

Home Price Analysis for Des Moines

By the Research Division of the National Association of REALTORS®

Executive Summary

With home prices rising strongly in most parts of the country, there has been widespread media coverage on the possibility of a housing market bust. A thorough analysis of the Des Moines metro market, as detailed below, reveals that there is very little danger of this. In fact, the local housing market is in excellent shape with a potential for significant housing equity gains, particularly for homebuyers who plan to remain in their house for the long run.

The local market has very favorable home price-to-income ratio and even better mortgage servicing cost-to-income ratio. The latter ratio is currently below the local historical average. It implies no widespread financial overstretching to purchase a home in the region. Any respectable gains in the local job market will translate into substantial home price gains. Furthermore, Des Moines is one of the few Midwestern markets with a positive net migration trend.

	Des Moines	Top 20 Metros	National Average	Comment
Price Activity				
Current Appreciation	2%	25%	13%	Modest
3-year Appreciation	12%	79%	32%	Modest
Affordability				
Home Price to Income Ratio*	1.5	3.8	2.3	Very Favorable
Mortgage Debt Servicing Cost to Income Ratio **	11%	30%	16%	Very Favorable
Local Fundamentals				
3-year Job Growth	1.7%	7.2%	2.4%	Favorable
Housing Starts to Total Employment	1.8%	1.0%	1.5%	Neutral
Net Migration	2,800	19,100	0	Favorable
Risk Factor	A higher usage of interest-only and ARM loans places a greater risk exposure to interest rate changes in upcoming years. Also an unexpected turn in the economy and a return to job cuts could strain the local market. But the region created over 5,000 jobs in the past 12 months to July, which is a very positive sign in minimizing risk factors. The region has very affordable mortgage debt servicing conditions, suggesting potential for respectable future price gains.			

* Income is per capita income times average number of person per household

** Servicing cost is the mortgage obligation relative to income at the prevailing mortgage rate

Price Activity

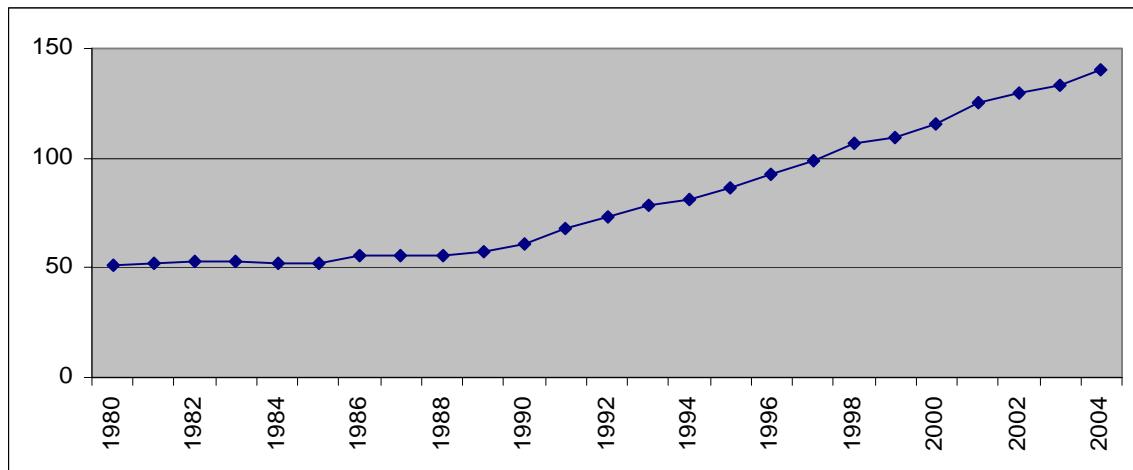
- The current price of \$145,100 is about 30% below the national average.
- The median home price grew by 5.5% in 2004 and by 12% in the past three years.
- Home price growth in recent years has been much weaker compared to the rest of the country. That also means there could be much more upside potential, particularly if the job market gets on track as recent data appear to imply.

Annual Data	2005*	2004	2003	2002	2001	2000
Existing Home Price (in \$thousand)	145.1	140.3	133.0	130.0	125.1	115.9
% change	3.4%	5.5%	2.2%	3.9%	8.0%	5.6%

Quick Glance	3-year Price Appreciation	Home Price-to-Income Ratio	Mortgage Servicing Cost to Income	Historic Local Average on Mortgage Servicing Cost	12-month job gain	Local price vs national
	12%	1.5	11%	14%	5,200	0.7

* 2005 price is as of second quarter and is usually a good estimate of the annual average price.

