began as a nonprime mortgage problem has evolved into a prime mortgage problem with the onset of the recession. The inability to afford a home has been replaced by declining house prices and high unemployment as the primary driver of new foreclosures. Clearly, these changes have implications for the design of housing policy: By recognizing the shifting face of foreclosures, policymakers can make more informed choices about the most effective forms of intervention and the groups of borrowers that could best be served by them.”¹⁴ - - Joshua Abel and Joseph Tracy, Federal Reserve Bank of New York

Commentary on Housing

Employment

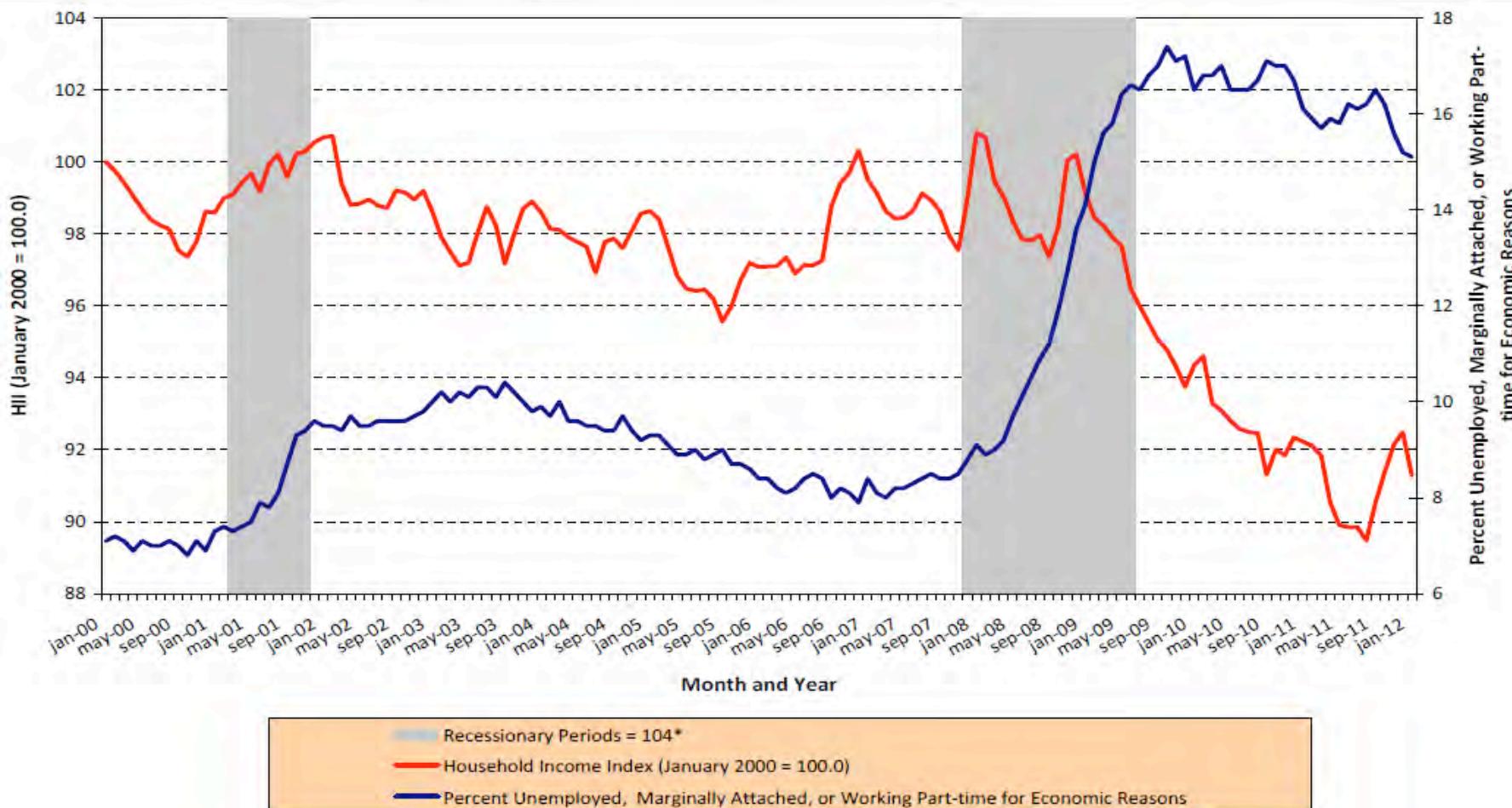
Full employment is not the only issue restraining home sales and prices: “I think the greater issue is that **“new” jobs, in the aggregate, pay less than “old” jobs.** Until that structural problem is fixed, housing prices will continue lower regardless of the unemployment rate.

The problem today is that employment is no longer rising as a function of the total population. Employment has improved but primarily in temporary and lower paying jobs which certainly isn't conducive for home ownership. One of the largest groups of potential home buyers coming up, 25-35 years of age, also has one of the highest unemployment rates. With tighter credit requirements, banks still flooded with delinquent properties and bad loans and stagnant wage growth being impacted by rising commodity costs – the “psychology” for individuals to buy homes remains suppressed.

It is crucially important to remember that the housing market is driven by those that are **actively seeking to buy a home versus those with a “For Sale” sign in the front yard.** With 1 in 4 homeowners underwater in their mortgage, employment dragging, incomes weak and outlooks poor – the swarm of demand necessary to create a real “recovery” in housing is going to be difficult.”¹⁵ - - Lance Roberts. More on employment in later slides.

