

# real estate insights

October 2006

Real Intelligence –  
Real Advantages

## In This Issue

**Existing-home sales** posted a seasonally adjusted annualized sales rate of 6.30 million units in August. The sales pace was off 0.5% from July and 12.6% below the level in August of 2005. August resale figures indicate that the housing market is beginning to stabilize at a sustainable pace, and 2006 is still expected to post the third highest sales rate on record. Home prices declined, as anticipated. The national median existing-home price for all housing types was \$225,000 in August, down 1.7% from August 2005. Total housing inventory levels rose 1.5% at the end of August to 3.92 million existing homes available for sale – a 7.5-month supply at the current sales pace. That is the highest inventory level since April 1993. **Read more.**

**(De-)Fault Line.** Normally, any decline in housing activity would herald a rise in unemployment, and a rise in mortgage rates would usher in a strong trend in households defaulting on their mortgages. But that's not happening. Why? Ken Fears looks at the role employment plays in helping to stabilize part of the housing market. **Read more.**

**Breaking with Tradition.** Strong home price appreciation over the past several years in an environment of flattening incomes has spurred some potential homebuyers to seek non-traditional mortgages in order to purchase a home. But these non-traditional loan instruments can be risky. Our market intelligence feature looks at what NAR is doing to educate its members about the risks involved with interest-only, payment option ARMs and other exotic mortgages. **Read more.**

**REnew, REconnect, REenergize ...** and help Rebuild New Orleans. It's that time of year again. NAR's Annual Conference and Trade Expo is just around the corner. And while you're there, you'll have a chance to hear the latest from David Lereah on the outlook for real estate and the economy, and recently released information about how baby-boomers look at real estate. **Read more.**

David Lereah's Economic Commentary column will return next month. In the meantime, visit [www.realtor.org/research](http://www.realtor.org/research) and see some of Dr. Lereah's latest presentations.

### Table of Contents

Real Estate Monitor	2
The Forecast	4
U.S. Economic Outlook Table	6
Some Cooling Markets Become Fragile – Others Bounce	7
Mortgages: Do Your Homework First	9
Links to Statistical Tables	11
Buy Research	12



