

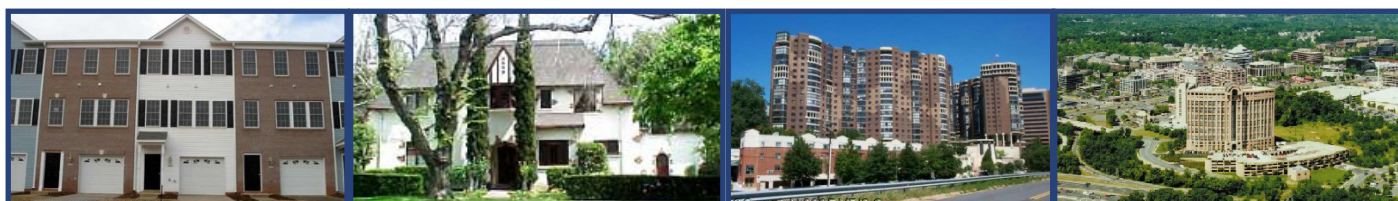
Understanding the Local Housing Market

or

Making the Case for Buying a House Now Before the Price Goes Up

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by
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MAIN FINDINGS

- The Washington DC area economy is one of the strongest in the nation. The region has generated more jobs over the past six years than any other major metropolitan area in the nation. Northern Virginia is a leader in the region, accounting for more than half of all jobs added to the Washington area between 2000 and 2006. This strong job growth will continue to support increasing demand for housing in the region.
- The Washington area's strong economy and nation-leading job growth resulted in a doubling of housing prices between 2000 and 2006. Since mid-2005, the region has experienced a deceleration in home price appreciation and July 2006 marked the first month in more than a decade that month-over-the-year home prices actually declined. Average prices were up just 1.96% in 2006.
- Housing market activity varies by housing type and jurisdiction. Condominiums have experienced the most significant price declines in late 2005 and 2006, while the average prices of single-family homes have been fairly flat. In addition, jurisdictions with more moderate housing prices continue to see gains despite regional price declines.
- The normalization of the region's housing market that began in 2005 will continue into 2007. Current trends indicate that the excess units on the market should be largely taken down by the first quarter of 2007 with price stability being achieved during the first half of 2007. Prices were up by 2.2% in the Washington DC metro area in March 2007.
- Housing remains a good investment for households in the Washington DC area. Long-term home price appreciation is 7%, substantially better than the rate of inflation or interest on U.S. Treasury Bonds. An annual 7% compounded rate of price increase over 10 years doubles the initial value. Housing is a sound investment because with only a small amount of equity, one can leverage a mortgage and the associated tax benefits resulting from the favorable treatment of home ownership.

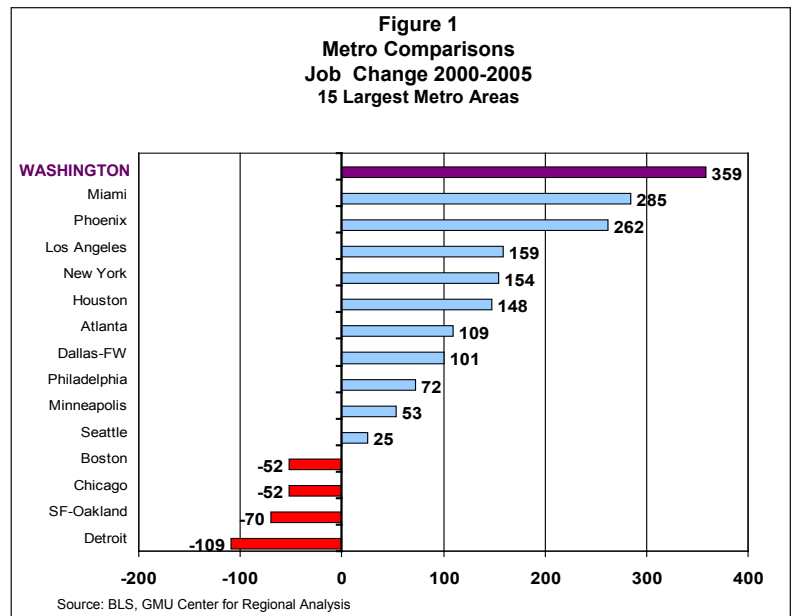
How does the Washington area economy compare to other areas?

