August 17 - Mid Month Pricing Update and Forecast

Mid Month Pricing Update and Forecast

Each month about this time we look back at the previous month, analyze how pricing has behaved and report on how well our forecasting techniques performed. We also give a forecast for how pricing will move over the next 30 days.

For the monthly period ending August 17, we are currently recording an average sales $/SF across all areas and types of $87.02 - down sharply by 2.7% from $89.41 on July 18. This is very close to the price prediction we made on July 18 of $87.36 (with a 94% confidence range of $85.61 to $89.11). Our pricing forecast model has proven very accurate over the last two months despite the sudden downward movement.

Today the pending listings for all areas & types show an average list $/SF of $87.58. This figure is very similar to the reading on July 18. This suggests little change in sales pricing over the next 30 days. Our mid-point forecast for September 16 is currently $87.08, which is a statistically insignificant 0.07% above today's actual reading, and we have a 94% confidence that it will fall within ± 2% of this mid point, i.e. in the range $85.34 to $88.82.

Average sales pricing per sq. ft. has fallen from a short term peak of $93.04 on June 16 to $87.02 today, dropping almost 6.5% in just two months. The short term fall in sales price per sq. ft. that we have experienced is due to a similar combination of effects to those we documented last month:

- Short sales are taking a larger share of a diminished market, at the expense of normal sales. They currently comprise 28.1% of monthly sales, up from 26.6% last month and 20.7% the month before that.
- REO are also taking a larger share of a diminished market, at the expense of normal sales. They currently comprise 42.9% of monthly sales, up from 41.0% last month.
- REO inventory has increased dramatically by 37% since June 8 putting additional downward pressure on lender owned pricing. Banks are not slow to respond and the average pricing per sq. ft. for REOs has fallen from $83.89 on June 8 to $78.51 today.
- Normal sales volume is very weak, down 44% in the last two months. Since normal sales are on average priced significantly higher than REOs (volume down 23%) and short sales (volume flat) this has a very negative effect on the overall average.

The recent downward movement in sales pricing was set in motion by contract signings a few months ago. We now expect to see a temporary sideways trend for the next 30 days. Will prices recover after that? Probably not. It is very likely that the downward trend will resume.

Sales pricing is a trailing indicator. It is useless for forecasting purposes. To predict the future we need to look at how demand and supply are behaving. Using accurate measures of supply and demand we can usually make sound predictions for the future. The main thing we cannot predict well is government intervention. Events like the extension to 2009's tax credit program and the passage of SB1070 can have large effects that can be measured in hindsight but are difficult to predict.

The Cromford Market Index™ is intended to give us a simple measure of the balance between supply and demand and hence the long term direction for pricing. The Cromford Market Index™ has been on a generally downward trend since peaking in November 2009. This trend was very mild at first but accelerated after mid June 2010. It is now on a strong downward path. This is caused by weakening demand and growing supply. In these circumstances, prices can only move in one direction. The Cromford Market Index™ is a long range indicator. The recent downward movement in pricing is NOT a result of the recent downward movement of the index. Instead we expect downward pressure on pricing to continue until long after the CMI reverses direction and starts to climb. So we will be looking to see how long and strong this downward CMI trend turns out to be. We have a little bit of good news in that sales volume has stabilized in the first half of August compared with the second half of July. This means demand is no longer falling fast as it was in the previous three months. However the upward trend in supply is continuing unabated, especially in the lower priced areas of the valley and most especially in areas with large Hispanic populations. If demand stabilizes at current levels but supply continues to increase we will still have an out of balance situation. To restart the recovery we will need either a significant improvement in demand or a significant fall in supply, neither of which are on the short term horizon.

In summary, the market recovery that prevailed from March 2009 to November 2009 was followed by stability between December 2009 and May 2010. We no longer have stability or recovery. The market is in decline.

August 2 - Market Summary for the Beginning of August

Market Summary for the Beginning of August

The market deteriorated sharply in July, and much faster than we have experienced for a very long time.

Since the changes during July were so dramatic we are going to spend a lot more time than usual examining what is going on.