NATIONAL ASSOCIATION OF REALTORS®









The Voice For Real Estate®

REALTOR®



EQUAL HOUSING  
OPPORTUNITY

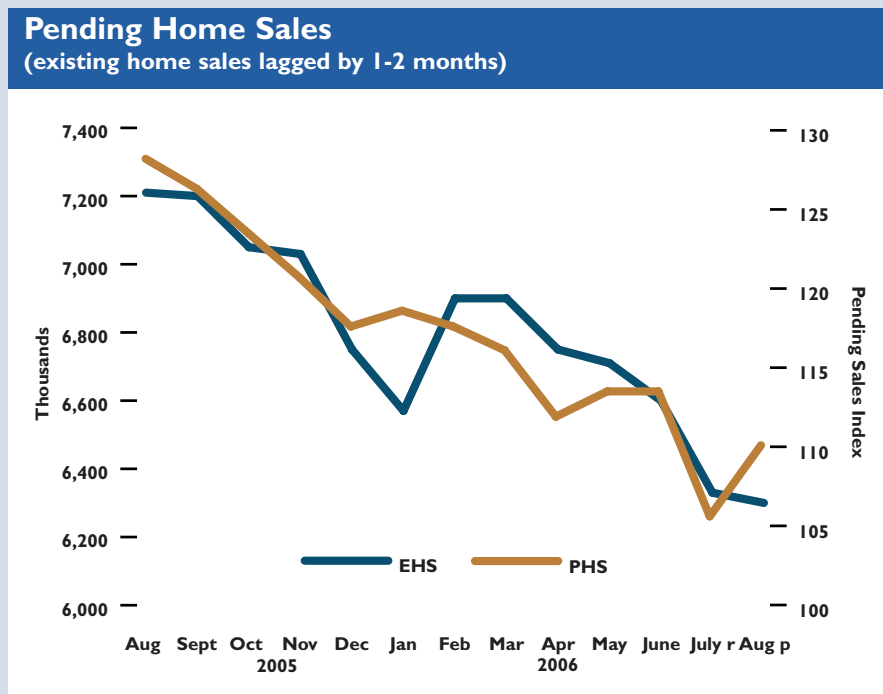
# Real Estate Monitor

Monthly Indicator	Recent Figures	Likely Direction Over the Next Six Months	Forecast
<p><b>Existing-home sales</b> fell 0.5% in August to 6.30 million seasonally adjusted annualized units – the lowest pace since January 2004. Sales are off by 12.6% from a year ago. The slowing sales pace contributed to an increased supply of homes available for sale. Existing-home inventory rose. <a href="#">Read more.</a></p>	June 6,600 July 6,330 Aug 6,300		Buyers in a wait-and-see mode and thereby holding back sales
<p><b>New home sales</b> rebounded 4.1% in August to 1.05 million seasonally adjusted annualized units, after falling the three previous months. The inventory of unsold new homes rose modestly and is at a 6.6-months' supply, the highest level in over 10 years. <a href="#">Read more.</a></p>	June 1,091 July 1,009 Aug 1,050		New homes in the coastal states are still very expensive
<p><b>Housing starts</b> fell 6% in August to 1.665 million seasonally adjusted annualized units – their lowest level since April 2003. Both single-family and multifamily starts declined. Builders' sentiment has continued to fall implying lower new construction activity in the coming months. <a href="#">Read more.</a></p>	June 1,833 July 1,772 Aug 1,665		Many builders are prudent to cut back production
<p><b>Housing affordability</b> NAR's housing affordability index rose 2.7% in August to 102.3. The increase in the index was due primarily to a decline in home prices. An index of 100 shows that a family earning the median income has just enough income to qualify for a loan on a median-priced home. <a href="#">Read more.</a></p>	June 101.0 July 99.6 Aug 102.3		Wages up 4% while home price rising minimally
<p><b>Mortgage rates</b> The 30-year fixed mortgage rate drifted lower in September to 6.41%. The lower rate is attributed to the recent slowdown in housing activity coupled with easing inflation fears. Affordable mortgage rates and softening home prices are favorable for the housing market. <a href="#">Read more.</a></p>	July 6.76% Aug 6.55% Sept 6.41%		Rising modestly in 2007
<p><b>Purchase applications</b> The Mortgage Bankers Association purchase applications index rose in September to 395.7. Mortgage demand for both home purchases and home refinancings increased mainly due to more favorable mortgage rate conditions. <a href="#">Read more.</a></p>	July 397.2 Aug 383.2 Sept 395.7		Lender's business sliding more than real estate agents due to declines in purchases and refinances
<p><b>Employment</b> Payroll employment rose by a meek 51,000 in September. Over the past 12 months, 1.77 million jobs have been added to the economy. The unemployment rate fell to 4.6% – a rate considered very near “full employment.” <a href="#">Read more.</a></p>	July 123 Aug 188 Sept 51		Housing slowdown hitting the broader economy and job growth to remain at a sub-par pace
<p><b>Inflation</b> The consumer price index (CPI) climbed 0.2% in August – lower than expected. The core index (excluding food and energy) also increased 0.2%. Fuel prices increased a moderate 0.3% in August. Expect the housing component to flatten out in the coming months and to leave the core component steady at a sustainable, 0.2% average monthly rate for the next three months. <a href="#">Read more.</a></p>	June 0.2% July 0.4% Aug 0.2%		Oil prices are coming down and oil speculators are losing their shirt

Notes: All rates are seasonally adjusted. Existing home sales, new home sales and housing starts are shown in thousands. Employment growth is shown as month-to-month change in thousands. Inflation is shown as a month-to-month percent change in the Consumer Price Index. Sources: NAR, Bureau of the Census, Bureau of Labor Statistics, Mortgage Bankers Association and Freddie Mac. This report reflects data as of Oct 6, 2006. Compiled by Wannasiri Chompoopet, Ken Fears, Kevin Thorpe and Lawrence Yun.

# NAR's Pending Home Sales Index

NAR's pending home sales index rose 4.3 percent in August. August's index, based on contracts signed in August, stood at 110.1, rising from July's level of 105.6. The index is a leading indicator for the housing sector, based on pending sales of existing homes. A sale is listed as pending when the contract has been signed but the transaction has not yet closed. Pending sales are usually finalized within one or two months of signing. An index of 100 is equal to the average level of contract activity during 2001, the first year to be examined, and was the first of five consecutive record years for existing-home sales. The rise in the index is a hopeful sign that a stabilization is taking place in the housing market. [Read more.](#)



Source: NAR Research

# THE FORECAST

by Lawrence Yun, Senior Forecast Economist

Home prices have come down..The 1.7% national price decline in August (from a year ago) was the first price decline since April 1995 when prices declined 0.1% for one short month. Prices also declined previously to that in both 1992 and 1993, but again for only a single month. The only sustained price decline was a mere two straight months in 1990. There have been no other nationwide price declines since NAR began tracking the data in 1968.

But as I've said before – and of more importance to homebuyers, sellers and their real estate professionals – all real estate is local. Locally, prices in some Florida markets are currently down by more than 10%. Prices in some counties in the D.C. region have also declined close to 10%. Over longer periods of time, some local markets have posted very prolonged price declines. Two examples are Los Angeles and Houston.

In Los Angeles, prices declined from \$224,600 in the second quarter of 1991 to \$167,100 in the fourth quarter of 1996. Los Angeles prices returned to their peak only in 2000. The catalyst for the decline was major job cuts – particularly in industries affected by cutbacks in federal defense spending after the collapse of the Berlin Wall and the subsequent disintegration of the Soviet Union. From peak (1989) to trough (1994) a total of 633,600 jobs were lost in the region.

The Houston housing market also crumbled under the weight of heavy job losses in the 1980s, the result of the oil price collapse and the savings and loan scandal. Home prices in the Houston area fell from \$83,700 in the third quarter of 1985 to \$56,800 in the fourth quarter of 1988. The \$26,900 decline (which now does not sound that large) corresponds to a 32% price correction.

But the current weakening in home prices is not due to any major job cuts that force people to sell their homes at any price. In fact, job creation has been quite robust in those markets currently

experiencing price declines (aside from Detroit). Florida added 243,300 net new jobs in the past 12 months. The D.C. region has been consistently adding about 70,000 net new jobs over the 12-month time span for the past three years – essentially a stadium full of people with new jobs every year (and causing similar stadium-related traffic jams).

