

January 24, 2010

## **Boone County Year End 2009 Real Estate Market Analysis**

**By Robert Wolverton, President R. Anthony Development Group, LLC**

As of the end of 2009, the market correction in the Boone County residential real estate market that began in July 2006 is over. The levels of sales we see in both pre-owned homes and new construction homes that we see today is our reality until there is something that significantly changes the demand side of the equation. We are right in the middle of the correction that is taking place in the commercial real estate market, which is going to get worse before it gets better. Hopefully, by the end of 2010, the commercial market correction will also be over and we can all get back to business.

A look at our market fundamentals is telling (see Exhibit 1). The unemployment rate in Boone County as of the end of November was 5.8% versus 9.2% at the state level and 9.4% at the national level. Our unemployment in Boone County is higher than at this time last year (4.2%), but still much better than the state and national rates.

The fixed 30 year mortgage as per a local bank website is 5.25% and has steadily hovered in the 5-5.5% range. At this time last year, the rate was 5.5%. This has been very stable for the last year and there is no reason to believe this will change significantly in the first half of 2010, if not longer. The prime lending rate is 3.25% which is the same as it was at this time last year.

The mean household income in Boone County is \$60,975. This level of income at today's lending rate indicates borrowing power of somewhere in the \$170,000 to \$190,000 range which shows why sales in the under \$300,000 price point have remained reasonably strong.

We do have areas of strength in our market, but there is no question that they are tenuous. Our inventory of detached single family homes for sale in the Columbia Public School District territory as of the time of this report was 679. There were 1,449 homes sold in the same area in 2009, which indicates a 5.62 months supply of homes on the market (see Exhibit 2). The inventory of new construction detached single family homes in the area was 106 versus sales of 170 in 2009, which indicates a 7.48 months supply of new construction homes on the market. Our inventory of single family detached homes is solid and should be of little concern.

Another area of strength is in the residential rental property market. Tightened lending requirements and a growing student population have combined to increase the number of renters in our market which has absorbed a large number of the vacancies we had just a few years ago. The anecdotal evidence I have received

indicates vacancy of less than 5% in well located, well managed, reasonably price rental units. However, poorly located, poorly managed, overpriced rental units remain with high levels of vacancy and will continue to do so.

Our areas of weakness are large and very concerning. First, our sales in 2009 of single family detached homes in the Columbia Public Schools territory was 1,449 versus 1,494 in 2008. Comparing our results in 2009 to 2008 is not terribly indicative of reality due to the volatility we witnessed in the last quarter of 2008 and the first quarter of 2009. So if we go back to 2007, there were over 1,800 sales in the same area and there were close to 2,200 as far back as 2004. The point of all of this is that we are at a time when the price of the commodities involved in real estate purchases (cost of money, cost of labor and materials for construction, and the cost of land) are all very affordable. We have homebuyer tax credits available, mortgage rates are down, construction costs are stable if not down slightly, and the cost of land is down from our peak years of 2004 and 2005. So why are our single family home sales down when all of the indicators show that it is a spectacular time to be a buyer? The answer is decreased consumer confidence due to higher unemployment and tighter borrowing standards.

Another area of weakness lies in the residential condominium market. In 2009 in the Columbia Public Schools territory, there were 159 condominiums sold and there are 128 on the market, which indicates 9.66 months supply of product on the market. This is high, but not such that a few good months will bring the supply in line. However, the new construction condominium market is very difficult. There were 27 new construction condominiums sold in 2009 and there were 44 for sale at the time of this report. This indicates a 19.56 months supply of product currently on the market. The problems in the condominium market lie in the availability of end financing for the homebuyer. The secondary markets and private mortgage insurance companies are scared to death of condominiums due to the issues of failed condominium projects in areas that were overheated during the boom years of 2004-2006. Because of this fear, the loan underwriter for a single end loan will place the entire project under great scrutiny including the homes association that manages the project. The secondary market entities and private mortgage insurers are placing requirements on condominium projects, particularly new construction condominium projects, that are extraordinarily difficult to meet. The bottom line is that the ability to get mortgage money for all condominiums, particularly new construction condominiums, is now very difficult to get through conventional lending channels. Therefore, end financing for the condominium market is falling to in-house lending through local banks. This decreases the amount of money available for end financing and also creates terms that are not nearly as strong as the terms of a detached single family home.

