



Trends in the Virginia Housing Market Second Quarter 2009 Report

By

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Highlights

- In May, 72.5% of residents were able to afford a median priced home across the nation, the highest percentage in 18 years. Starts were up in May and June. Interest rates remained low and the Dow Jones Index increased during the second quarter. June saw an increase in the Consumer Confidence level; year-over-year, more people intend to purchase a home this year than last.
- The national economy continued to suffer in the second quarter. Year-to-date job losses totaled 3.4 million through the first half of 2009. A lagging indicator, the national unemployment rate reached 9.5% in June and will likely continue to increase. Foreclosures in the second quarter increased by the highest percentage in a single quarter.
- Like the rest of the country, Virginia lost jobs in the second quarter. Job losses totaled almost 3% from June 2008 to June 2009. The unemployment rate reached 7.2% in June but, Virginia's rate was the 11th lowest in the country and the lowest in the Mid-Atlantic. Starts in the south region have stabilized around 270,000 units per quarter.
- The existing home industry had a good quarter. Sales and median prices both increased in May while inventories declined. The new home industry had mixed results with decreased month-over-month sales in May but increasing median prices and essentially flat inventory levels.
- Virginia's second quarter home sales statistics indicated an improvement over the first quarter but are lagging behind 2008 and 2007 results. Sales are improving at the highest percentage level in the northern tier of the state but generally, prices are still on the decline almost everywhere.



National Economic Backdrop

Employment

In the first half of 2009, total non-farm payrolls declined by over 3.4 million jobs. While every month this year showed declines, the pace of job losses is slowing. In fact, losses declined by 37% from the first to the second quarters. Since December 2007, when the current recession began, the national economy lost nearly 6.5 million jobs.

Unemployment Rate

Not since August of 1983 have initial claims for unemployment reached June's 9.5% rate. During this decade, unemployment remained in the 5% range until August 2008 when it began to rise steeply and steadily. Unemployment across the nation has risen for the last nine consecutive months and fourteen of the last eighteen months. Unemployment is a lagging indicator and will not recover at the same pace as the rest of the economy as excess inventories are absorbed.

Dow Jones Index

The Dow Jones Index advanced 838 points during the second quarter of 2009 with particularly strong growth in April (+559) and May (+332). June recorded a slight decline (-53). The second quarter average was 8,331 - up 7% from the average of 7,757 in the first quarter.

Consumer Confidence

The Consumer Confidence Index surveys 5,000 households in the country about their confidence in the overall economy, both present and future. The overall

| Source: The Conference Board | Jun 09 | vs. May 09 | vs. Jun 08 |
|------------------------------|--------|------------|------------|
| Overall Index | 49.3 | -10.0% | -3.3% |
| Present Index | 24.8 | -16.5% | -62.1% |
| Expectations Index | 65.5 | -8.4% | 58.2% |

Index reached an all-time low since the surveys began in 1967 of 26 in March 2009. Overall consumer confidence rebounded in the second quarter with two strong increases in April and May. The June Index stands at 49.3, down 10% from May 2009 and 3.3% from June 2008. The Present Situation Index which measures how respondents feel about the current economy, at 24.8, was down 62% from last June. While the long term outlook as measured by the Expectation Index declined compared to May 2009, it registered a 58.2% increase compared to June 2008.



The Conference Board also surveys Americans about their home buying plans. In June 2009, the percentage of survey respondents who planned to buy a home within six months (2.7%) declined 3.6% from May but was 12.5% higher than in June 2008. Compare June to the 3.6% in August 2007. The percentage of respondents who plan to purchase a *new home* decreased by 25% in June from May and is down 40% compared to June 2008. Conversely, those respondents who plan to purchase an *existing home* increased in June by 6.7% over May and 14.3% year over year. The year-over-year increases signal improving conditions in the housing market.

Plans to Purchase a New Home

| Source: Fulton Research | Jun 09 | vs. May 09 | vs. Jun 08 |
|---|--------|------------|------------|
| Plan to Purchase a Home within 6 months | 2.7 | -3.6% | 12.5% |
| Plan to Purchase a New Home | 0.3 | -25.0% | -40.0% |
| Plan to Purchase an Existing Home | 1.6 | 6.7% | 14.3% |
| Uncertain | 0.8 | -11.1% | 60.0% |

Mortgage Modification Program

The success of the Treasury Department's mortgage loan modification program, announced in mid February and designed to help beleaguered homeowners avoid foreclosure, is mixed. The government allocated \$75 billion to subsidize payment reductions and provide incentives for servicers and borrowers to participate in the program. However, many borrowers did not qualify for the program if equity losses increased their loan to value ratio beyond acceptable limits. Program details continue to evolve, including the announcement in April that mortgage investors would be paid to decrease the interest rate set on second liens for risky loans made in the 2004 to 2007 timeframe. Freddie Mac sweetened the deal for its borrowers on July 1 by offering home mortgage refinancings of up to 125% loan-to-value ratios. Qualified borrowers must be current on existing Freddie Mac owned (or guaranteed) mortgages.

