Written Statement
of the
NATIONAL ASSOCIATION OF REALTORS®
submitted to the
Senate Banking, Housing and Urban Affairs' Subcommittee on Housing & Transportation and Subcommittee on Economic Policy
On
"The Housing Bubble and Its Implications for the Economy"
September 13, 2006

Chairmen Allard, Bunning and Ranking Members Schumer and Reed, and Members of the Subcommittees, My name is Tom Stevens, and I am the former President of Coldwell Banker Stevens (now known as Coldwell Banker Residential Brokerage Mid-Atlantic) – a full-service realty firm specializing in residential sales and brokerage. Since 2004, I have served as senior vice president for NRT Inc., the largest residential real estate brokerage company in the nation.

As the 2006 President of the National Association of REALTORS®, I am here to testify on behalf of our nearly 1.3 million REALTOR® members. We thank you for the opportunity to present our views of the current real estate market as well as prospects for the future. NAR represents a wide variety of housing industry professionals committed to the development and preservation of the nation's housing stock and making it available to the widest range of potential homebuyers. The Association has a long tradition of supporting innovative and effective housing programs and we continue to work diligently with the Congress to fashion housing policies that ensure housing programs meet their mission responsibly and efficiently.

For the past five years, the housing market has been a steadfast leader in the U.S. economy. In 2005, mortgage rates remained near 45-year lows while the nation's economy generated 2 million net new jobs. Existing-home sales rose 4.4 percent in 2005, resulting in five successive record years. Both new-home sales and new single-family housing starts also set new high marks in 2005. Overall, the housing sector directly contributed more than $2 trillion to the national economy in 2005, accounting for 16.2 percent of economic activity. In addition, commercial real estate contributed an additional $330 billion to the nation's economy.

After five years of outstanding growth and being the driving force of the U.S. economy, the housing market is undergoing a period of adjustment. I have experienced this first hand as my prior home has been on the market, in Northern Virginia, for over a year. Existing home sales in July fell 11.2 percent from a year ago. New home sales are down 22 percent from a year ago. The inventory of unsold homes on the market is at an all-time high of 3.9 million, which is a 40 percent rise from a year ago. Given the falling demand and increased supply, home prices have seen less than 1 percent appreciation from a year ago compared to the double-digit rate of appreciation in 2005.

While recent developments raise concerns, it is important to remember that the housing market varies significantly across the country. One-third of the country (by population) is still seeing rising home sales. They include Alaska, Vermont, New Mexico and many states in the South (excluding Florida). The remaining two-thirds of the country is experiencing lower sales with some states feeling acute adjustment pains. Sales are down significantly in Florida, California, Arizona, Nevada, Virginia, and Maryland. These regions experienced the greatest rise in home prices in recent years and affordability has become a major issue. The sharp decline in sales have resulted in a much higher housing inventory (tripling and quadrupling in some cases) and these areas are vulnerable to outright price declines, particularly if interest rates were to rise further.

The industrial Midwest region did not participate in the nationwide housing market boom of the past five years due to weaker job market conditions. Job gains have been minimal in Ohio and Indiana during the recent nationwide economic expansion. Job losses have been continuing in Michigan - for five straight years.

Purchase discounted products and services from REALTOR BENEFITS® Partners

Contrary to many reports, there is not a "national housing bubble." All real estate is local. For example, the housing market in California is extremely different from Oklahoma. Home price-to-income ratio, home price-to-rent ratio, and more importantly, mortgage debt servicing cost-to-income ratio have greatly increased in some markets to worrisome levels. Markets in Florida, California, Arizona, Nevada, Virginia, and Maryland exhibit trends far above the local historical norm, thus it would not be surprising for these markets to experience a price adjustment. However, these states have solid job growth – Because of solid job growth, price declines are likely to be short-lived as new job holders provide demand and support for the housing market.

If the mortgage rates were to rise measurably - to say 7.5 percent or 8 percent from the current 6.5 percent - for whatever reasons (be it Chinese dumping dollars on the market, higher inflationary expectations, or monetary tightening by the Federal Reserve) then the housing market would certainly come under more pressure and many markets would likely undergo price declines.

The most influential factor is the rising mortgage rates. Many homebuyers in coastal markets have resorted to more exotic mortgages. Due to very high home prices, interest-only, adjustable rate, and/or option-ARMS became the only way to enter the housing market for some homebuyers. In essence, the homebuyers in the coastal markets are at their financial capacity. With rising mortgage rates, homebuyers are becoming exhausted financially, which explains why sales have tumbled in high priced regions of the country. In the industrial Midwest, as I said earlier, the housing market is more job market dependent and less mortgage rate dependent.