Only prolonged job losses, subsequent forced home sales and rising foreclosures will lead to sustained home price declines. So what's going on with the price declines? It's the fact that the

---

## Only prolonged job losses, subsequent forced home sales and rising foreclosures will lead to sustained home price declines.

---

artificially high demand for homebuying has dissipated. What I mean by “artificial” is those buyers who were looking to net quick bucks from flipping properties. At the same time, with prices falling these non-owner occupied homes are being put on the market. That, in turn, artificially elevates housing inventory levels. Higher inventory (more supply) lessens pressure on prices. Hence, prices fall even as the job market continues to steamroll. It will take several months for inventory to ease back down to more manageable, balanced levels. When that happens, home prices will quickly re-enter positive territory.

Some have a hard time accepting this common sense logic. UCLA's Anderson School predicted prices to fall 30% in Las Vegas. That was in 2002. (In fact, home prices in Vegas rose from \$160,000 in 2002 to \$319,000 currently.) Moody's Economy.com has been getting a lot of headlines recently about its

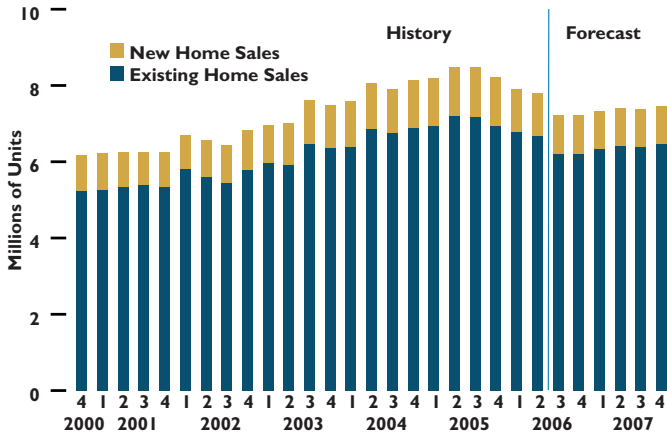
home price forecasts. They call for nation-wide price declines of 3.5% and much more significant declines in some local markets: Las Vegas to correct by 13% with no price pickup until 2009, and Cape Coral, Florida to fall by 19%.

Our forecast is for price to begin increasing in both of these markets from mid-2007 if not sooner. I am particularly bullish on the Salt Lake City market, which could experience double-digit price appreciation in 2006 and 2007. (Moody's Economy.com forecast is for a price decline in Salt Lake City. I'll revisit this paragraph in 2007 to see who came closer to reality.)

As for the national picture, the elevated inventory will be worked off over the next two quarters. Wages are rising at better than 4% and jobs continue to be created – not robustly – but nonetheless respectably with 1.7 million net new payroll jobs in the past 12 months. With home prices falling, the demand will inevitably pick up. The low point will be the fourth quarter of this year. Sales will then steadily climb and with it will come strengthening home prices. In summary, the housing slump is nearly over.

## Home Sales

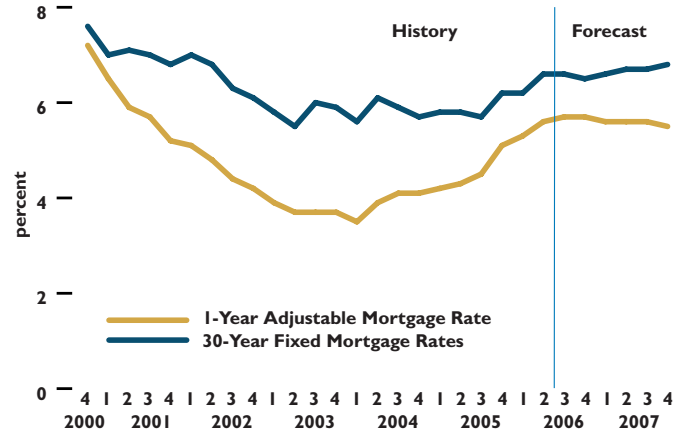
Despite slowdown, 2006 third highest volume ever



