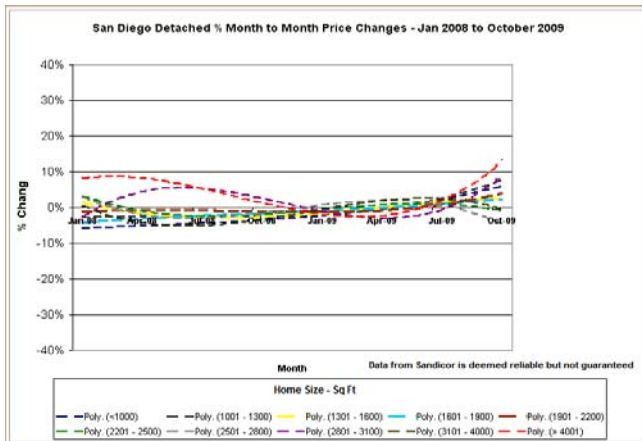


SAN DIEGO HOUSING RESEARCH

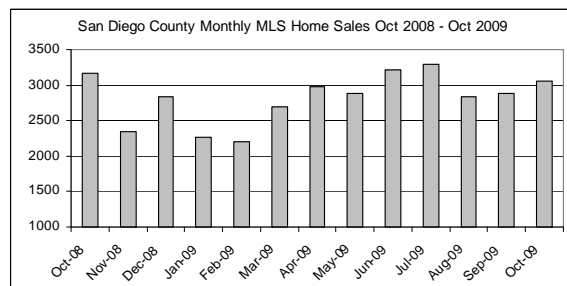
Bubble-mania

The Great Housing Correction is aborted by our government, eager to stop house prices from reaching equilibrium with wages and rents. Prices on homes under \$600,000 are up 15 – 20% since March. Last month we moved slightly down to 2.6 months supply, well below the price-neutral 4 month level. When we remove the many unaffordable homes from the mix, months supply is well below 2 months.

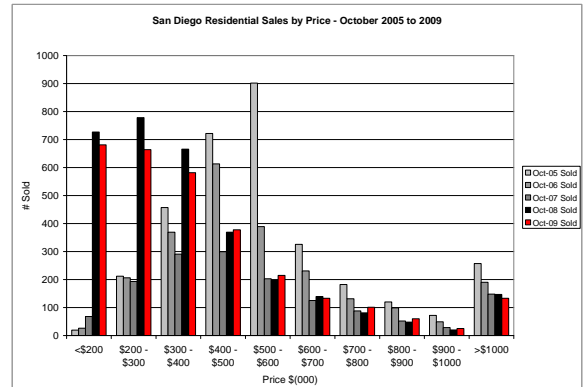
Price increases are slowing however. Does this signal a turning point in the market?



Sales fell 3.5% year over year, yet rose 6% last month to 3,063 homes sold.

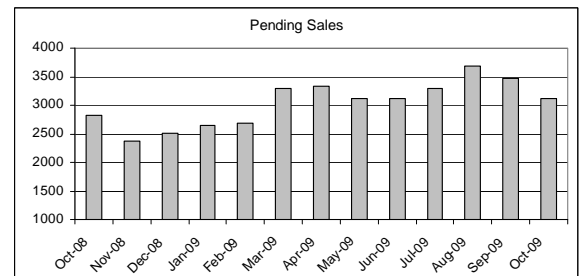


Since last year, sales are down significantly in the lower price ranges.



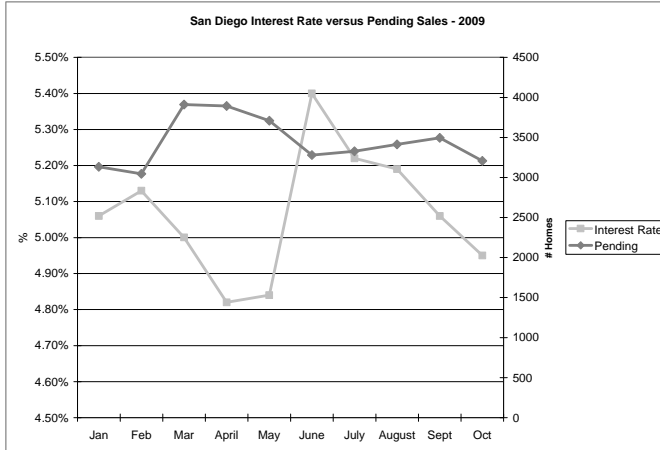
In a sign that seasonality is overcoming the euphoria, pending sales declined for the second month in a row, falling 10% to 3,126 homes. Year over year, pending sales fell 5%.