Commentary on Housing

Median Household Income Index (HII) and Percent Unemployed, Marginally Attached, or Working Part-time for Economic Reasons by Month, January 2000 to February 2012



Sentier Research analysis of unemployment and household income suggest consumer income is decreasing and U6 unemployment still remains elevated – not good news for any market.¹⁶

Commentary on Housing

Employment

From The Hamilton Project:

“As of February, our nation faces a jobs gap of 11.4 million jobs, 5.2 million from jobs lost since 2007, and another 6.1 million jobs that should have been created in the absence of the recession.”

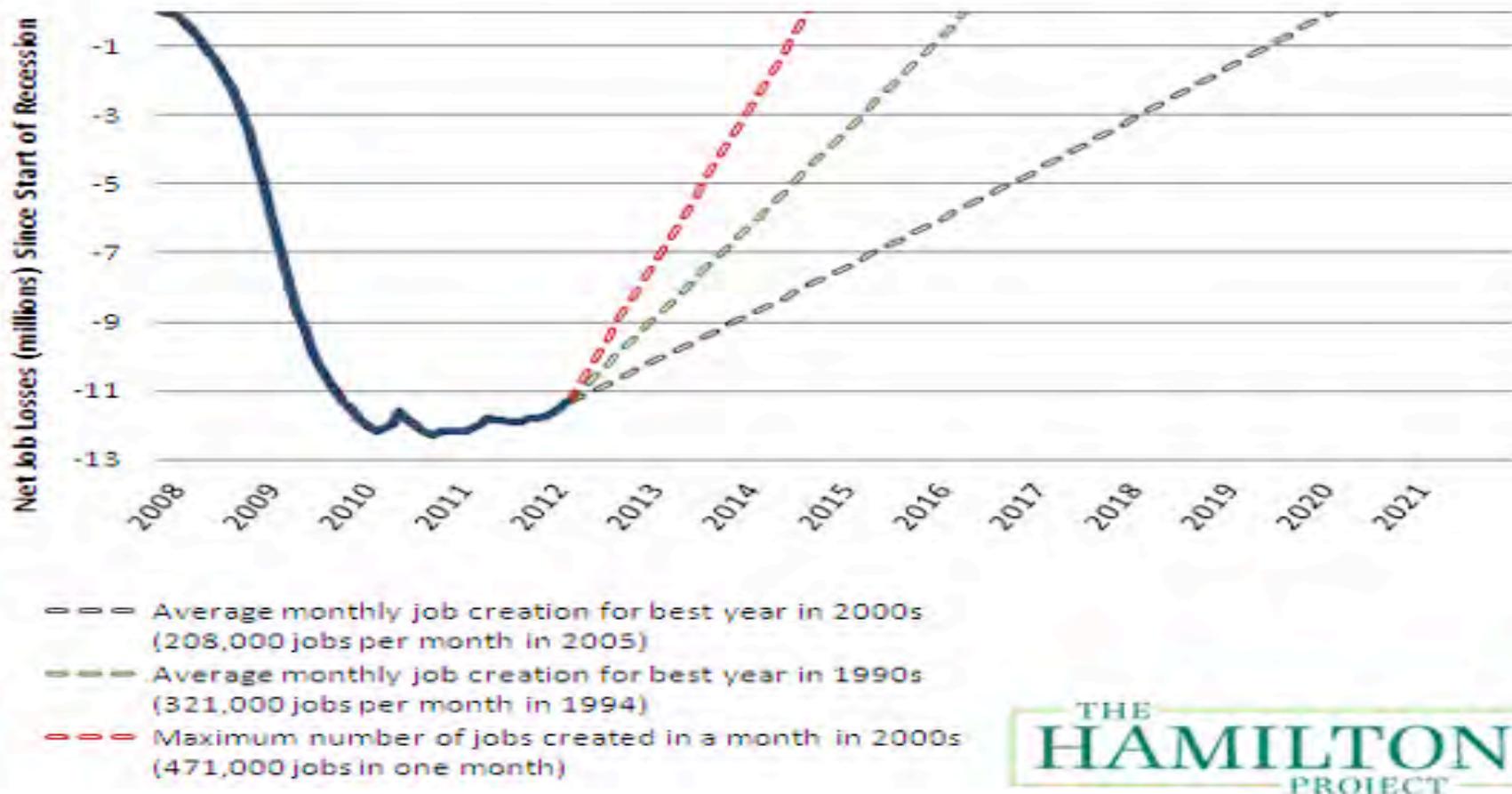
“...to account for new entrants to the labor force ... a job creation rate of 208,000 per month (the average rate for the best year of job creation in the 2000s), it will take until 2020 to close the jobs gap

“...a more optimistic rate of 321,000 jobs per month, which was the average monthly rate for the best year of job creation in the 1990s, the economy will reach pre-recession employment levels by April 2016 — not for another four years.