Sources: NAR, Bureau of the Census, NAR Forecast

## Mortgage Rates

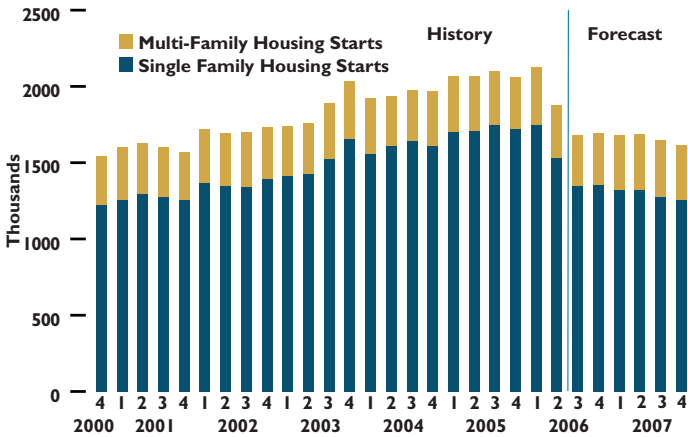
No major shifts in rates



Sources: Freddie Mac, NAR Forecast

## Housing Starts

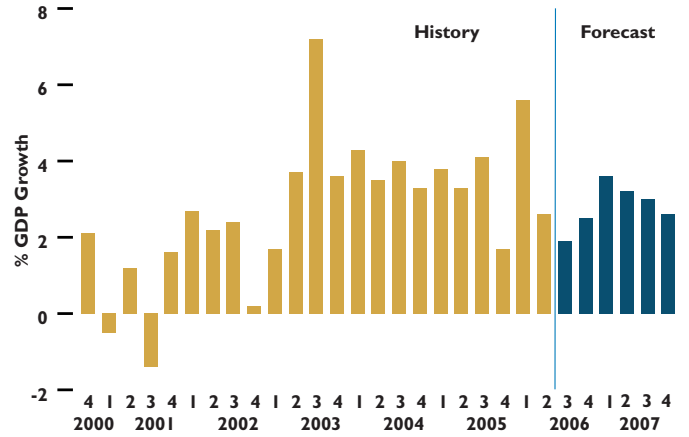
Builders' sentiment points to slowing construction



Sources: Bureau of the Census, NAR Forecast

## Economic Growth

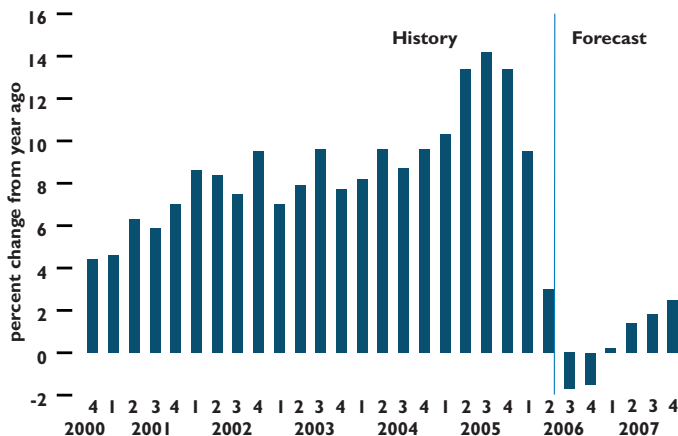
Healthy growth spurt in early 2007



Sources: Bureau of Economic Analysis, NAR Forecast

## Home Price Appreciation

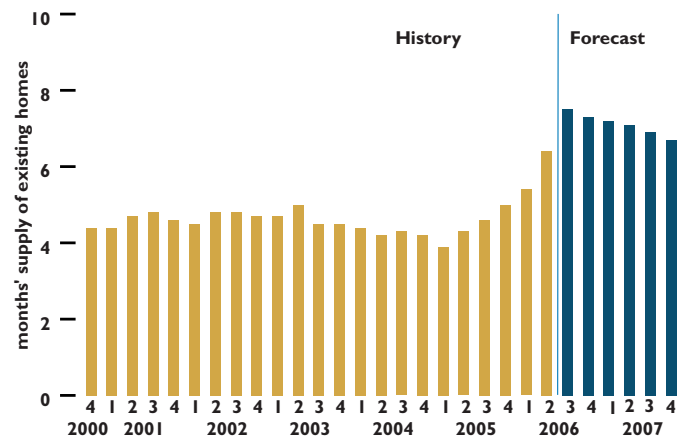
The "heady" times of double-digits are over for a while



