- FEBRUARY 16, 2010

Foreclosures Seen Still Hitting Prices

By JAMES R. HAGERTY

More waves of foreclosures will keep downward pressure on home prices in parts of the U.S. over the next several years, two new studies project.

The studies—by John Burns Real Estate Consulting Inc. and Standard & Poor's Financial Services LLC—both conclude that most efforts to modify loans with easier terms will delay, not prevent, the loss of homes to foreclosure.

The Treasury Department is expected to give its latest update this week on government efforts to avert foreclosures.

The John Burns study estimates that five million houses and condominiums on which mortgages are now delinquent will go through foreclosure or related procedures that put them on the market over the next few years. That would represent the bulk of the estimated 7.7 million households behind on their mortgage payments.

This "shadow inventory" of homes expected to hit the market is enough to last about 10 months, based on the average sales rate over the past decade, the Irvine, Calif., firm says.

The problem is largely concentrated in Arizona, California, Florida and Nevada. The shadow inventory is equivalent to 27 months of sales in Orlando, 24 months in Miami and 18 months in Las Vegas, the study estimates.

Over the past nine months, home prices as measured by the S&P/Case-Shiller index have increased modestly after a three-year plunge. That is largely because efforts to avert foreclosures have slowed the flow of foreclosed homes onto the market, temporarily constricting supply.

John Burns, chief executive of the consulting firm, said investor demand for foreclosed homes remained strong. Thus, he said, prices were likely to be about level over the next few years, despite the looming foreclosure supply, if the economy continued to recover and mortgage interest rates didn't rise sharply. But if the economy slumped anew and interest rates jumped, he said, "that's going to cause prices to fall further."

The S&P study also says that the "overhang" of foreclosed homes expected to go on the market points to lower home prices.

Some borrowers are catching up on payments after having their loan terms modified, but S&P says current trends suggest that 70% of such borrowers eventually will redefault.

Loan modifications "may be helping marginally, but they are not going to solve the whole problem," said Diane Westerback, a managing director at S&P.

Loan servicers, firms that collect payments and handle foreclosures, seem to have "nearly exhausted the supply of plausible candidates for loan modifications" and will find that many loans are "unredeemable," the S&P study says.

As a result, servicers increasingly are looking to arrange "short sales," in which homes are sold for less than their loan balances.