Another area of concern is a national withdrawal of capital from the commercial real estate market. It is difficult, if even possible, to accurately predict where the commercial markets will land. However it appears that there is a fundamental lack of trust in the valuations of commercial properties, which leads to a general distrust

of the balance sheets of the borrowers. The net affect of this is that the value of property and equity in property has become virtually irrelevant. The only measure that seems to have any relevance in the lending equation is cash flow. Therefore, properties that are speculative in nature and are not cash flow producing have fallen out of favor and are coming under great pressure.

We do have opportunities in our market for those with a high level of liquidity. The amount of inventory available in new construction single family homes is down to a level where there is little choice for those who want and can afford new construction. This has created a significant amount of homes that are pre-sold or custom build jobs. Most custom build jobs do not go through the Columbia Board of Realtors MLS, so it is difficult to know the actual number. However, in my current subdivision, I know that 35-40% of the homes currently under construction are pre-sold or custom build homes.

Another area of opportunity is in the rental property market. There are three areas that are steadily increasing the number of renters in our market:

- 1) A growing student population has driven the demand for student rentals higher over the last few years.
- 2) Tighter lending standards for homebuyers are pushing more people from the home buying market to the home rental market.
- 3) Many people who are here for a limited period of time who would have been buyers in the past have become long-term renters. Parents who a few years ago would buy a home to house their college age children or a doctor who is here for a three or four year stint in years past would buy a small home or condominium. Now, there is a higher level of concern about being able to sell the property when they are ready to move in a few years, so many have chosen the safer route of signing a long term lease.

We have to date shown great resilience in this market in the face of all of the national economic meltdown that has occurred over the last two years. The average home sale price in 2004 was \$158,621. The average home sale price in 2009 was \$164,327, which is an upward change of around 4% in five years (see Exhibit 3). The fact that our market has held its value in the face of a national economic meltdown is extraordinary. There are individual circumstances where people bought at the height of the market and were forced to sell at the bottom of the market who have lost money on their home. There are also individual circumstances where people bought a home that was over-built for their area who were forced to sell at the bottom of the market and have lost money. However, these circumstances are the exception and not the norm for our area. The main change that I perceive is that a person will need to own a home for a longer period of time before buying becomes advantageous to renting. The old rule of thumb is that a person needs to own a home for at least three years before the natural appreciation will increase the value enough to offset expenses of sale. During our peak time, I witnessed people owning a home for less than two years who had enough growth in value to offset expenses

of sale. Now, I believe that a person will need to own a home for four to five years before the natural appreciation of the home will grow the value enough to offset expenses of sale. This, of course, assumes the home was bought under normal circumstances and was not a forced sale or a "fixer-upper" where part of the growth in value is sweat equity.

There are three areas that I believe are threats to our market.

First, the unexpected loss of a significant employer would have a very detrimental effect on our market. There are a few employers that we all know are struggling and no one would be surprised if they were to go away. The market expects these jobs to go away, so the psychological impact of the job losses is not nearly as great as the unexpected loss of an employer.

Second, government policies made at the state and federal level can have an enormous impact on us at the local level. A few of the ideas currently being tossed around such as placing a tax on the banks to punish them for lending mistakes made in the past are nothing short of crazy. In a time when we desperately need liquidity, penalizing those who control our liquidity makes no sense.