Sources: NAR, NAR Forecast

## Housing Inventory

More supply = softer price appreciation



Sources: NAR, NAR Forecast

# U.S. ECONOMIC OUTLOOK

## October 2006

	2005		2006				2007				2004	2005	2006	2007
	III	IV	I	II	III	IV	I	II	III	IV				
<b>U.S. Economy</b>														
<i>Annual Growth Rate</i>														
Real GDP	4.2	1.8	5.6	2.6	1.9	2.5	3.6	3.2	3.0	2.6	3.9	3.2	3.3	2.9
Nonfarm Payroll Employment	1.6	1.2	1.7	1.2	0.2	0.8	0.9	1.2	1.7	1.3	1.1	1.5	1.3	1.0
Consumer Prices	5.5	3.2	2.2	5.0	2.6	1.0	2.2	2.3	1.7	1.8	2.7	3.4	3.4	2.1
Real Disposable Income	-0.6	5.5	4.6	1.7	5.1	5.0	4.1	2.8	2.4	2.1	3.6	1.2	3.4	3.7
Consumer Confidence	99	96	106	107	104	106	106	105	106	106	80	100	106	106
Percent Unemployment	5.0	4.9	4.7	4.6	4.7	4.8	4.9	4.9	4.9	4.8	5.5	5.1	4.7	4.9
<i>Interest Rates, Percent</i>														
Fed Funds Rate	3.5	4.0	4.5	4.9	5.3	5.3	5.3	5.2	5.0	4.8	1.4	3.2	5.0	5.1
3-Month T-Bill Rate	3.4	3.8	4.4	4.7	5.1	5.1	5.0	5.0	4.8	4.5	1.4	3.1	4.8	4.8
Prime Rate	6.4	7.0	7.4	7.9	8.3	8.3	8.3	8.2	8.0	7.8	4.3	6.2	8.0	8.1
Corporate Aaa Bond Yield	5.1	5.4	5.4	5.9	5.7	5.6	5.8	5.8	6.0	6.0	5.6	5.2	5.6	5.9
10-Year Government Bond	4.2	4.5	4.6	5.1	4.9	4.8	4.9	5.0	5.0	5.1	4.3	4.3	4.8	5.0
30-Year Government Bond	4.4	4.7	4.6	5.1	5.0	5.0	5.1	5.2	5.3	5.3	5.1	4.6	4.9	5.2
<i>Mortgage Rates, percent</i>														
30-Year Fixed Rate	5.7	6.2	6.2	6.6	6.6	6.5	6.6	6.7	6.7	6.8	5.8	5.9	6.5	6.7
1-Year Adjustable	4.5	5.1	5.3	5.6	5.7	5.7	5.6	5.6	5.6	5.5	3.9	4.5	5.6	5.6
<b>Housing Indicators</b>														
<i>Thousands</i>														
Existing Home Sales*	7,180	6,943	6,790	6,687	6,211	6,207	6,335	6,406	6,391	6,462	6,779	7,075	6,445	6,395
New Single-Family Sales	1,297	1,280	1,111	1,124	1,003	997	978	985	972	981	1,203	1,283	1,061	979
Housing Starts	2,101	2,060	2,123	1,873	1,680	1,696	1,679	1,683	1,651	1,618	1,956	2,068	1,843	1,658
Single-Family Units	1,748	1,718	1,747	1,530	1,348	1,356	1,322	1,322	1,278	1,257	1,611	1,716	1,495	1,295
Multifamily Units	353	342	376	343	332	340	357	361	372	360	345	352	348	363
Residential Construction**	620	619	619	601	568	543	535	533	532	527	560	608	582	532
<i>Percent Change -- Year Ago</i>														
Existing Home Sales	6.5	0.9	-2.2	-7.0	-13.5	-10.6	-6.7	-4.2	2.9	4.1	9.8	4.4	-8.9	-0.8
New Single-Family Sales	11.9	3.1	-11.5	-12.5	-22.7	-22.1	-11.9	-12.4	-3.1	-1.6	10.8	6.7	-17.3	-7.8
Housing Starts	6.3	4.8	2.6	-9.3	-20.0	-17.6	-20.9	-10.1	-1.7	-4.6	5.2	5.7	-10.9	-10.0
Single-Family Units	6.5	6.7	2.6	-10.4	-22.9	-21.1	-24.3	-13.6	-5.1	-7.3	6.6	6.5	-12.9	-13.4
Multifamily Units	4.9	-3.7	2.9	-3.8	-5.9	-0.5	-5.1	5.2	12.0	6.0	-0.9	1.9	-1.2	4.3
Residential Construction	9.1	9.0	6.1	-1.5	-8.5	-12.3	-13.4	-11.2	-6.4	-2.9	10.3	8.6	-4.2	-8.7
<b>Median Home Prices</b>														
<i>Thousands of Dollars</i>														
Existing Home Prices	227.3	225.3	218.7	226.7	223.5	222.0	219.1	229.9	227.5	227.5	195.4	219.6	223.0	226.4
New Home Prices	236.6	240.1	244.8	242.2	237.0	238.5	245.5	245.6	242.3	244.7	221.0	240.9	240.5	244.5
<i>Percent Change -- Year Ago</i>														
Existing Home Prices	14.2	13.4	9.5	3.0	-1.7	-1.5	0.2	1.4	1.8	2.5	9.3	12.4	1.6	1.5
New Home Prices	10.5	5.4	6.5	5.2	0.2	-0.7	0.3	1.4	2.2	2.6	13.3	9.0	-0.2	1.6
Housing Affordability Index	109	107	109	103	105	108	109	105	107	108	134	122	106	107

Quarterly figures are seasonally adjusted annual rates. / \* Existing home sales of single-family homes and condo/coops; \*\* billion dollars / Source: Forecast produced using Macroeconomic Advisers quarterly model of the U.S. economy. / Assumptions and simulations by Dr. David Lereah and Dr. Lawrence Yun.

# Some Cooling Markets Become Fragile, Others Bounce

by Ken Fears, Manager, Regional Economics

As the tremendous wave of home sales recedes in the face of climbing mortgage rates, many market observers have voiced worries about the fragility of once-hot housing markets. In fact, the strong price appreciation that many of those hot markets experienced over the last six years cut deeply into affordability in those areas. Simultaneously, income growth has been flat, providing no boost to homebuyers. As a result, homebuyers were forced to make larger monthly payments or to use risky mortgage products in order to afford their homes. The percentage of persons using adjustable-rate mortgages and other exotic loans such as interest-only mortgages grew sharply after 2002. The share of adjustable rate mortgages rose from a historic low of 12 percent in 2001 to 35 percent of all loans in 2004. This figure slipped to 30 percent in 2005.