“Under even the most optimistic projections for employment growth, it will take many years to return to “normal”....”¹⁷

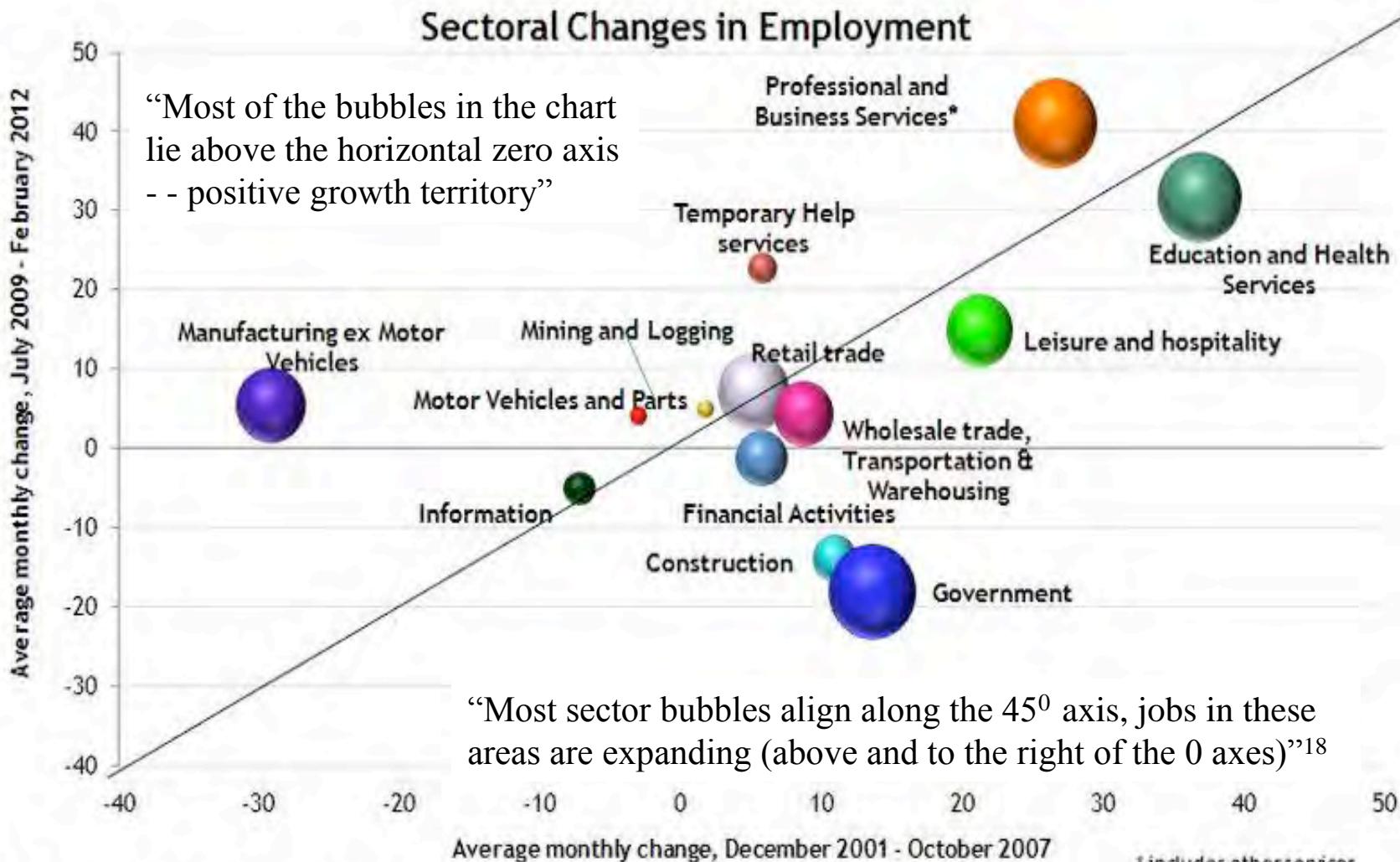
Commentary on Housing

The Evolution of the Jobs Gap To Date and in the Future Under Different Rates of Job Creation (Through Feb. 2012)



THE
HAMILTON
PROJECT

Commentary on Housing



Note: compares changes in employment July 2009-February 2012 vs. December 2001-October 2007

Source: Bureau of Labor Statistics

Housing Market Projections

Demographic Trends: Urban Institute Study

Study projections include:

Total households, owners, and renters by age for the 2010 to 2030 time period in three growth scenarios -- low, medium, and high.

Highlights:

2020 homeownership rate: 63.1% to 65.4% (from 65.1% in 2010).

2020 homeowners: 79.8 to 86.0 million (76.0 million in 2010).

Number of renters: 45.6 to 46.6 million (40.7 million in 2010)¹⁹.

Housing Market Projections

Demographic Trends: Urban Institute Study

Demographic trends that will impact the still unfolding housing crisis and projects the number of homeowners and renters by age to 2030.

