

# Mortgage Experts: BETTER DAYS AHEAD, GROWTH WILL BE SLOW

BY TERRY WARD



Midlands mortgage and real estate professionals are hoping that an increase in the number of property transactions in the second half of 2009 is an indicator that the real estate market is getting its heart-beat back to pace a strong 2010.

“October was a good month for the housing market in South Carolina. With a 17 percent increase in total sales from October of last year, this is the largest monthly increase in activity we have reported this year.” said Jay Rinehart, president of South Carolina Realtors. He said that the (federal) first-time home buyer tax credit has had a significant impact on recent sales.

Rinehart is not the only one who is hopeful that things are thawing in an industry that influences the fiscal health of businesses ranging from large appliances to personal wealth. But there is still a ways to go.

Mary Winter Teaster, is the principal, managing director and Broker-In-Charge of Columbia’s CB Richard Ellis Brokerage. She offers a detailed insight into what has happened recently that signals better days ahead.

“The month of November showed the first real signs of pending recovery and potential optimism on the part of banks,” said Teaster, “On the national scale, two significant transactions occurred in the fourth quarter (of 2009). First was the successful CMBS (commercial mortgage backed securities) offered by Developers Diversified Realty. It was evidence that REITs (Real Estate Investment Trusts) were able to refinance. This was the first of these in over 18 months. Second was General Growth Properties’ restructuring of \$8.9 billion of mortgage debt. General Growth is a huge mall REIT; it sought bankruptcy protection in April. The (move by General Growth Properties) is viewed as a significant step toward their strategy to emerge out of bankruptcy in full by June of this year. Both these instances indicate the credit market is opening up and refinancing is a reality.”

Teaster also said there are signs that more business people, and customers, are ready to get back into the game. “Another bright spot is shopping center REITs reported increased leasing activity in the third quarter and may be showing signs of stabilization,” said Teaster. “Vacated retail ‘big box’ space on a national and regional scale is being leased and that is a result of retailers’ predictions that consumers and shoppers are starting to spend.”

While there are indications that the worst may be over, recovery could be slow. According to a report written by Joseph C. Von Nessen, Ph.D., of the University of South Carolina’s Moore School of Business, which stated that, “the recession is most likely over. Most economic indicators suggest that we are now in a period of economic growth.”

But Nessen’s report, that was published by the SC Association of Realtors warns of trouble spots in other areas of the real estate industry.

“The banking industry is just beginning to absorb the losses from defaulting commercial real estate loans, which will make future loans of all kinds harder to acquire,” it states. “Thus, despite the fact that the residential real estate market is showing signs of recovery, the recovery will be slow because of the increased difficulty for the home-building industry to obtain loans.”

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In his report, Nessen also addressed other economic factors that could influence real estate in South Carolina stating that, “The high U.S. and South Carolina unemployment rate is expected to persist for the remainder of 2009 and into 2010. Nevertheless, this is not an indication of a deteriorating overall economy. High unemployment generally lingers through the initial stages of economic recovery and is usually one of the last signs of recovery from a recession.”

The report also stated: “Additional foreclosures and increased housing vacancy rates are likely to accompany high unemployment. This will lead to additional inventory and reduced housing prices at the national level. South Carolina, however, has experienced house price appreciation throughout 2009, an increase in permit activity, and only small increases in foreclosure rates. These facts suggest not only that South Carolina is a relatively stable housing market, but also that much of the excess inventory has been eliminated. In turn, South Carolina will be spared from some of the national consequences of additional foreclosures.”

Data supports Nessen’s assessment. Home sales in Greater Columbia rose about 21 percent in October 2009 compared to October 2008, according to the SC Association of Realtors. It was the first increase from a comparable month of a previous year in several quarters and coincided with an \$8,000 federal tax credit for first-time homebuyers. The current increase in home sales follows a period that has seen a decrease in the median price of homes in the Midlands. But the median price for a home in the Greater Co-

lumbia area in October was \$144,000. That number shows stabilization. It is the same median price for a home in October 2008.

The trend of stabilizing prices or affordability of home prices is being marketed as an impetus to buy by national industry associations. Affordability conditions remain historically high, said Charles McMillan, National Association of Realtors president. McMillan is a residential broker based in the Dallas-Fort Worth, Texas area.

“Potential first-time buyers can take heart in that affordability conditions this year are the highest on record dating back to 1970,” he said.