Third, we have no margin for error in the new construction market. We cannot afford to misread short-term market conditions and mistake them for long-term trends. An example of this is in 2006, we had a great first quarter. This was mistaken to be a long-term trend, when in reality we were seeing pent up demand from a poor end to 2005 due to the after-effects of Hurricane Katrina. The second quarter of 2006 produced a huge number of new construction starts that were finished in the fall and winter of 2006. When our market peaked in July of 2006 and began its correction, we immediately had a large over-supply of new construction homes that took a very long time to absorb.

In our current market, we have seen an increase in single family detached home building permits in the City of Columbia (see Exhibit 4) from 237 in 2008 to 280 in 2009 (down from over 1,000 in our peak market years of 2004-2006). This indicates an 18% increase in the amount of new construction demand from 2008 to 2009. I do believe in taking our good news anywhere we can get it, but this increase is fool's gold. A significant number of building permits in the City of Columbia were pulled in the last few weeks of 2009 because the cost of building permits increased .25 per square foot on January 1, 2010. Therefore, a large number of these permits would have been pulled in 2010 but were instead pulled in 2009. The impact of this .25 increase is that a 1,800 square foot ranch style home on a basement with a two car garage would see an increase of approximately \$1,000 in permit fees. Therefore, I do not expect to see any increase in building permits in 2010 over 2009 and I would not be surprised if there is a decrease in permits in 2010.

I get asked regularly about the effectiveness of homebuyer tax credits. I believe homebuyer tax credits are highly successful, but maybe not for the reasons we first anticipated.

It is nearly impossible to tell if there are more sales or less sales due to tax credits. Homebuyers still have to have a down payment, good credit, good income, and confidence to buy a home whether or not there are tax credits available. It is also my theory that people do not buy a home for tax benefits. They buy a home because of life changes such as a growing family, a shrinking family due to death or divorce, children leaving the nest, health reasons, job changes, and many other reasons. So I do not believe that available tax credits have created any new buyers. In fact, the breakdown of homes sold per price range (see Exhibit 5) has seen a fairly constant percentage of home sales in each price category. The lion's share of the Boone County residential real estate market has always been in the under \$200,000 price point and I do not see this changing in the near future.

What I do believe is that the existence of tax credits and their impending expiration has encouraged some buyers who would have been 2011 buyers to move up to being 2010 buyers. This is a good thing for a struggling economy. I also believe that many have taken the tax credit and used it to buy the things that go along with buying a new home such as lawn mowers, blinds, appliances, or general home improvements. In years past, most buyers have to beg borrow and steal to get a down payment and closing costs, so these other items would go on credit cards or other short-term debt. Now I see buyers using their tax credit money to buy these items rather than going in debt. This is also a very good thing for a struggling economy.

Bottom line is that homebuyer tax credits are highly effective for removing money from the federal coffers and injecting the money directly into our economy. Any movement of money from federal control into private control is positive and should be supported.

2010 will be an interesting year to watch. I see us having a big first half of the year, due to the homebuyer tax credits that are due to expire at the end of April. The credit must be used by the end of April or a property must be under contract by the end of April and closed by the end of June in order to enjoy the benefits of the credit. Who knows whether or not Congress will extend the credit. However, anyone who is in the market would be foolish to allow this opportunity to go by unless they have no other choice.

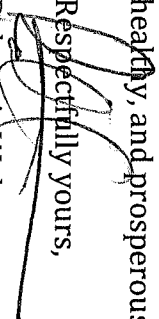
I also see that it is a great time to be a "move-up" buyer. A move-up buyer with a solid home to sell that is under \$300,000 will be selling to a market that is solid and moving into a market that is very soft. The market up to the \$250,000 mark is solid and in balance. The market from \$250,000 - \$300,000 is still solid, but not quite as good as below \$250,000. The market deteriorates some from \$300,000 to \$350,000. It is a great time to be a buyer and a tough time to be a seller for anything above

\$350,000. Homes that require a jumbo loan (anything above \$417,000) are hurting badly.

