A Win-Win Situation

by Lawrence Yun, *NAR Chief Economist*

The recently passed – and signed – housing stimulus bill means a housing recovery is on its way. This legislation will go a long way to help stabilize the housing market and make the dream of homeownership more attainable for many Americans. In addition, more families will be able to refinance into safer, more affordable mortgages, in many cases helping those households avoid a devastating foreclosure.

There are many facets to the recently enacted law. The one that I am most excited about is the home buyer tax credit. Up to $7,500 will be given to first-time purchasers as they file their income tax returns. The amount will be phased out above a certain income level and is to be no more than 10 percent of the home purchase price – though first-time buyers will qualify for the full amount. (see page 8 for more details.) This is in fact almost like a "credit" – the amount is equivalent to cash on tax returns. For example: you do your normal tax return and find that you owe $1,000 next year. You then apply the $7,500 credit and the government will send you a tax refund check for $6,500.

The first-time home buyer tax credit – part of the recently enacted Housing Stimulus Bill – will likely have a big impact in getting the housing market moving again.

Yes, it's not all candy and roses. This credit has a time window and will not be available after July 2, 2009. And technically it is not a full credit because households will have to pay back this amount over a 15 year time period after the second year. In addition, the payback provisions have many conditions. (NAR Research will continue to analyze those.) But the worst-case scenario is that households would need to pay back the $7,500 over a 15 year time span beginning in 2010. In the case of the 2010 tax filing, taxpayers who took advantage of this home buyer credit would need to pay $500.

Even in this worst-case scenario, the tax credit is still a huge benefit to home buyers. Here's why. Money loses value over time – today's dollar is worth more than tomorrow's and certainly far more than it will be worth 15 years from now. That is due to inflation and the loss of interest income one could gain by squirreling it away. For instance, a winning strategy for the smart consumer would be to pay off a high-interest credit card debt with the tax credit money.

In addition, the tax credit it will likely have a big impact in getting the housing market moving again and so will contribute to lessening the foreclosure pressure. As foreclosures retreat, fewer need to be written down by banks and other lenders. Credit markets strengthen and mortgage capital flows more freely. The availability of loans grows, meaning more mortgages on more home sales. Increased home sales tend to foster improving home prices. Homeowners across the country will benefit as home prices strengthen. The economy will also improve - with higher aggregate income for U.S. workers and a lower unemployment rate. Basically, it's win-win.

I estimate nearly 3 million home buyers will have taken advantage of this benefit by the time the tax credit expires next year. These first-time buyers will also stimulate sales for trade-up, trade-down purchasers as they will be able to sell their homes.

The timing for all this is good, as the housing market is already poised to make a bit of a turnaround. Yes, on a national basis existing home sales fell in June to their lowest level in 10 years (4.86 million units, seasonally adjusted annualized rate). But even so, the pace is not too far off the 5 million sales mark. Furthermore, pending home sales rose in June, pointing to more closings in the months ahead. In addition, there were significant local market variations. Sales have continued to ramp up in markets where prices have come down by 20 percent to 30 percent. Bargain hunters and first-time home buyers who had been priced-out during the boom years have returned to the market. Sales are rising strongly on a year-over-year basis in a number of markets: Ft. Myers FL, Las Vegas NV, Riverside CA, Sacramento CA and Prince William County, VA. Other markets beginning to experience rising sales include Orlando, Phoenix, and Oakland.

I am also hopeful that home prices will soon begin to stabilize. The latest data on prices showed a mild deceleration from the recent past. The national median existing home price in June was $215,100, which is a decline of 6.1 percent from one year ago. The declines in the four previous months had been -8.4 percent, -8.0 percent, -8.5 percent, and -6.6 percent. Regionally, the price decline was the sharpest in the West region, falling 17.2 percent – this also explains the overall sales increase in that region. Prices declined 12.6 percent in the Northeast and 2.4 percent in the South. The median price actually rose in the Midwest by 2.8 percent. The speedy price declines of 20% to 30% in a short 12 to 18 month-span in some of the hard-hit markets have been very painful for homeowners who bought during the peak years. But the price declines and the recent rising sales in these regions suggest most of the price declines may have already occurred.