First Time Home Buyer's Credit

The First Time Home Buyer's Credit continued to develop. It was \$7,500 in 2008 and had a repayment requirement. It morphed into the current \$8,000 credit with no repayment requirement available to first time buyers who could close between January 1 and December 1, 2009. In late May, HUD announced that these funds could be used to pay closing costs and a portion of a buyer's down payment on FHA loans. However, there is a movement afoot to raise the credit amount to \$15,000 and allow all buyers to participate (not just low end, first time buyers). While partially intended to aid the new home industry, only those builders with

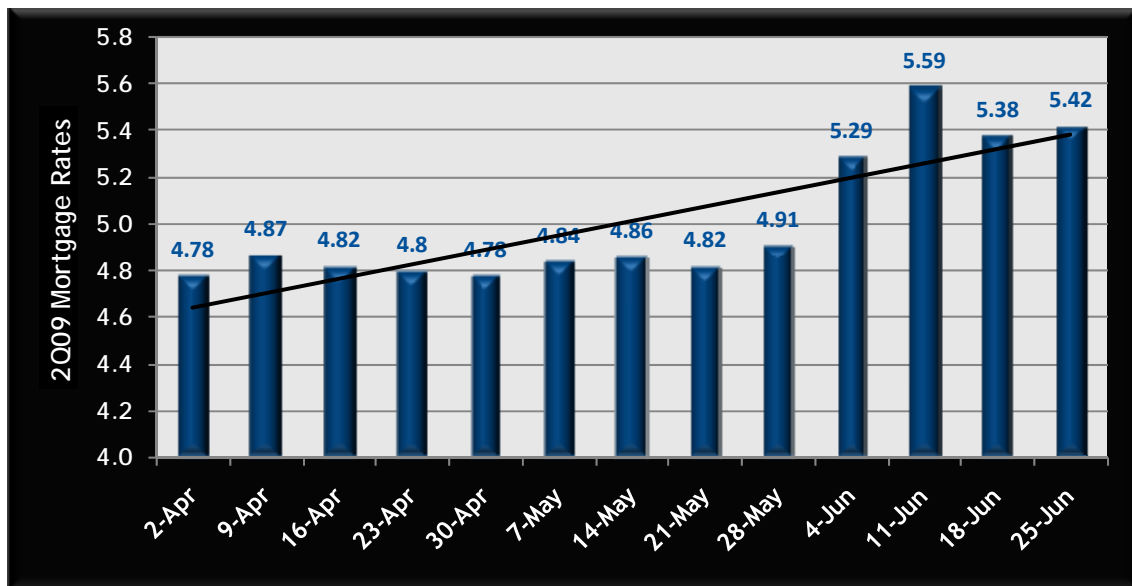


standing inventory can benefit from spurred demand at this late point in the year. (It is unlikely a new start would be able to close by December 1.)

Mortgage Rates

Mortgage rates were trending up by the end of the second quarter. Weekly conventional mortgage rates rose 13% from 4.78% in early April to 5.42% in late June. Rates hovered within 9 points of 4.78% for eight weeks but remained above 5% for the last four weeks of the quarter. Monthly rates followed a similar trend, up from 4.81% in April to 5.42% in June resulting in a year-to-date average of 5.05% which compares favorably to the 5.99% year-to-date average as of June 2008.

30 Year Weekly Conventional Mortgage Rates
2Q09



Source: Federal Reserve Board

Mortgage Delinquencies

Low mortgage rates in the spring helped to delay the expected onslaught of new loan defaults among the 564,000 outstanding adjustable-rate mortgages (ARMs). Monthly mortgage payments typically reset when either the debt exceeds some cap on the loan’s value or within a certain timeframe. Interest rate declines helped to stave off the rash of foreclosures but



the usual timeframe to reset is five years. Since most of the ARMs were issued between 2004 and 2007, they should begin to reset this year¹.

Housing Affordability

The percentage of US residents able to afford a median priced home surged 10 points in May to 72.5%, the highest point since the NAHB/Wells Fargo Housing Opportunity Index (HOI) series began 18 years ago. The underlying catalysts were low interest rates, declining home prices and the \$8,000 First Time Buyer's Credit.

Building Permits

Building permits reached an annualized pace of 563,000 units in June, 8.7% above May's revised figure but 52% below those issued in June 2008.

Housing Starts

Annualized housing starts fell to the lowest level on record in April 2009 (479,000 units) but increased 17% in May (562,000 units) and another 4% in June (582,000 units). In June, new construction was 46% below June 2008 levels. While encouraging, two months of increases may not represent the beginning of a strong recovery.

Foreclosures

In the second quarter, the United States posted the highest number of foreclosures recorded in a single quarter since the indicator began in 2005 thereby exceeding the previous high recorded just last quarter. New foreclosures increased by 11% compared to the first quarter of 2009 and by 20% compared to the second quarter of 2008.

USA Foreclosures

| 2Q09 | 1Q09 | 2Q08 |
|-------------|-------------|-------------|
| 889,829 | 803,489 | 739,714 |
| | 10.7% | 20.3% |

Source: RealtyTrac

Existing Home Market

Preliminary existing home statistics in May showed an annualized sales rate of 4,770,000 units, up 2% from April and down slightly from May 2008 (-3.6%). Median sales prices rose to \$173,000 in May, up 4% from April and down 16.8% from one year ago. The month's supply of inventory fell to 9.6 months in May, down from 10.1 months in April and from 10.9 months in May 2008.

¹ "New Wave of Mortgage Foreclosures may be Coming," DailyPress.com, July 14, 2009.



Price distortion (disproportionally high sales of distressed homes) plagues many areas in the country implying that a large percentage of homeowners are underwater. Recognizing that only 5% of the nation's owner-occupied homes will change hands, the large percentage of distressed sales is unduly warping perceptions about mortgage health and will continue to decrease median sales prices.

