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STATE OF THE MARKET REPORT

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It is not all about insurance and taxes that affect the housing market. Many variables affect the values of our properties. Some things directly affect how much home a buyer can afford. For example, there is principle, interest, insurance, taxes, HOA fees, supply of homes, demand for homes, average household income, etc. However, changing technologies, banking policies, federal government policy, supply of money, interest rate, and even the stock market are affecting our home's value like never before.

This paper explores some of the topics that affect the value of our homes now. The net affect of these topics has created a tremendous buyers market that is causing a decrease in our family's net worth.

INVESTORS - When I last looked, there were over 112,000 homes for sale in our SE Florida tri-county area. As I said in a previous newsletter, many investors left real estate for fear of losing equity in their investments. When investors bail out, the local incomes often cannot sustain the inflated home prices that they leave behind. Home prices can fall until local incomes can afford the homes, investors return, or interest rates decline. The chart below means that only 27.7% of the homes in our area are affordable by local family median incomes. Our median *family* income is at $58,400 per year. To see the rest of the list, go to the National Homebuilders Assoc Web Site. There were so many investors in our market that according to one article in the S. FL Business Journal, they distorted the housing statistics causing local governments to overstate some needs. For example, school officials were surprised when enrollment actually dropped last year when they expected an increase.

Housing Opportunity Index: 1st Quarter 2007

Metro Area	HOI 1st Qtr 2007 Share of Homes Affordable for Median Income	2007 Median Family Income (000s)	1st Qtr 2007 Median Sales Price (000s)	1st Qtr 2007 Affordability Rank	
				National	Regional
Ft Lauderdale-Pompano-Deerfield Bch	***27.7***	***58.4***	270	169	64
Miami-Miami Bch-Kendall, FL	10.0	45.2	288	204	71
WPB-Boca Raton-Boynton Bch, FL	28.8	61.2	275	164	63

INSURANCE PROBLEMS: Insurance costs have hurt our housing market due to several factors. The hurricanes of recent years have given the insurance companies excuse to keep raising our rates. The insurance companies keep claiming they are losing money in Florida. NOT TRUE! A loophole in State law allowed them to pool all Florida homes in one independent corporation, wholly owned by the parent company, such Allstate Insurance. This is much like charging all male teenagers higher auto insurance rates because a large percentage of them relative to the general population have accidents while the vast majority never has an accident. The independent Florida subsidiary could theoretically declare bankruptcy after a disaster and not affect the parent company. *They declared a loss even while the parent company declares billions of dollars in profits with only an imaginary state and corporate boundaries between them*. The Florida legislature and Governor Crist closed this loophole.

PROPERTY TAX PROBLEMS - Its up to the voters to choose between, "The 3 percent cap on increases in the appraised value of your home minus the old $25,000 homestead exemption or a higher homestead exemption of 75 percent of the first $200,000 and 15 percent of the next 300,000 of value but with uncapped appraisals at the winds and whims of the surrounding area?" (Source: Palm Beach Post).

Can we act on the outcome of the vote in January? Probably not right away. Most laws inevitably have the constitutionality challenged in the courts by special interest groups. This means, it *could be* years before the laws are implemented. Sometimes a challenge of constitutionality means the new legislation is never implemented.

The root of the problem is that the local people who live in Florida year around needed protection from the snowbirds and investors (domestic and foreign). The outsiders drive up the real estate prices through higher demand and thereby drive up real estate taxes. The answer, it seemed was the Florida constitutional amendment for a homestead exemption and the Save our Homes Act. The two laws did exactly what they were intended to do. The shifted the tax burden onto the owners who were investors and part time residents.

The unintended side effects? We cannot afford to move locally because our property taxes would double or triple depending on how long we lived in one place. This greatly affects our market today.

MOVE-UP OR MOVE-DOWN PROBLEMS: Historically, senior citizens whose kids have moved out would move to a smaller home. That smaller home now costs thousands more per year in taxes due to the loss of their homestead exemption. When you move, you start over with the homestead exemption and pay taxes at the prevailing market rates. This causes them to stay where they are at, tying up larger homes needed by emerging families.

FORECLOSURES: June 2007 foreclosure notices are up 87% over June 2006 (S FL Bus Journal, July 07). During the recent boom years, many buyers wanted to get on the bandwagon for fear of being left behind and never being able to afford a home. Many buyers did exactly what many investors did. They bought into adjustable rate mortgages (Arms) that keep the payment low for about 5 years. Then their payment usually doubles forcing them to refinance. These ARMs usually come with a prepayment penalty. Look for your ARM "rider" attached to the back of your mortgage to see the prepayment penalty ("Rider" is what the industry calls an attachment that changes, by overriding them, the terms of the mortgage it is attached to).