Overall, the market is ready to start recovering. The tax credit should prove to be a big shot in the arm for first-time buyers. In addition to the tax credit, the stimulus package permanently raises the loan limits for FHA and GSE loans, thereby saving consumers thousands of dollars in mortgage interest costs. NAR, of course, has been working diligently for years for some of the provisions in the Housing Stimulus Package – all that hard work has paid off and both home buyers and sellers will benefit.

The Forecast

by Lawrence Yun, *NAR Chief Economist*

As we know from the REALTOR® mantra - location, location, and finally, location – matters a lot. Contract signings to buy homes (i.e., pending sales) rose significantly in Sacramento, Riverside, Las Vegas, Orlando, and other markets that experienced significant price reductions. This has been evident for the past several months. What *is* new is that we are now beginning to see year-over-year increases in affordable mid-America markets. Columbus, Oklahoma City, Colorado Springs, Charleston (WV), and Spartanburg are examples. Pending sales increases appear to be broadening.

On the opposite end, pending sales have weakened sharply from a year ago in the Pacific Northwest and Texas. These areas have the strongest employment conditions in the country. Dallas, for example, has gained 57,800 net new jobs in the past 12 months - essentially a stadium full of people with new jobs. Yet, pending sales are trending low in Dallas. Because of the strength of the job market, many homes in both Texas and the Pacific Northwest have not experienced price declines.

As with any monthly data, there will be bounces and noises in the statistical measurement. I am encouraged by the rise, particularly in the hard hit areas, but several more additional months of similar gains would be needed to assure that a firm recovery is taking place. I am also encouraged by some cases of multiple-bidding in San Diego and other markets where prices have plunged from just one year ago. The multi-bidding suggests that there are buyers out there and that we may be hitting a price floor in these markets.

The near-term outlook is for gains in actual closings at the settlement table. The housing stimulus package that was recently enacted will also be a factor in helping to raise sales and carry the momentum into 2009. Many home buyers will want to take advantage of the home buyer tax credit. Consumers who have been facing outrageously high interest rates on "jumbo" loans will also get a break because of the permanently higher loan limits for FHA and Fannie/Freddie backed mortgages.

But before celebrating too early, we should be mindful of the fact that the pending home sales data coverage is less robust than the closings measured in the existing-home sales figures. So the trend in closings may not show a direct one-to-one relationship to pending sales. Furthermore, with lenders scrutinizing every mortgage origination, some of the contracts may fall out at the last moment.

The housing stimulus package that was recently enacted will be a major factor in helping to increase home sales and carry that momentum into 2009.

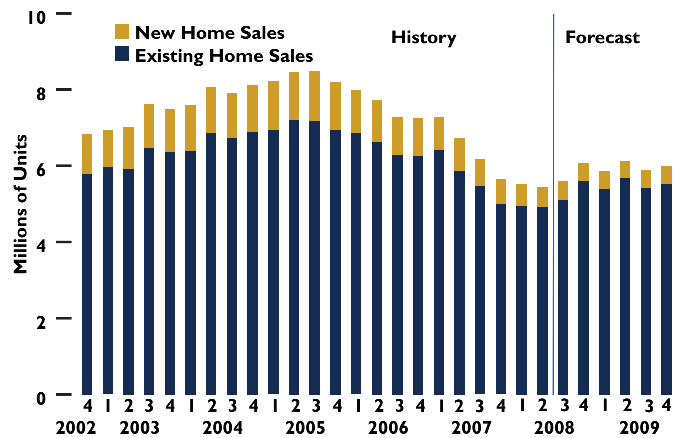
The longer-term forecast also contains many uncertainties. Despite some growth in economic output as measured by GDP, the job market is unusually soft. Recent stock market gains could be genuine signs for better economic times ahead or could simply be a "head-fake" for stock traders who love volatility. Mortgage rates are still at near historically favorable terms, but that could change for the better or worse depending upon how stubbornly inflation stays elevated. Another thing to watch for is foreigners' appetite for U.S. government and Fannie/Freddie bonds. Then there's oil – these days, always a wildcard. If the price of oil slides to less than $100 a barrel, then it is likely the U.S. economy would growth much faster.