During the second quarter, establishing a protocol for appraisals became an issue at the NAR as real estate agents became increasingly aware of inconsistencies among appraisers on the use of distressed comparables and the affect they have on loan-to-value ratios and contract fallouts.

New Home Market

After strong sales in April, May new home sales declined slightly (1%) to an annualized rate of 342,000. That represents a 33.6% decrease over new home sales in May 2008. The median sales price for new homes increased for the second consecutive month (\$221,600, +4%) but prices were still 4.1% below the median last May. Inventories declined slightly but remain at the 10 month level.

NVR, Inc., a leading homebuilder in the state, recorded a 35% drop in revenue in the second quarter but a 2% increase in sales.

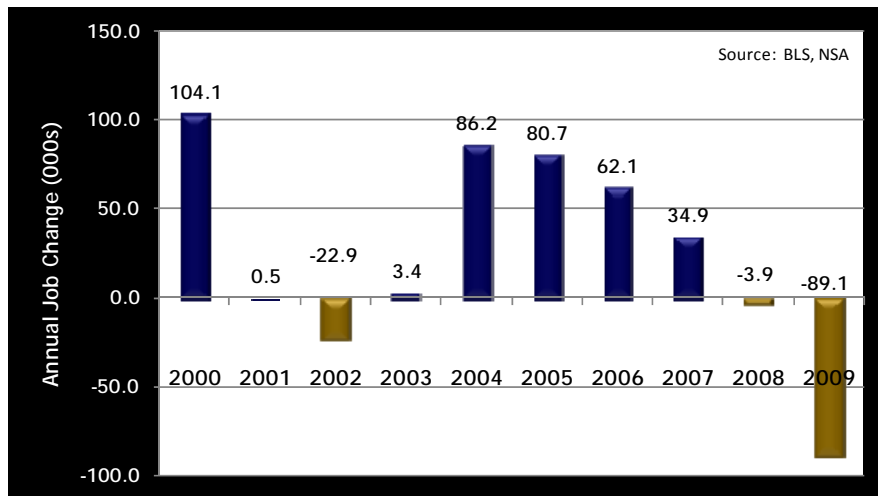


Statewide Economic Backdrop

Employment

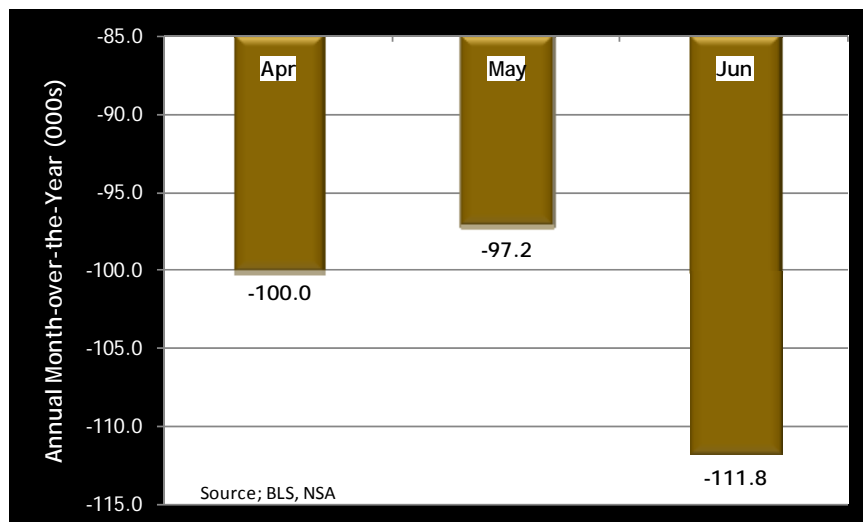
Through June 2009, the Commonwealth has lost 89,100 jobs, an enormous increase in losses compared to 2008 and to the rest of the decade.

Virginia's Annual Job Change: 2000 - 2009



In 2009, the trend established during the first quarter worsened. In fact, average monthly losses in the second quarter exceeded those in the first quarter by 27% and in June reached a milestone of -111,800 jobs.

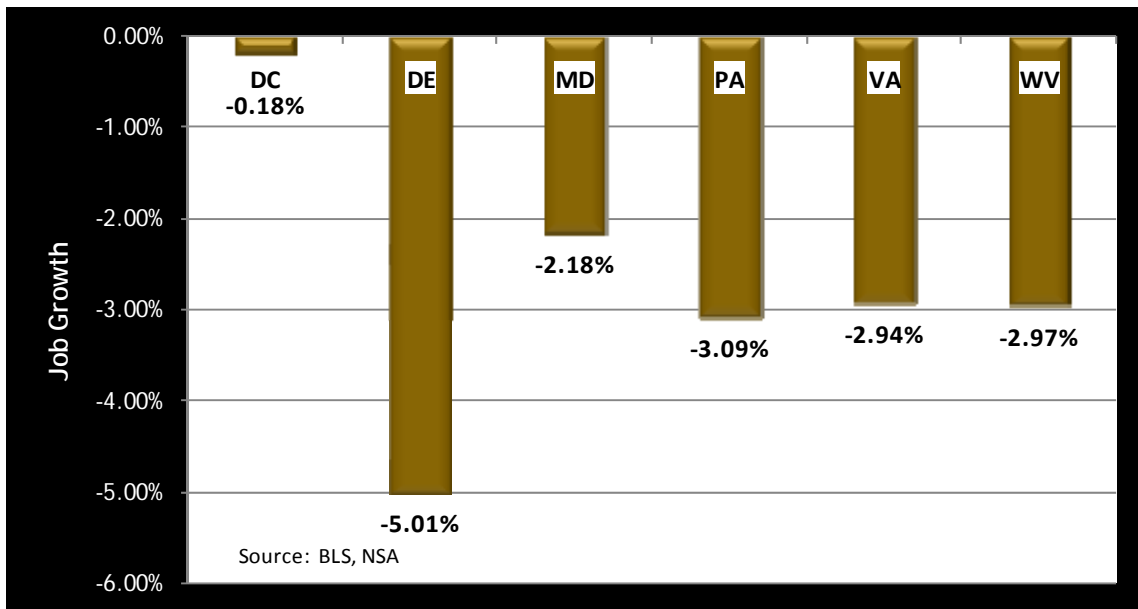
Virginia's Annual Month-over-the-Year Job Change: 2Q09