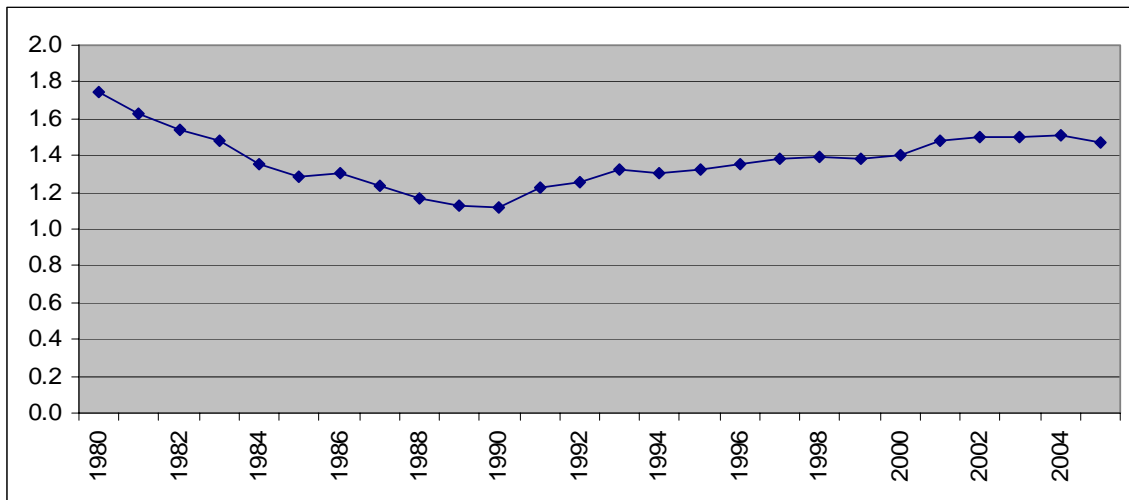
Home Price (in \$thousand)



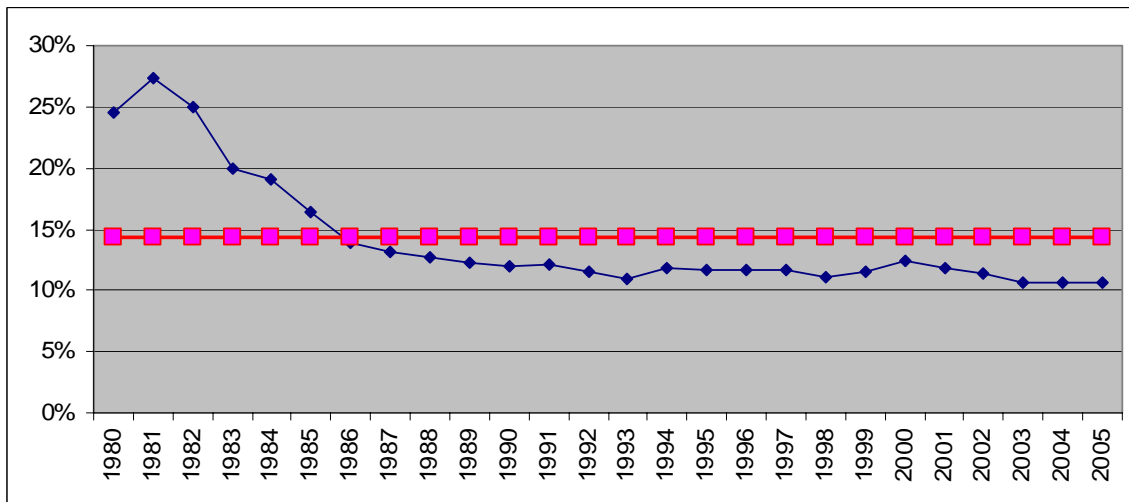
Affordability

- Affordability conditions are one of the best in the country. The price to income ratio has been remarkable stable over many years.
- Mortgage rates declining to 45-year lows have been a major force in boosting home prices in recent years. Lower rates allow homebuyers obtain a larger loan without necessarily increasing monthly mortgage payments.
- A more relevant measure for assessing the risk of a home price bubble is the median mortgage servicing cost relative to the median income. This ratio is well below the local historical average. It implies no widespread financial overstretching to purchase a home in the region. It in fact implies a capacity for a robust rise in home prices.

