

# Housing Market Outlook for 2011

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The short-term direction of the housing market seems as murky today as it has at any point in recent years. Following the expiration of the federal homebuyer tax credit program in June, housing demand has been lackluster, even by today's standards. Additionally, mounting foreclosures and short sales threaten to erode home values further. Meanwhile, the stalled labor market serves as a backdrop to these housing woes. Daunting as these problems may be, the conditions are right for a recovery as prices have come down and interest rates are low. However, it may be some time before consumers are confident enough to jump back into the housing market in large numbers.

## Housing Market Tries to Stand on Its Own

The dramatic decline in the U.S. housing market in recent years has been well documented. The sale of new homes dropped 71 percent from a peak of about 1.4 million units in 2005 to 374,000 units in 2009. Existing single-family home sales fell 27 percent over the same period and home values have declined in much of the country. In response to these conditions, the federal government initiated its tax credit program for homebuyers in hopes of boosting demand. It seems clear that this program, which ran from early 2009 through April 2010, did at least help to break the free fall in home sales and values. However, it is difficult to know if these tax credits simply hastened the purchase of homes by those who would have bought anyway or if they induced new buyers into the market.

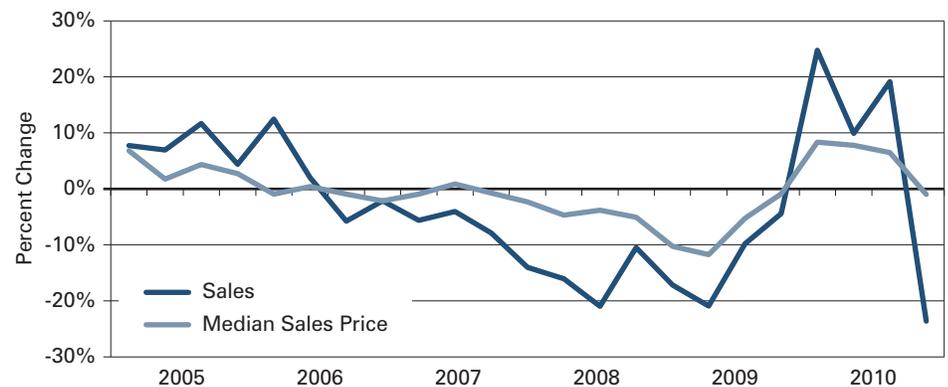
Whichever the case may be, **Figure 1** suggests that we are in the midst of a predictable post-homebuyer-tax-credit hangover. After declining at an average rate of 3.1 percent per

**FIGURE 1: New Home Sales and Case-Shiller 20-City Home Price Index, 2000 to September 2010**



Note: The shaded area indicates the period that federal home buyer tax credits were available. Both variables are seasonally adjusted. New home sales are reported as an annual rate. Hash marks indicate January and July of each year. Source: IBRC, using Standard & Poor's and U.S. Census Bureau data

**FIGURE 2: Year-over-Year Change in Indiana Home Sales and Median Price, 2005:1 to 2010:3**



Note: Hash marks indicate quarters of each year. Source: IBRC, using Indiana Association of Realtors data

month between July 2005 and April 2009, new home sales stabilized and grew at an average monthly rate of 1.1 percent through April 2010. Without the aid of federal stimulus, however, new home sales fell sharply in May 2010 and have remained low. In fact, the five months since the expiration of the tax credits are the five lowest monthly new homes sales figures on record dating back to 1963. Home values, as measured by the Case-Shiller Home Price Index, also steadied while the tax credits were active but ticked downward in July and August.

The situation has been similar in the market for existing homes. According to the National Association of Realtors, existing home sales increased nearly 5 percent between 2008 and 2009 and the rate of sales remained relatively strong through the first half of 2010. The expiration of the tax credits, though, triggered a 27 percent drop in the seasonally adjusted rate of existing home sales between June and July.<sup>1</sup> In contrast to new home sales, the existing home market has bounced back more sharply with the

September sales figure up 18 percent over the July mark.

Much of this instability has been driven by troubles in the once booming housing markets of the South and West. States like Florida, Nevada, Arizona and California have headlined this crisis. Yet the Indiana housing market has experienced similar trends. As **Figure 2** shows, both median home prices and sales declined year-over-year for most quarters between 2005 and the early 2009, but these measures rebounded over the next year and a half. However, the demand pulled forward by the tax credits left Indiana with a 24 percent year-over-year decline in sales in the third quarter of 2010 and a 1 percent decline in the median sales price.

