The Economics of the American Dream

(Ajusted for Inflation and Fluctuating Interest Rates)

1982	1989	1996	2003
Typical Home Cost: $196,000	**Typical Home Cost:** $270,000	**Typical Home Cost:** $205,000	**Typical Home Cost:** $425,000
Avg Mortgage Rate: 15.3%	**Avg Mortgage Rate:** 10.1%	**Avg Mortgage Rate:** 7.7%	**Avg Mortgage Rate:** 5.6%
Typical Mortgage Payment: $2,021	**Typical Mortgage Payment:** $1,912	**Typical Mortgage Payment:** $1,169	**Typical Mortgage Payment:** $1,952

For North County homeowners, the last eight years have been one heck of a party. Adjusted for inflation, the price of a typical home has doubled since a painful recession ended in 1996, pouring a staggering $155 billion of new wealth into the 63 percent of households in the county that own their homes.

Fueling the boom has been the lowest interest rates in modern history, which enabled families to buy starter condos, slash mortgage payments or move up to dream homes. Lenders stuffed mailboxes with pitches promising cheap and easy money, so thousands dipped into their newfound assets to finance big vacations, build fancy master bedrooms and survive their kids' college bills.

People felt richer because they were richer, and experts say all that spending insulated the local economy from a national recession.

Yet tempering the celebration was the plight of families living in rental units, a third of the county's households. Most saw any prospect of home ownership vault impossibly out of reach.

And haunting the market were memories of crashing values in the early 1990s. Now, with houses trading at unbelievable prices and with interest rates suddenly on the rise, some experts have stepped up warnings that San Diego County's housing market—the nation's hottest—is heading for trouble. Still others say that the nation's market is poised for collapse, taking the banking industry and the overall economy down with it.

Bubble trouble?

Have buoyant prices inflated a housing "bubble" that's about to burst? And what should you do now?

They are favorite topics around water coolers in North County, where a typical tract house cost $599,000 last month, up $70,000 since March.

Analysts who work for the lending and real estate industries are reassuring.

"In California, we don't have a bubble," said Amy Crews Cutts at a recent housing conference. She is the deputy chief economist at Freddie Mac, the federally chartered company that, together with its larger cousin Fannie Mae, hold a staggering $3.6 trillion in mortgages, nearly half of the nation's total.

Crews Cutts explained that the local and national economies are expanding, with businesses adding workers again after a long slump. In modern economic history, a region has simply never experienced falling housing prices during a period of job growth, she said.

But considerably less sanguine is a cadre of academics who see a growing threat that rising interest rates could kill the housing market and send the local and national economies tumbling into recession.

Prominent among the skeptics is Ed Leamer, the UCLA economist who heads the widely respected Anderson Forecast.

"My view is we've created a very fragile market and it doesn't take a very big increase in rates to have a significant impact," Leamer said.

He advises homeowners to avoid adjustable-rate loans and instead lock in fixed-rate, 30-year mortgages while rates remain below historic averages. He also cautions buyers against purchases involving very small down payments. If prices fall, many families could end up owing more than they can get for their houses if job loss or health problems force them to sell into a soft market.

Interest rates and recessions

Leamer says he doesn't know precisely how high rates must go to trigger a slowdown.

Rising interest rates—and weakening housing markets—have preceded and probably caused eight of the last 10 recessions since World War II, he says. Careful study of the downturns reveals that they were preceded by interest rate jumps that varied from 0.8 to 4.6 percentage points.

But home buyers in North County have been handed a more recent demonstration of the power of rising borrowing costs.

Consider the typical, single-family house, which cost $599,000 in June and just $529,000 in March. Four months ago, the average 30-year, fixed-rate mortgage stood at 5.3 percent. By June, the rate had jumped to 6.25 percent.

Assuming that a family could come up with a 20 percent down payment, the double-whammy of higher prices and rising rates in just four months meant that buyers were faced with an extra $600

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And there's little chance conditions will soon improve: Economists say that even if home prices retreat, it will be because mortgage rates have gone higher, thus pushing up payments and wiping out any benefit from lower prices.