All of the jurisdictions in the Mid-Atlantic region that make up Virginia’s neighbors suffered job losses comparing June 2009 to June 2008. Virginia lost 2.94% which compares favorably to Pennsylvania, West Virginia, and particularly to Delaware.

**Job Growth: Mid-Atlantic Region
June 2009 vs. June 2008**



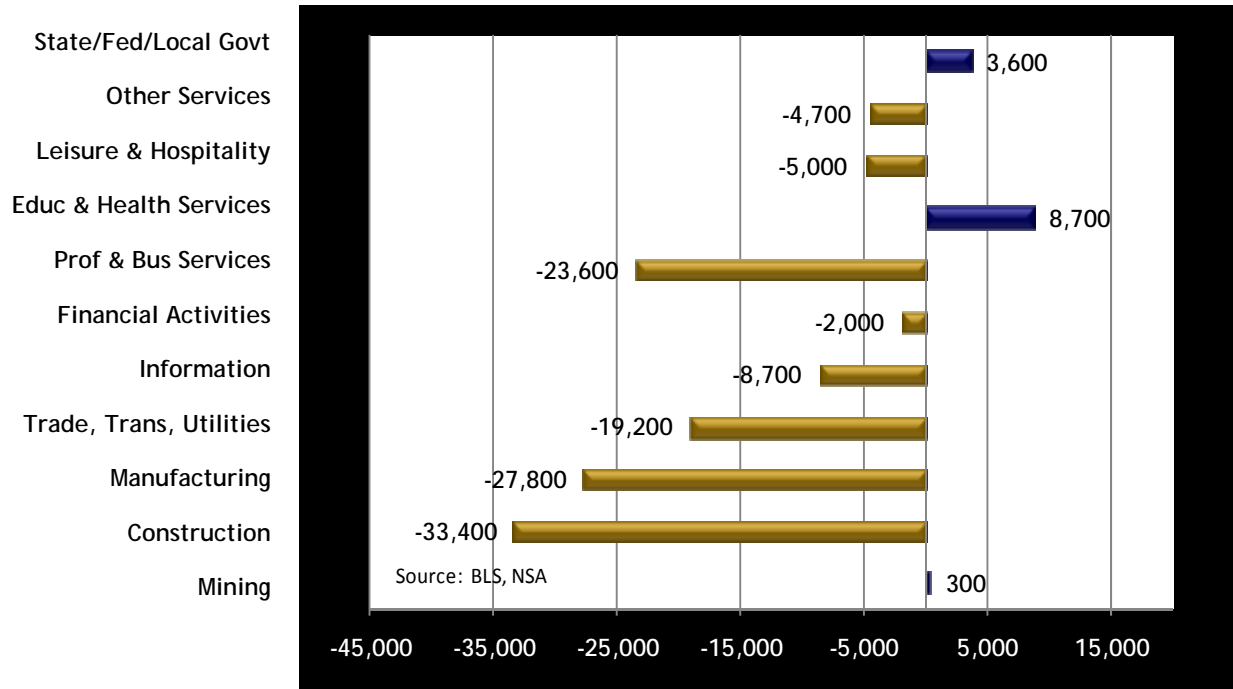
During the course of the second quarter, most of Virginia’s employment sectors saw improvement - including construction and manufacturing.

| Sector | 2Q09 Trend |
|---|------------|
| Mining/Logging; Construction; Trade, Transportation, Utilities; Financial Activities; Education/Health; Leisure/Hospitality; Federal Govt; Local Govt | ↑ |
| Manufacturing; Information; Professional & Business; Other Svcs; State Govt | ↓ |

However, compared to June 2008, every employment sector except for Government, Education & Health Services, and Mining/Logging has declined. The highest declines occurred in the Construction, Manufacturing and Professional and Business Services sectors, a recurring trend.