The Washington area has generated more new jobs in recent years than any other metropolitan area in the nation (Figure 1) and is projected to grow faster than the U.S. economy over the next four years. Northern Virginia continues to outpace both the District of Columbia and Suburban Maryland in job growth. In fact, if Northern Virginia was considered a separate metropolitan area, it would rank 4th in job growth among all major metro areas in the U.S.

The Washington area economy remains one of the strongest in the U.S. in 2007. The region added 49,900 jobs in 2006, it has the lowest unemployment rate among major metropolitan areas nationwide, and it is projected to continue out-performing the national economy going forward as it has each year since 1996. The strong job growth will support increasing demand for housing in the region

What is driving housing prices?

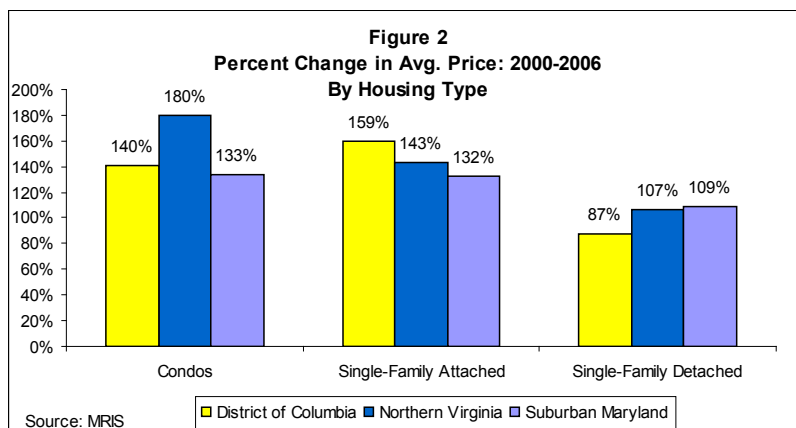
The Washington area rarely produces enough new housing to accommodate the demand generated by new workers moving to the region to fill its new jobs. Job growth and housing prices have been shown to have a .95 correlation; that is, areas with above-average job growth have rising housing prices. On average over the past 10 years, new household demand in the region has exceeded new housing unit production by approximately 15,000 units. This excess demand has driven housing prices up and has also driven many workers to markets outside of the Washington metropolitan area (e.g., Winchester, Baltimore) who would have preferred to live closer to where they work. Rising gasoline prices and growing traffic congestion



have refocused these commuters' desires to relocate back to the Washington area, further increasing the local housing demand and underpinning housing prices.

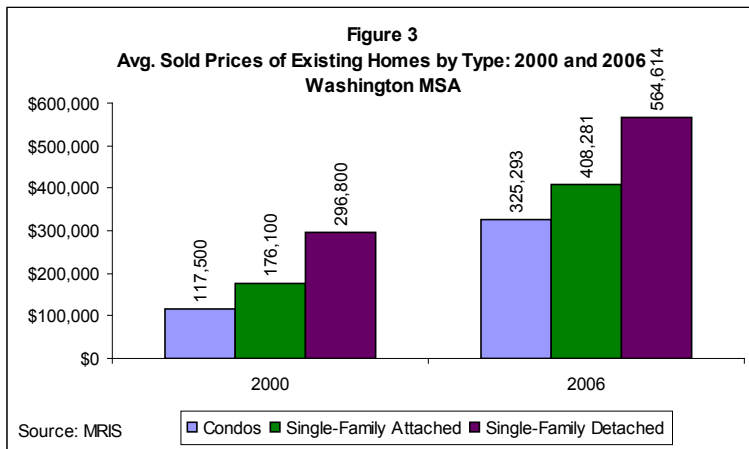
How has the regional housing market performed over the past six years?