Price to Income Ratio



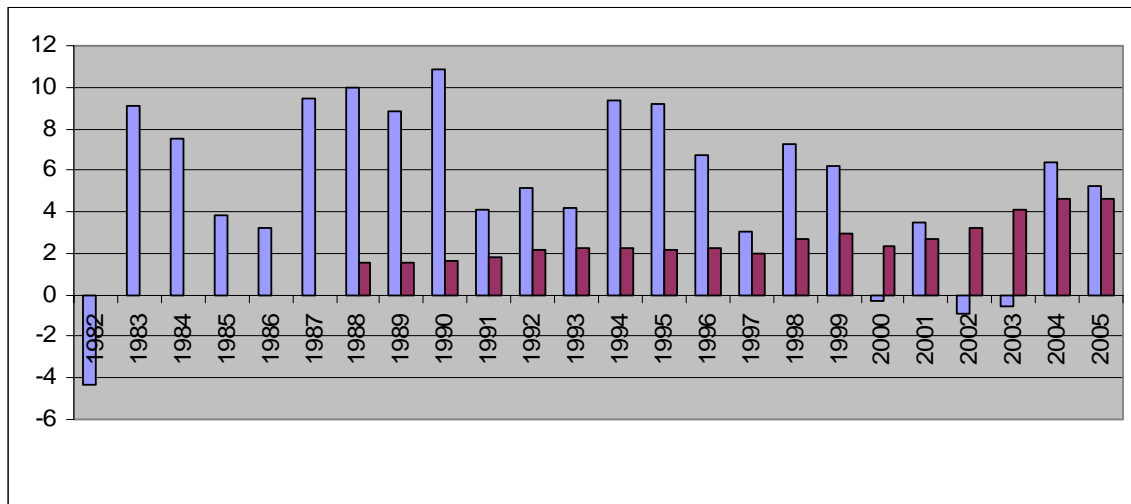
**Mortgage Servicing Cost to Income Ratio
(Historical average shown as square boxes)**



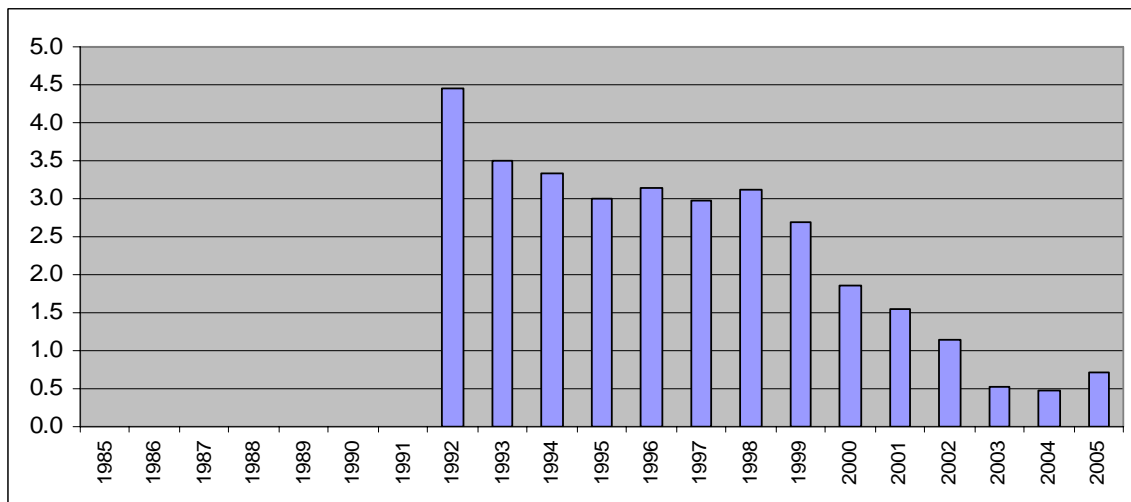
Local Fundamentals

- Jobs are returning. There have been 5,200 payroll job additions in the past 12 months to July. Many new job holders seek their own housing units.
- The region added in the past five years an estimated 24,000 new housing units of which 19,000 were single-family units.
- The ratio of five-year job gains to five-year new home construction shows the “hangover” impact of the housing shortage, or housing surplus. In our case, the local market is suffering from a mild housing surplus as the ratio is under one. With recent job gains and the expected continued economic expansion, the jobs-to-new home ratio will steadily improve.

