

'Shadow' Looms Large Over Shaky U.S. Housing Market

By Bill Freehling

The Free Lance-Star, October 3

THE U.S. housing market has been picking up of late, with sales rising and prices seemingly stabilizing.

That's led many commentators to declare a recovery in the housing market, and the optimism may be partly responsible for the Dow Jones Industrial Average's push toward 10,000 points.

Not so fast, warns a report published late last month in Amherst Mortgage Insight, a publication of fixed-income investor Amherst Securities Group LP.

Amherst acknowledges some positives. The \$8,000 tax credit for first-time home buyers is bringing people into the market, and homes are more affordable than they've been in decades. But the report warns that the optimism is "premature" and notes that a huge "shadow inventory" of homes exists in the U.S. The mortgage loans on these homes aren't being paid, but they're not yet listed on the market.

"We are concerned that, in light of this housing overhang, the stabilization we have seen in home prices the last few months is temporary," the report says.

Amherst calculates that there are 7 million homes in the U.S. that haven't hit the market but that are likely to eventually default. That could get worse if prices fall further, leaving more people under water on their loans.

To put the 7 million "shadow inventory" figure in context, existing home sales for the year are on pace to total about 5.2 million. The shadow inventory is growing by about 300,000 mortgages per month. When those homes get released onto the market, prices could fall.

The shadow inventory is growing rapidly because loans continue to go delinquent at a fast pace, but they're taking a long time to make it through the foreclosure process.

The slow pace of delinquent loans being moved through the foreclosure process is in part due to political pressure on the banks. Amherst doesn't believe mortgage modification efforts can save more than 1 million of the 7 million units of shadow inventory.

Of course not all markets are equal. The report shows that the markets hit hardest by the housing bust--including parts of California and Nevada--have shadow inventories that are twice the size of the active listings. In the Washington area, by contrast, the shadow inventory adds 34 percent to the number of homes that are listed.

Still, that 34 percent is significant. In the Fredericksburg area, for example, there were 2,435 homes on the market at the end of August. Adding 34 percent to that total would push the inventory to about 3,260.

At the sales pace from August, that changes the inventory of homes from a 6.4-month supply to an 8.6-month supply. That doesn't count the people who want to sell but can't afford to.

Further, as the Amherst reports notes, the U.S. housing market is coming off its peak summer sales months. Should sales drop off in the fall and winter as they usually do, and if the shadow inventory

begins to hit the market, prices could be pressured. Lower prices mean more under-water loans, and some people might walk away rather than paying what are now above-market rates.

A dire report, to be sure. But one that people would be wise to consider.

Staff reporter Bill Freehling writes this weekly column on business, personal finance and investing. He can be reached at 540/374-5405 or
Email: bfreehling@freelancestar.com.