As for the housing market forecast, I would say that given the unprecedented speedy price declines in those hard-hit markets, most of the price cuts have already occurred. There is better upside potential than down from this point onwards. Though the national home price forecast is important for lenders and other macro players as they need to evaluate the overall national portfolio, it means very little to consumers. With so much variation, consumers need to do their local homework – and so do local REALTORS® – to assess what may happen in their market.

Unfortunately, there is a downside for this forecast for homebuilders. They will need to cut back further on production, as it will take some time to absorb the still-high inventory of both new and existing homes. And an important note: yes, both housing starts and permits rose significantly in June – total starts were up 9.1 percent from May and permits rose by 11.6 percent. But a big part of those increases was in the Northeast multifamily sector, most likely due to an unusually large number of permits issued for multifamily residential buildings in New York City – the result of new construction codes in the city effective July 1 of this year. If we discount the Northeast multifamily figures, permits were actually down 0.7 percent and starts decreased 4.0 percent. Housing starts are likely to decline through the middle of next year and then settle at around 800,000 units (compared to over 2 million during the boom years). Consequently, I anticipate further declines in new construction and new home sales into 2009.

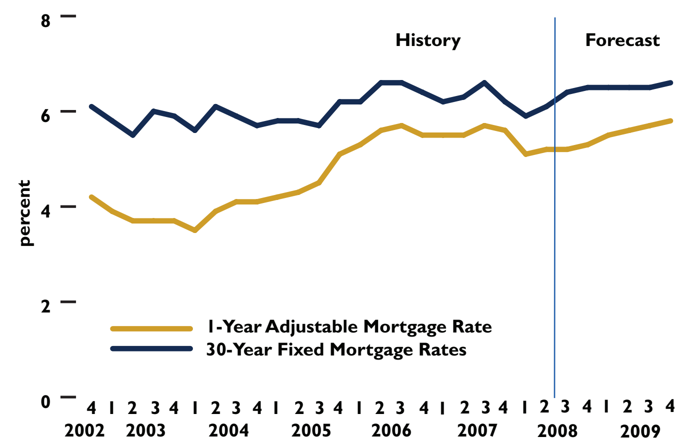
For existing-home sales, I am more optimistic. Resales will likely rise in coming months, as the impact of the recently signed housing legislation is felt.

Home Sales
Housing stimulus package jump starts recovery



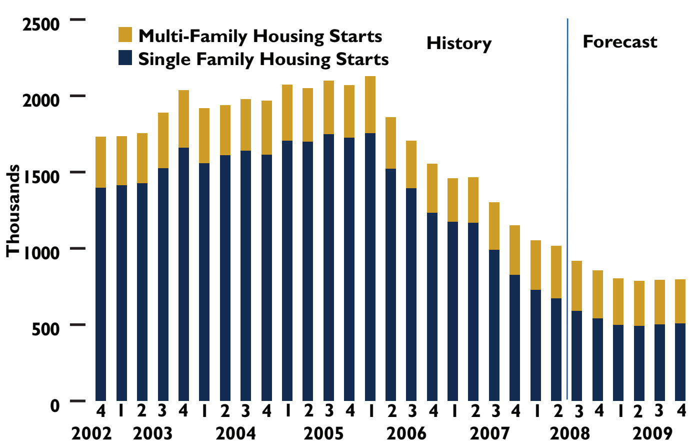
Sources: NAR, Bureau of the Census, NAR Forecast

