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Creative Investment Solutions

WHEN WILL THE HOUSING SLUMP END?

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New home construction represents about 5% of the overall US Gross Domestic Product (GDP). Historically, economic recoveries are not sustainable without a recovery in housing. So with housing being an important factor to economic growth, the question is....when will the slump end?

It was reported this week that average home prices declined 3.1% from last year to this year. This is based on the S&P/Case- Shiller Home Price index, the leading measure of U.S. home prices. This index is based on a composite of 20 metropolitan areas. Even more dramatic, is that from the peak in 2005, average home prices are down over 20%. Home prices in Wisconsin have declined about 14% from the peak, according to statistics compiled by the Wisconsin Realtors Association.

Additionally, the building of new houses continues to decline. We reached a peak of activity in 2006, with over 2 million units being built. The latest statistics indicate an annual level of activity of about 400,000. In Wood County there were only 36 new permits applied for in 2010, which was a decline from the previous year of 26%.

As first glance these two sets of data, price and building declines, appear to be bad news, and in the near term they probably are. The housing slump has definitely been a drag to the US economic recovery. While many parts of the economy have rebounded, housing has not. One of the issues limiting this recovery is the excess supply generated by over building in the early 2000's. In order to see a recovery in the housing market, we need to see a reduction in inventory. Fortunately, there has been some good news on this issue. In February, new home inventories declined from the previous month on a non-seasonally adjusted basis. New home inventory has now recorded 42 straight months of declines, (based on US census data), and has not recorded a monthly increase since May 2007. New home inventory levels are at new all-time record lows. This is good news for the housing market.

The upside to less homes being built and lower prices is we should continue to work off the excess inventory/supply in the marketplace. We have also been seeing modest improvements in employment, which should help home sales. For 2011, it will be important to monitor the housing statistics going forward and to pay especially close attention to housing sales this summer when the Federal Reserve's QE2 program is scheduled to end. While the trend is improving, current data suggests that we will not see a significant recovery in housing for some time to come. This is likely to continue to put a drag on overall economic growth.

In summary, it appears prices may be close to a bottom. Combine that with the likelihood that mortgage rates will be higher in the very near future. And we come to the conclusion that for someone looking to buy a house, this may be one of the best opportunities they will see for a long time.