

STATE OF THE MARKET

## 2007: The Year in Housing

By [KELLY BENNETT](#) Voice Staff Writer

**Monday, Dec. 31, 2007** | Where 2006 launched with some optimists downplaying signs of trouble in the county's housing market, the tenor of real estate shifted to leave such voices in the minority by last New Year's Eve.

And then 2007 proved, from start to finish, a year of [slump](#).

Any first-quarter hopes of a turnaround sunk with the revelation in February that [subprime loans](#) were defaulting nationwide at a much higher rate than had been expected. Many [mortgage companies](#) and storefronts went broke, backing disappeared and fewer borrowers could refinance their loans with ballooning payments to avoid foreclosure. Then, the tightened mortgage financing climbed up the ladder to better-credit borrowers. California was especially hit by the tightening of jumbo loan financing in August -- funding dwindled for loans more than \$417,000.

At the same time, the number of homes on the market from individual sellers grew to near-record highs. Selling conditions weeded out many homeowners who didn't have to sell; some took their homes off the market to wait it out. With [foreclosures](#) and desperate homebuilders slashing prices on resale and new homes, individual sellers found making dramatic price reductions to be the only way to generate interest in their properties. [Cities](#), states and other government agencies that had counted on the revenue from development fees and property taxes found themselves swallowing a truth along with some over-zealous homebuyers: real estate doesn't always go up.

After the first three quarters of 2007, prices for detached homes in the county were more than 10 percent lower than they were at the peak in November 2005. Sales activity in the first 11 months of 2007 totaled 32,000 homes sold -- the lowest number for the period since 1995, and about half as many as sold in the same period in 2004. And among every hundred homes in the county, about three were hit by some stage of foreclosure between January and October.

Though the uncertainty of the [housing market](#) gave rise to a popular "how could we have seen this coming?" mindset, some economists found vindication in the market's trouble this year.

"The problem with the market is, prices got bid up to exceptionally high levels, and this is the back end of that," said Chris Thornberg, an economist with Beacon Economics, a California real estate research firm. "What we're seeing is a market in the painful throes of a downturn."

Conditions tied to the downturn are hardly unfamiliar for longtime San Diegans who've sustained other real estate cycles. But many economists and analysts found the conditions in 2007 to form a unique set of circumstances. Where the economy's health typically affects the housing market, this year, it was the other way around -- an unprecedented occurrence, some analysts said. Still, most predicted a bottom to the slump before the end of 2008.

Realtors and mortgage professionals and office assistants related to the real estate industry lost income, or their [jobs](#) entirely. People who'd avoided getting into the market in the first place, even those with six-figure incomes, saw 2007 as another year of wait-and-rent. Still, boosters touted the fact that interest rates were lower than they were in previous decades, and pointed to a large number of homes to choose from as reasons why it was a good time to buy.

### **'This Is Just Real Uncharted Territory'**

But the impact of the credit crunch and the persistence of weakness in the housing market without the same kind of deep recession the region saw in the 1990s leave most real estate analysts hesitant to issue a definitive prognosis. Government programs promising help to distressed homeowners have stipulations that leave out most of the troubled borrowers in Southern California. And the tighter regulations and dwindled backing for mortgages has restricted many would-be buyers from jumping in, even in these conditions.

"I think that basically, this snapshot in time -- it's a real period of unknown," said Gary London, a local real estate analyst with the London Group Realty Advisors. "We can speculate -- 'this was worse, that was worse' -- but this is just in real uncharted territory."

The median price of a home in San Diego County exploded by 210 percent between 2000 and 2005 and has since dropped about 10 percent. Some in the region whose fiscal gut told them to stay out of the overheated market cheer the price drops, looking forward to the day when [their incomes](#) match up more closely with the price of a house.

But many others saw the housing market as an appreciation train that would leave them behind if they didn't buy something, anything. Those who eschewed a traditional down payment and fixed-rate loan in favor of the 100 percent financed adjustable mortgages with teaser introductory payments find themselves trapped in houses that are worth less than they owe.

Those newer types of loans began to reset this year -- hitting the point where payments can double or triple -- and homeowners defaulted on their mortgages in droves, leaving the houses to the banks to auction or sell as repossessed properties. Some spots in the southeastern part of the city of San Diego, some [downtown](#) condo buildings and swaths of [Chula Vista](#) in particular, felt the pain of foreclosure acutely this year. Individual homes hit by some stage of foreclosure in the first 10 months of 2007 totaled 23,093 -- about three homes in every hundred in the county, according to RealtyTrac.

### **'They're in Competition for the Same Buyer'**

In 2007, buyers were scared, scarce or both. The number of homes sold each month hit decade lows, month after month. Where in the first 11 months of 2004, at the height of the real estate heyday, there were nearly 63,000 homes sold, the same period in 2007 saw just more than 32,000 homes sold. That was the fewest homes sold for that same period in any year since 1995, statistics from DataQuick Information Systems show.