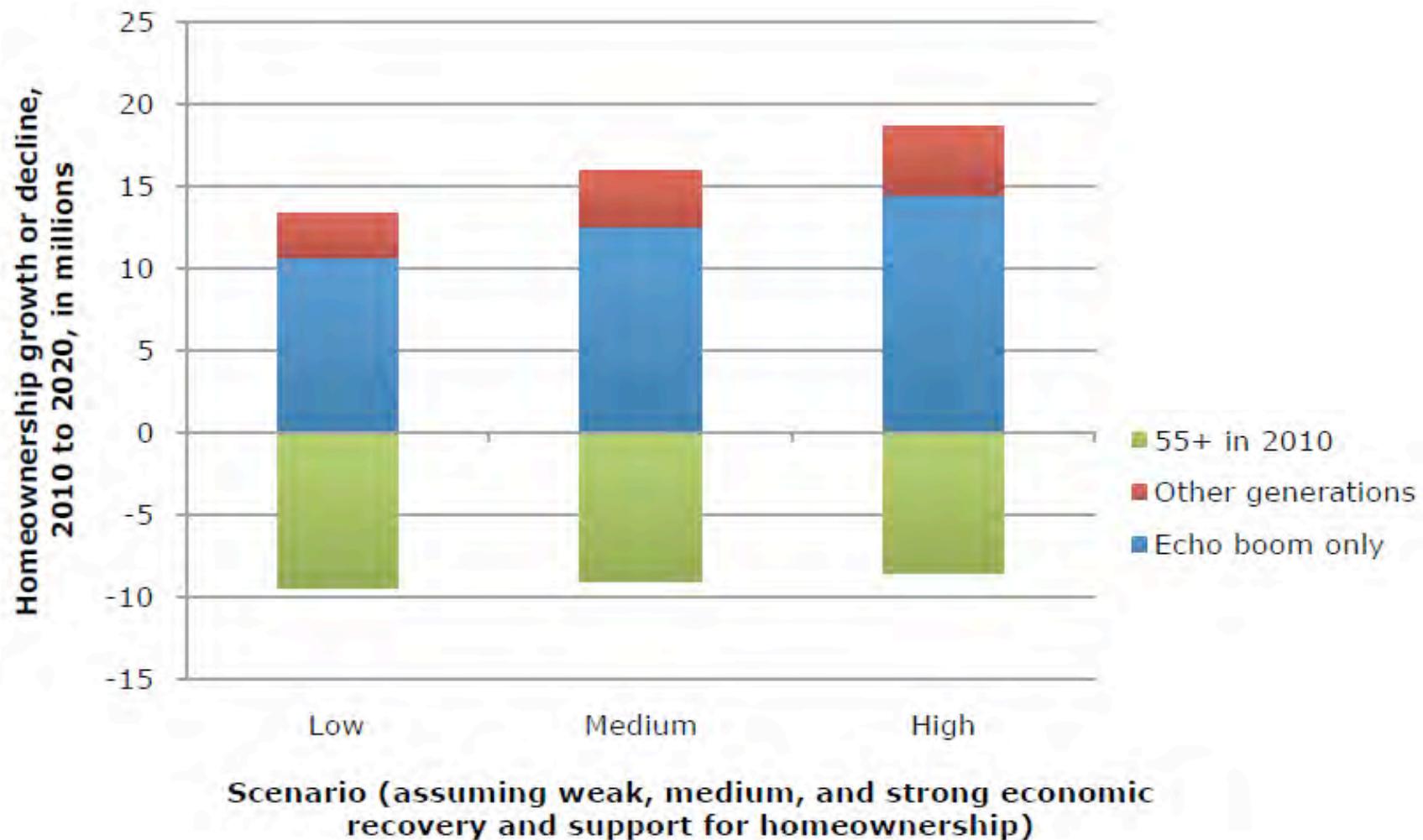
Some of key demographic trend projections...

“Older Americans will contribute increasingly to housing supply, Just as the Baby Boom will swell the number of seniors in the next two decades, it will also swell the number of dwellings released into the housing market over the next 4-decades.

Millennial generation (Gen Y): drives home markets for the next 2-decades.