Job Gains (light/blue) versus New Single-family Housing Starts (dark/red)

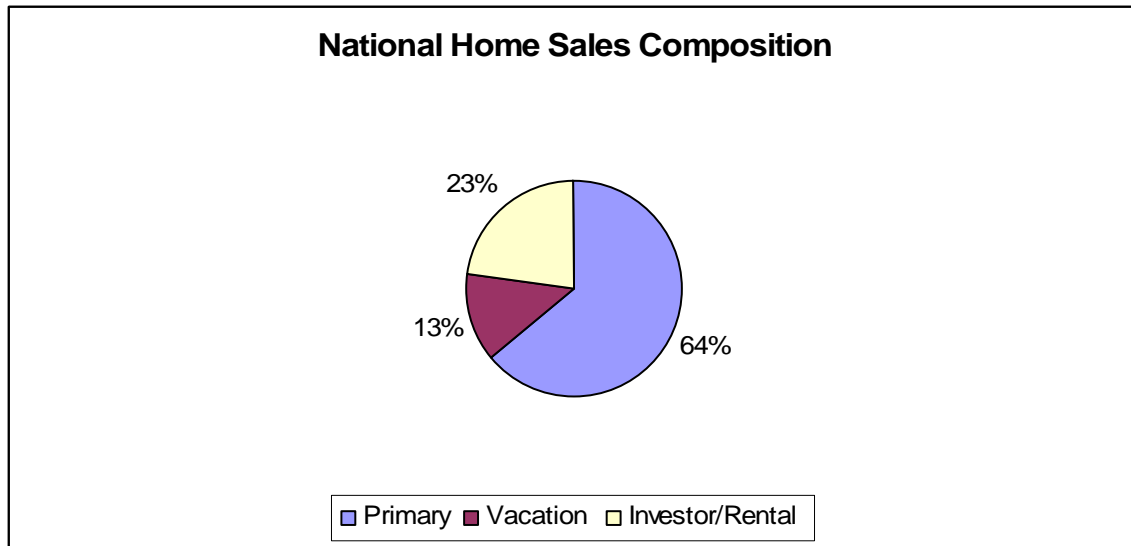


Ratio of 5-year Job Gains -to- 5-year New Single-family Home Construction



Other Factors

- ARMS and interest-only loans have risen across the country, including in large Ohio markets. Though data are not readily available, a similar trend is likely taking place in this local market. Therefore, some homeowners could feel the pinch of higher rates over time.
- The baby boomers in their peak earning years and have been active in purchasing second homes, which many consider their future retirement homes. The baby boomer impact could continue for another decade.
- With many top retirement destinations getting quickly unaffordable in the past five years, some retirees may turn to more affordable regions of the country. Similarly, investor purchasers could be forced to look for more affordable places. Perhaps, the local region gets a slight lift as a result.



Stress Test

- Price declines in the local market are unlikely according to our stress test.
- The local housing market will experience a price decline of 5% only under extreme unlikely scenarios of much higher mortgage rates. For example, mortgage rates rising to 19.5% in combination with 21,000 job losses could lead to a price decline.
- Various scenarios that could lead to a price decline of 5% are shown below.

Mortgage Rate	Job Gains/Losses
19.5%	-21,000
20.5%	-5,000
21.0%	2,000

- Such scenarios are highly unlikely. Most credible forecasts predict the region will create at least 10,000 jobs over the next 24 months and mortgage rates will hover around 7% by the end of 2006, which bodes well for future price gains.
- Even in the unlikely event of prices declining by 5%, most homeowners will maintain sizable equity build-up in their homes. The table below shows the home equity gains if prices were to fall by 5% by homebuyers at various years of purchase.