June 2009 vs. June 2008 Job Change by Sector: Virginia



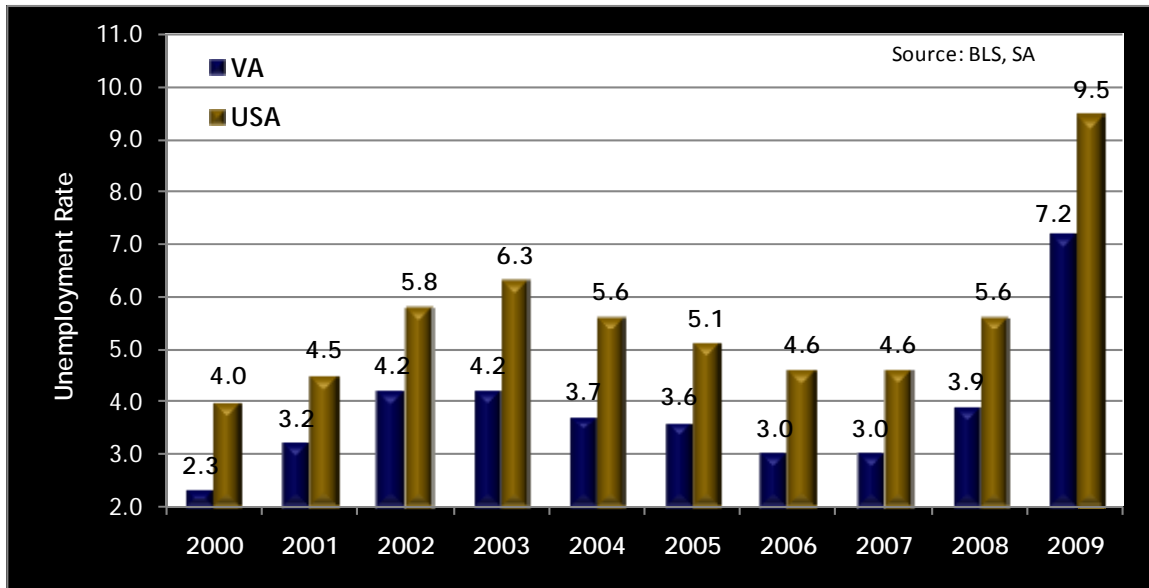
Unemployment

Unemployment in Virginia continued its upward progression in the second quarter, reaching 7.2% in June. It hasn't been this high since March 1983. For the sake of comparison, the monthly average since January 2000 was 3.8%. While troubling, it is important to look at the broader picture. The following graph illustrates the relationship between Virginia and the nation. The national unemployment rate is now at 9.5% and since 2000 has exceeded Virginia's rate by a minimum of 1.3% (2001) and a maximum of 2.3% (2009) in June. Even as it struggles, Virginia's economy continues to outperform other states. Virginia's 7.2% unemployment rate ties with Arkansas for the 11th lowest in the nation².

² States with the lowest June unemployment rates are North Dakota (4.2%), Nebraska (5.0%), and South Dakota (5.1%).

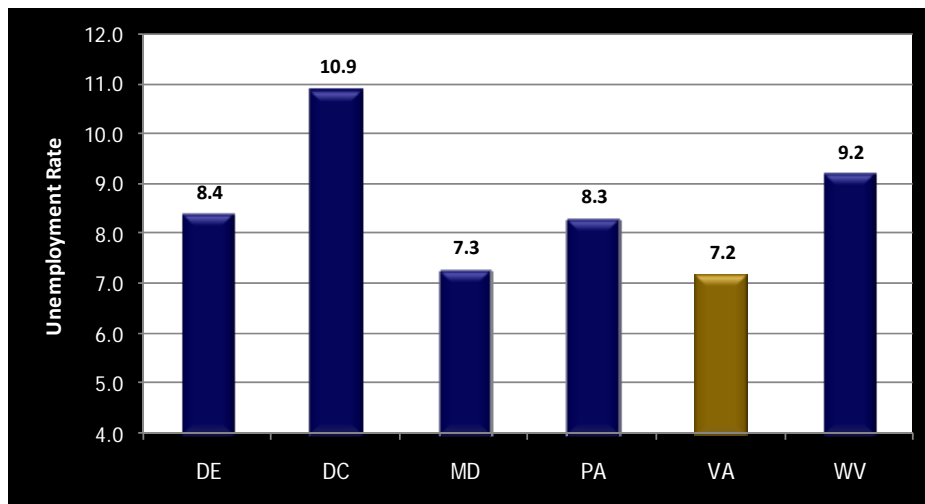


Virginia/USA Unemployment Rate: June of each Year



The graph below illustrates how Virginia is faring compared to the other states in the Mid-Atlantic region. In June 2009, Virginia again had the lowest unemployment rate among its five neighbors. The unemployment rate in the District of Columbia is approaching 11%.