There is no reason to believe there will be any significant changes in sales volume in the residential market from 2009 to 2010. I see 225 building permits for single family detached homes in the City of Columbia and I do not see any new residential development for at least two to three years. I also see no reason that we will see any extraordinary change in market values for 2010.

My wife Christi, my daughters Katie and Lauren, and I wish each of you a happy, healthy, and prosperous year in 2010.

Respectfully yours,



Robert A. Wolverton  
President

R. Anthony Development Group, LLC

Exhibit 1

Boone County Real Estate Market Analysis  
Year End 2009

Market Fundamentals

2009                      2008

Unemployment

Boone County	5.80%	4.20%
Missouri	9.20%	6%
United States	9.40%	7.20%

Mortgage Rates

Fixed 30	5.25%	5.50%
Fixed 15	4.50%	5%
Prime Rate	3.25%	3.25%

Other Indicators:

Mean household income in Boone County	\$60,975
Median household income in Boone County	\$45,723

Sources: REDI website, local bank website

Exhibit 2

Boone County Real Estate Market Analysis  
Year End 2009

Analysis of Supply vs. Demand

Detached Single Family Homes  
Columbia Public Schools

Type	Closed in 2009	For Sale	Months Supply
Detached Homes - All Homes	1,449	679	5.62
Detached Homes - New Construction	170	106	7.48
Condominiums - All	159	128	9.66
Condominiums - New Construction	27	44	19.56

Source: Columbia Board of Realtors MLS

Exhibit 3

Boone County Real Estate Market Analysis  
Year End 2009

Average and Median Home Sale Prices

<u>Year</u>	<u>Average</u>	<u>Median</u>
2009	\$164,327	\$141,532
2008	\$172,263	\$147,000
2007	\$171,278	\$144,900
2006	\$170,506	\$142,900
2005	\$166,502	\$142,000
2004	\$158,621	\$133,500

Source: Columbia Board of Realtors MLS

Exhibit 4

Boone County Real Estate Market Analysis  
Year End 2009

Building Permits  
Single Family Detached Homes  
City of Columbia

<u>Year</u>	<u># Of Permits</u>	<u>Total Value</u>	<u>Average</u>
2009	280	\$46,958,005	\$167,707.16
2008	237	\$43,747,240	\$184,587.51

Source: City of Columbia website

Boone County Real Estate Market Analysis  
Year End 2009

Homes Sold per Price Range  
Single Family Detached Homes  
Located in Columbia Public Schools

All Homes

Year	<\$200k	% of Total	\$200k-\$299k	% of Total	\$300k-\$399k	% of Total	400k-\$499k	% of Total	Over \$500k	% of Total
2009	1,088	75.09%	237	16.36%	78	5.38%	26	1.79%	20	1.38%
2008	1,052	70.32%	297	19.85%	99	6.62%	26	1.74%	22	1.47%
2007	1,316	71.17%	364	19.69%	105	5.68%	39	2.11%	25	1.35%
2006	1,463	72.71%	348	17.30%	119	5.91%	54	2.68%	28	1.39%
2005	1,545	74.67%	351	16.96%	107	5.17%	41	1.98%	25	1.21%
2004	1,716	78.97%	282	12.98%	118	5.43%	38	1.75%	19	0.87%

New Construction Homes

Year	<\$200k	% of Total	\$200k-\$299k	% of Total	\$300k-\$399k	% of Total	400k-\$499k	% of Total	Over \$500k	% of Total
2009	111	65.29%	36	21.18%	16	9.41%	2	1.18%	5	2.94%
2008	113	50.22%	70	31.11%	31	13.78%	5	2.22%	6	2.67%
2007	211	55.38%	115	30.18%	38	9.97%	9	2.36%	8	2.10%
2006	304	61.04%	110	22.09%	53	10.64%	21	4.22%	10	2.01%
2005	358	65.09%	128	23.27%	36	6.55%	19	3.45%	9	1.64%
2004	440	77.46%	82	14.44%	36	6.34%	9	1.58%	1	0.18%