The average 30-year fixed rate mortgage in September stood at 6.41%, an increase of 64 basis points since September of 2005. But the rate did climb as high as 6.76% and the shock to consumers' psyche hit home sales hard. Furthermore, when ARM and interest only rates are reset at higher rates, many homebuyers again will face significant increases to their monthly payments. In most cases, this will call for penny pinching by households. But in some cases this will push homeowners into foreclosure. The good news is banks are keenly aware of this problem and so will be quick to help owners restructure their loans to make payments. Banks and other lenders have learned from past downturns and realize that it is better to help homeowners pay their loans than for the bank to absorb the financial brunt of any mortgage defaults.

There is another new trend that bodes well for the housing market in this

## Employment and Default Rates, by Region

	12-month job gain	Unemployment rate (percent)		Default Rate		
		Aug 05	Aug 06	2nd Quarter 2005	2nd Quarter 2006	percent change
U.S.	2,237,000	4.9	4.6	4.30	4.37	0.07
Northeast	147,800	4.5	4.6	3.96	3.99	0.03
Midwest	334,600	5.0	4.9	4.93	5.08	0.15
South	938,100	4.9	4.6	5.03	5.18	0.15
West	512,500	5.0	4.5	2.44	2.48	0.04

Sources: Bureau of Labor Statistics, Mortgage Bankers Association

down cycle. Unlike past housing market downturns, this cycle is *not* accompanied by rising unemployment. In fact, employment growth continued as home sales fell. Over the last 12 months, more than two million household jobs were added to the U.S. economy.\* The unemployment rate fell in nearly every region across the country. Recently, employment growth has sputtered over the last few months (see page 2), but it is not expected to fall.

### Regional Developments and Default Activity

Because of the strong employment situation, the effects of rising mortgage rates on default rates have not been as strong as they could have been. In the Midwest and South, the figure has increased, but only mildly so. Default rates surged in both Louisiana and Mississippi (up 3.99 and 2.83 points, respectively, over the last 12 months) as a result of hurricanes Katrina and Rita, pushing the regional figure upward. In addition, Florida and Georgia, which hold large shares of loans in the region, both

experienced a mild increase in defaults. However, eleven states in the South experienced a decline in the default rate over this same period. The result has been a mild increase in the default rate for the entire South.

In the Midwest, rising mortgage rates have been concentrated in Michigan, Ohio, Wisconsin and Minnesota. Loans in Michigan and Ohio account for nearly a third of all loans in this region. Several states in the Midwest posted flat or slightly lower default rates (Nebraska's rate tumbled 0.88 basis points), but these improvements were not enough to offset the sharp increase in defaults in the northern Midwest. Large job losses in Michigan and Ohio have no doubt contributed to the rise in defaults.

Surprisingly, even with the extensive use of exotic loans in California and Nevada, the default rate in the West has only increased four basis points over the last 12 months. Loans in California account for almost 50 percent of the loans in the West. But falling default rates in a large proportion of the rest of that region including Arizona, Idaho, Montana,

\*The household employment data, which is cited in this article, is based on a survey of households about having a job. This figure differs from *payroll* data, which is derived from a survey of companies about the number of employees. Payroll data is cited in the Real Estate Monitor on page 2.

## Cooling Markets (continued)

New Mexico, Utah, Wyoming, Oregon, and Washington, helped to mitigate the impact of California's default activity.

Similarly, default rates in the Northeast have only risen three basis points over the last year. However, in the Northeast, nearly every state experienced an increase in default rates except in the loan heavy states of Pennsylvania and New Jersey. This trend helped to keep the default rate for the Northeast in check.

### **Toward the Future**

The strength of the U.S. labor market makes this housing market downturn unlike any other in recent memory. In those few areas where employment has been soft for several years or where it is softening, default rates will rise following the traditional pattern of a housing cycle downturn. However, default rates are also likely to continue to rise in those areas that have experienced the sharpest price appreciation over the last five years and which have seen the most extensive use of exotic loans. But this trend will be slow and drawn out as not all loans will reset to higher interest rates at the same time. Furthermore, in these areas strong employment trends and rising incomes will help to ameliorate the erosion of affordability caused by rising rates and banks will be more cooperative with lenders in all markets having learned valuable lessons from previous downturns.

There is no doubt that many local housing markets have become more fragile, but most remain healthy with little threat of falling employment or over-exposure to exotic loans. But it is clear that employment will play a crucial role in the U.S. housing market's soft landing.

For more information about your local market, visit [www.realtor.org/research](http://www.realtor.org/research).

# Mortgages: Do Your Homework

by NAR Staff

Homeownership is a major part of the American Dream. Homeowners realize that owning a home is a solid investment and their home “works for them” in terms of helping them build wealth. Currently, well over 72 million households own their own home and the U.S. has a homeownership rate of 69 percent.

For most consumers, purchasing a home is the largest financial investment they will ever make. Over 90 percent of homebuyers take out a mortgage in order to buy their property. During the real estate boom (2000-2005), mortgage rates were at historical lows. In fact, even today 30-year fixed mortgage rates are under seven percent.

But not all households opt for a traditional 30-year mortgage. Some are drawn to adjustable-rate mortgages or shorter-term loans (15-year mortgages). Because home prices in many housing markets are still at very high levels, some homebuyers are looking to specialty, nontraditional mortgages – including interest-only and negative amortization mortgages – in order to purchase a home. But some of these “nontraditional mortgages” can pose greater risk to households. NAR has developed several educational tools to help REALTORS® and consumers understand the differences among various loan instruments so consumers can make the best choice.