Mortgage Rates
Inching up as housing activity recovers



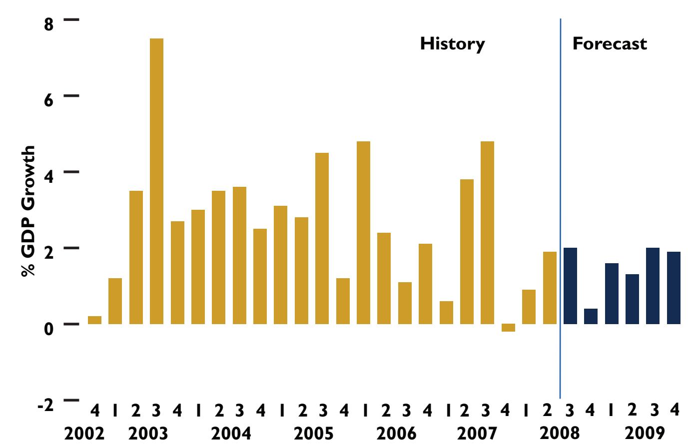
Sources: Freddie Mac, NAR Forecast

Housing Starts
Decreasing due to rising construction costs and high inventory



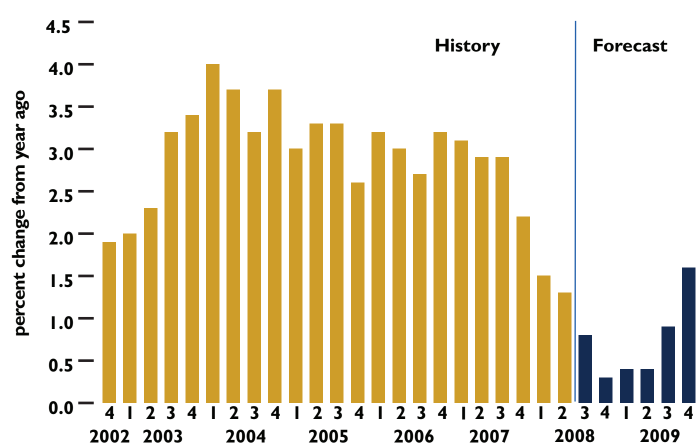
Sources: Bureau of the Census, NAR Forecast

Economic Growth
Avoiding recession despite "bad news" from media



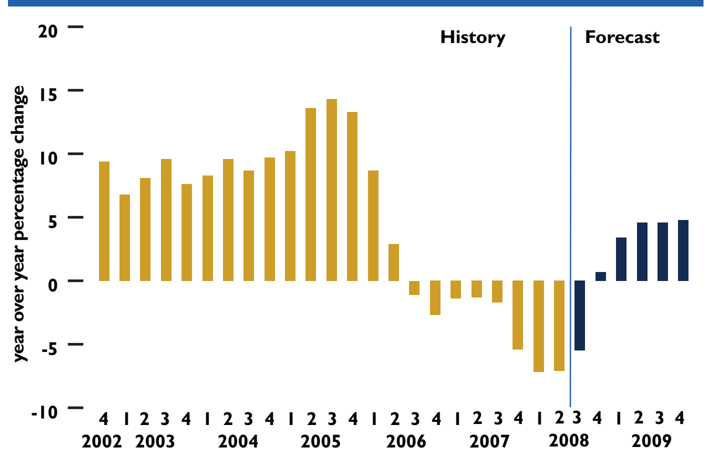
Sources: Bureau of Economic Analysis, NAR Forecast