The Washington area's strong economy and nation-leading job growth resulted in a doubling of housing prices of all existing units sold between 2000 and 2006 (112.8% increase). Some product types have experienced greater price appreciation than others. The condominium market accelerated fastest in the 2000-2006 period. The average price of a condominium in the Washington area grew from \$126,100 in 2000 to \$325,300 in 2006, an increase of 158%. The prices of single-family attached and single-family detached homes grew by 138% and 105%, respectively, between 2000 and 2006.



Different parts of the Washington metropolitan area experienced somewhat different patterns of home price appreciation (Figure 2). The average condominium price in Northern Virginia increased by 180% between 2000 and 2006, compared with 140% in the District of Columbia and 133% in Suburban Maryland. The District of Columbia had the fastest growing prices of single-family attached homes (townhouses), while Suburban Maryland had the fastest price growth among single-family detached homes.

Since mid-2005, the region has experienced a de-



acceleration in home price appreciation and July 2006 marked the first month in more than a decade that month-over-the-year home prices actually declined. During the first few months of 2007, average homes prices have rebounded a bit. Prices in March 2007 were 2.2% higher than in March 2006, following upticks in both January and February.

As an investment, housing values in the Washington area market have increased at an average rate of 7% annually over the past 28 years (Figure 4). This annual growth rate includes the gain of 21.7% in 2005 and two years in which the annual average housing price of units sold fell (1994, 1995) and four years where the average annual price gain was less than 2%. In each of the lower-performing years, the Washington area economy experienced below average job growth accompanied by near double-digit mortgage rates and high inflation. None of these negative fundamentals exists today or is projected to occur over the coming four years.

Recent trends in the housing market vary notably by product type and across jurisdictions. The percent change in the average price of existing single-family detached homes was -1.8% between March 2006 and March 2007. Prices of single-family detached homes were up slightly in January and February (Figure 5).

After five months of declines, prices of single-family attached homes rose in March. The average price of a single-family attached home sold in March 2007 was 5.5% higher than the average price in March 2006. Prices had been down 2% in February (Figure 6).

A substantial portion of the regional price adjustments in recent months is due to a softening of the condominium market; however, prices were up slightly in February and March. This jump is likely an anomaly and not a sign of the beginning of

a steady uptrend. Average condominium prices were 2.5% higher in March 2007 compared to March 2006 (Figure 7).

Prices of existing homes in Northern Virginia have dropped more than prices in the rest of the region. (See Figures 8 through 11.) The larger declines were observed because prices in Northern Virginia were generally higher than the rest of the region at the start of the transition period. In March 2007, home prices were down 1.4% over March 2006.

Suburban Maryland has weathered the recent downturn better than the rest of the region, mostly because of lower than average home prices in parts of Suburban Maryland outside of Montgomery County (Calvert, Charles, Frederick and Prince George's counties). In Suburban Maryland, only condominiums have experienced slight price drops in recent months. (See Figures 12 through 15.)

The District of Columbia housing market is more volatile than the suburban markets. (Average home prices fluctuate more in the District of Columbia because it is a relatively small market.) Prices in the District of Columbia have dropped more substantially than in the suburbs. However, in March 2007,