Meanwhile, real estate agents say they started to pick up signs that the local market has cooled, if just a bit.

In June, the number of unsold homes on the market doubled in San Diego County. In Orange County, where prices are even higher, the condominium market has gone soft and some neighborhoods have seen a sixfold jump in the number of homes for sale, said Steve Rogers, president in Orange County for Prudential California Realty.

While few predict falling prices, Rogers and other real estate agents say that sellers may have lost the inordinate clout they had this spring, when buyers were topping asking prices and furiously competing for houses.

"I think it's just becoming more of a healthy market," said Rogers.

Signs of strain

In addition, bankers point to a key indicator that buyers are beginning to struggle to absorb the high prices: Last month, adjustable-rate mortgages comprised 50 percent of new loans in Southern California, up sharply from 15 percent in March, said Robert Camerota, a director of the California Mortgage Bankers Association.

The association predicts that mortgage origination will drop by half in the next 18 months, leading lenders to step up sales efforts and roll out new adjustable loans that trade increased risk to homeowners for cheaper initial payments.

At the same time, use of computerized credit scores and other techniques by lenders has reduced the risk that they will experience ruinous default rates, Camerota said.

"We're not making risky loans; I think we're shifting the emphasis to make it affordable to them," he said. "We have to keep the economy moving, and we have to keep getting people into homes."

Others are skeptical, arguing that sloppy lending has done much to pump up the housing market. Many see a day of reckoning approaching.

Sounding the loudest alarm is John Talbott, a former investment banker and author of "The Coming Crash of the Housing Market: 10 Things You Can Do Now."

National decline has begun

Talbott points out that home prices began declining last summer in most of the nation outside of California, Florida and parts of the Northeastern coast.

He argues that the lending industry has been feasting for years on risky home loans, offering mortgages with no down payments, no proof of income and terms of up to 40 years in an effort to snare more customers.

A particular concern is the popularity of adjustable-rate mortgages, which allow homeowners to borrow more money at low introductory rates but leave them with the risk that payments will increase later if interest rates rise.

"First of all, you shouldn't qualify for more money just because you're willing to take more risk," Talbott said.

Meanwhile, innovations in international lending markets have moved the risk of default from banks to a secondary market dominated by Fannie Mae and Freddie Mac. The two giant, politically powerful private companies use borrowed money to buy mortgages. They were created by the federal government to promote home ownership.

Many analysts share Talbott's fear that rising rates or a housing downturn will topple Fannie Mae and Freddie Mac, leading to a massive federal bailout.

"I don't know if you can bail this one out; they are holding $4 trillion in mortgages," he said. "We did this once with the savings and loan crisis. Now we've gone and done it again."

This report cites figures from County Assessor Greg Smith, the Census, the U.S. Department of Commerce, the Mortgage Bankers Association and the California Association of Realtors.