Consumer Spending
As housing recovery takes hold, spending will increase



Source: Bureau of Economic Analysis, NAR Forecast

Home Price Growth
Price appreciation turning positive



Sources: NAR, NAR forecast

U.S. Economic Outlook
August 2008

	2007			2008				2009			2006	2007	2008	2009
	III	IV	I	II	III	IV	I	II	III	IV				
U.S. Economy														
Annual Growth Rate														
Real GDP	4.8	-0.2	0.9	1.9	2.0	0.4	1.6	1.3	2.0	1.9	2.8	2.0	1.7	1.5
Nonfarm Payroll Employment	0.8	0.8	-0.3	-0.6	-0.4	0.0	0.3	0.4	1.0	0.8	1.8	1.1	0.1	0.2
Consumer Prices	2.8	5.0	4.3	5.0	3.3	2.1	1.9	2.3	3.7	2.2	3.2	2.9	4.1	2.6
Real Disposable Income	3.1	0.6	-0.1	11.3	-5.0	-1.2	3.2	1.8	1.0	1.3	3.5	2.8	1.7	1.1
Consumer Confidence	106	91	77	57	54	60	65	72	75	75	106	103	62	72
Percent Unemployment	4.7	4.8	4.9	5.3	5.7	5.9	6.0	6.0	6.0	6.0	4.6	4.6	5.5	6.0
Interest Rates, Percent														
Fed Funds Rate	5.1	4.5	3.2	2.1	2.0	2.1	2.5	3.0	3.5	3.5	5.0	5.0	2.3	3.1
3-Month T-Bill Rate	4.3	3.4	2.0	1.6	1.9	2.1	2.8	3.2	3.5	3.6	4.7	4.4	1.9	3.3
Prime Rate	8.2	7.5	6.2	5.1	5.0	5.1	5.5	6.0	6.5	6.5	8.0	8.1	5.3	6.1
Corporate Aaa Bond Yield	5.8	5.5	5.5	5.6	5.8	5.9	6.1	6.1	6.0	6.0	5.6	5.6	5.7	6.0
10-Year Government Bond	4.7	4.3	3.7	3.9	4.1	4.2	4.5	4.5	4.5	4.5	4.8	4.6	4.0	4.5
30-Year Government Bond	4.9	4.6	4.4	4.6	4.5	4.6	4.9	4.9	4.9	4.9	4.9	4.8	4.5	4.9
Mortgage Rates, percent														
30-Year Fixed Rate	6.6	6.2	5.9	6.1	6.4	6.5	6.5	6.5	6.5	6.6	6.4	6.3	6.2	6.5
1-Year Adjustable	5.7	5.6	5.1	5.2	5.2	5.3	5.5	5.6	5.7	5.8	5.5	5.5	5.2	5.7
Housing Indicators														
Thousands														
Existing Home Sales*	5,457	4,997	4,953	4,913	5,108	5,597	5,399	5,675	5,414	5,513	6,478	5652	5148	5,506
New Single-Family Sales	731	651	561	535	489	464	458	455	468	476	1,051	775	509	464
Housing Starts	1,298	1,151	1,053	1,016	917	855	805	785	793	798	1,801	1,355	960	795
Single-Family Units	986	826	728	670	590	540	497	489	500	507	1,465	1,046	632	498
Multifamily Units	311	325	325	345	327	315	308	296	293	291	336	309	328	297
Residential Construction**	445	412	383	367	362	346	333	325	323	325	553	454	365	326
Percent Change – Year Ago														
Existing Home Sales	-13.8	-20.7	-22.2	-16.3	-6.4	12.0	9.0	15.5	6.0	-1.5	-8.5	-12.8	-8.9	7.0
New Single-Family Sales	-27.3	-33.6	-33.1	-37.2	-33.1	-28.7	-18.4	-14.9	-4.4	2.6	-18.1	-26.3	-34.3	-8.8
Housing Starts	-23.8	-26.7	-27.5	-30.4	-29.4	-25.8	-23.5	-22.7	-13.5	-6.6	-12.9	-24.8	-29.2	-17.2
Single-Family Units	-29.1	-33.9	-37.4	-42.2	-40.2	-34.7	-31.7	-27.0	-15.1	-6.1	-14.6	-28.6	-39.6	-21.1
Multifamily Units	-0.1	1.7	12.2	15.0	5.1	-3.2	-5.3	-14.3	-10.5	-7.4	-4.5	-8.0	6.2	-9.5
Residential Construction	-17.0	-19.0	-21.3	-22.2	-18.7	-15.9	-13.1	-11.5	-10.8	-6.2	-4.6	-17.9	-19.7	-10.5
Median Home Prices														
Thousands of Dollars														
Existing Home Prices	221.2	207.5	198.5	208.1	209.0	209.0	205.2	217.7	218.6	219.0	221.9	218.9	206.7	215.8
New Home Prices	241.0	237.0	235.7	234.0	243.9	244.6	247.2	246.2	258.5	258.8	246.5	247.2	239.8	253.0
Percent Change -- Year Ago														
Existing Home Prices	-1.7	-5.4	-7.2	-7.1	-5.5	0.7	3.4	4.6	4.6	4.8	1.0	-1.4	-5.6	4.4
New Home Prices	2.0	-3.3	-7.9	-2.9	1.2	3.2	4.9	5.2	6.0	5.8	2.3	0.3	-3.0	5.5
Housing Affordability Index	109	121	132	125	120	120	123	117	118	117	106	112	125	117

