



RADAR LOGIC OPINION

FROM THE CEO: August 2010

BEWARE THE “FALL” OF 2010

Moody’s housing economist Celia Chen has released a forecast of housing that is pretty dire. If the U.S. enters a double-dip recession, writes Chen, home prices could fall another 20% before stabilizing in early 2012. That compares to a baseline forecast that calls for another 5% decline in home prices and a bottom early next year. Chen puts the odds of a near-term double-dip at one in four. As observers of the actual housing market, while we cannot say these numbers are right, we certainly support Chen’s concern. However, we think the order of events will be reversed: it is our belief that housing prices will decrease in the autumn, perhaps precipitously, and that may cause a second dip in the U.S. economy.

History says the summer is the time of year that we see strength in housing, both activity and prices. This makes sense given the propensity of families to move in time for the school year. So, naturally, we look for activity, and thus prices, to strengthen during the summer and then soften in the fall. This year the numbers are somewhat distorted by the effect of the legislated tax credit. Much has been said about the impact of the home buyer tax credit. Our own view is that it has not done much to help. But we do agree with the consensus view that it has probably “pulled forward” some demand. If you were going to take advantage of lower prices, it makes sense that you would do so in a manner that also got the benefit of the tax credit. So we looked at what seasonal activity would have been without this “pull through.” To keep it simple, we assumed that 15% of the activity (transaction counts) came from this accelerated demand. By backing these transactions out of the actual numbers and comparing the pro-forma to history, we see some pretty alarming statistics.

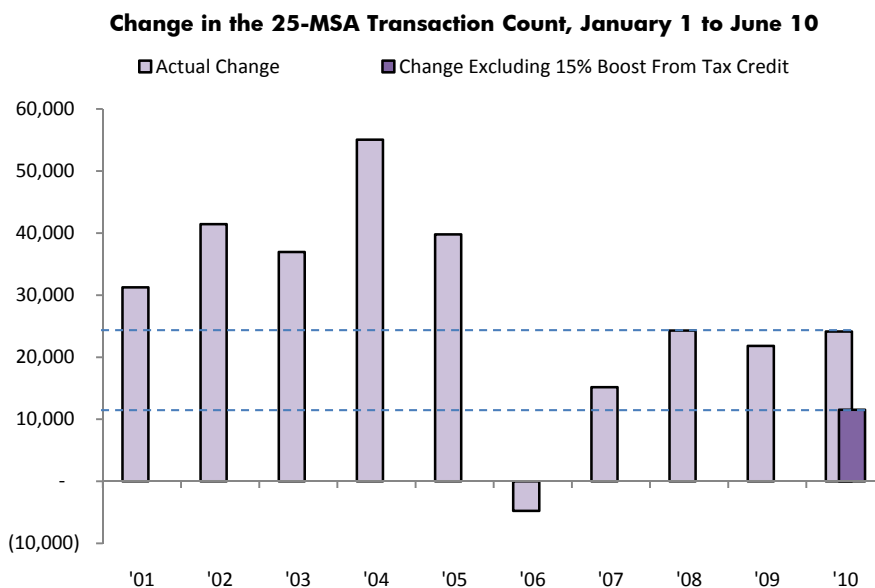


Figure 1: January-to-June change in the 25-MSA RPX transaction count for each of the last ten years. To illustrate the impact of the homebuyer tax credit on housing demand, the actual change in transactions in 2010 is shown alongside the change assuming June transactions were reduced by 15%. This reduction reflects an estimate of sales that would not have occurred in June without the tax credit.

If this analysis is even close, then the housing market dynamics are weak at best. RPX composite prices have not really moved since January of 2009. And if the pull through had any effect on prices, it was probably positive. Without it, activity remains well below history at a time when it should 'naturally' have been stronger. Add to this the overwhelming supply of 'distressed properties', those with delinquent or defaulted mortgages and the dynamics are bleak at best. There are simply too many homes for sale relative to the natural demand. And home buyers are not demonstrating any perceivable confidence that we have found the bottom, yet. As we begin to see the data for the fall, we expect it will be soft, that volumes and prices will move lower, perhaps precipitously.

If we need consumer confidence to generate the spending needed to revive our economy, housing does not seem to be a likely source. If anything, housing is going to make consumer psychology worse. If we are right, the odds of a double dip in the economy may well be more than one in four.

Of course, time will tell.

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