Most people thought they could sell or refinance before the payment doubled. You cannot refinance if you do not have enough equity in the property. Equity is the value your home will appraise for minus what you owe (do not forget to include the pre-payment penalty). When home values go down, there is not enough equity to refinance. The same goes for selling the property. If you do not have enough equity in the property to cover the sellers closing costs, you cannot sell without putting in money. When the payment doubles, the lender forecloses and the property is sold at auction at the courthouse.

Alan Greenspan said at a conference in Boca Raton, "there is no problem that rising prices can not fix", referring to the present real estate market. That is true. An ARM is a great product for investors as long as the property values go up. I would not recommend an ARM for homebuyers when rates are at a historical low like the last 6 years.

TIGHTER LENDING STANDARDS: Due to the number of foreclosures in the sub-prime market share of loans, lenders are getting much stricter about the loans they approve. The sub-prime market simply means loans to buyers with low credit scores. The FICO score is used almost exclusively in the mortgage industry. As less home sell, more lenders are going out of business along with all the people they helped get into foreclosure.

PUBLIC CONFIDENCE AND PERCEPTION: Media bombardment in reporting on the housing slowdown has hurt the market and has become a "self fulfilling prophecy."

NEW COMER BUYING PATTERNS: The constant barrage of bad news press from our media has contributed to the negative expectations from people moving into Florida. We are still growing regardless of all the people we know who left. However, the newcomers want to rent for a while until they think it is safe to buy.

NEW CONSTRUCTION COMPETITION: Builders are now selling at a lower price than the existing home market. From personal experience, a client bought a home in Palm Beach County. Four months later during construction, the builder lowered the price $74,000. They were not the only ones. A friend was shopping for a new home in Orlando. Saw the one she wanted but could not quite fit the budget. The builder lowered the cost and she bought.

A joint report issued last week by the Orlando Regional Realtor Association and the Attorneys Title Insurance Fund in Orlando shows that 6,845 existing single family homes sold in the metro Orlando area, while 4,084 new homes were purchased in the same four-county area during the same three-month period. Source: FloridaRealtor.org.

THE TIGHTENING MONEY SUPPLY FOR MORTGAGES - For the first time, the stock market became directly tied to the real estate market when new technology allowed packaging of high risk, high interest rate, sub-prime mortgages into a sellable "bond" form for investors seeking higher returns on their money. The 1990's began a boom of these bond funds. A decade later, when the housing market began waning, the mortgage companies feeding these bond funds began making more risky loans. During 2005, the issuance of these risky loans peaked with the housing market. Now a flood of adjustable rate mortgages is due to have the payments adjusted *up* in the coming months. The flood of foreclosures will saturate an already saturated market with under-priced housing.

WHAT IT ALL MEANS – Hold on for the ride because prices will continue to fall for the rest of this year. The supply of homes for sale on the market is still growing and will probably continue to grow. The continued growth in inventory and decline in prices will be caused from an increase in foreclosures, short sales (when the bank agrees to let the owner sell the home for less than what they owe), and people wanting or having to move but there are no buyers. The demand for homes will probably not increase until we see the outcome of the vote on the property tax situation. The FHA, who used to exclusively help buyers with great credit, is implementing programs to help families in the sub-prime category. When these programs are fully deployed, the sub-prime category of buyers will have a safe place to go for their mortgages instead of being taken advantage of by unscrupulous mortgage brokers.

If you are a buyer and have cash, just smile and look for bargains. If you are an owner and do not have to move, do not. If you are an owner with an ARM and are thinking, “my payments will stay low for a couple of more years, then I will refinance,” you may be in for a rude awakening. When you try to refinance, your house will be worth less, you will have built no equity (or maybe even increased the principle because you have a negative amortization ARM), and probably will not be able to refinance. You either make the high payments of the mature ARM, or lose the house (depending on credit, assets, etc.).

If you are an investor with an ARM, you have a tough decision to make; ask yourself, "should I sell?" On the other hand, "should I refinance to a fixed rate now or sell NOW?" If you wait to refinance or sell because your payments will not double for another year or two, the value will not be there to refinance. That 20% you put down has melted away. You are risking being upside down with a very high payment and having to put money in every month because the rent will not cover the payments, insurance, maintenance fees, etc.

However, do not worry because the real estate market will turn upward again. It always does. Do you have the patience, equity, or management juggling skills to survive until it does? Call me because talk is always FREE!

Article written in 2007 by Velie Real Estate Services, Inc., founder & owner Eddie Velie
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