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# Outlook sours for real estate

**Many indicators point to a major slowdown in home prices.**

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*By Les Christie, CNN/Money staff writer*

**NEW YORK (CNN/Money) - Did homeowners who sold in September get out just in time?**

The latest report on third-quarter home prices, released Tuesday by the National Association of Realtors, showed continued strength. But increasingly there are signs that prices have plateaued.

Of 147 markets tracked, 69 had gains from a year ago of more than 10 percent -- only six metro areas experienced declines.

But from the second quarter to the third quarter, the national median home price rose to $215,900, up just 3.8 percent. That contrasts with a 10.4 percent jump in the prior quarter.

And more and more leading indicators are pointing to a slowdown.

In Boston, real-estate investor Matthew Martinez reports recently having spoken to five condo converters. "They all said the party was over," Martinez said.

In Florida, Elena Filipa, vice president of the Corcoron Group in West Palm, said "We've leveled off. I would say prices will go up this year, but not as fast as they have."

None of this surprises the many economists who have been waiting for a downturn.

Richard DeKaser, chief economist for mortgage banker National City, has been reluctant to call the top, but thinks it has finally passed.

"We're coming down the other side of the mountain," said DeKaser.

The signs include:

**Builder pessimism** The builders DeKaser surveys are less optimistic than they were even a few months ago. Separately, one leading builder, Pennsylvania-based Toll Brothers, announced last week that expected demand for 2006 would be down, resulting in moderating price increases and fewer sales.

**New-home sales declining** DeKaser also notes that the number of new homes sold have fallen sharply since peaking in July at an annual rate of 1.3 million units.

DeKaser calls new-home sales (rather than existing-home sales) the canary in the coal mine. "Developers tend to be more sensitive to market conditions," he said. They have cash flow issues, payrolls, and loans that put more pressure on them to sell.

Ordinary home sellers are often more selective than developers, even taking properties off the market if they don't get the price they want. Developers have to drop prices to move inventory.

**Inventories rising** Supplies of new homes are way up, to nearly 500,000 units, from 350,000 a few months ago. "That's an all-time high for new homes," says DeKaser. The higher the inventory, the more likely prices will fall.

**Sell times are up** Houses are sitting on the market longer. New homes now take about 4.1 months to sell and existing homes 4.7; both figures are up substantially.

## What to expect

In a recent survey, NAR members say they predict home prices to rise only 5 percent in the next 12 months. Nearly half of the realtors predict prices will rise less than five percent and 6.4 percent actually expect prices to fall.

"You can't expect double-digit price increases to go on forever," said Walter Molony, spokesman for NAR. "We're seeing a market in transition in which there'll be an easing of price increases in the future."

While DeKaser expects a slowdown, he predicts an "orderly transition" for the most part, with some exceptions. "There will be busts in some markets," he said. "Mostly, we'll come out of it unscathed."

For the most part, DeKaser doesn't envision losses on that scale. He thinks home prices will decline 1.7 percent during the fourth quarter of 2005 and stay almost flat all the way through 2007.

But history shows that some over-valued markets could fare much worse.

Molony points out that the most severe drops in real-estate prices are usually triggered by an underlying economic crisis. After oil prices went into a six-year decline in the late 1970s, housing prices in oil cities experienced steep drops.

In Oklahoma City, prices plummeted 26 percent in real dollars from 1983 to 1988. With inflation, the "real" loss was more than 40 percent.

Houses in many oil patch cities are worth less in real dollars than they cost more than 20 years ago.

## How to protect yourself

It may already be too late to cash out at the top, which some residents of hot markets have already done. About 500,000 California residents moved out of state since 2001, according to economy.com, many to take advantage of lower housing prices elsewhere.

But houses are not really investments in the same way stocks or bonds are.

As an investment, timing the market is touchy -- miscalculate and it can cost you. If, for example, you cashed out a year ago in Los Angeles, expecting to buy back in at a lower price, you'd have to spend nearly 23 percent more for a similar house this year.

Add closing and moving costs and commissions and it could cost 30 percent more to get back into the market. Cashing out just doesn't make sense except for retirees or others in a position to relocate or downsize.

People looking to buy right now should shop carefully. Look at a number of homes, try not to fall in love, and be realistic about prices. Don't be afraid to bid low. The days of multiple bids may be over for a while.

With interest rates rising, try to get into a fixed-rate loan. Adjustable rate loans could adjust to a much higher level when they come due, making monthly bills much costlier. ARMs rates are so close to fixed at this point, it costs little extra to forego the risk of higher rates in the future.

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Just as the good times may be ending, the Chicago Mercantile Exchange is beginning to offer futures trading in home prices. For more click here. ■