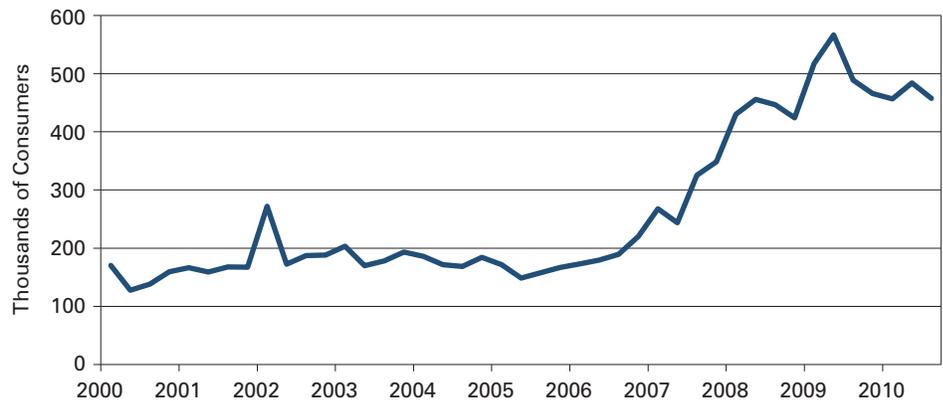
### Foreclosure Problems Persist

One major force that continues to place downward pressure on home values is the continued foreclosure crisis. **Figure 3** indicates that the quarterly flow of individuals with new foreclosures has improved from peak levels recorded in 2009 but continues to be elevated. In contrast to the slight decline seen in new foreclosures in the third quarter, the New York Fed also reports that the share of mortgages that transitioned into delinquency increased for the first time since 2009. An uptick in delinquencies could signal another rise in foreclosures.

Compounding this problem is the recent revelation of improper documentation for many properties in foreclosure. Efforts to remedy the so-called “robo-signing” practices could lengthen the time it takes to clear foreclosed properties from the market, which would act as a further drag on the housing recovery.

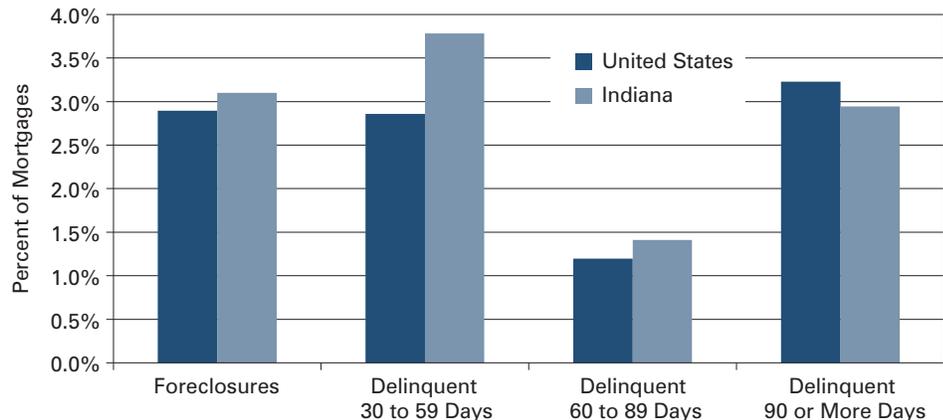
The foreclosure crisis has hit Indiana harder than the United States as a whole. **Figure 4** shows that the share of Indiana’s prime mortgages in foreclosure in August 2010 is slightly higher than the U.S. average.

**FIGURE 3: Number of U.S. Consumers with New Foreclosures, 2000:1 to 2010:3**



Source: IBRC, using Federal Reserve Bank of New York data

**FIGURE 4: Percent of Prime Mortgages in Foreclosure or in a Stage of Delinquency in Indiana and the United States, August 2010**



Source: IBRC, using Federal Reserve Bank of New York data

**TABLE 1: National Association of Realtors (NAR) and Mortgage Bankers Association (MBA) Forecasts, 2010:2 to 2011:4**

	Housing Starts (SAAR, thousands)		Existing Home Sales (SAAR, thousands)		30-Year Fixed Rate Mortgage		Median Existing Home Price (Thousands)	
	NAR	MBA	NAR	MBA	NAR	MBA	NAR	MBA
2010:2	602	602	5,570	5,570	4.9%	4.9%	\$176.6	\$176.6
2010:3	594	589	4,150	4,026	4.5	4.6	177.6	161.0
2010:4	653	580	4,531	4,232	4.5	4.4	168.6	163.6
2011:1	698	595	4,765	4,650	4.7	4.7	165.9	170.1
2011:2	746	635	5,202	4,701	4.9	4.8	177.0	169.9
2011:3	791	670	5,391	4,900	5.1	5.0	179.2	171.4
2011:4	843	735	5,188	5,051	5.4	5.1	170.4	173.5

Notes: Actual values are reported for 2010:2. Figures were taken from each organization’s October 2010 forecasts.  
Source: National Association of Realtors and Mortgage Bankers Association

Perhaps more alarming is the share of the state’s prime mortgages in the early stages of delinquency.