Mid-Atlantic Unemployment Rate: June 2009

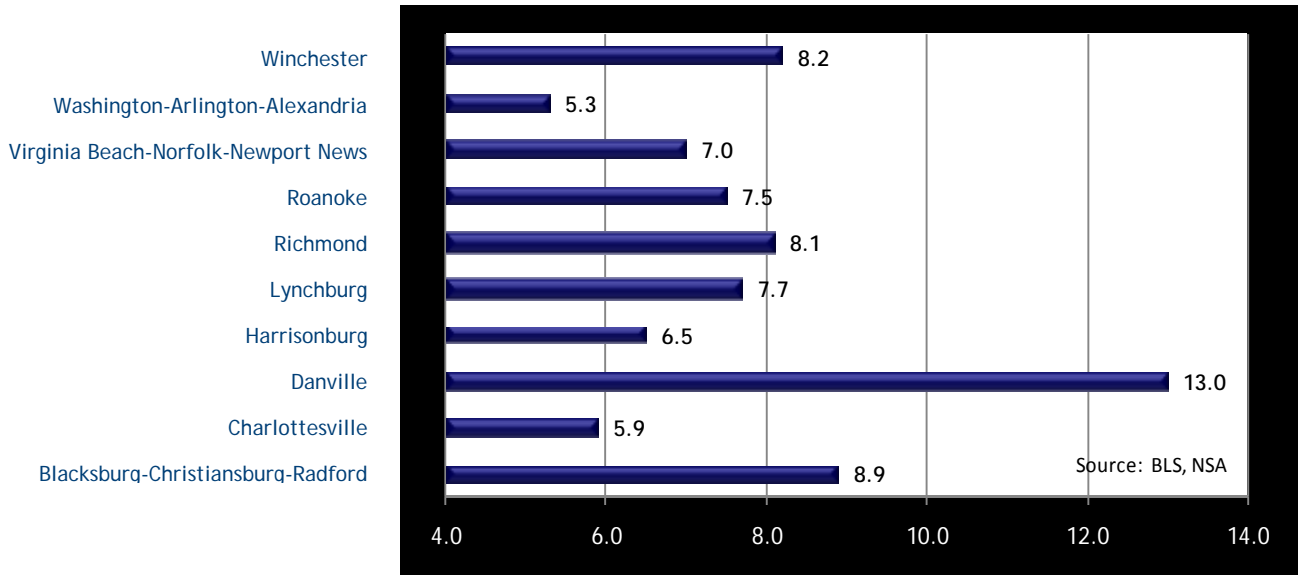


Source: BLS, SA



The following graph compares the June 2009 unemployment rate among the major metropolitan areas across the state. The Danville MSA, with its heavy manufacturing base, stands out for its atypical unemployment rate of 13%.

Virginia Unemployment Rate by Metropolitan Area: June 2009



Mortgage Delinquencies

According to the Federal Reserve Bank of Richmond, 17.63% of Virginia’s prime or subprime loans were ARMs as of March 2009. However, the highest concentrations are in Northern Virginia (27.02%), Winchester (15.86%), Charlottesville (12.69%), Virginia Beach-Norfolk (11.68%) and Richmond (10.96%). Other Commonwealth MSAs have less than 7% of outstanding ARM loans. Another potential foreclosure concern is the effect that declining equity will have on interest only loans. Again, it is a regional phenomenon centered primarily in Northern Virginia and Winchester. As of March 2009, 19.21% of the loans in Northern Virginia were interest-only. Of those, 4.55% were 90+ days past due in March and 4.01% were in foreclosure. Particularly worrisome is the situation in Prince William County where 7.15% of interest-only loans were 90+ days past due and 6.74% were already in foreclosure.

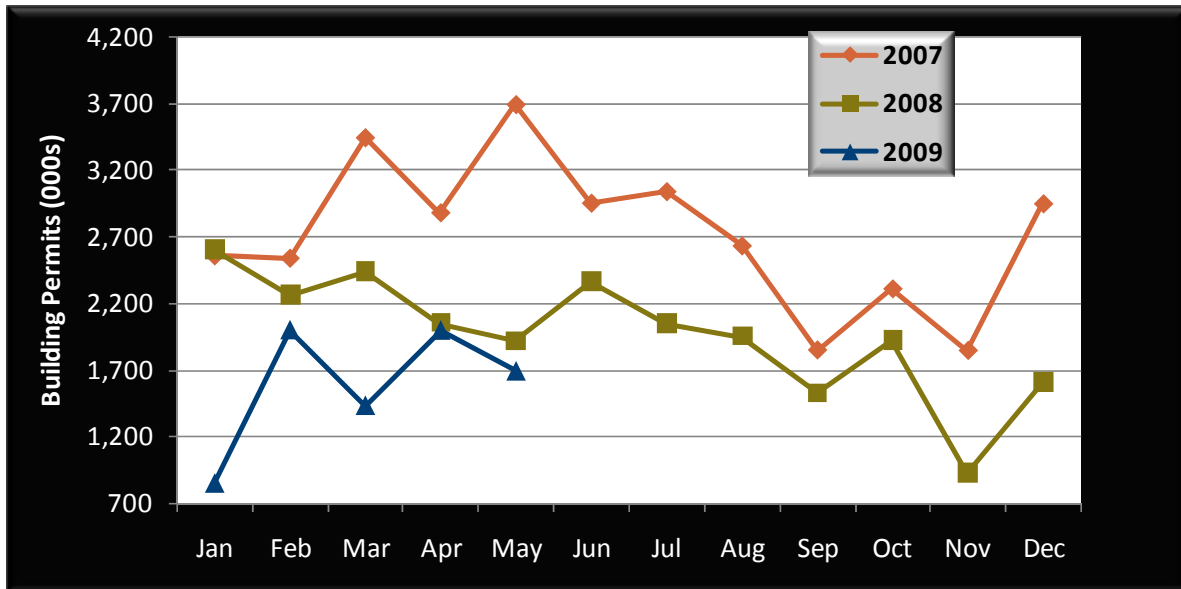
Building Permits

Trends in building permits are used as an indicator of upcoming activity in both the new home and existing home markets as existing home sellers frequently have a home to sell before buying a new move-up home. Building permits issued in 2009 across the state (as shown on the following graph) lag behind 2008 and significantly behind 2007 levels. Through May, the



number of building permits issued in Virginia during 2009 was 29.3% below the first five months of 2008 and 47.2% below those issued during the same period in 2007.