Another factor is the insufficient presence of Government Sponsored Enterprises (GSEs) and the Federal Housing Administration (FHA) in the high priced regions. The increases in GSE/FHA loan limits have not kept pace in places like California, Florida, and parts of New York among others. For example, loan limits rose 7.8 percent in 2005 while home prices rose 19 percent in Los Angeles, 25 percent in the D.C., and 30 percent in Miami. Consider, for a moment, that FHA's share of loans in Los Angeles went down from nearly 20 percent in 2000 to essentially zero today.

As you know, FHA loans often serve neglected demographic segments of the housing market – first time, lower income, minority, and immigrant homebuyers. NAR applauds the Bush Administration's FHA reform proposal currently being considered in Congress. A modernized FHA will be a valuable tool to people seeking to buy a home in softer housing and mortgage markets. As we have seen in the past, in soft local and regional markets, FHA has filled significant gaps in the private sector lending market, becoming the predominant tool to achieve homeownership and helping to carry regions out of an economic downturn. In the mid 1980s, in Colorado, Oklahoma, Louisiana, and Texas, the FHA loan program stepped in, while private mortgage providers left those in distressed economic areas, and took over a substantial role in providing available mortgage credit to those in affected states. An FHA with the tools to complete the task will be important to thousands of Americans hoping to buy a home, but in particular, in those markets that really need the help.

Florida has also been hit by another unique factor - the lack of affordable property insurance. The unprecedented number of strong hurricanes hitting the Florida shores in 2004 and 2005 has resulted in a dysfunctional insurance market where premiums have either increased - literally through the roof - or are simply not available. We have heard many stories from our membership in Florida about how potential homebuyers backed away at the last moment either due to the insurance sticker shock or due to outright unavailability of insurance.

The national forecast for the coming year, based on stabilizing mortgage rates and a modestly expanding economy through 2007, predicts that existing home sales will fall 8 percent in 2006 followed by another 2 percent decline in 2007. New home sales will fall by an even greater amount of 16 percent in 2006 and then 7 percent in 2007. Home price growth will be minimal (less than 3 percent) in both of these years, again, it is important to remember that all real estate is local. Therefore, some local markets will not comport with the national forecast. Any significant shift in mortgage rates and the state of the economy will also alter the outlook.

Based on the housing market forecast mentioned above, the residential construction spending portion of the economy will contract 3.4 percent in 2006 and 8.5 percent in 2007. In other words, $21 billion will be subtracted from GDP in 2006 and another $49 billion slashed in 2007. That would be a sharp contrast to the near $50 billion in additions during the housing market boom.

The more important contribution of the housing sector has not been in the direct employment of real estate agents, mortgage lenders, construction workers, or expansion of Home Depot and Lowe's to name a few. Consumer spending of all things (from furniture and autos to travel

and education) has been greatly supported by the increase in housing equity accumulation. A typical homeowner in the U.S. gained $72,300 in housing equity in the past five years, including over $20,000 just last year. Nearly all economists will say that consumer spending has been far more robust than can be explained by income growth, job gains, and stock market gains. GDP growth would have been 1.5 percent points lower had the housing market not provided the wealth accumulation in recent years.

NAR understands that the housing sector could not maintain a record setting pace indefinitely. A soft landing is certainly possible and under the right circumstances likely, but that soft landing is critically dependent upon policies that support a transition to a more normalized market and mitigate changes in local markets in the availability of mortgage financing and other essential elements to homeownership.

In conclusion, the National Association of REALTORS® commends the Subcommittees for holding this important hearing and for its leadership in fashioning housing and economic policies that stimulate the U.S. economy. The NAR stands ready to work with Congress to continue to open the door to the American Dream – Homeownership. This concludes my testimony and I look forward to answering any questions you may have.

Real Estate Trends Presentation

Copyright NATIONAL ASSOCIATION OF REALTORS®
Headquarters: 430 North Michigan Avenue, Chicago, IL. 60611-4087
DC Office: 500 New Jersey Avenue, NW, Washington, DC 20001-2020
1-800-874-6500
Terms of Use | Privacy Policy | REALTOR.com | Contact NAR | Site Map