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New Slip in Housing Prices Undercuts Fragile Optimism

By [DAVID STREITFELD](#)

Just as the economy is finally beginning to strengthen, the real estate market is showing new signs of deterioration.

Prices slipped in many cities in October, new figures show, despite low mortgage rates and a generous tax credit meant to spur sales. Now rates are starting to rise, making it harder for many buyers to afford a house, and the tax credit seems to be losing its capacity to lure them into the market.

The renewed worries about housing come against a backdrop of improvement in the broader economy. Surveys suggest consumers are growing more confident. That better mood probably helped improve holiday retail sales. The number of people joining the ranks of the jobless is dwindling, while the hiring of temporary workers is up, a traditional harbinger of recovery.

Still, economic growth for the third quarter was more modest than originally reported; it was revised down to an annual rate of 2.2 percent from 2.8 percent. Many economists are fretting that housing could drag down the tenuous recovery.

“I’m worried. Everyone’s worried,” said Karl E. Case, the Wellesley College economist who helped design the housing index that provided fresh cause for alarm on Tuesday. “If prices sink 15 percent from here, which is a possibility, and the 2008 and 2009 loans go bad, then we’re back where we were before — in a nightmare.”

The figures released Tuesday showed that the [Standard & Poor’s/Case-Shiller](#) home price index, a widely watched measure of housing markets in 20 metropolitan areas, rose 0.4 percent in October from the previous month on a seasonally adjusted basis.

It was the fifth consecutive month that prices were up, but the rate of increase has dropped sharply from the impressive gains of the summer. Prices in nine of the 20 cities were flat or down.

Some analysts see little cause for alarm. Dan Greenhaus of Miller Tabak said that if prices fell “a bit further” it would sop up some of the excess inventory still weighing on the market.

But others said that the Case-Shiller index showed an increase only because each report is an average of the preceding three months, meaning the strong August market was still a component of the October report. Another factor supporting the index is the seasonal adjustments, which tend to hide any weakness in the cooler months as the pace of home-buying slows.

On an unadjusted basis, the index was flat. [A different housing price index](#), compiled by the research firm LoanPerformance, fell 0.7 percent in October.

Mr. Case, who chided himself for his optimism over the summer, said he now believed “the probability is very high of a serious double dip like 1982.”

The federal government has mounted an extensive and expensive effort to repair housing. While these actions undoubtedly staved off a total collapse, they are showing signs of fatigue.

The tax credit for first-time buyers has been extended until next spring, but the urgency that buyers showed this summer, when they believed the credit was about to end, has drained away. The Federal Reserve has intervened in the market to push 30-year mortgage rates to the lowest level in decades, but says that program will end by March 31. Rates have already crept back above 5 percent.

[Fannie Mae](#) and [Freddie Mac](#), the government-controlled mortgage giants, are tightening policies for loans in their portfolios. Lenders who sell their mortgages to Fannie and Freddie are becoming more skittish about extending credit.

The [Federal Housing Administration](#), which has become an important part of the entry-level housing market, is expected to tighten its standards in the next few weeks. That would further crimp the pool of eligible buyers.

Faramarz Moeen-Ziai of [Bank of Commerce](#) Mortgage in San Ramon, Calif., said many of his clients were struggling to complete deals. “All this is adding to the downward pressure on prices,” he said.

Falling prices are in theory good for buyers. Some housing commentators say prices need to fall much further before houses will be truly affordable. But the drop over the last three years, however necessary, has caused tremendous damage to wallets and to the lubricant of commerce, confidence in the future.

Falling prices have put as many as a quarter of mortgage holders under water, where the loan balance is greater than the amount the home would fetch. If they lose their jobs, they have little choice but to opt for foreclosure. In a vicious circle, every new foreclosure puts more pressure on the housing market.

Neree Dastous, a 39-year-old firefighter in a San Francisco suburb, would like to move from his condominium into a three-bedroom house. But the condo is under water, so he cannot sell. Keeping it as a rental pushes his debt-to-income ratio above the new Fannie Mae guidelines. Interest rates are not helping, either.

“Anything I can afford, I wouldn’t want my kids to live in,” Mr. Dastous said. “I need prices to come down, but if they do the value of my condo goes down, too. It’s very complicated.”

Mr. Case, the Wellesley economist, said he was heartened by the minimal pace of housing starts by builders and the exuberant sales volume of existing houses. These two forces should ultimately clear the backlog in the market and prop up prices.

Yet for now, prices in many cities are weakening. “There’s no historical data for falling house prices” on such a scale, he said. “We don’t know how this ends.”

While the Case-Shiller index has managed gains for the last several months, it is still down 7.3 percent from October 2008 and is off 29.5 percent from its peak. Some analysts predict prices will fall as much as an additional 10 percent. That could swiftly undermine consumers’ frail confidence.

[The Conference Board](#) reported Tuesday that the consumer confidence index increased in December to 52.9 from a revised 50.6 in November. In February, when talk of another Depression was rife, the index was at 25.3.

“Part of the reason people are turning more optimistic is a perception that the real estate market has turned,” said Joshua Shapiro, chief United States economist for MFR. “If that proves to be false, and we think it will be, it is going to come as a surprise to many.”

Mr. Dastous, the foiled buyer, is already deeply disappointed. He is exploring foreclosures and fixer-uppers, but has no confidence he and his family will be able to move any time soon.

Housing bloggers have given a name to this phenomenon: house arrest.

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