Foreclosures and the State of the Housing Market in Alabama

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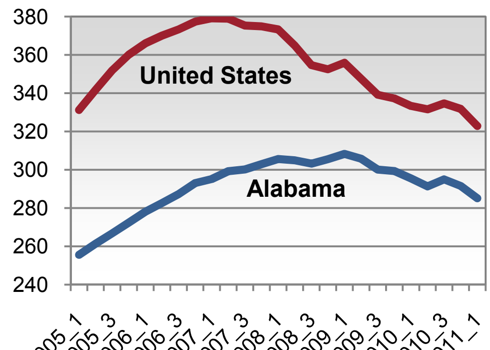
A key factor in the recession in the United States and Alabama has been the downturn in housing prices and subsequent drops in sales and construction activity. With the U.S. foreclosure rate at 4.63 percent in the fourth quarter of 2010 (and the seriously delinquent rate at 8.57 percent), foreclosures also remain a concern for struggling housing markets and economies overall (MBA National Delinquency Survey). While not hit as hard as such states as Florida, California, and Michigan, Alabama and its metro areas have been no exception to these problems.

As is true with most of the nation, housing prices in Alabama fell during the recession and have continued to fall since. The House Price Index compiled by the Federal Housing Finance Agency clearly shows that while Alabama and its metro areas did not experience as big of a boom as many parts of the country, their housing markets have shown continued decline following peaks generally around 2008. Data from the Alabama Center for Real Estate confirms this fact; the year-to-date peak median sales price for 2011 is down about 4.2 percent from 2010, and about 11.1 percent from 2008.

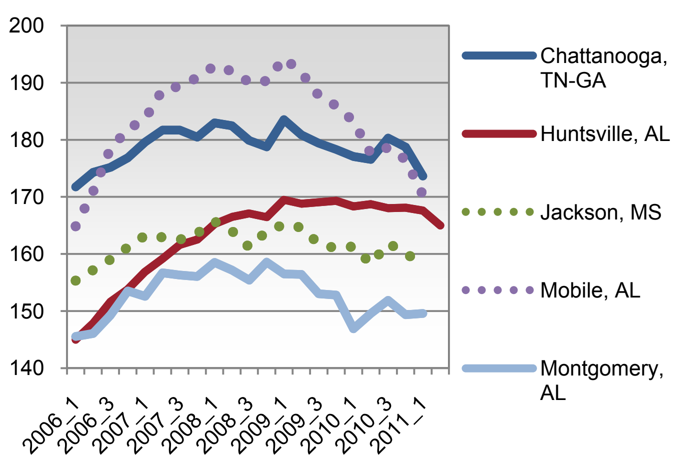
FHFA House Price Index



Source: Federal Housing Finance Agency.

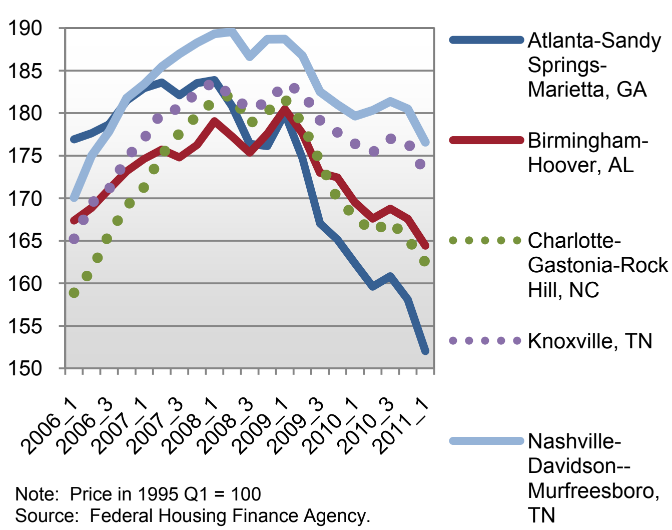
Looking more closely at Alabama's metro areas in the context of similarly sized metros in the Southeast, one sees the rise and fall of prices across metro areas over the last five years. Compared to similar metro areas (Atlanta is included, as the largest metro in the Southeast), Birmingham-Hoover's prices peaked among the lowest, but have taken a tumble similar to that of the other metros shown. Alabama's mid-sized metros are a mixed bag. Prices in Montgomery have remained relatively flat, while Mobile's peaked rather high, probably due to its coastal location and demand for vacation homes. While home values in Mobile continue to fall significantly, Huntsville's have remained steady following significant increases from 2006 to 2009. Huntsville's housing market is buoyed by a better than average unemployment rate and relatively high incomes brought by large proportions of professional and technical workers.