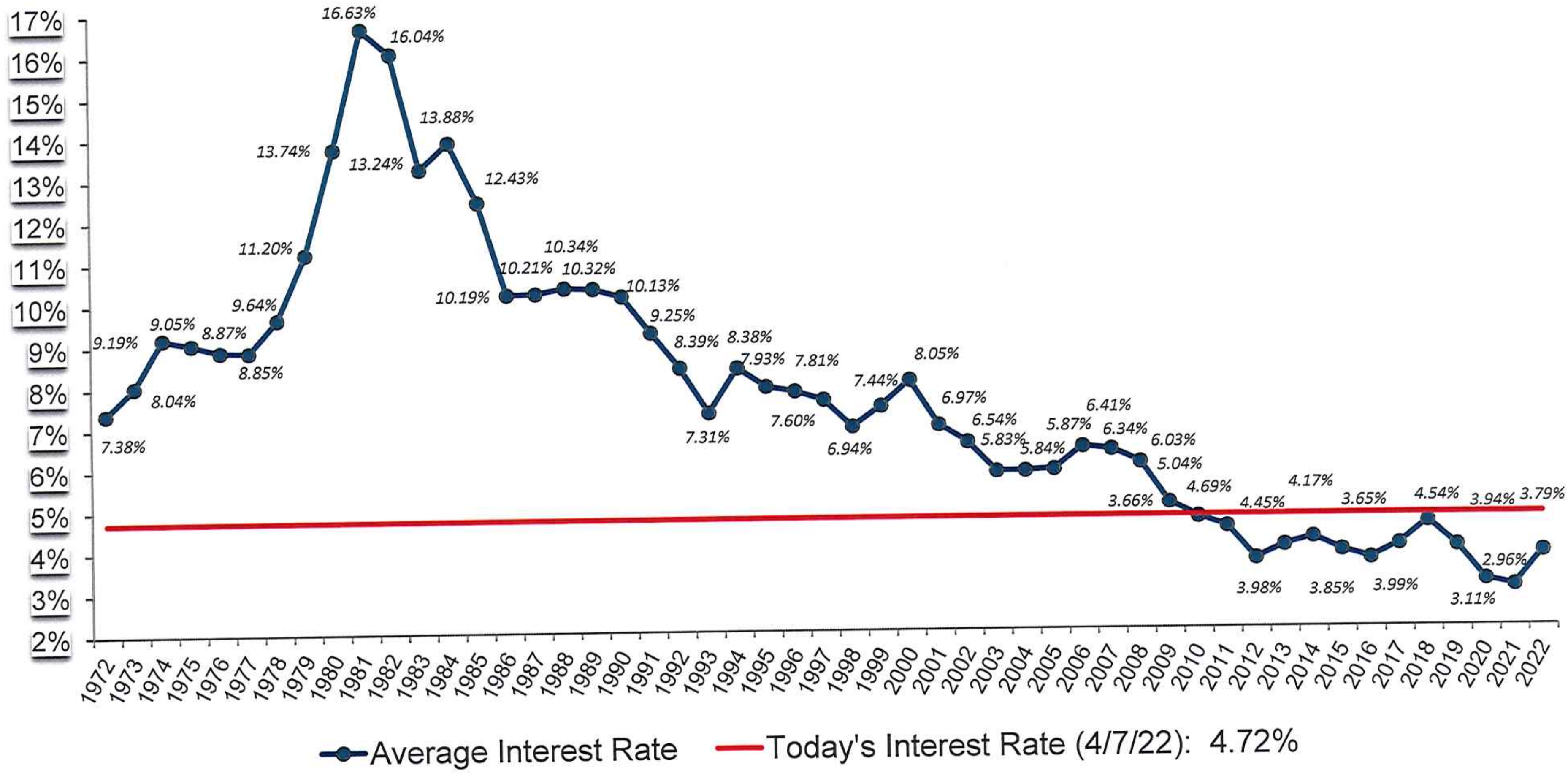
Dan McSwain · North County Times · July 11, 2004

San Diego County median prices for single-family homes VS. Average single-family mortgages

HOME PRICES (in 2003 dollars)		MORTGAGE RATES (national averages)	
1982	$195,619	1982	15.33%
1983	$190,224	1983	12.75%
1984	$184,779	1984	12.49%
1985	$190,598	1985	11.64%
1986	$206,376	1986	10.18%
1987	$216,990	1987	9.28%
1988	$238,569	1988	9.32%
1989	$269,881	1989	10.12%
1990	$257,665	1990	10.05%
1991	$253,036	1991	9.33%
1992	$239,974	1992	8.08%
1993	$225,064	1993	7.12%
1994	$218,362	1994	7.49%
1995	$206,996	1995	7.84%
1996	$204,572	1996	7.73%
1997	$212,142	1997	7.67%
1998	$233,747	1998	7.10%
1999	$255,629	1999	7.29%
2000	$287,821	2000	8.05%
2001	$310,073	2001	7.03%
2002	$372,393	2002	6.54%
2003	$424,900	2003	5.57%
2004	$448,276	2004	n/a