Building Permits: Virginia 2007/2008/2009

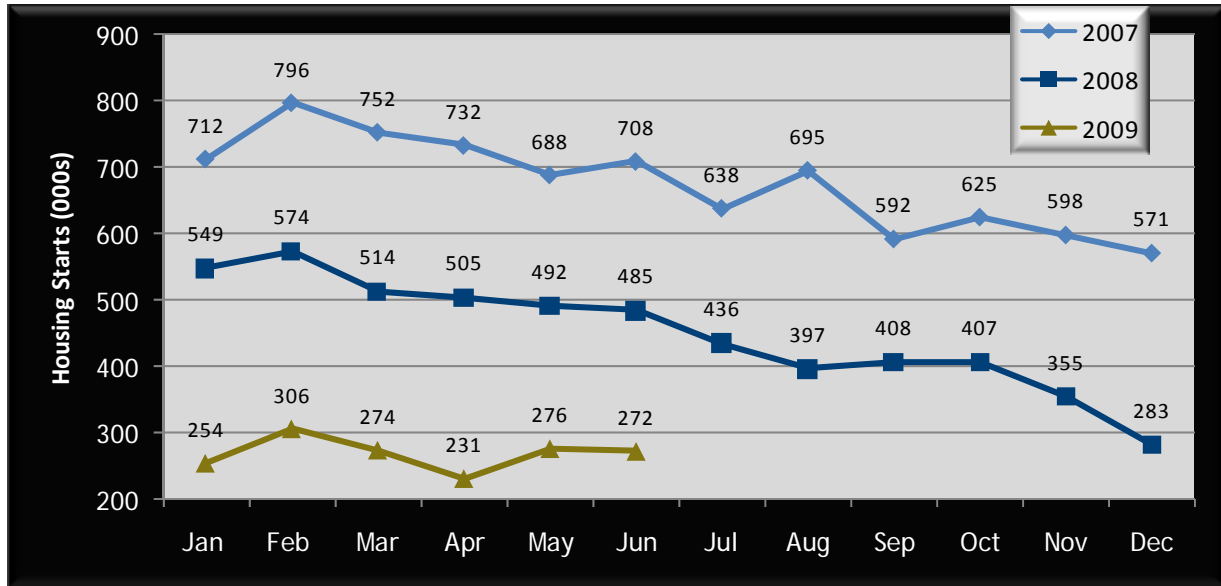


Housing Starts

Total quarterly starts in the South Region (of which Virginia is a component), declined 6.6% from the first to the second quarters but they seem to be stabilizing at around 270,000 units per month. The following graph clearly illustrates how dramatically the new construction industry has constricted over the last two years or so.