Year of Purchase	Housing Equity after 5% price decline (home price appreciation + principal payments on mortgage)
1980	\$112,077
1985	\$99,787
1990	\$89,610
1995	\$61,853
2000	\$27,508
2001	\$18,351
2002	\$12,111
2003	\$8,485
2004	-\$631
2005	-\$7,255

- Housing equity will most likely continue to accumulate to local homeowners. The equity gains under three price growth scenarios are presented below. One scenario assumes a historical conservative price appreciation of 1.5% above consumer price index inflation. With most credible inflation forecasts pegged at 2.5%, home prices can expect to rise by 4% per year under normal circumstances. The two other scenarios assume slightly below (1.5%) and slightly above (6.5%) the normal rate of appreciation.
- The local market is more likely to appreciate at an above-normal rate because of the current very attractive low mortgage servicing cost conditions.

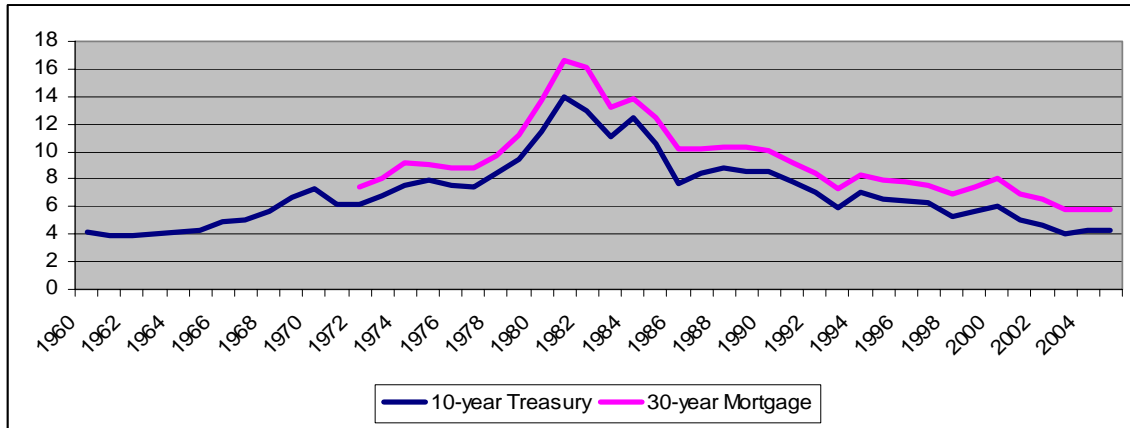
Housing Equity Gain			
Appreciation Rate	1.5%	4.0%	6.5%
2010	\$23,983	\$44,205	\$66,468
2015	\$46,946	\$93,335	\$150,924
2020	\$78,388	\$158,296	\$270,153
2030	\$165,551	\$341,832	\$655,518
2040	\$244,331	\$572,578	\$1,314,933

Additional Discussion Points

- Home price declines are very rare. In fact, the national median home price has not declined since the Great Depression of the 1930s. Stock market collapses, the OPEC oil crunch, economic recessions, and even wars have not negatively impacted national home prices since the 1930s.
- There have been few times when local prices declined. In nearly all these cases, the price declines were accompanied by sharp prolonged job losses. It is difficult to foresee a price decline in a job creating economy.
- Homes trade far less frequently than financial assets (about one home sale every 7 to 10 years for most homeowners). There are also larger transaction costs associated with selling a home due to the lengthy careful examination demanded by home buyers and sellers. Therefore, home prices are not prone to fluctuations as in the stock market. There are neither panic sells nor margin calls associated with homes.
- Many non-quantifiable factors could be important for this metro market in determining home prices. Access to cultural life, the quality of museums, nearby local and national parks, water views, exclusive neighborhoods, weather, the international airport, city vibrancy, restaurants, and a host of other non-quantifiable factors could have an important influence on the overall pricing.
- There are immense tax benefits to owning a home. These tax considerations were not considered in the analysis. For example, the 1998 law permitting primary owner occupants to trade down without having tax consequences. Also most home sales results in no capital gains tax. In addition, long-term capital gains tax rates were reduced in 2003, thereby providing higher return for home investors. These positive benefits, if accounted for in the analysis, would have shown an even stronger case for housing fundamentals in supporting home prices.