FHFA Mid-sized Metro House Price Indices



Note: Price in 1995 Q1 = 100
Source: Federal Housing Finance Agency.

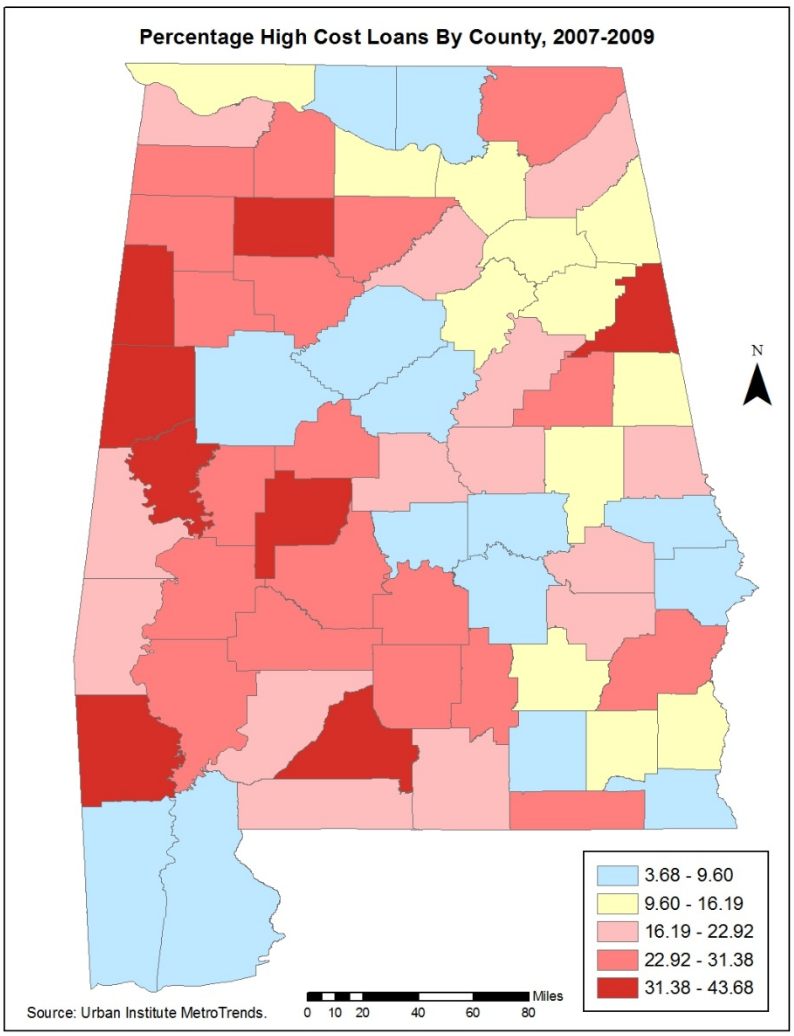
FHFA Large Metro House Price Indices



Note: Price in 1995 Q1 = 100
Source: Federal Housing Finance Agency.

Falling prices threaten to compound the problem of foreclosures. While not completely understood, foreclosure rates are believed to be related to a number of factors. Research indicates that falling home values increase the probability of foreclosure, due to the homeowner's loss of equity in the property. The trend of falling prices has probably been exacerbated by the fact that incomes have been largely stagnant since the recession. This, of course, has negatively affected demand for housing. Furthermore, studies on foreclosures have demonstrated that high-cost loans are more likely to end in foreclosure, even after controlling for other characteristics of the mortgage holder and the neighborhood they live in (Immergluck and Smith 2005).

A data set comprising all home purchase loans for structures of 1 to 4 units and manufactured homes in Alabama from 2007-2009 was compiled for this brief. Data indicates that most of Alabama's MSAs had a higher proportion of high-risk loans (defined as loans with rates of 3 points or more above the U.S. Treasury rate) than the nation as a whole. Proportions of these loans in Florence-Muscle Shoals, Gadsden, and Anniston-Oxford, in particular, were more than twice the U.S. rate. The state as a whole saw high risk loan rates of 10.06 percent from 2007-2009, compared to just 6.69 percent for the U.S. In addition, examining county-level data on high-risk loans illustrates that, in general, rural counties have a much higher proportion of these loans. While foreclosures may be less harmful overall in terms of their effect on property values and crime in less densely populated areas, their potential increase in Alabama's rural areas is still troubling.