Starts in the South Region: January 2007 through June 2009

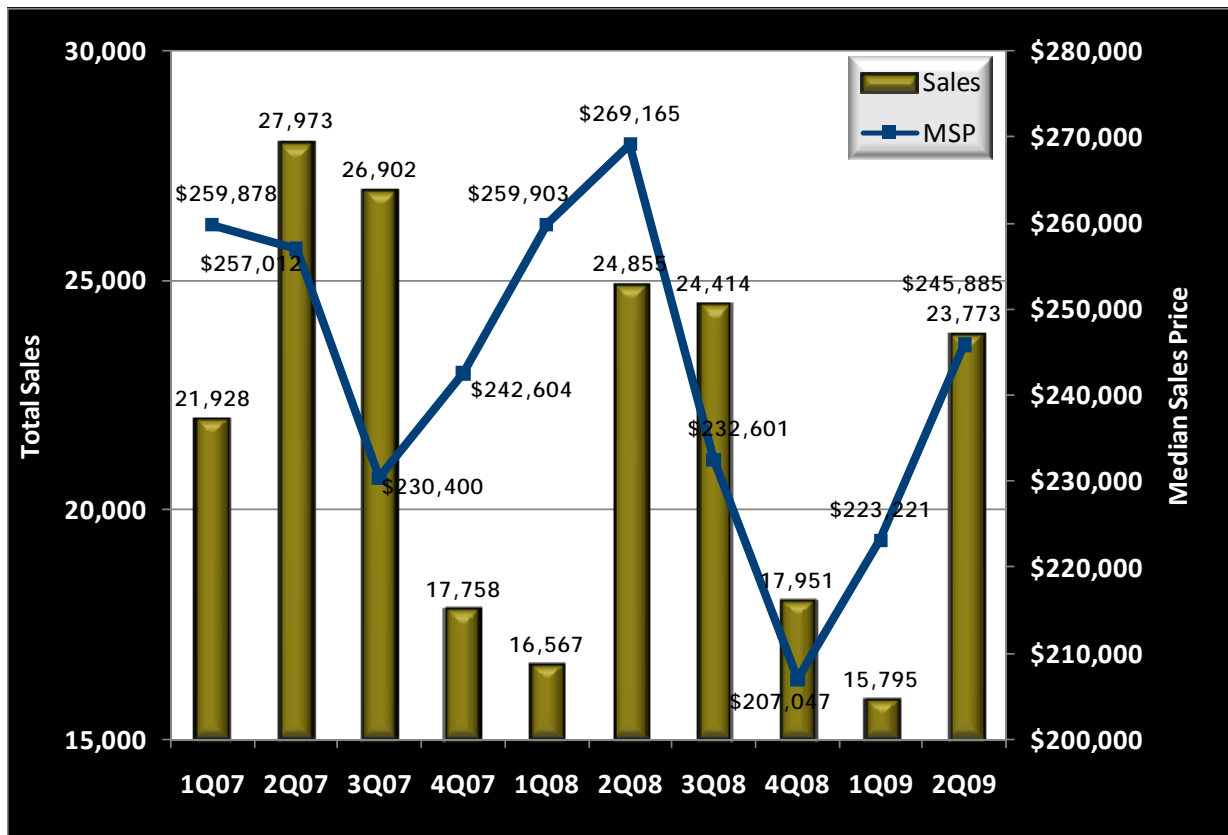




Housing Market Activity in Virginia

Although still lagging corresponding levels in 2008, statewide existing home indicators showed strong improvement during the second quarter of 2009 compared to the first quarter. But, for the last three years, the second quarter has had the highest sales volume of the year (please see graph below) suggesting that total sales will decline in the remainder of 2009. A good deal of the second quarter 51% increase in total sales (23,733 in the second quarter vs. 15,795 in the first) can be attributed to the first time buyer credit and normal cyclical sales patterns. Total sales were 4.4% lower than in 2Q08. Median and average sales prices followed a similar trend. Virginia's median sales price of \$245,885 was 10.2% higher than the median in the first quarter but 8.6% below the second quarter of 2008. The average sales price was 34.4% higher than in the first quarter and 10.7% less than corresponding 2008 prices.

Sales and Median Sales Prices
Virginia: 1Q07 - 2Q09





The local associations with the highest percentage sales volume increase year-over-year were Fredericksburg (+25.2%), Blue Ridge (18.7%) and Northern Virginia (+8.6%) - all in the northern tier of the state. Generally it is believed this area leads others and can serve as an indicator of what's to come for other associations in the future. However, median sales prices in the second quarter showed the strongest improvement on a percentage basis over last year at this time in Lexington/Buena Vista (+32.9%), Southern Piedmont (+10.3%) and Williamsburg (+6.3%). Average sales prices showed the highest percentage increase in Williamsburg (+13.2%), Southwest Virginia (+7.2%), and Southern Piedmont (+5.9%) compared to 2Q08.

Foreclosures

The following table summarizes the foreclosure activity in Virginia during the second quarter of 2009 by local association. Foreclosures across the state continued to climb - they were up 5.5% from the first quarter of 2009. The highest percentages of the total statewide foreclosures occurred in Northern Virginia (21.3%), Prince William (18.6%), and Hampton Roads (17%). The rural areas served by the Northern Neck, Southern Piedmont, South Central, and Eastern Shore associations all had around .1% of the total foreclosures in the Commonwealth.



| LOCAL MULTIPLE LISTING SERVICES | Apr | May | Jun | 2Q09 | % of VA Total |
|---------------------------------|--------------|----------------------|--------------|---------------|---------------|
| Blue Ridge Area | 196 | 219 | 179 | 594 | 3.5% |
| Charlottesville Area | 96 | 60 | 35 | 191 | 1.1% |
| Chesapeake Bay & Rivers | 37 | 32 | 24 | 93 | 0.6% |
| Dan River Region | 38 | 53 | 28 | 119 | 0.7% |
| Dulles Area | 377 | 291 | 470 | 1,138 | 6.8% |
| Eastern Shore | 12 | 6 | 5 | 23 | 0.1% |
| Fredericksburg Area | 453 | 455 | 428 | 1,336 | 7.9% |
| Greater Augusta | 24 | 20 | 2 | 46 | 0.3% |
| Greater Piedmont | 182 | 178 | 206 | 566 | 3.4% |
| Hampton Roads/Peninsula | 1,103 | 885 | 871 | 2,859 | 17.0% |
| Harrisonburg/Rockingham | 31 | 24 | 15 | 70 | 0.4% |
| Lexington/Buena Vista | 13 | 13 | 0 | 26 | 0.2% |
| Lynchburg | 46 | 44 | 12 | 102 | 0.6% |
| Martinsville/Henry/Patrick | 14 | 11 | 3 | 28 | 0.2% |
| Massanutten | 41 | 42 | 54 | 137 | 0.8% |
| New River Valley | 116 | 107 | 83 | 306 | 1.8% |
| Northern Neck | 8 | 5 | 0 | 13 | 0.1% |
| Northern Virginia Area | 1,360 | 1,198 | 1,031 | 3,589 | 21.3% |
| Prince William Area | 1,161 | 954 | 1,023 | 3,138 | 18.6% |
| Richmond Metro | 525 | 470 | 456 | 1,451 | 8.6% |
| Roanoke Valley | 231 | 138 | 89 | 458 | 2.7% |
| South Central | 30 | 18 | 14 | 62 | 0.4% |
| Southern Piedmont | 9 | 13 | 1 | 23 | 0.1% |
| Southwest Virginia | 9 | 6 | 3 | 18 | 0.1% |
| Tri Cities | 96 | 88 | 63 | 247 | 1.5% |
| Williamsburg | 30 | 42 | 87 | 159 | 0.9% |
| <i>Total</i> | <i>6,238</i> | <i>5,372</i> | <i>5,182</i> | <i>16,792</i> | |
| <i>Others</i> | <i>16</i> | <i>13</i> | <i>6</i> | <i>35</i> | |
| <i>2Q09 Virginia Total</i> | <i>6,254</i> | <i>5,385</i> | <i>5,188</i> | <i>16,827</i> | |
| | | <i>1Q09 Virginia</i> | | <i>15,943</i> | |
| <i>Source: RealtyTrac</i> | | <i>2Q09 vs. 1Q09</i> | | <i>5.5%</i> | |