

NATION'S HOUSING KENNETH HARNEY

## Housing slump not all doom and gloom

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October 15, 2006

WASHINGTON – With all the dismal reports about the home real estate market, don't lose track of something critically important: Mortgage interest rates have been falling quietly but steadily for weeks, and are now at their lowest level in half a year, barely a percentage point above 40-year lows.

New mortgage applications are up sharply, the number of pending home sales is up, the national economy continues to expand moderately, and the rate of unemployment just declined again – to 4.6 percent.

All of which raises the question: Just what kind of housing bust is this anyway? With gloom-and-doom purveyors forecasting imminent crashes in dozens of metropolitan areas, how could such key fundamentals as jobs, interest rates and even pending home sales simultaneously be trending in the opposite direction?

Donald L. Kohn, the Federal Reserve's vice chairman, took a stab at that seeming conundrum in a speech Oct. 4 at New York University. His views are worth keeping in mind if you want to put the negative news on home prices and sales in perspective.

To begin with the fundamental point: Kohn sees no imminent bust or crash in housing at all. It is a “correction” that's under way – a cyclical rebalancing of a marketplace that got too hot for too long in some parts of the country, and is now heading back toward more “normal” conditions, where prices are more in line with what consumers can afford.

“The reported declines in house prices in a number of areas should help to facilitate the rebalancing of supply and demand in those markets,” said Kohn.

Not all home sellers have fully grasped the altered realities in their own local markets – that they've got to reduce their asking prices if they truly want to sell – so the process is still unfolding. Re-priced houses, in turn, should stimulate greater numbers of potential buyers to get off the sidelines and make offers. The unexpected 4.3 percent increase in the latest monthly number of pending home sales contracts heading for closing nationwide reported Oct. 2 by the National Association of Realtors could be a sign that Kohn's prediction is already taking shape.

Second, said Kohn, the housing correction – expressed through new home starts – “may be closer to (its) trough than to (its) peak.” Translating from Fed-speak, this means that we appear to be well on our way toward bottoming out and eventually returning to positive growth in new home starts and resales.

Now to interest rates. Today's “unusually low” long-term mortgage rate environment “stands in sharp contrast to some past downturns in the housing market that followed actions by the Federal Reserve to tighten credit conditions significantly.” Translation: Affordable mortgage money should help shorten the current housing down cycle compared with credit-squeezed periods in the 1980s, when mortgage rates sometimes exceeded 16 percent for fixed-rate loans.

A final key factor, according to Kohn: “Continuing growth in real incomes should underpin the demand for housing, and as home prices stop rising, help erode affordability constraints.”

Add it all up: Lower asking and selling prices on houses are integral parts of the self-correction and should help shorten the whole process. Lower interest rates should make those lower prices affordable to a broader number of potential buyers. That could become an even more important factor if mortgage rates dip below 6 percent in the coming months, as some Wall Street capital market analysts expect.

James Glassman, a managing director at JP Morgan Chase, says 30-year fixed-rate mortgages at 5¾ percent are a distinct possibility if long-term rates in the global bond market continue to ease. The current cyclical downturn in housing “is not your classic interest rate story” he says. Money is available at low cost, and there’s a good possibility “it won’t be long before we work through this.”

The source of some of the confusion about just where housing is headed, and how bad things are likely to get? Mike Moran, chief economist of Wall Street’s Daiwa Securities America, minces no words: The financial press and TV news shows are overly dramatizing what is a normal and long-predicted cyclical rebalancing, and “portraying it as a catastrophe.”

Housing “is going through a correction that’s badly needed,” he said. “The key issue is whether it is orderly or disorderly” – and all signs point to a continued orderly process, not a breakout bust or panic.

Doug Duncan, chief economist of the Mortgage Bankers Association, points out that national housing sales numbers are merely rolling back to 2003 levels – “and that was a record year.” Serious sellers and buyers shouldn’t be misled by predictions of imminent crashes, said Duncan. Not only do the doom reports ignore the positives out there in the marketplace – mortgage rates in particular – but “the rhetoric is just way overwrought.”

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