Housing Decline: Only Halfway Home

When Reuters and CNBC.com announced the awful housing numbers from February, most observers were surprised. The housing market appeared to have found a bottom last fall, and many economists were expecting small but predictable improvements every month.

The Commerce Department, however, doused whatever positive expectations there were when they announced that new home sales for February compared to January declined by 16.9 percent (a record low) and average prices were the weakest in seven years. Year over year, new home sales dropped 28 percent. This was backed up by the announcement that housing starts recorded their biggest decline in 27 years. The median sales price for a new home also declined by a remarkable 13.9 percent, to $202,100, the lowest since December of 2003. To top it off, the supply of new homes on the market now represents nearly a 9-months' supply, up from 7.4 months in January. In simple terms, the housing market has just fallen off a cliff.

However, such numbers were not surprise as predictions of substantial further declines have appeared on this website here and here, as well as by the Economic Collapse Blog and by Gary Shilling.

The February numbers were simply an extension of the inevitable array of economic numbers illustrating reality in the housing market:

• U.S. housing prices have already fallen further during this recession than they did during the Great Depression

• Approximately 11 percent of all homes are standing empty

• Mortgage delinquencies and foreclosures reached record highs in 2010, and are expected to continue well into this year

• Unemployment numbers remain stubbornly high

• Some formerly great industrial or commercial cities are turning into ghost towns: in Dayton, Ohio, and New Orleans, Louisiana, for example, nearly one home in five is empty.

• Mortgages are more difficult to get

• The middle class is out of cash, unable to come up with the down payments required under the new loan qualification requirements

• Between two-thirds and three-quarters of all loans modified under the Obama administrations HAMP program are expected to go into default

• As housing prices drop further, more mortgage holders will find themselves underwater, and under increasing pressure to walk away.

• Less than half of working-age Americans hold a full-time job.

• Household formations, usually around 1½ million a year, are currently at about 500,000.

• More than 40 percent of 25-34 year olds are living with their parents

Shilling points out in his members-only newsletter that bank-owned real estate (REO) continues to climb as banks are forced to take back homes through walkaways and foreclosures. He says "A major share of the 7 million houses that have delinquent mortgages or are in some stage of foreclosure … will be dumped onto the market, adding to the already huge excessive inventory glut."

Shilling expects that housing prices will decline at least another 20 percent, which will take at least another 4 years before the housing market regains its footing. The impact of such further declines will be felt as federal government revenues continue to fall, thus increasing the deficit each year as government spending fails to be reined in by those who say they represent the Tea Party. All of this hastens the day when default on major federal entitlement programs will occur, either through large reductions in benefits, increases in taxes to pay for those benefits, or, most likely, defacto default through inflation of the currency and the resultant invisible reduction in the purchasing power of those promised benefits.

Even Shilling's estimate of another 20 percent decline in housing prices may be too conservative. He writes:

> Prices may well end up [all the way] back to their long-term trendline, but fall below [that trendline] in the meanwhile. Just as they way overshot the trend on the way up, [house prices] may do so on the way down, as is often the case in cycles.

It is difficult to uncover much in the way of optimism. The housing bubble was so vastly larger than most observers knew that it's going to take much lower prices and more time to get back to normal balance between supply and demand. The lesson to be learned is that government interference always and forever has its unintended consequences. The continued decline in the housing market, and the pain associated with such decline, is just one of them.