## Traditional Mortgages

For most consumers, the traditional fixed-rate mortgage and adjustable-rate mortgage (ARM) continue to be excellent options. The key choice for a fixed rate mortgage is how long the borrower will have to pay back the loan. The most common lengths of a fixed-rate loan are 15 and 30 years. Obviously, a shorter-

## Fixed-Rate Mortgage Scenarios

	15-Year Loan	30-Year Loan
Interest rate	5.5%	6%
Amount financed	\$200,000	\$200,000
Monthly payment	\$1,634	\$1,199
Loan balance after 5 years	\$150,578	\$186,109
Loan balance after 10 years	\$85,553	\$167,371

Source: NAR

term mortgage will give the consumer a lower interest rate but higher monthly payments. Adjustable-rate mortgages generally have a lower initial interest rate, but that rate may decrease or increase over the life of the loan. The size of monthly mortgage payments will fluctuate along with the rate. ARMs are probably most appropriate for consumers who have sufficient financial resources to handle potential payment increases or who plan to sell their home around the time the loan’s interest rate is set to change.

There are some potential risks with ARMs. Even small changes in interest rates could increase monthly payments significantly. For instance, if the interest rate increases from four to six percent, a household’s monthly mortgage payment could rise by as much as 50 percent.

## Specialty, Nontraditional Mortgages

The dramatic increase in home prices in many areas over the past several years has made housing affordability difficult for some households. Indeed, NAR’s housing affordability index consistently decreased over the past 3 years, from 130.7 in 2003 (its peak) to its current rate (as of August 2006) of 102.3. Consequently, more homebuyers are

using one of several new types of non-traditional mortgages that allow them to stretch their income in order to qualify for a larger loan.

Here are some examples of nontraditional mortgages:

**Interest-only loans.** With this type of mortgage, the monthly payment covers only the interest owed on the loan for the first five to 10 years of the loan. Until then, the borrower pays nothing to reduce the total amount of the “principal”.

**Option Payment ARM.** Borrowers with this type of mortgage can choose to make different types of monthly payments: a minimum payment that is less than the amount needed to cover the interest (which, of course, increases the amount of the loan); an interest-only payment; or payments calculated to pay off the loan over 30 or 15 years.

**40-Year Mortgages.** As would be expected, a borrower who takes out a 40-year loan pays it off over 40 years instead of the traditional 15 or 30. This type of mortgage reduces a homebuyer’s monthly payment – thus enabling some less credit-worthy homebuyers to afford a home. But the borrower pays off the loan much more slowly and pays much more interest.

\*NAR has produced a variety of educational tools to help REALTORS® teach their clients about various mortgage products available. Brochures on traditional mortgages and nontraditional mortgages are already available. Visit [www.realtor.org/housopp.nsf/pages/mortgages?OpenDocument](http://www.realtor.org/housopp.nsf/pages/mortgages?OpenDocument) for more information. In addition, NAR is preparing educational brochures on FHA mortgages and predatory lending, to be available soon at the same web site.

## Mortgages (continued)

### Potential Risks of Specialty, Nontraditional Mortgages

While these mortgage instruments have helped some households qualify to purchase a home, they do come with risks. Like “traditional” adjustable rate mortgages, some nontraditional mortgages begin with a low introductory interest rate or payment plan. But the monthly mortgage payments can increase significantly in the future. That means that borrowers will have to stretch their finances in order to keep their mortgage up to date. In addition, some of these loans require less stringent credit standards in order for a household to qualify, and may also come with higher interest rates or higher fees. In some cases, lenders will loan a borrower 100 percent or more of the home’s value. This could present big financial risks if the value of the home goes down.

Another risk of nontraditional mortgages is how the home equity builds up over time. With a traditional mortgage, as the borrower pays down the loan, the “worth” (or equity) of the home to the owner – the value of the home minus the amount left on the loan – increases over time. Indeed, this is how the majority of U.S. households build their household wealth. Those buyers who utilize some nontraditional mortgages build equity in their home much slower than with a traditional loan. In fact, under some nontraditional mortgages the amount borrowers owe on their home could increase over time, and so building up home equity only occurs if the value of the home increases.

#### NAR Efforts

NAR has been concerned about whether consumers fully understand nontraditional mortgages. REALTORS®

### Payment Shock

Here’s an example of how payment shock can occur with a non-traditional mortgage.