Quarterly figures are seasonally adjusted annual rates.
* Existing home sales of single-family homes and condo/co-ops; ** billion dollars

First-time Home Buyers Get a "Break."

by Danielle Hale, *Research Economist*

On July 30 of this year, President Bush signed the Housing and Economic Recovery Act of 2008. One of the provisions of this law creates a new, temporary tax credit as an incentive for first-time home buyers. In his commentary (see page 4), NAR Chief Economist Lawrence Yun discussed some of the broader impacts of this provision. This article examines more of the details of the first-time home buyer tax credit.

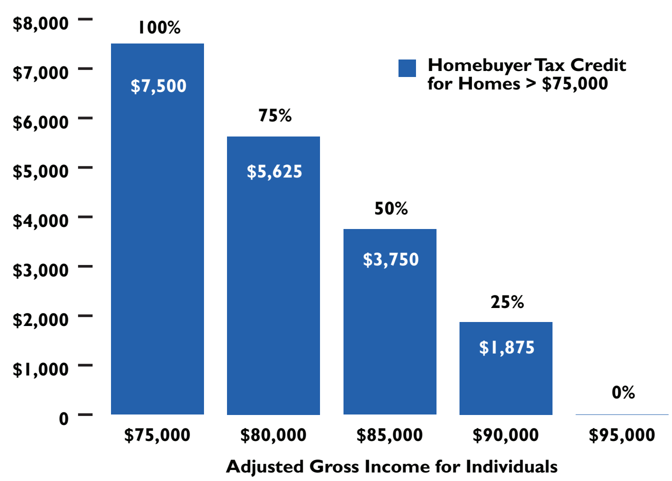
Buy a home and get a tax break! As part of the Housing and Economic Recovery Act of 2008, a first-time home buyer tax credit is now available. That is good news – both for those first-time buyers who have been "on the fence" waiting to purchase a home, as well as for REALTORS® who can help put those buyers into homes.

Who is Eligible?

First-time home buyers who purchase(d) a principal residence on or after April 9, 2008 and before July 1, 2009 are eligible for the credit. A first-time home buyer is defined as an individual who has not had an ownership interest in a principal residence in the three-year period before the date of home purchase, and someone who has never taken advantage of the first-time home buyer credit available to residents of Washington, D.C. (see below). In the case of married couples, both must be first-time buyers.

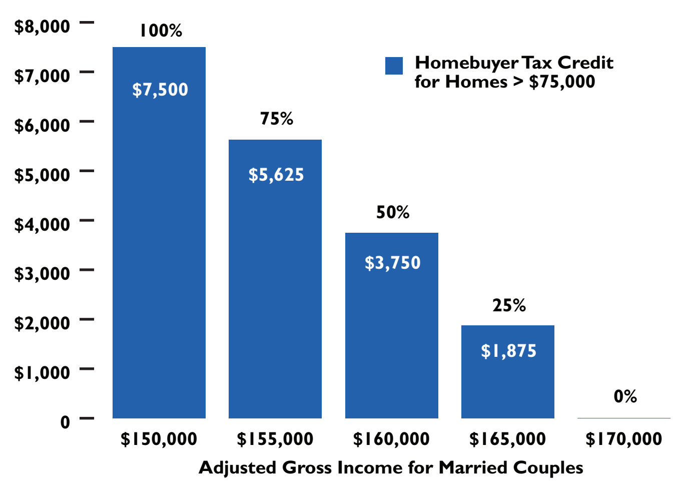
For other groups purchasing a home, the statute is less clear. Take a couple who is planning to be married in 2009. The bride-to-be and her fiancé purchased a home on June 1, 2008. She previously owned a home in 2006 while her fiancé has never owned one. The bride will not qualify for the tax credit for the 2008 purchase because she owned a home after June 1, 2005 (three years before the date of the couple's purchase). But, since both were single when they purchased the home, *the groom* may qualify for the credit. He may be eligible because both of them will file tax returns as Single for 2008. (If they married in

