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The riskiest housing markets

A new report projects home-price declines for the next two years. The riskiest markets are in Florida, California, Nevada and Arizona. Here's how to ride out the hard times.
By Marilyn Lewis



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As if the housing market isn't bleak enough. The [Standard & Poors' Case-Shiller Home Price Index](#) reported in late June that home prices dropped more in the first quarter of this year than at any other quarter in the last 17 years. Now, a report from PMI Mortgage Insurance says home values could decline across much of the country for at least two more years.

There's a 34.6% chance on average that home prices will drop in the nation's top 50 markets in the next couple of years, according to PMI Mortgage Insurance's new U.S. Market Risk Index, which heavily factors in recent price volatility.

How far and how fast prices actually fall remains to be seen. But the report underscores the fact that today's market is decidedly different from that of recent years, when homeowners could bank on rapid home-value appreciation. (See the report or hear a podcast [here](#).)

Headed for decline

Not surprisingly, the riskiest markets identified by the index are located in areas that saw rapid price appreciation, a reduction in affordability followed by a rapid decrease in the rate of price appreciation. Of the 15 biggest cities with the greatest risk for price decline -- with more than a 50% chance of lower home values by mid-2009 -- five were in California

and four were in Florida.

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At the highest end of the spectrum, the following major markets all have a greater than 60% chance of declines, according to PMI:

- Riverside-San Bernardino-Ontario, Calif. (65.2%);
- Phoenix-Mesa-Scottsdale, Ariz. (64.6%);
- Las Vegas-Paradise, Nev. (61.4%);
- West Palm Beach-Boca Raton-Boynton Beach, Fla. (60.7%).

"There's no question that our housing prices are declining here," says Jay Thompson, an agent with Century 21 Aware near Phoenix. "Our appreciation rate was 54% average at one point in mid-2005-2006, so it is no surprise to anybody here ... that prices were going to go down."

The inventory numbers tell the story: In January 2005, Thompson's multiple listing service showed 3,500 homes for sale. Today: about 54,000.

Also at risk for dropping values

The next-riskiest top 50 metro areas on the PMI index, with a 50% or greater chance of dropping values in two years, are:

- Los Angeles-Long Beach-Glendale, Calif. (58.6%);

- Santa Ana-Anaheim-Irvine, Calif. (57.7%);

- Oakland-Fremont-Hayward, Calif. (57.2%);

- Orlando-Kissimmee, Fla. (56.3%);

- Sacramento-Arden-Arcade-Roseville, Calif. (56.0%);

- San Diego-Carlsbad-San Marcos, Calif. (55.5%);

- Fort Lauderdale-Pompano Beach-Deerfield Beach, Fla. (54.2%);

- Miami-Miami Beach-Kendall, Fla. (52.4%);

- Tampa-St. Petersburg-Clearwater, Fla. (50.6%);

- Boston-Quincy, Mass. (50.1%);

- Washington, D.C.-Arlington-Alexandria, Va.-W.Va. (50%).

Even where PMI found relatively low risk for dropping prices, sales have slowed way down. In Everett, Wash., in the Seattle-Bellevue-Everett region with a 34.3% risk of lower prices in two years, homes are sitting on the market an average of 59 days before selling, says Susan Funk, agent with Keller Williams Realty. "Last year, you knew you were overpriced if you did not have offers within the first 10 to 14 days," Funk says.

Rust belt less risky

You might expect the list of high-risk regions to include Midwestern industrial cities like Detroit, where prices fell 9.3% in the last year and foreclosures rose 140% between May 2006 and May 2007, according to RealtyTrac.

But Detroit hasn't had much volatility, just steadily falling prices and a huge backlog of properties for sale. There's less risk there because prices already have fallen a good deal, says Mark Milner, chief risk officer at PMI Mortgage Insurance. "Simply put, prices can't fall forever," PMI's report says.

"The more volatile it is, the more likely it will be volatile in the future," says Milner, explaining how risk is calculated. Phoenix, the second-riskiest city, saw a precipitous drop in the rate of home appreciation -- from 37.3% in the first quarter of 2006 to 4.52% in the first quarter of 2007.