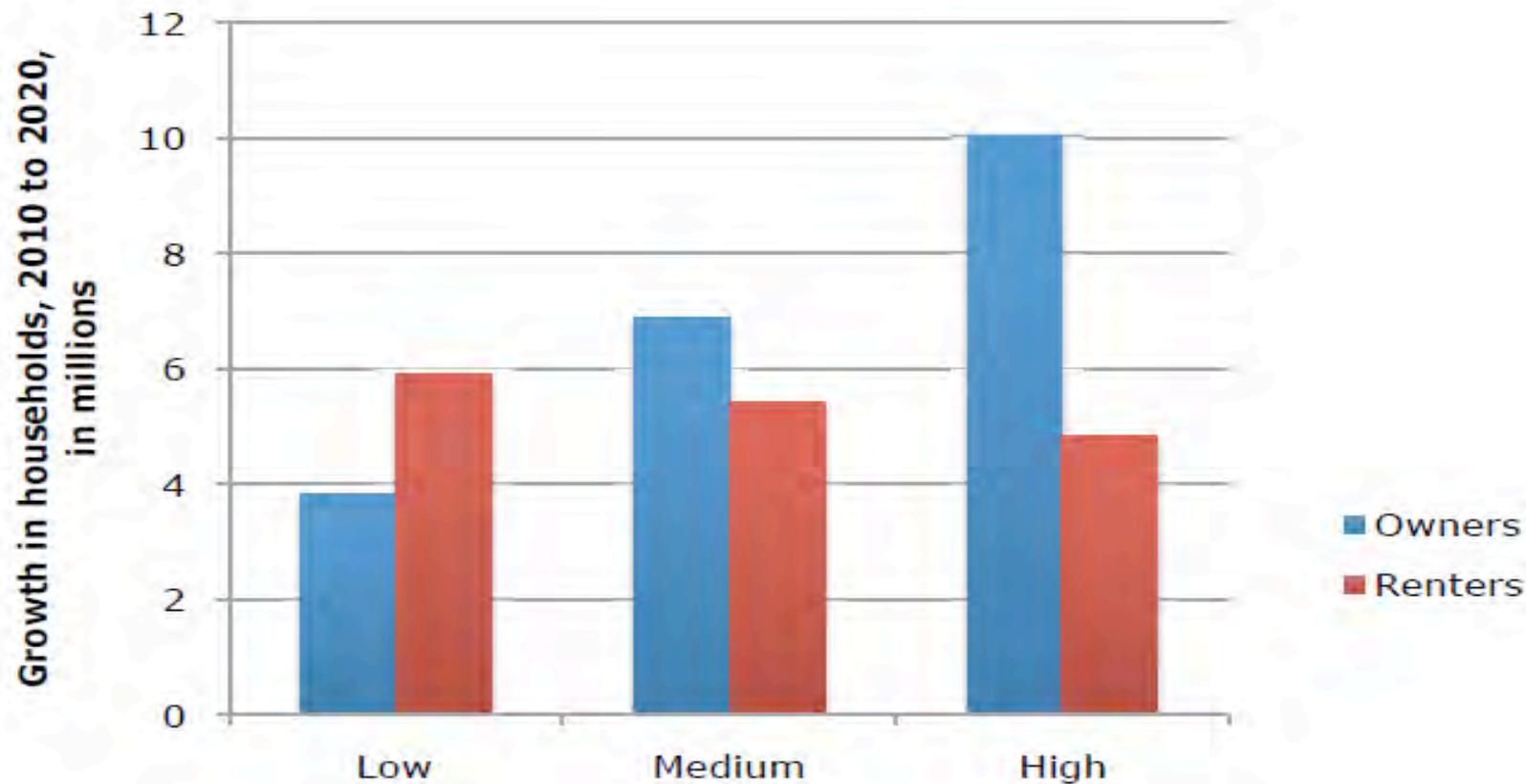
The volume of housing demand over the next 20 years, especially for owner-occupied housing, will depend heavily on the economic and housing policy environment that confronts Echo Boomers as they mature from young adulthood into middle age”¹⁹.

Housing Market Projections



Projected change in owner-occupied households, 2010 to 2020.¹⁹

Housing Market Projections



Scenario (assuming weak, medium, and strong economic recovery and support for homeownership)

Projected growth in owner-occupied and renter occupied households, 2010 to 2020.¹⁹

New Home Construction Developments

New Home Size

Last month, new house size was reported to be trending to smaller dimensions -- well, not so fast my friends.

Data from the US DOC has house dimensions trending upward:

From 2,367 ft² in 2009 to 2,505 ft² in the 4th quarter of 2011

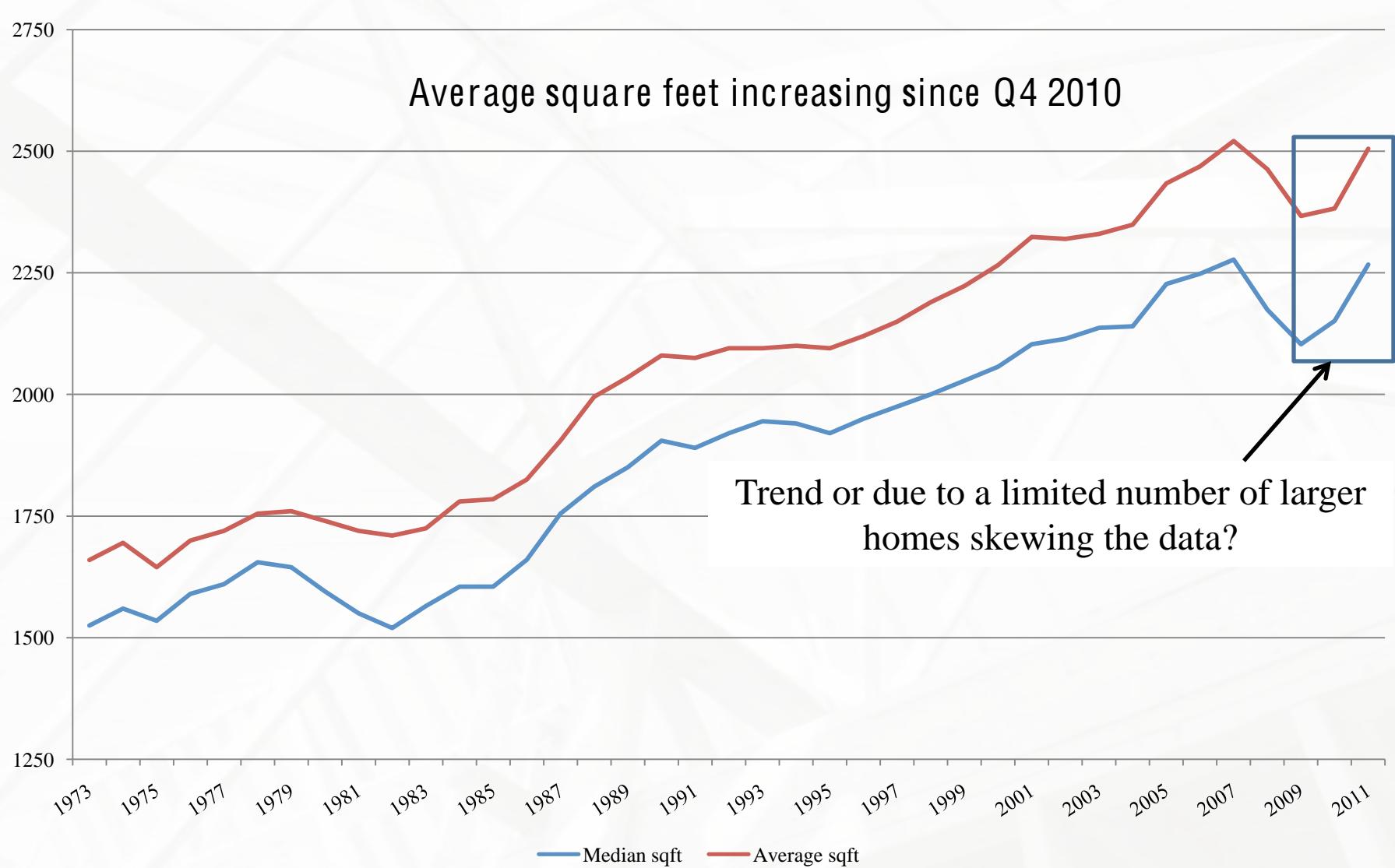
What gives?