Much of the weakness in demand can be explained by the "air pocket" caused by the expiry of the tax credit at the end of April. Many eligible buyers brought forward their home buying decisions into April from May, June and July. Sales were temporarily boosted in May and June, but like a hangover, the sales volume dropped very sharply in July.

If this were the only issue, we could look forward to a recovery by September. However when we look deeper into the supply numbers we can see clear evidence that other factors are working to deteriorate the market further, particularly at price ranges below $225,000. The market above $300,000 has been affected much less, in part because homes priced above $800,000 were ineligible for the tax credit.

Let's review a few key numbers, all of which are giving negative signals. These are for all areas and types within ARMLS:

Measurement	May 1, 2010	August 1, 2010	% Change
Active Listings	40,990	42,489	+3.6%
Pending Listings	14,406	9,822	-31.8%
Sales per Month	9,182	6,999	-23.8%
Under Contract	22,410	16,394	-26.8%
Listing Success Rate	66.3%	58.8%	-11.3%
Cromford Market Index™	107.0	92.2	-13.8%
Market Distress Index	62.2	68.8	+10.6%
Months Supply	4.6	6.0	+30.4%
Days Inventory	157	162	+3.2%

Note that the overall supply of active listings has only increased by 3.6%. It is the fall in demand that has had by far the largest impact.

Let's review how sales per month and pending listings have performed over the last six months:

These charts tell a obvious story, but a dramatic fall in demand was largely expected after the expiry of the tax credit, so this potentially masks other factors affecting the market balance.

Although the increase in supply is much less obvious, it is highly concentrated in particular market segments and more detailed analysis tells us much more about what is going on. The details are quite ominous for the low end of the market once we look more closely. The trend is also running counter to the normal seasonal pattern, which also tells us something unusual is going on here.

The overall weekly active listing counts look like this for the past three years:

At first sight this does not look remarkable. But note that the upward trend between May and August is not something we saw in 2008, even though the market in 2008 was still struggling to break out of its precipitous price decline. It is completely different to 2009 when the supply plunged at an unusual rate. In normal years active listings decline between May and August because this is the prime selling season of the year. In fact the only years we have seen active listing increase between May and August are 2005 to 2007 when the residential real estate bubble was in its collapsing phase and active listings were rising very fast almost all the time.

Let's break out the supply into various market sectors to see what is really going on. The following table is for single family detached in Greater Phoenix and segments the market by price range. It counts active listings but excludes those in AWC status (with a signed contingent contract).

List Price Range	Active May 1, 2010	Active Aug 1, 2010	% Change
Less than $25,000	63	94	+49.2%
$25,000 to $49,999	618	961	+55.5%
$50,000 to $74,999	1,322	2,036	+54.0%
$75,000 to $99,999	2,563	3,774	+47.2%
$100,000 to $124,999	2,355	3,142	+33.4%
$125,000 to $149,999	2,620	3,185	+21.6%
$150,000 to $174,999	1,863	1,984	+6.5%
$175,000 to $199,999	1,729	1,950	+12.8%
$200,000 to $224,999	1,039	1,072	+3.2%
$225,000 to $249,999	1,262	1,186	-6.0%

$250,000 to $274,999	799	738	-7.6%
$275,000 to $299,999	922	856	-7.2%
$300,000 to $349,999	1,084	986	-9.0%
$350,000 to $399,999	1,015	941	-7.3%
$400,000 to $499,999	1,154	1,045	-9.4%
$500,000 to $599,999	763	629	-17.6%
$600,000 to $799,999	999	841	-15.8%
$800,000 to $999,999	637	527	-17.3%
$1,000,000 to $1,499,999	685	539	-21.3%
$1,500,000 to $1,999,999	422	344	-18.5%
$2,000,000 to $2,999,999	361	292	-19.1%
Over $3,000,000	283	243	-14.1%
Overall (SF-D)	24,558	27,365	+11.4%

We note four major things:

1. The split at $225,000 where supply below that point has increased but supply above that point has declined
2. Single family detached supply has increased by 11.4%, much more than other dwelling types
3. The large reduction in supply of homes above $500,000
4. The huge increase in supply of homes below $100,000

The large reduction in supply above $500,000 would be excellent news for the luxury sector if it weren't for the fact that demand has also retreated by a significant percentage for most price levels. Only the market above $3,000,000 has seen demand persist at the same level over the last three months.