30-Year Fixed Mortgage Rates National Yearly Averages[1]

(for conventional mortgage balances below $647,200)



[1] Source: *Freddie Mac Primary Mortgage Market Survey (U.S. Weekly Averages)*. The values, figures, opinions and statistics contained in the chart above are not compiled, researched, or validated by Prosperity Home Mortgage, LLC nor does the chart represent the views of our company. We are not responsible for the accuracy or content of the information provided and cannot guarantee that the information is current, valid or suitable for a particular purpose. Rates are subject to change without notice; the chart is not indicative of rates available to borrowers.

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NMLS ID #75164 (NMLS Consumer Access at http://www.nmlsconsumeraccess.org/)

California and U.S. Existing Single-Family Home
Annual Median Sales Price and Annual Sales Activity 1968 - 2020

		Median Sales Price				Annual Sales Activity			
		CALIFORNIA		UNITED STATES[1]		CALIFORNIA		UNITED STATES[1]	
	Year	Median	Year-to-Year % Change	Median	Year-to-Year % Change	Sales*	Year-to-Year % Change	Sales*	Year-to-Year % Change
	1968	$23,210	N/A	$20,100	N/A	N/A	N/A	1,569,000	N/A
	1969	$24,230	4.4%	$21,800	8.5%	N/A	N/A	1,594,000	N/A
	1970	$24,640	1.7%	$23,000	5.5%	216,054	N/A	1,612,000	1.1%
	1971	$26,880	9.1%	$24,800	7.8%	293,361	35.8%	2,018,000	25.2%
	1972	$28,810	7.2%	$26,700	7.7%	346,046	18.0%	2,252,000	11.6%
	1973	$31,460	9.2%	$28,900	8.2%	329,461	-4.8%	2,334,000	3.6%
	1974	$34,610	10.0%	$32,000	10.7%	326,389	-0.9%	2,272,000	-2.7%
16	1975	$41,600	20.2%	$35,300	10.3%	369,678	13.3%	2,476,000	9.0%
	1976	$48,630	16.9%	$38,100	7.9%	454,688	23.0%	3,064,000	23.7%
	1977	$62,290	28.1%	$42,900	12.6%	466,187	2.5%	3,650,000	19.1%
	1978	$70,890	13.8%	$48,700	13.5%	491,974	5.5%	3,986,000	9.2%
	1979	$84,150	18.7%	$55,700	14.4%	477,526	-2.9%	3,827,000	-4.0%
	1980	$99,550	18.3%	$62,200	11.7%	377,664	-20.9%	2,973,000	-22.3%
	1981	$107,710	8.2%	$66,400	6.8%	271,244	-28.2%	2,419,000	-18.6%
	1982	$111,800	3.8%	$67,800	2.1%	189,345	-30.2%	1,990,000	-17.7%
	1983	$114,370	2.3%	$70,300	3.7%	278,007	46.8%	2,697,000	35.5%
	1984	$114,260	-0.1%	$72,400	3.0%	309,020	11.2%	2,829,000	4.9%
	1985	$119,860	4.9%	$75,500	4.3%	328,274	6.2%	3,134,000	10.8%
	1986	$133,640	11.5%	$80,300	6.4%	393,983	20.0%	3,474,000	10.8%
	1987	$142,060	6.3%	$85,600	6.6%	413,545	5.0%	3,436,000	-1.1%
	1988	$168,200	18.4%	$89,300	4.3%	454,814	10.0%	3,513,000	2.2%
	1989	$196,120	16.6%	$94,600	5.9%	435,521	-4.2%	3,010,000	-14.3%
	1990	$193,770	-1.2%	$97,300	2.9%	319,060	-26.7%	2,914,000	-3.2%
	1991	$200,660	3.6%	$102,700	5.5%	300,020	-6.0%	2,885,000	-1.0%
	1992	$197,030	-1.8%	$105,500	2.7%	304,810	1.6%	3,150,000	9.2%
<7yrs>	1993	$188,240	-4.5%	$109,100	3.4%	311,080	2.1%	3,427,000	8.8%
	1994	$185,010	-1.7%	$113,500	4.0%	350,360	12.6%	3,544,000	3.4%
	1995	$178,160	-3.7%	$117,000	3.1%	307,440	-12.3%	3,519,000	-0.7%
	1996	$177,270	-0.5%	$122,600	4.8%	344,830	12.2%	3,797,000	7.9%
	1997	$186,490	5.2%	$129,000	5.2%	379,070	9.9%	3,964,000	4.4%
	1998	$200,100	7.3%	$136,000	5.4%	432,650	14.1%	4,495,000	13.4%
	1999	$217,510	8.7%	$141,200	3.8%	464,050	7.3%	4,651,000	3.5%
	2000	$241,350	11.0%	$147,300	4.3%	470,730	1.4%	4,604,000	-1.0%
	2001	$262,350	8.7%	$156,600	6.3%	448,560	-4.7%	4,733,000	2.8%
11	2002	$316,130	20.5%	$167,600	7.0%	511,740	14.1%	4,974,000	5.1%
	2003	$371,520	17.5%	$180,200	7.5%	550,550	7.6%	5,443,000	9.4%
	2004	$450,770	21.3%	$195,200	8.3%	571,440	3.8%	5,959,000	9.5%
	2005	$522,670	16.0%	$219,000	12.2%	576,240	0.03%	6,180,000	3.7%
	2006	$556,430	6.5%	$221,900	1.3%	438,970	-23.8%	5,677,000	-8.1%
	2007	$560,270	0.7%	$217,900	-1.8%	292,420	-33.4%	4,420,000	-22.1%
	2008	$348,490	-37.8%	$196,600	-9.8%	381,420	30.4%	3,660,000	-17.2%
	2009	$274,960	-21.1%	$172,100	-12.5%	474,860	24.5%	3,870,000	5.7%
1	2010	$305,010	10.9%	$173,100	0.6%	416,520	-12.3%	3,708,000	-4.2%