Given the economic situation and new lending requirements -- the assumptions were that buyers who were employed, could afford a 20% down-payment and qualify for a loan -- were building/purchasing larger houses.

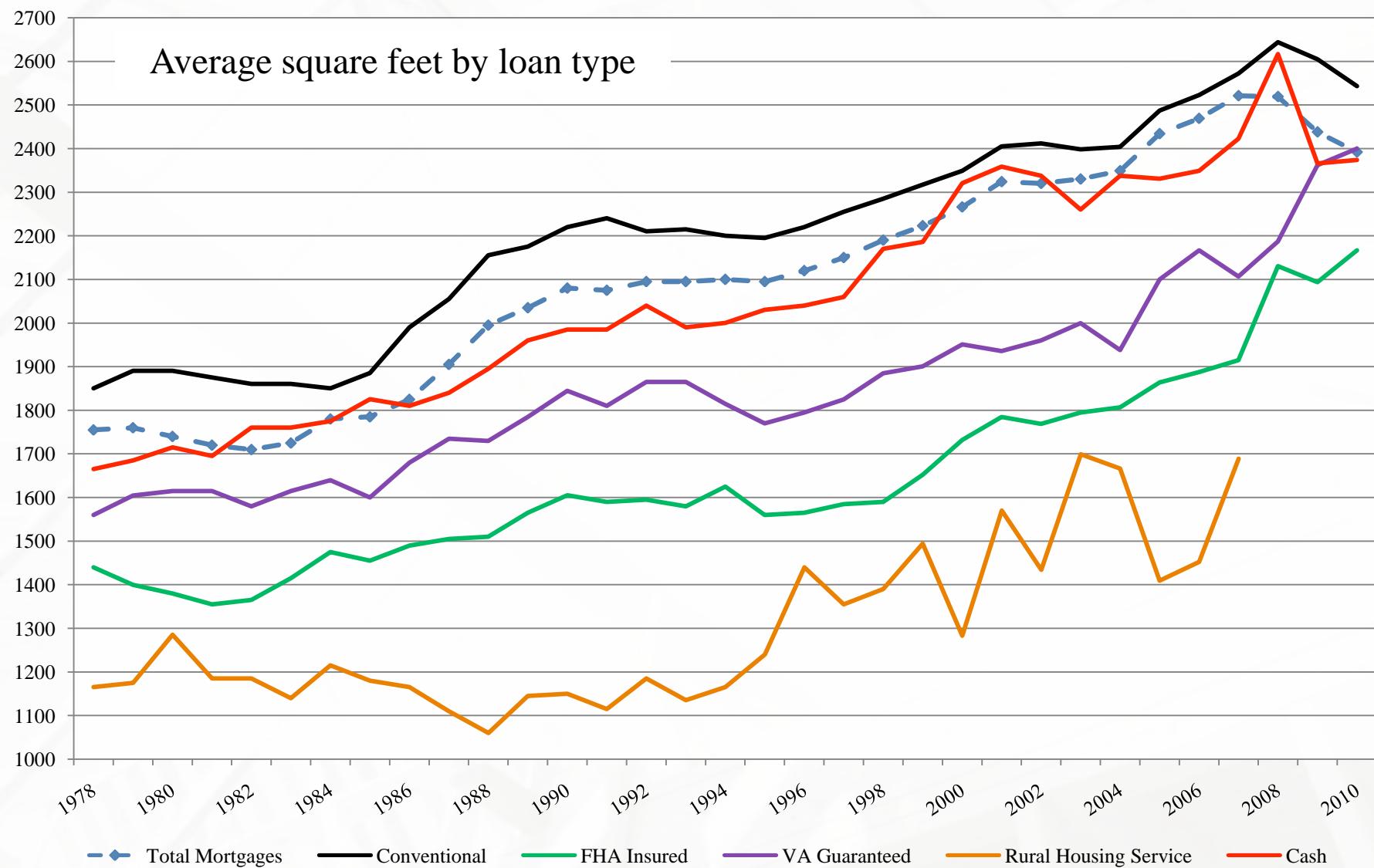
With the limited number of new homes being built, it would not take a large quantity of “bigger” houses to skew the data.

