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Housing recovery: Where do we stand?

By Chris Kissell • Bankrate.com

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After years of withering on the vine, the nation's housing market finally is showing signs of new life. Home prices are up while mortgage rates are at historic lows, and bidding wars have broken out in some formerly down-and-out locales.

William Hardin, director of real estate programs and Tibor and Sheila Hollo research fellow at Florida International University in Miami, says that while housing prices will recover in nominal terms, a "real" recovery will take "much longer." In the interview below, he outlines his thoughts about the challenges facing today's buyers, sellers and homeowners.

Q: **As home prices rise, do you think they'll ever go back to the levels seen in 2005 during the housing boom?**

A: When economists look at housing prices, they focus on real prices or levels. This means the level adjusted for inflation. In the present case, we will assuredly see nominal (unadjusted) prices reach the 2005 level.

When we look at housing prices in real terms, the adjustment will take much longer. We will see, in many markets, double-digit nominal price increases. This is not necessarily a sign of a boom, but a reversion to normal pricing. We should not forget that if a price declines by 50 percent, it will then need to increase by 100 percent to return to the same price. If we go back to the real or inflation-adjusted price, we can note that 3 percent appreciation is required when we have inflation on 3 percent to just stay even in real terms.

Q: **As the inventory of homes for sale shrinks, many homebuyers are willing to pay more than the asking price. However, the appraisal doesn't always support the price the buyer is willing to pay. How big of an obstacle do you think this is for the housing recovery?**

A: Bidding wars and appraisals are not really a big issue. Most of these get resolved, but agents like to talk about these events. Let's be straightforward -- if an agent is actually working as a buyer's agent, this should be less of a problem. However, most agents are either transaction agents and brokers or work for the seller. My guess is that a person buying a home with a true buyer's agent with a fiduciary responsibility to the buyer will not really face this problem.

Bidding wars are really about a marketing strategy (list low and solicit bids), as we know from much research that a bidding or auction situation has the potential to distort prices.

Q: **The high end of the market is doing well, with foreign buyers and wealthy Americans buying houses. The low end of the market is targeted by investors. What can be done to stimulate the middle layer of the housing market?**

A: The middle market, depending on how you define it, is dependent on trade-up buyers. These trade-up buyers should be using equity that accrued in their prior ownership cycle. Given the changes in values over the last five to seven years now, there is little accrued equity for many of the cohort that would be trade-up buyers. This means that these buyers need to be offered mortgage options with lower down payment requirements.

The truly affluent have a greater percentage of wealth in equities and other financial assets and are now benefiting from increased values in those markets. The midtier households are dependent on income and extending that income. Hence, a benefit from more access to credit and lower rates for those who qualify for debt.

There is also a question of the value of real estate if you have to stretch to own. While most all indicators point to a buy now, some people are just not inclined to buy.

Q: **Federal regulators are imposing a "qualified mortgage" rule that will require lenders to determine whether borrowers can repay their mortgages. How will the qualified mortgage rule affect middle-class homebuyers who have jobs and collect salaries and get W-2s?**

A: These are the easiest people to have their income verified. They will have more access to mortgages. This is just like the old days, pre-2004. People and mortgage brokers got accustomed to poor underwriting. The mortgage business is actually one of the easiest businesses in terms of underwriting. Forget (loan-to-value), look at cash in the deal, and make sure the debt-to-income ratios are correct.

In the normal days, it was not uncommon that applicants would make sure they looked "good" by reducing debt, car leases, etc., prior to applying for a mortgage.

Q: **How will the qualified mortgage rule affect middle-class homebuyers who own small businesses or who get much of their income from commissions?**

A: This has always been an issue. I come from a family of entrepreneurs. You just, unfortunately, have to have better financials and perhaps have to settle for less housing. We know commission incomes fluctuate. People in these industries need to be honest with themselves on the sustainability of their commission streams. The people who are dependent on commissions and variable cash flows that survive long term know this and plan.

Small-business owners need to have as much transparency as possible and good financial records.

The entire idea of a qualified mortgage is really government interventionism. In truth, people with a history in mortgage underwriting know what to do and what is good underwriting. Wall Street and institutional and large investors were the ones that got it wrong. If you have a verified debt-to-income level of 28 (percent) or less on housing debt, and 26 (percent to) 38 (percent) on total debt, you will not have a mortgage "market" issue. You will have defaults, but you will not have market-level issues.

Some of the proponents of higher ratios are actually members of the affordable housing community who want these levels upward of 50 percent on total debt. This does no one any good.

We would like to thank William Hardin, director of the Hollo School of Real Estate and Tibor and Sheila Hollo research fellow at Florida International University in Miami, for his insights. Holden Lewis, assistant managing editor for Bankrate.com, contributed the questions for this interview.

Posted: March 26, 2013

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