"If you look at two houses for sale in the same neighborhood, they're in competition for the same buyer," said Mark Goldman, a local mortgage consultant and broker with Windsor Capital Mortgage Corp.

When sales activity picked up, it was usually due to an increase in the number of homes sold as repossessed properties or as [short sales](#), a negotiated deal where a seller found a buyer to pay a price for the home that was less than the initial mortgage amount.

And where there were buyers, they paid less for homes than they did last year. The Standard & Poor's/Case-Shiller home price index, which measures prices on repeat sales prices of the same detached homes over years, showed a 10.99 percent price reduction between the peak in November 2005 and September 2007, the most recent data available for that index as of Dec. 21.

Individual sellers faced price pressure from the ultra-motivated homebuilders with new inventory and lenders with [repossessed properties](#) to unload. Many homeowners pulled their listings off the market if they didn't find it absolutely necessary to sell. Real estate agents found themselves becoming more picky with the houses they would invest money to advertise -- if the [seller wasn't realistic](#) about the state of the current market, many agents passed on the listing.

"There was a lack of recognition on the part of sellers that in order to move product they'll have to lower prices," London said.

And the financing spigot that flowed easily to borrowers earlier this decade was tightened to a trickle due to investor unease, further winnowing the number of potential buyers. The hurdle applied not just to those poor-credit consumers usually painted as the face of the subprime debacle, but to just about everyone looking to buy a home in the second half of the year.

"Certainly, the credit crunch has bled well beyond subprime and is part of the new lending environment," London said. "The end of the stated-income era is definitely going to have an impact."

### **'There Are Fewer Builders Today Out There'**

By 2007, builders of new homes had drastically scaled back their operations, laid off workers and shelved some of the plans they'd made during the housing euphoria a few years ago. And this year, they continued to cut prices, hoping to lower their stock of unsold homes, said Peter Dennehy, vice president of Sullivan Group Real Estate Advisors, a local market research firm.

Many large homebuilders, including KB Homes and William Lyon Homes have closed San Diego offices, while others like Lennar and D.R. Horton have substantially reduced local staff, Dennehy said.

"What's different than, say, a year ago? Builders have reduced inventory," he said. "And there are fewer builders today out there than there were a year ago."

Where in the week of Dec. 17, 2006, there were 321 new home projects actively selling units, the week of Dec. 9, 2007 saw 284 such active projects. The rest have sold out or converted to rental units, Dennehy said.

In new homes especially, incentives like free granite countertops, cash for closing costs, trips to Tahiti and new cars -- mixed with lower prices -- are starting to lure some sidelined buyers to the table, Dennehy said. And builders of some projects are considering "mothballing" -- finishing part of a development but waiting to start building the rest until the market improves, potentially in late 2008, Dennehy predicted. And that means the days of incentive-laden homes are numbered, he said.

"What I'm hearing from people is that they're starting to see signs of life," he said. "The transaction volume

will at least pick up and start moving somewhat. ... Builders will bring some projects back to market in 2009, but (then) it'll be, 'If you want granite, you pay for it.'"

### **'We're Going to Feel Like We're in the Bottom'**

A December report from Moody's [Economy.com](#) labeled the peak for San Diego's housing market the first quarter of 2006, and predicted the trough in fourth quarter 2008. By then, the group predicted, the region's home prices will have fallen by 14.1 percent from the peak, as measured by the Case-Shiller index.

"I think 2008's going to be another tough year," Dennehy said. "I think a lot of people believe that this will be the year that the elusive bottom is reached."

London echoed: "Probably in 2008, we're going to feel like we're in the bottom of the market."

Still, the health of the greater economy plants a giant [question mark](#) at the end of the most confident predictions.

"As far as I can tell, we're in an unprecedented situation," said Alan Gin in remarks to an industry group at the University of San Diego in mid-December. "Typically, the economy influences housing. But for the first time, that situation will be reversed. ... The concern that people have is that the weakness in housing is going to spread to other parts of the economy."

The economy weakened further this year with the disappearance of the wealth effect -- the tendency of American homeowners to tap into their newfound equity and draw out cash for home improvements, cars, trips and other big-ticket items.

"We won't really see the direction of the economy until we're a few months into the year," Dennehy said. "You have to believe that at some point this housing crisis will work itself out. Even if they go ahead and sell all of the foreclosures for cents on the dollar, that would be better than talking about them all the time."

For an industry that grew in workforce as rapidly as housing prices bounded up this decade, real estate has some adjusting to do, said local market consultant Dan Holbrook. He recently switched his business from focusing mostly on making mortgages to negotiating short sales and bank-owned deals. And he's picked up coaching real estate professionals on how best to weather the market.

"We, in order to get through this, need to get creative," he said. "The distressed market is the market. And I'm focused on the distress. I'm almost a distressed real estate evangelist."

But residents in many county neighborhoods don't need to be told about the distress in the market. They can see the real estate signs in their neighbors' yards, the colors faded by the sun. And they can see the property lines in the grass -- brown, dead grass on foreclosed properties juxtaposed with the green in the yard of another homeowner just trying to hold on.

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