These assumptions may have merit as the NAHB, in a recent interview with Claire Easley, posited similar statements.²⁰

New Home Construction Developments

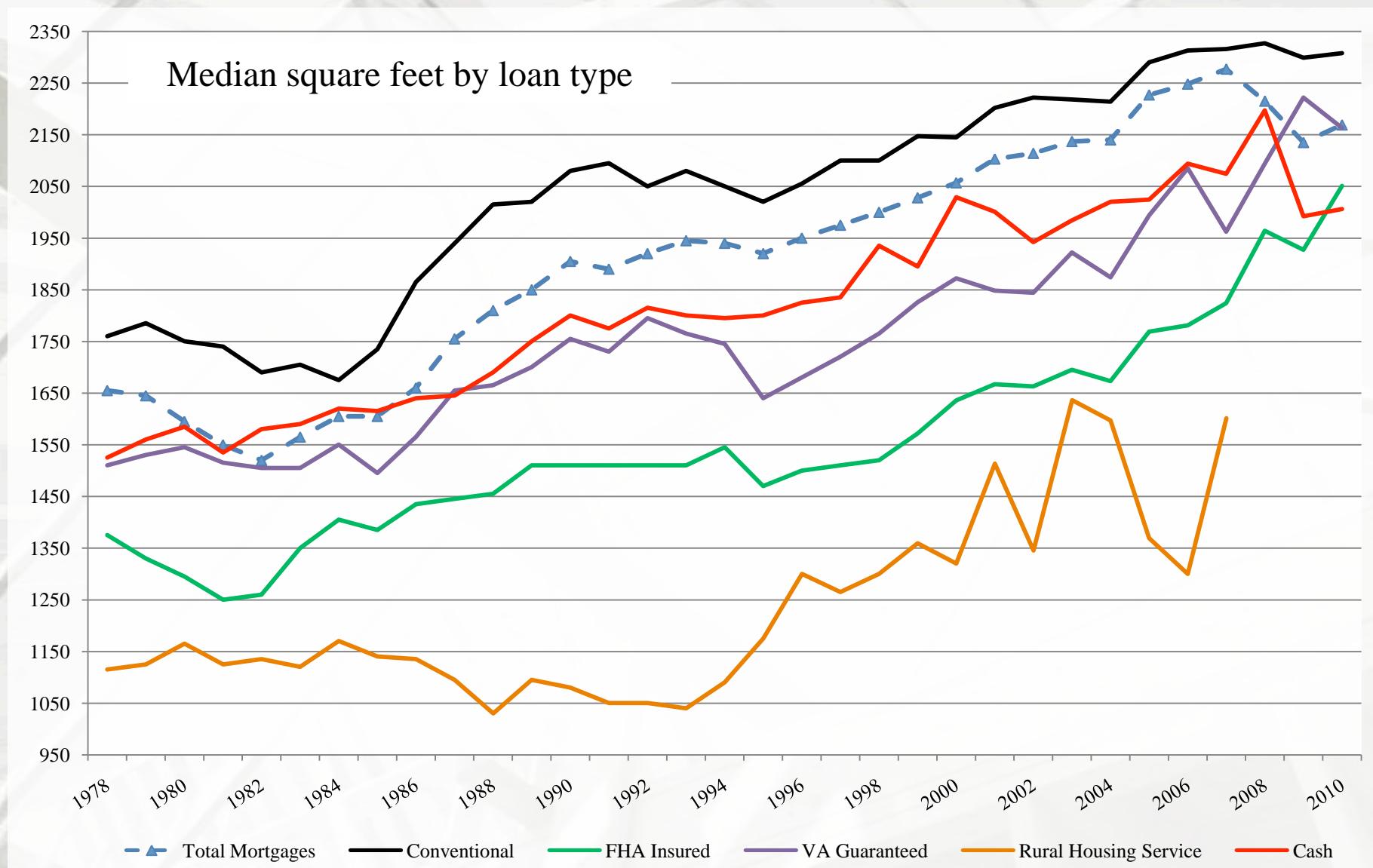


New Home Construction Developments



Source: U.S. Department of Commerce-NAICS 23, Construction

New Home Construction Developments



Source: U.S. Department of Commerce-NAICS 23, Construction

New Home Construction Developments

New Home Size – “Tiny” Homes

Continuing on the topic of home size – recently there have been several articles written about “Tiny” homes:

“I Can't Stop Looking at Photos of Absurdly Tiny Homes”

www.theatlanticcities.com/design/2012/03/i-cant-stop-looking-photos-tiny-homes/1443

“Smaller homes, urban lifestyles attractive to new homebuyers: ULI”

www.housingwire.com/article/smaller-homes-urban-lifestyles-attractive-new-homebuyers

“A growth spurt for tiny house trend”

www.chicagotribune.com/classified/realestate/sc-cons-0322-umberger-tinyhouses-20120323,0,5978638.column

“Project Focus: Little House in the Back Yard”

www.coastalcontractor.net/article/541.html

Is this a trend? Who knows, but it may bear watching to see if “Tiny” home starts measure up to their recent hype.

New Home Construction Developments

Construction Entrepreneurs

According to the *Wall Street Journal*:

More entrepreneurs are starting construction companies

Why? “...construction workers who lost their jobs during the slump in the housing market start their own businesses, taking advantage of a recent uptick in home remodeling and a modest boost in new home construction.”