Affordability -- how much of your income is eaten up by housing -- is another component of the risk scores. To arrive at risk scores, the PMI economists use a formula that includes data on house sales (including prices, volatility, acceleration and deceleration), affordability (including per-capita income, appreciation and mortgage rates) and employment.

One encouraging note: In most markets where price reductions are predicted there are strong local economies and low unemployment. Nationally, "on average, employment is very strong," says LaVaughn Henry, PMI's director of economic

analysis.

The least-risky areas

The major metros with the least risk of price decline by 2009 were in Texas and the Midwest, stable markets largely untouched by the real estate boom:

- Cincinnati-Middletown, Ohio-Ky. (9.7%);

- Columbus, Ohio (9.3%);

- Indianapolis-Carmel, Ind. (8.4%);

- Houston-Sugar Land-Baytown, Texas (7.9%);

- Dallas-Plano-Irvington, Texas (7.5%);

- Fort Worth-Arlington, Texas (7.4%);

- Pittsburgh (6.4%).

Lessons from a changed market

What does all this mean to buyers and sellers? In short, says one agent, forget what you thought you knew about real estate.

For buyers

- **Consider whether and where to leap.** For buyers, the changing market may mean it's time to think about buying if homeownership previously was too costly. "Yes, there are affordability problems in California, the Southwest and Florida," says PMI's Milner. "But there are also huge swaths of the country where housing is still very affordable, and in some cases more affordable (in percentage of income spent on housing) than it was 10 years ago." The most affordable regions are the South and Midwest. Just be certain you can weather the storm if home values drop after you buy.

- **Realize it's a home, not a cash machine.** Think of your home as a place to live, not as a way to make quick money. "Instead of a stock, which is just a piece of paper, you get to consume shelter," says Milner. Your home probably will appreciate, but slowly. Historically, homes appreciate at a rate of about 4% to 6% a year, on average, over any given 10-year period, he says.

- **Choose a mortgage by interest rate, not payment amount.** Proceed cautiously when shopping for a mortgage. Consider a traditional fixed-rate loan so you'll know exactly what your payment will be for the entire life of the loan. You may find adjustable-rate mortgages (ARM) with lower payments that later adjust up, but don't gamble that you can make a higher payment when the introductory period is over or when interest rates rise, as they are likely to do.

- **Don't bet on house appreciation.** Don't make financial plans or take on debts that bank on the near-term rising value of real estate. In the post-bubble world, the risk to your financial stability is just too great. A number of the 176,137 foreclosures filed in May -- a 90% increase from last year at this time, according to RealtyTrac -- were by borrowers who'd gambled they could refinance a risky mortgage once their home had appreciated. Buyers "are going to need to be very prudent because they are not going to be bailed out by an appreciating home," says Milner.

For sellers

- **Sweeten a sale by helping a buyer with closing costs.** Potential buyers may be sitting on the sidelines because, although they can make monthly payments, they haven't got a down payment saved up, says Steven Schafer, an agent with Boca Executive Realty in Boca Raton, Fla., one of the riskiest markets identified by the PMI study. Consider contributing up to 3% of closing costs. (Just be aware that states and lenders often limit seller contributions.)

- **Exploit the Internet.** Open houses, while still an important sales tool, are being eclipsed by the Internet. Buyers now use Web research to learn what's for sale locally before stepping a foot out of their homes. With scads of homes on the market, you must figure out how to distinguish your home from others like it on the Internet. Schafer and Thompson, the Phoenix-area agents, create a Web site for each house they represent, usually using the home's address as the site address. If your agent can't register the link for you, do it yourself. You can also set up a Web page yourself with a modicum of computer skills or pay a Web site creation company to do it for around \$30, says Schafer.

- **Load your listing with pictures.** Schafer advises "visually communicating" with buyers by choosing an agent with an outstanding Web site and contributing plenty of great photos of the house.

- **Use a "virtual" tour.** Sophisticated real-estate sites use panoramic photo features or streaming video so buyers can get a 360-degree view of the property from a single vantage. With virtual tours, buyers in other states and other countries can get a good feel for your home without actually stepping foot inside.

You can find additional selling tips in "[How to sell in a homebuyer's market.](#)"

Just remember, even this tough market will pass. Time is needed for wages to catch up to prices so more people can afford to buy homes. "It takes time to adjust back to affordability," says PMI's economist Henry.

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