**Note: in May, many Pending moved to the new Contingent field

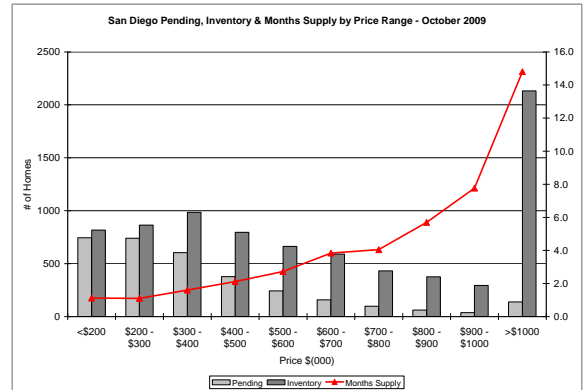


We did not expect pending sales (homes entering escrow in October) to fall, since we are still seeing multiple offers on every transaction. There is a backlog of summer buyers whose offers have been ignored and rejected, and who are still out there looking to buy. Last year, there was no seasonal decline, and we did not expect it this year either. Besides that, pendings moved inversely from interest rates. Since interest rates fell again in October, we expected pendings to rise.

The drop in pendings is seasonal, and we expect an increase in pendings starting in January.

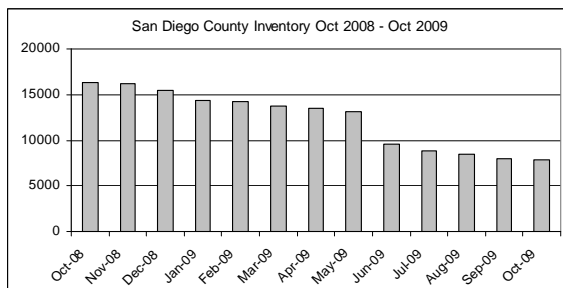


Yet all is not rosy. The high end is impaired. Months supply is 14 months for homes over \$ 1 million, and 3 years for homes over \$ 2 million. Homes over \$ 1 million are only 4% of sales even though they make up 25% of the inventory.

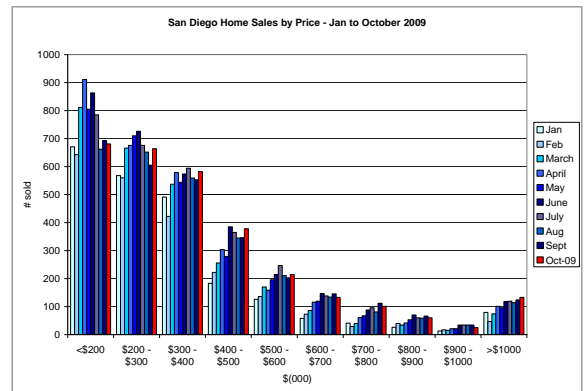


The number of accepted offers is 10,000, exceeding the 8,000 homes listed for sale!

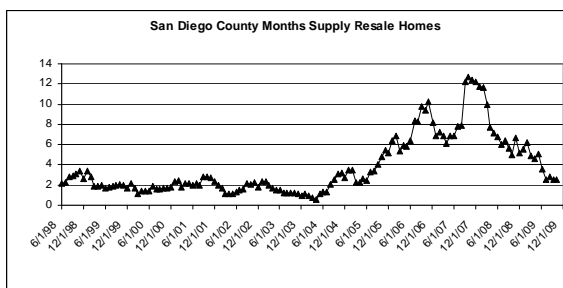
In a sign that seasonality is impacting sellers as well, inventory rose 1.4%, the first increase in 18 months.



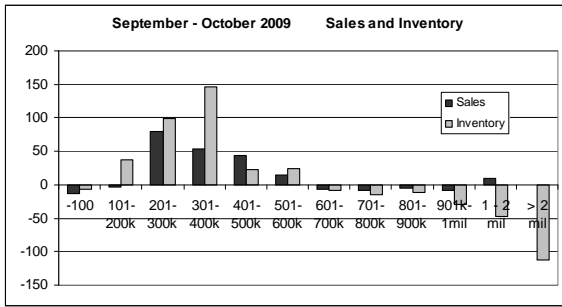
Most sales continue to be at the low end.



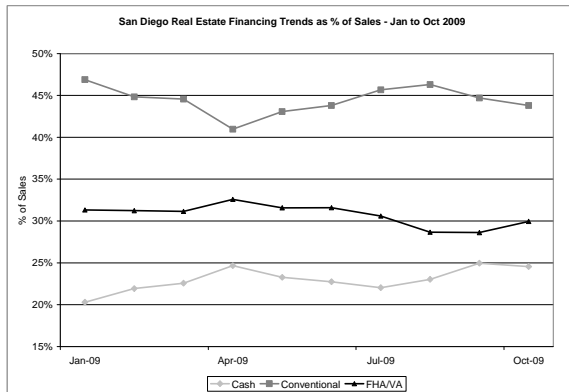
Months supply countywide fell slightly to 2.6 months.