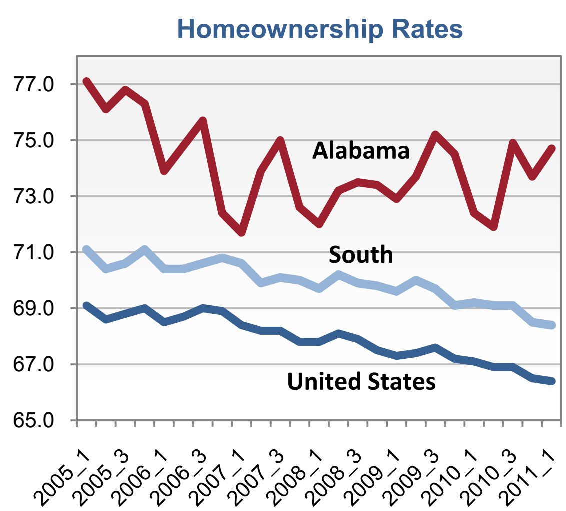


A predictive model for foreclosure rates created by the U.S. Department of Housing and Urban Development, which utilizes unemployment rates, percentage of high-risk loans, and the percent drop from the peak of the house price index, was also used to create foreclosure estimates for Alabama and its metro areas for the aforementioned set of loans. The model predicts Alabama's foreclosure rate at 6.24 percent, near the U.S. rate of 6.37 percent. Certain metro areas, such as Anniston-Oxford, Gadsden, and Mobile have higher foreclosure estimates.

	May 2011 Unemployment	Percent high risk loans 2007-2009	Percent change in FHFA house price index	Foreclosure Estimate
United States	8.7	6.69	-14.84	6.37
Alabama	9.5	10.06	-7.50	6.24
Anniston-Oxford	9.6	13.56	-9.09	7.02
Auburn-Opelika	8.1	6.30	-8.62	5.26
Birmingham-Hoover	8.8	9.74	-8.89	6.09
Decatur	9.3	12.04	-2.27	5.77
Dothan	8.7	12.69	-7.41	6.31
Florence-Muscle Shoals	8.5	15.26	-4.82	6.28
Gadsden	9.6	14.31	-6.69	6.82
Huntsville	7.9	4.08	-2.64	4.06
Mobile	10.6	8.71	-12.34	7.10
Montgomery	9.4	8.15	-5.68	5.67
Tuscaloosa	9.3	7.56	-6.30	5.62

Source: Alabama Department of Industrial Relations, MetroTrends, U.S. Department of Housing and Urban Development.

The housing bubble was relatively weak in Alabama; therefore, the state has avoided the full-blown foreclosure crisis a precipitous drop in values might have caused. However, the prospect of foreclosure rates remaining relatively high, or even increasing, in the state in the long term is a serious concern. Alabama's high home-ownership rate, which has remained several percentage points above the U.S. rate throughout the recession, increases its exposure to problems like foreclosures, since foreclosure rates that are similar to the rest of the nation will result in more foreclosures overall in Alabama. In addition, some studies suggest that areas with higher homeownership rates will have high foreclosure rates, because in these areas many residents who are not already homeowners may be more economically fragile and thus not good candidates for homeownership. This is to say that the population comprising marginal borrowers in such locations are likely less able to sustain long-term mortgage payments.



Source: Current Population Survey/Housing Vacancy Survey, Series H-111 Reports, Bureau of the Census,

Furthermore, some research suggests foreclosure rates and even economic performance in general of regions is related to such factors as sprawl and vehicle miles traveled (Lee and Gordon 2007). This is likely tied to the higher average transportation costs that accompany sprawl and higher VMT. Compared to other states, Alabama as a whole performs poorly on these measures; Alabama ranks 47th among states in per capita VMT. The state's metros also do not fare well compared to other U.S. metros. Therefore, if income growth and net migration struggle, the housing market will almost certainly continue to struggle as well, even if housing markets nationwide improve significantly.

All of these factors illustrate serious concerns about the trajectory of housing markets in Alabama. This is especially troubling considering the fact that metrics such as the unemployment rate have worsened or shown little improvement in the past few months. Therefore, positive labor market trends helping the housing markets seem unlikely in the near term. If high rates of foreclosure continue, they will strain housing markets, as short sales by banks as well as households exiting the homeownership market will hold prices down. This will in turn have a negative impact on new construction.

Alabama's traditionally low-density development and lack of development regulations helped the state avoid a large price bubble and a serious housing crash during the recession. However, in the short and long term, a number of factors threaten to create a drag on the Alabama housing market and, in turn, the economy as a whole. Leaders and policymakers should pay closer attention to the state of housing markets and, in particular, foreclosure rates in Alabama and its metro areas, and consider possible relevant interventions.

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