List Price Range	Under Contract May 1, 2010	Under Contract Aug 1, 2010	% Change
Less than $25,000	87	75	-13.8%
$25,000 to $49,999	659	637	-3.3%
$50,000 to $74,999	1,802	1,395	-22.6%
$75,000 to $99,999	3,362	2,422	-28.0%
$100,000 to $124,999	2,698	1,880	-30.3%
$125,000 to $149,999	2,558	1,780	-30.4%
$150,000 to $174,999	1,752	1,219	-30.4%
$175,000 to $199,999	1.337	915	-31.6%
$200,000 to $224,999	800	569	-28.9%

$225,000 to $249,999	840	592	-29.5%
$250,000 to $274,999	520	404	-22.3%
$275,000 to $299,999	509	383	-24.8%
$300,000 to $349,999	594	431	-27.4%
$350,000 to $399,999	483	368	-23.8%
$400,000 to $499,999	452	337	-25.4%
$500,000 to $599,999	252	181	-28.2%
$600,000 to $799,999	236	177	-25.0%
$800,000 to $999,999	110	80	-27.3%
$1,000,000 to $1,499,999	88	62	-29.5%
$1,500,000 to $1,999,999	60	38	-36.7%
$2,000,000 to $2,999,999	32	14	-56.3%
Over $3,000,000	12	12	0.0%
Overall (SF-D)	19,243	13,971	-27.4%

We want to combine the measurement of supply and demand into a single statistic. The short term change in the balance of supply and demand is probably best illustrated by the inventory based on monthly sales (i.e. months supply). This is a volatile measure but has the advantage of reacting quickly to change over the short term, emphasizing where the changes are strongest.

List Price Range	Months Supply May 1, 2010	Months Supply Aug 1, 2010	% Change
Less than $25,000	1.1	2.7	+145.5%
$25,000 to $49,999	2.2	3.2	+45.5%
$50,000 to $74,999	2.9	4.6	+58.6%
$75,000 to $99,999	3.5	5.6	+60.0%
$100,000 to $124,999	3.1	5.1	+64.5%
$125,000 to $149,999	3.6	5.3	+47.2%
$150,000 to $174,999	3.5	4.9	+40.0%
$175,000 to $199,999	3.8	5.8	+52.6%
$200,000 to $224,999	4.1	5.9	+43.9%
$225,000 to $249,999	4.5	5.2	+15.6%
$250,000 to $274,999	4.2	5.7	+35.7%
$275,000 to $299,999	4.7	5.8	+23.4%
$300,000 to $349,999	5.2	5.1	-1.9%

$350,000 to $399,999	6.4	6.1	-4.7%
$400,000 to $499,999	6.4	8.5	+32.8%
$500,000 to $599,999	8.6	8.6	0.0%
$600,000 to $799,999	11.9	9.5	-20.2%
$800,000 to $999,999	14.7	15.0	+2.0%
$1,000,000 to $1,499,999	18.7	14.7	-21.4%
$1,500,000 to $1,999,999	24.8	35.7	+44.0%
$2,000,000 to $2,999,999	37.7	26.8	-28.9%
Over $3,000,000	47.8	24.6	-48.5%
Overall (SF-D)	4.1	5.6	+36.6%

The market below $225,000 is clearly suffering by far the worst. The months supply numbers are not desperately bad in absolute terms. We saw much worse ones in 2007. It is the rapid nature and scale of their deterioration that is alarming and we conclude that the short term outlook is poor for the market under $225,000. Above $300,000 the picture is more mixed with several ranges improving over the last three months: $300,000 to $399,999, $600,000 to $799,000, $1,000,000 to $1,499,999 and in particular over $2,000,000. In fact the range above $3,000,000 is recording its lowest months supply (24.6) since the summer of 2006. At 9.5, the inventory for the range $600,000 to $799,000 is also the lowest we have recorded since the summer of 2006. So these price sectors are doing pretty well. Yet the ranges $400,000 to $499,999 and $1,500,000 to $1,999,999 are doing relatively poorly.

Obviously this is a complex picture. We will come back to look further at geographic segments, foreclosures and pricing in subsequent posts.