Riding a wave of increased activity in the real estate market, a new wave of tax credits has been implemented. Those incentives will hopefully aid in continued recovery in the real estate and mortgage markets. The new legislation allows for an extension of the \$8,000 tax credit for first-time buyers, the same as the tax break offered in the second half of 2009. But there is also a \$6,500 tax credit for buyers who already own their home. Both tax credits have limits placed on the amount of income home buyers earn. For first-time buyers those limits are: \$75,000 for single taxpayers and \$150,000 for married taxpayers filing joint returns. For existing homeowners the limits are: \$125,000 for single taxpayers; and the limit is \$225,000 for married taxpayers filing a joint return. Existing homebuyers must have been in their existing residence for five of eight years to take advantage of the tax break.

If loaning money for homes to borrowers who may have not had adequate

ability to repay the money was a part of the problem that helped cause the real estate sales decline, it may not have been the only one. In some cases, houses were appraised at rapidly increasing values. But in a matter of 24 months, the value of some of those properties decreased at an alarming rate. For home values to appreciate at such steep rates, the practices of some appraisers have been called into question. It was a national problem. To help stem the problem of unrealistic appraisals, the Home Valuation Code of Conduct. HVCC, which went into effect on May 1, 2009, has been implemented. The HVCC intends to stop collusion between lending institutions and appraisers and mandates that individual banks and mortgage brokers who sell conventional loans in the secondary market to Fannie Mae and Freddie Mac cannot personally select their own appraisers as they were allowed to do in the past. Now brokers are required to let an appraisal management company choose an appraiser from a pool of appraisers. Experts say the HVCC can result in low appraisals of homes because alien appraisers are not likely to be familiar with the nuances that make neighborhoods appealing, which adds to their value.

Al Edens, owner of Columbia’s Edens and White Mortgage, Inc. does not like the new HVCC and said it leads to appraisers who are not familiar with local properties determining values.

“It is not a productive practice,” he said.

Teaster says other government involvement in the banking business is having mixed results.

“The first attempt of government stimulus funds (TARP) fell far short of its intended goal. In a ‘Catch 22’ scenario, banks found themselves being zealously regulated by the OCC (Office of the Comptroller of the Currency) via increased required downgrading, or de-classification of loans in their portfolio,” she said. “Those downgrades require increased funding of larger cash reserves on the part of the bank, depleting the same funds the government was sending the bank’s way to alleviate borrower’s needs. The double whammy was the announced plans by the FDIC to ask for 3 years insurance premiums to be paid in advance. Again, the same pool of cash in reserve is being depleted by another government agency,” she said.

Teaster went on to explain how legislation has influenced the mortgage business. “Considering some banking institutions saw their premiums increase as much as three to five times in a single year - 2007 to 2008 -

the impact was total depletion of banks availability of funds to lend. Not surprising, but a continuing burden to the lenders and borrowers is the fact that these two government regulatory divisions are not communicating in any form or fashion with each other, a problem that must be rectified for future recovery and rebound to occur.”

Teaster said decreasing property values are another issue that is adding to the complexity of the situation. “The second stimulus fund (TALF) is beginning to roll out, but in an environment of continued decreasing values of commercial properties, the challenge is evident,” she says. “If a performing borrower (credit worthy and maintaining payments as agreed) has an upcoming loan renewal pending, the property may need to be re-appraised and that decreased appraised value may dictate a capital reduction, i.e. additional cash down payment in an amount that is simply unexpected, unplanned and unattainable for the borrower. Thus, a performing, stable borrower is penalized for items beyond his control and may become unable to perform under new terms. Lenders simply do not know how to underwrite in this environment.”

As far as the extended future of the lending and real estate industry, Teaster sees reason for optimism in some markets, but caution and slower going elsewhere.

“On a local basis, the third quarter (of 2009) showed an up-tick in the way of executed leases, accepted contracts and sales transactions on retail and office properties primarily. Industrial and light

manufacturing continues to be soft as large companies continue to consolidate and downsize locations to maximize cost efficiencies. However, until unemployment rates drop and constrained bank lending alleviates, no real strides in the local commercial real estate market will occur. Quite frankly, at this point, it is simply too soon to tell

as we head into 2010. While certain battles have been won, the economic war is far from over. Cautious optimism prevails in hopes that current trends will continue and foster the recov-

“While certain battles have been won, the economic war is far from over” .-Teaster

ery that is so desperately anticipated,” she says.

Getting past 2010, and look at the next three years, Teaster says, “Landlords will need to continue to respond to tenants. The supply of occupiable space is greater than the demand. The environment will continue to be competitive for tenant attraction.”

Teaster also said “Government regulatory authorities must justify their means and will be forced to communicate with each other and revise methods in order to alleviate the restrictions on banks and get intended relief to the intended recipient – business borrowers.”

With so much complexity in the market, Teaster said, “Real estate brokers will be trusted advisors and not just transaction artists. Their success will be determined by their ability to understand client issues and be problem solvers. We will need to seek not only the best answer for our clients, but the right answer.”