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Annual Median Sales Price and Annual Sales Activity 1968 - 2020

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	Median Sales Price				Annual Sales Activity			
	CALIFORNIA		UNITED STATES[1]		CALIFORNIA		UNITED STATES[1]	
Year	Median	Year-to-Year % Change	Median	Year-to-Year % Change	Sales*	Year-to-Year % Change	Sales*	Year-to-Year % Change
2011	$286,040	-6.2%	$166,200	-4.0%	422,550	1.4%	3,787,000	2.1%
2012	$319,310	11.6%	$177,200	6.6%	439,790	4.1%	4,128,000	9.0%
2013	$407,150	27.5%	$197,400	11.4%	414,900	-5.7%	4,484,000	8.6%
2014	$446,890	9.8%	$208,900	5.8%	382,720	-7.8%	4,344,000	-3.1%
2015	$476,320	6.6%	$223,900	7.2%	409,410	7.0%	4,646,000	7.0%
2016	$502,930	5.6%	$235,500	5.2%	417,720	2.0%	4,838,000	4.1%
2017	$537,860	6.9%	$248,800	5.6%	424,890	1.7%	4,892,000	1.1%
2018	$569,480	5.9%	$261,600	5.1%	402,640	-5.2%	4,742,000	-3.1%
2019	$592,230	4.0%	$274,600	5.0%	397,960	-1.2%	4,765,000	0.5%
2020	$659,380	11.3%	$300,200	9.3%	411,870	3.5%	5,066,000	6.3%

1 Source: National Association of REALTORS®

52 Year Period
<11> Years Median Price Negative
41 Years Median Price Positive