The increase in both sales and inventory were mainly in the \$100k - \$400k segments. Higher priced homes were taken off the market last month. The high demand at the low end continues to come from cash and FHA buyers, who each make up 25% of market share.

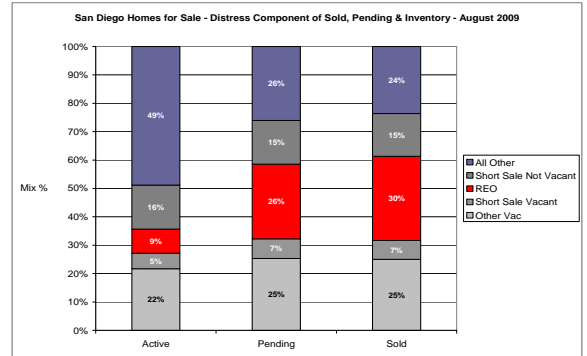


We believe the price increases are the reason that pendings are declining. Let's look at an entry-level home, a detached house from 1000 – 1300 sq ft. The monthly payment for that house is up 10% this year, because price increases are greater than the fall in mortgage rates. Buyers who finance their homes are shifting down to attached homes, buying smaller homes, or leaving the market. Both price increases and interest rates increases are the major risks to the San Diego market moving forward.

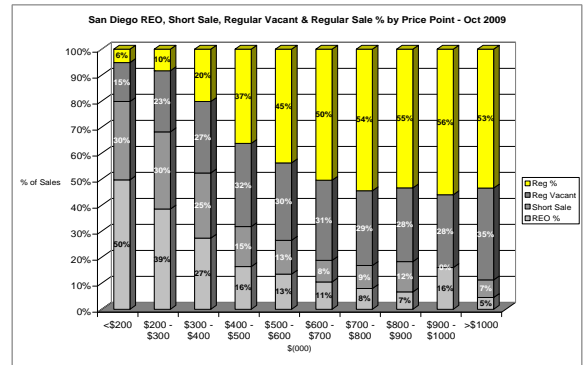


Distress Properties

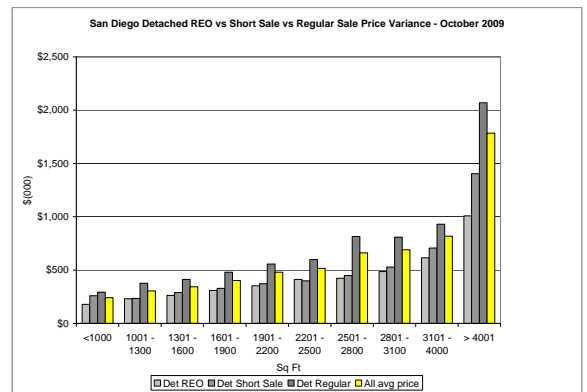
Over half of sales are distress properties: REOs and short sales.



Distress properties are concentrated at the low end.



Distress homes sell for less because of their poor condition and high seller motivation.



We broke the story last month about servicers ignoring about half of delinquent borrowers. Let's put a face to the story: we know a couple that has not made a mortgage payment in 24 months, and still has not received an NOD (Notice of Default), the first step in the foreclosure process.

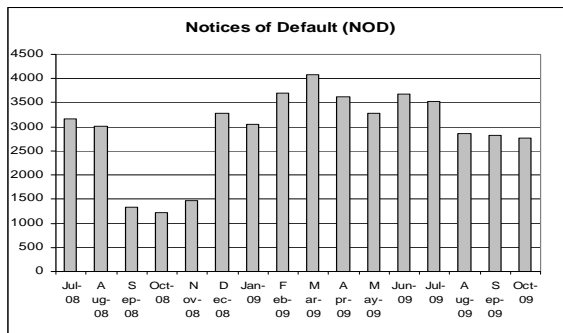
Delinquent borrowers doubled in California in the past year from 5% to 10% of mortgages.



Does everyone see a problem here? Delinquencies rise while foreclosures fall - how long can this continue? At least we know why there is a shortage of bank owned homes on the market. Banks are choosing to not foreclose on delinquent mortgages. Fannie Mae announced an REO rental program, and we expect more "extend and pretend" games to boost housing prices by keeping down supply and boosting demand.

Investors figured it out too, and stepped up their purchases all year. At foreclosure sales last month, investors bought 25% of auctioned properties. Before the auction even starts, 40% of sales are cancelled. That leaves little to put on the market for sale. Last month, 2100 properties were scheduled to be auctioned, and only half ended up going back to the lender for sale by realtors.

At the same time, NODs are falling....



...and NTS (Notices of Trustee Sale) are falling.