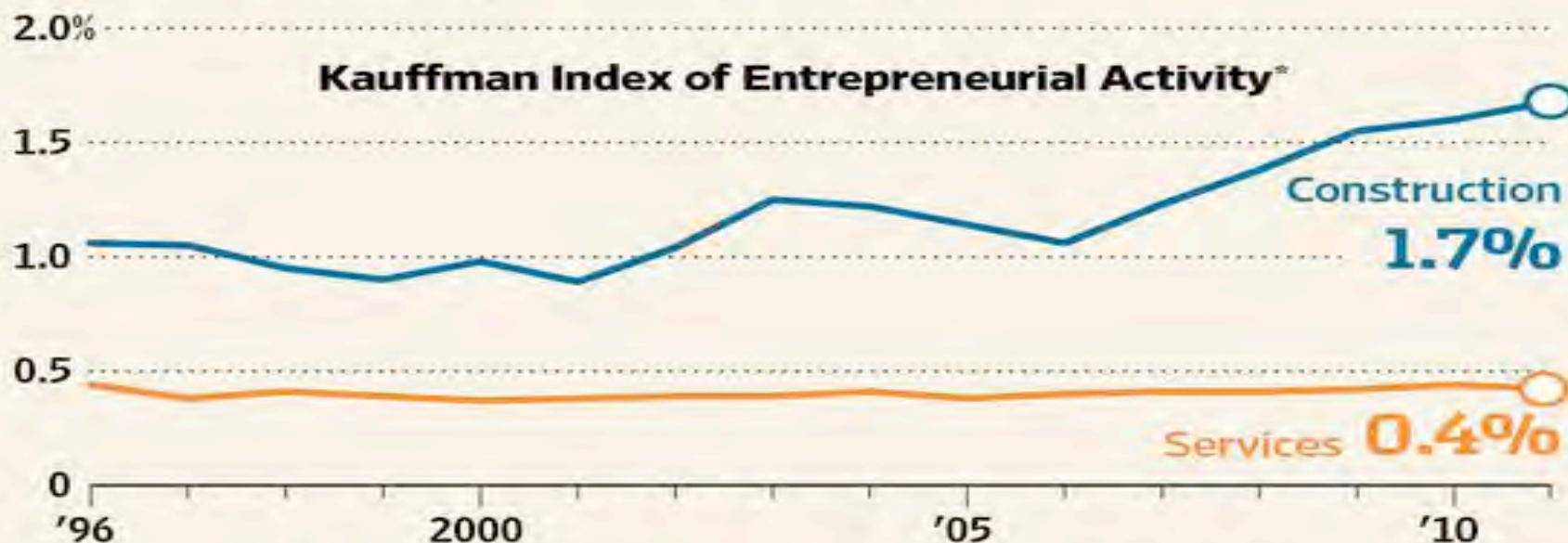
“New entrepreneurs entering construction accounted for 24% of all U.S. entrepreneurial activity in 2011, a year when overall business creation dropped by about 6%, according to recent estimates by the Ewing Marion Kauffman Foundation, a nonprofit that studies entrepreneurship.”

“The rate of entrepreneurial activity in construction was 1.7% in 2011, up from 1.6% in 2010 and 1.2% in 2007... .”²¹

New Home Construction Developments

Construction Start-Ups Grow

The rate of new business creation in the construction industry has increased steadily in recent years, while the rate of business creation in the services industry has remained stagnant.



*The percentage of the adult, non-business-owner population that starts a business each month, calculated using data from the Current Population Survey.

Source: Ewing Marion Kauffman Foundation

The Wall Street Journal

Conclusions

Of the construction industry sectors, housing has been the hardest hit and no relief appears in sight. Yes, there are pockets of improvements – but these in and of themselves are not sufficient at this point-in-time to propel us into a full-fledged housing recovery. We must ask, will housing return to the 1.5 to 1.6-million start levels? Or, will the “New Housing Normal” be significantly less?

February’s data – all monthly declines for housing starts, new home sales and existing home sales (decreased by 1.0%, 1.6% and 0.9%, respectively) were not statistically significant. Nor were the reported increases for other housing data. Since December 2008, housing starts have averaged 589,000 SAAR (monthly average = 49,100). February’s starts also are below any level reported since 1946.

According to several analysts, the foreclosure “fire sale” is just now getting underway. In addition, we have troublesome news from the New York Fed regarding the potential for “safe” or prime mortgage foreclosures. Obviously, we do not know the effect these sales will have on pricing or consumer psychology.

Conclusions

While recent monthly employment data indicates improvement, we need to know if these jobs pay well enough for consumers to purchase homes or are they lower paying jobs that only afford workers to become a member of the “Renter Nation?”

The good news in this month’s report is the continual increase in remodeling expenditures; both BuildFax and US DOC data indicate positive news for remodeling. And future projections bode well, too.

As stated last month, JOBS are the key to a housing recovery – not just a job, but a well paying job. When this occurs, and housing prices regress to their historic mean – we should have the foundation for a housing recovery.

Next month we will report on China and the Eurozone. Both have significant implications for the housing industry – direct and indirect.

Finally, we would love to write this commentary with a “Pollyanna” bent, and we will when housing fundamentals indicate positive improvement. But at present, we prefer not to ‘sugarcoat’ the data and news and so we are presenting what we believe is a truthful description of current housing events.