The pattern is similar for mortgages owned by Fannie Mae and Freddie Mac, with 8.4 percent of Indiana’s

# Indiana's Outlook for 2011

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mortgages held by these entities either delinquent or in foreclosure compared to 7.3 percent nationally. Indiana's above average mortgage delinquency situation should come as no surprise given that the state has had one of the nation's highest unemployment rates in recent months.

## Home Construction

The trends in residential building permits and housing starts largely mirror what we saw in new home sales. Each indicator stabilized in 2009 and 2010 but neither has risen appreciably. While it is welcome news that these indicators have steadied, they have settled at levels that are roughly one quarter of 2005's peak of construction activity. In 2009, Indiana recorded its lowest level of residential building permits since 1982.

## Conclusion

The housing markets in the U.S. and in Indiana will likely see growth in 2011, but with the broader economy, this growth will be modest. As **Table 1** outlines, two industry trade groups forecast that housing starts and home sales will climb somewhat but, in the case of home sales, the numbers are not likely to reach the level seen prior to the tax credit deadline. While there is currently some slack in demand, reduced prices and low interest rates should keep home purchases attractive. The housing market is now simply waiting on a robust economic recovery to spur consumers into taking advantage of very favorable affordability conditions. Unfortunately, that strong recovery appears to be at least a year or two away. ■

## Notes

1. The data sources for new and existing homes show that each market responded to the expiration of the tax credit at different times. This discrepancy is due to how home sales are counted. New home sales are counted when a sales contract is signed while existing home sales are counted when the sales contract is closed.

One year ago, Indiana's economy was reeling from major hits caused by the deepest recession in decades. As 2010 draws to a close, we've seen measurable, if modest, improvement, and the prospects for the year ahead are mildly encouraging.

## Employment: A Mixed Picture

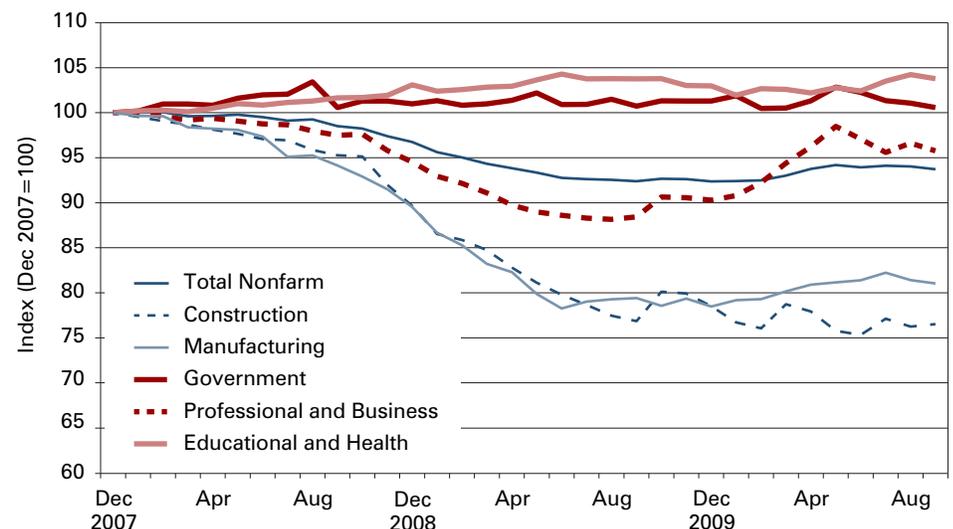
The recession that began in December 2007 hit Hoosiers very hard. By the time Indiana employment bottomed out two years later, 227,900 payroll jobs had disappeared—the 13th highest rate of decline in the nation. Fortunately, 2010 has been a relatively good year: we've recovered 40,000 jobs between December 2009 and September 2010 (preliminary). This gain of 1.4 percent so far is the fifth fastest in the nation, and the state has received national media attention for its job creation. However, the pace of growth is unsteady, with some slippage in recent months. And despite this year's net gain, 82 percent of the lost jobs have yet to return.

Some sectors are faring better than others in this recovery. **Figure 1** shows relative change in Indiana payroll employment since the start of the recession. Private education/health services jobs actually increased nearly 4 percent, and government jobs have not slipped into negative territory.

In contrast, the construction and manufacturing sectors together shed more than 138,000 jobs, nearly one-fifth of their start-of-recession levels before they started slowly rebounding. Manufacturing has inched upward slowly, but construction remains near the bottom. And the professional and business services sector, which saw substantial job gains during the past decade, slipped 12 percent during the recession but has regained much of that loss this year.

We expect Indiana employment to complete 2010 about 2 percent, or 55,000 jobs, above where it started and for 2011 to show similar gains. This is well above job growth in recent years, but even so, at this

**FIGURE 1: Relative Change in Indiana Employment, December 2007 to September 2010**



Note: September 2010 data are preliminary.  
Source: IBRC, using Bureau of Labor Statistics data