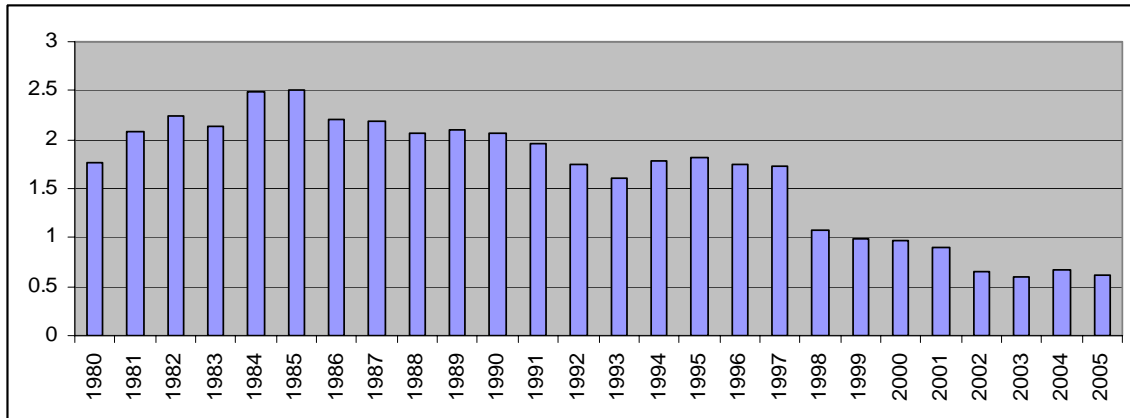
Additional Informative Charts

45-year Low Mortgage Rates



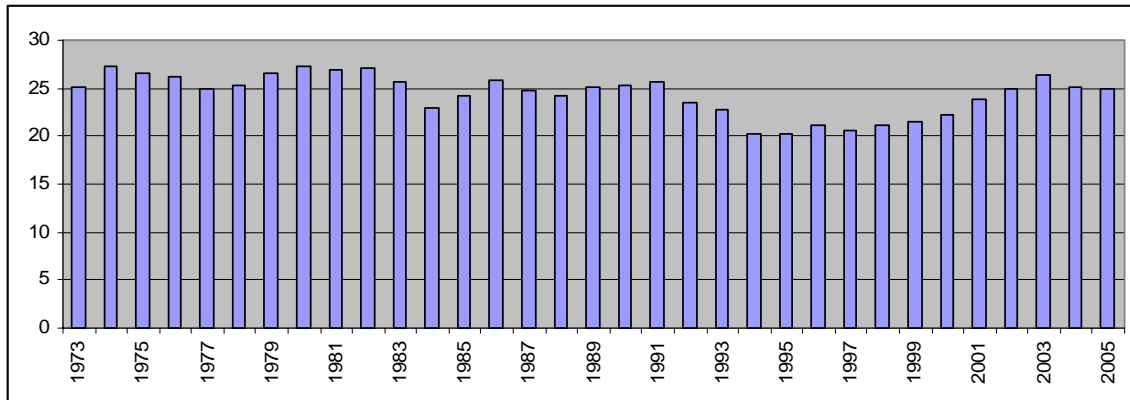
Source: Freddie Mac, Federal Reserve

Historic Low Fees and Points for Mortgage Origination



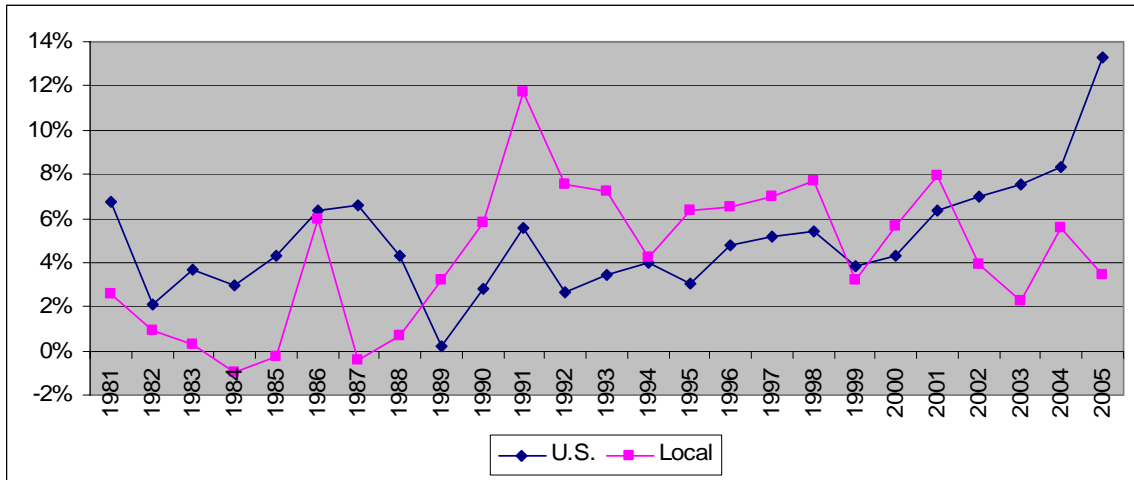
Source: Freddie Mac

Typical Down-payment Percentage Returning to Historic Norms



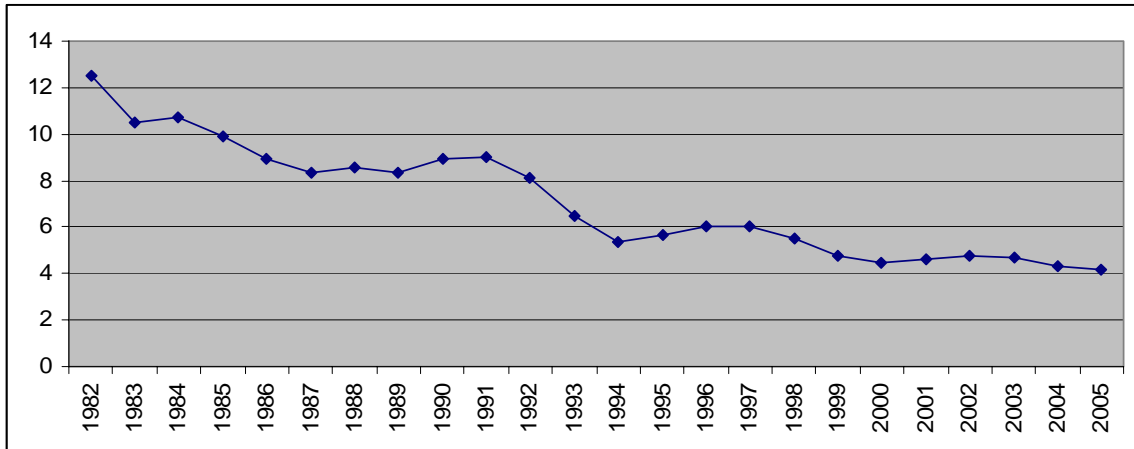