<b>Price of home:</b>	\$300,000
<b>Downpayment:</b>	10 percent
<b>Mortgage:</b>	5.75% interest-only adjustable rate
<b>Terms:</b>	Mortgage requires interest-only payments for 5 years, Interest adjusts every year thereafter, based on rates in effect
<b>Monthly payment for first 5 years:</b>	\$1,294
<b>Monthly payment after 5 years (with no interest-rate increase):</b>	\$1,699
<i>Payments increase because they begin to include principal in addition to interest</i>	
<b>Monthly payment after 5 years with 3% interest rate increase (to 8.75%):</b>	\$2,220

have been educating would-be homebuyers about traditional and nontraditional mortgages for quite some time. The Association strongly supports other efforts to educate consumers about non-traditional mortgages, and those efforts are bearing fruit. Guidance on non-traditional mortgages was issued recently by federal banking regulators will help ensure that federally insured banks inform consumers about the risks related to nontraditional financing options, including interest-only and option-payment adjustable rate mortgages. State regulators are considering similar requirements for other mortgage lenders. NAR supports the federal banking agencies’ new guidance requiring lenders to explain these mortgages and their associated risks to consumers. In addition to proposing that lenders educate consumers about the risks of nontraditional mortgages, the final guidance also recommends that lenders

review current underwriting standards and improve risk management strategies. While lauding consumer education efforts, NAR cautioned federal regulators in its submitted comments on the proposed guidelines not to restrict innovation in mortgage lending or, by extension, opportunities for homeownership.\*\*

#### Achieving the American Dream of Homeownership

Buying a home is a major decision for all households. From finding the right property to learning about the various loan options, households can rely on their real estate professional to help them make the largest financial decision they are likely to make in their lifetime. By educating their clients about the potential advantages and risks associated with various types of mortgages, real estate professionals can help their clients realize the American Dream of Homeownership.

\*\*You can read the recently issued guidelines on non-traditional mortgages at [www.occ.gov/ftp/release/2006-107a\(Guidance\).pdf](http://www.occ.gov/ftp/release/2006-107a(Guidance).pdf). To see NAR’s comments on the guidelines visit [www.realtor.org/fedistrk.nsf/files/nontradmort.pdf/\\$FILE/nontradmort.pdf](http://www.realtor.org/fedistrk.nsf/files/nontradmort.pdf/$FILE/nontradmort.pdf).

# Links to Statistical Data Series

To view the latest housing statistics from NAR, click on the links below.

## Existing Home Sales – Monthly series

- [August existing home sales and median sales prices](#) – single-family and condominiums/co-ops
- [Single-family home sales and median sales prices](#)
- [Condominium/co-op sales and median sales prices](#)
- The latest EHS statistics in spreadsheet format available [here](#)

## Existing Home Sales and Metropolitan Area Median Home Sales Prices – 2nd Quarter 2006

- 2nd Quarter 2006 [existing home sales by state](#)
- Existing home sales by state in [spreadsheet format](#)
- 2nd Quarter 2006 [Median Home Prices by Metropolitan Area](#)
  - [2nd Quarter Single-family median home prices](#)
  - 2nd Quarter Single-family median home prices in [spreadsheet format](#)
  - [2nd Quarter Condominium/Co-op median sales price](#)
  - 2nd Quarter Condominium/Co-op median sales price in [spreadsheet format](#)

## NAR's Pending Home Sales Index

- [August pending home sales index](#)
- The latest pending home sales index in spreadsheet format available [here](#)

## NAR's Housing Affordability Index

- [August HAI Index](#)
- August Housing Affordability Index in spreadsheet format available [here](#)
- Quarterly Housing Affordability Series
  - [2nd Quarter 2006 Affordability Index](#)
  - 2nd Quarter 2006 Affordability Index in spreadsheet format available [here](#)
  - [First-time homebuyer Affordability Index, 2nd Quarter 2006](#)
  - First-time homebuyer Affordability Index in spreadsheet format available [here](#)

Click [here](#) for more details about NAR's existing home sales, pending home sales, and housing affordability index series, including methodology, links to the latest news releases, statistical release schedule, and how to access historical information.

# REnew, REconnect, REenergize, and help REbuild New Orleans

The National Association of REALTORS® annual Conference and Trade Expo will be held in New Orleans, LA November 9-14, 2006. While you're there, don't forget to attend these valuable session from NAR's Research Divisions:

## **Housing and the Baby-Boomer: An Insightful Perspective**

Saturday, November 11, 11:00 a.m. – 12:30 p.m.

Baby-boomers have been a major economic force for the past several decades. Now the oldest baby-boomers are entering their 60s. Do baby-boomers believe housing is a good investment? Are today's real estate professionals providing the services boomers want? Join NAR's Vice President of Real Estate Research Robert Barr as he discusses key findings from **Baby Boomers and Real Estate**, providing insights on what boomers think about real estate.

## **Economic Issues and Residential Real Estate Business Trends Forum**

Friday, November 10, 9:00 a.m. – 11:00 a.m.

Get the latest forecast for housing and the economy from NAR Chief Economist David Lereah. And hear from Steve

Murray, editor of *RealTrends Magazine* on the impact of emerging trends on the residential real estate business.

## **Economic Issues and Commercial Business Trends Forum**

Friday, November 10, 1:00 p.m. – 3:00 p.m.

This three-part forum begins' with NAR Chief Economist David Lereah discussing the continuing hot pace of the commercial real estate sector. Then, James Fetgatter, chief executive of The Association of Foreign Investors in Real Estate (AFIRE) shares results of AFIRE's latest survey on foreign investment in U.S. commercial real estate. The program ends with a presentation by Jim Hochman, an expert on real estate law, who will address commissions in a tightening market.

Still not registered for the annual meeting? Visit [www.realtor.org](http://www.realtor.org) for details.

