REAL ESTATE

# The Great Housing Rebound of 2012: How the Fed Helped Sellers Beat the Odds

By Christopher Matthews | Dec. 27, 2012 | 11 Comments

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Construction crews work at the site of the Arista at the Crosby development in Rancho Santa Fe, Calif., on Dec. 21, 2012

Without a doubt, the U.S. housing market has been the most successful sector of the economy this year, and Wednesday's Case-Shiller home-price index report — which showed a fifth consecutive month of year-over-year increases in home prices nationwide — was a late Christmas present for homeowners across the country.

The housing-market "bottom" was one of the biggest business stories of 2012. After years of falling home values, the data clearly showed that the bleeding stopped somewhere in the first part of 2012 and that home prices have actually begun to slowly rise since then. In addition, other indicators like housing starts, new home sales and foreclosure statistics all point toward a healing housing sector.

These dynamics have gotten some economists and market analysts excited about the growth prospects for the U.S. economy in 2013. Robert Johnson, director of economic analysis for Morningstar, called housing "the big change factor in 2013″ and believes that "direct housing investment will be a meaningful contributor" to economic growth in 2013. He also sees industries related to housing — like furniture manufacturing and sales — adding to economic growth in 2013 as the housing market begins to pick up.

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There's no doubt that we're finally seeing the beginnings of what economists call a positive feedback loop when it comes to housing. Rising home prices allow lenders to be more generous with home financing, which allows even more prospective home buyers to access the market, further driving up home prices. And higher home values give consumers and builders more confidence to go out and spend money or make investments, which also stimulates the real estate market and broader economy.

**But with all this enthusiasm for the housing-market recovery, it's important to take a step back and think about the real driving force behind rising home prices.** Jonathan Miller, president and CEO of the real estate appraisal and consulting firm Miller Samuel Inc., astutely asks the question of how home prices can rise in an environment in which unemployment remains high, there is little growth in take-home pay, taxes seem poised to rise and lending standards continue to be tight.

One of the answers to this riddle, according to Miller, is the Federal Reserve. Record low mortgage rates, primarily (though not exclusively) due to the Fed's decision to buy up mortgage-backed securities, have done much to boost home prices. Last month I wrote about an analysis done by Tim Iacono of Iacono Research that illustrated just how significant Fed stimulus efforts can be when it comes to home prices. He showed that today's superlow rates can enable a home buyer to purchase a house that is 50% more expensive than she would have been able to afford under the average mortgage rates over the past 20 years.

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In addition, there is reason to be concerned that distressed home sales — like foreclosures or short sales — will hamper the housing recovery in 2013. Miller notes that distressed home sales began to increase yet again in the second quarter of 2012, as banks started to ramp up their foreclosure mechanisms after the resolution of the robo-signing scandal earlier this year. Homes sold under these conditions are usually done so at a steep discount, and large amounts of distressed properties on the market will drive down home prices more generally.

This is not to say that the recent trend of rising home prices isn't a good thing. It's very difficult to imagine a significant economic recovery in an environment of falling real estate prices, as a house is most Americans' single most significant asset. But any sober analysis of the recovery must admit that Federal Reserve stimulus is probably the single most important factor driving rising home prices. And until we see a significant drop in unemployment, or a significant increase in wages, we won't get a housing-market recovery that can sustain itself without unprecedented intervention from the central bank.

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