First-time Homebuyer Credit Phase Out for Individuals



Percentages indicate the remaining part of credit available at the given AGI

First-time Homebuyer Credit Phase Out for Married Couples



Percentages indicate the remaining part of credit available at the given AGI

First-time Home Buyers Get a "Break." (continued)

2008, neither would be eligible). When purchasers file a joint tax return, *both must be first-time buyers*.

Obviously there are other types of households, and in some of these cases the statute could be somewhat ambiguous. As for any major financial investment, purchasers should consult a tax advisor.

Income restrictions

There are some income restrictions with this program. Those restrictions are based on the tax filing status the purchaser claims when filing his/her income tax return. The maximum income for individuals filing as "Single" (or "Head of Household") is $95,000; individuals filing a joint return may have income of no more than $170,000.

How does it work?

The credit directly reduces the total amount of taxes owed and is refundable. When the buyer files his/her taxes, for the year he or she purchased the home (2008 or 2009), the taxpayer will be able to subtract the amount of the credit from his/her Federal income tax liability, increasing their refund or reducing the amount owed.

The amount of the credit is based on the price of the home being purchased. The tax credit is equal to 10 percent of the purchase price of the home up to $7,500. The full credit is available for single buyers whose adjusted gross income is less than $75,000. If the buyer's adjusted gross income is greater than $75,000 and his/her home purchase qualifies the buyers for the full credit, the credit phases out. For married couples filing jointly, the credit begins to phase out at an adjusted gross income of $150,000 (for details, see charts).

The tax credit is not completely free money for buyers to keep. It has a payback provision that makes it similar to an interest free-loan. Two years after the credit is claimed, buyers will have to begin repaying that "loan" so that the credit is paid back in full over the course of 15 years. For first time buyers who qualify for the full credit, the payback amount is $500 per year. Those getting less than the full credit pay equally over the 15 years (which is a rate of 6.67% per year).

If a qualifying home is resold before the credit is repaid, the seller will have to immediately pay the outstanding balance of the credit. If the home is sold at a loss, then nothing more is owed.

Other eligibility conditions

A home buyer tax credit has been available for first-time buyers in Washington, D.C. for many years. But buyers cannot claim both the DC and the national first-time home buyer tax credit. In addition, purchases by non-resident aliens and purchases financed by proceeds from a qualified mortgage issue are not eligible. Home purchases between relatives and other gifts of residences are not eligible for the credit. Also, the credit is good only for a principal residence located in the United States. This includes single-family detached housing, condos or coops, townhouses or any similar type of new or existing dwelling.

Ceteris Paribus

Even with the above exclusionary factors, first-time buyers purchasing a home will reap the other benefits of homeownership. They will be able to deduct their mortgage interest payments on their taxes, as well as their property taxes. In addition, when they sell that home, those owners will be entitled to the capital gains tax exclusion. And of course, these first-time buyers will at last be able to feel the pride and security of owning their own home.

For more information

Buying a first home is a big step. And first-time home buyers have historically accounted for around 40 percent of all home purchases in any given year. But the downturn in the housing market, the credit crisis, a soft job market, and slowing economy have placed many of these first-time buyers "on the fence" -- waiting for the right encouragement to make that important decision to purchase a home. REALTORS® are experienced in dealing with first-time home buyers. Knowing about the first-time home buyer tax credit and how it works can help REALTORS® serve those first-time clients even better.

*NAR has a variety of information available on the First-time Homebuyer Tax Credit. For further details, visit **www.realtor.org**. A brochure for REALTORS® to share with their clients interested in the provisions of the tax credit will be available in late summer. For more information about the brochure, contact Thomas Doyle at tdoyle@realtors.org.