Source: Federal Housing Finance Board

Home Price Growth

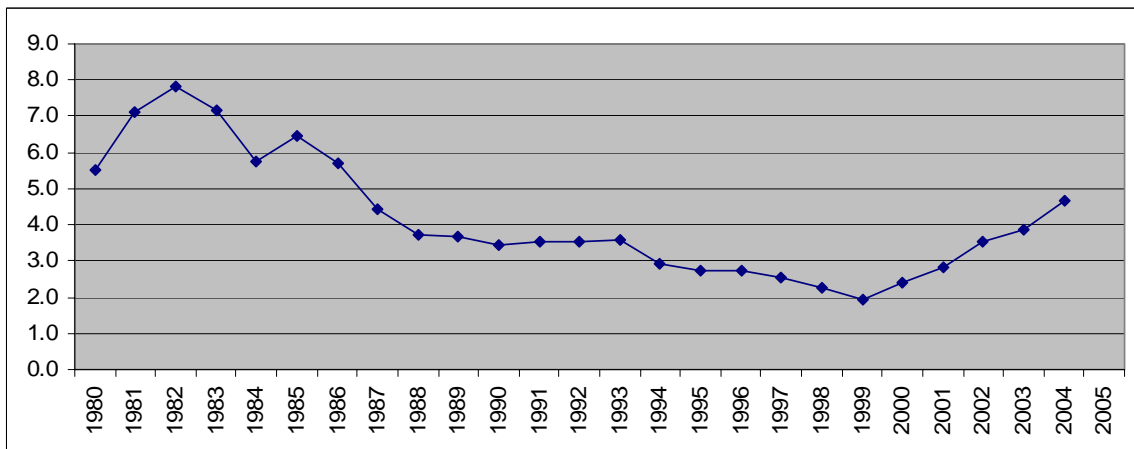


Historic Low National Months Supply of Homes on the Market

(The number of months it would take to sell all current homes on the market at the current sales pace)



Local Unemployment Rate



Source: BLS

NAR Research

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