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The housing bubble: Part 2 - Delayed hangover from the last bubble

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There are some fundamental reasons for recent increases in prices, particularly when gauged over the last few years experience. These year-to-year price increases are measured from, what has been in many markets, historically low prices. Primary reasons for increases in prices are a return of consumer confidence and an increase in underlying demand. It is important to note that nationally, experts believe we need slightly over a million new housing units per year - on average. Housing completions last year totaled only 650,000 units, which was actually an increase over the several prior years.

Another factor affecting increased demand clearly is the historic low levels of mortgage interest rates. These interest rates have helped buyers enormously through increasing their monthly purchasing power due to the corresponding lower mortgage payments.

Timothy Warren, CEO of The Warren Group, has long been an observer of price and sales volume trends, nationally and in the local area. In reporting The Warren Group Home Price and Sales Statistics through June, he said "...the housing market continues to boom locally and nationally, as long as mortgage rates and home prices don't spike too high, we will see a very strong recovery of the market in 2013." He does point out, however, that "...no monthly median price has been this high for any month since August of 2007. Buyers have come out to the market in droves and are aggressively bidding up prices. While not a problem at this juncture, he hopes for more modest increases in the future - primarily because we don't want to see prices rise to the point where home ownership becomes unaffordable."

Reviewing these commentaries and the statistics which prompt them, clearly this is a time to carefully watch the trends and motivations of buyers. The year over year change in the Boston Metropolitan area, as reported in the Case-Shiller Home Price Index, is +7.5%. Although on the strong side, this is a well-justified and modest price increase for the local market which is recovering well. Noting some of the dramatic price increases in other markets nationally, including Las Vegas, Los Angeles, and Atlanta, it is important to realize that these are markets where prices dropped dramatically during the recent recession. This type of recovery may very well be a return to more stable and justified price levels in these markets.

The recent reports of strong increases in prices and sales volumes increasing steadily, is a sign that our housing markets are returning to a more stable and strong condition. The answer as to whether this is a dangerous bubble in the making will be seen in the figures from the next six to twelve months. Increasing supply, both in terms of REO properties released to the market and new construction can be expected. These responses to a constrained supply in the face of strong demand are the way free markets work.

In many ways we can look to government financial policies for the supports of this recovery. The concerns on the downside are how these supports will be eased out to allow the market to function on its own - and the degree of negative impact on demand and purchasing power. This could be the delayed 'hangover' from the last bubble.

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