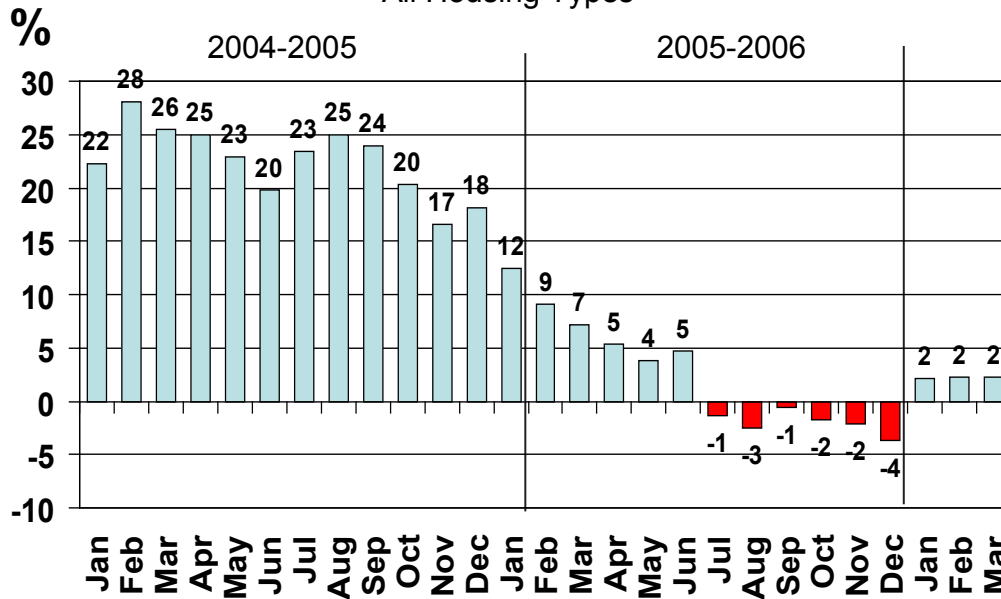
Table 1. Month-Over-The-Year Price Change Selected Washington Area Jurisdictions

Area	% Chg Mar 06 - Mar 07
District of Columbia	14.6%
Frederick County, MD	-4.5%
Montgomery County, MD	2.6%
Prince George's County, MD	0.3%
Arlington County, VA	-3.1%
Fairfax County, VA	-1.3%
Loudoun County, VA	-5.6%
Prince William County, VA	-6.4%
Spotsylvania County, VA	-7.2%
Stafford County, VA	-1.6%
Warren County, VA	4.3%
Alexandria City, VA	7.2%
Washington MSA	2.2%

Source: MRIS

Figure 4
Average Sales Price Percent Change
Month-over-the-year, 2004 - 2007

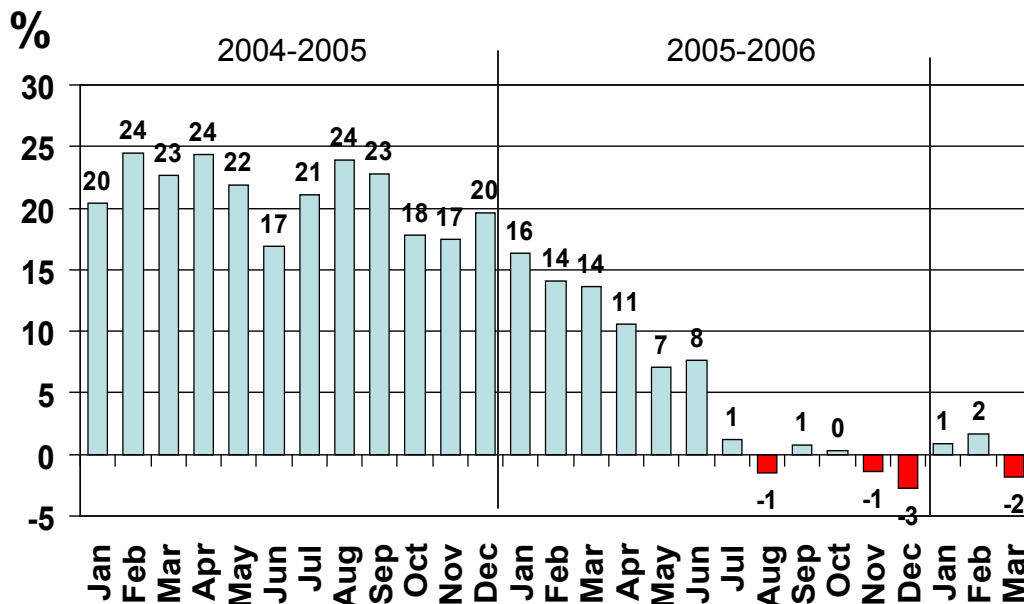
Washington MSA
 All Housing Types



Source: MRIS, GMU

Figure 5
Average Sales Price Percent Change
Month-over-the-year, 2004 - 2007

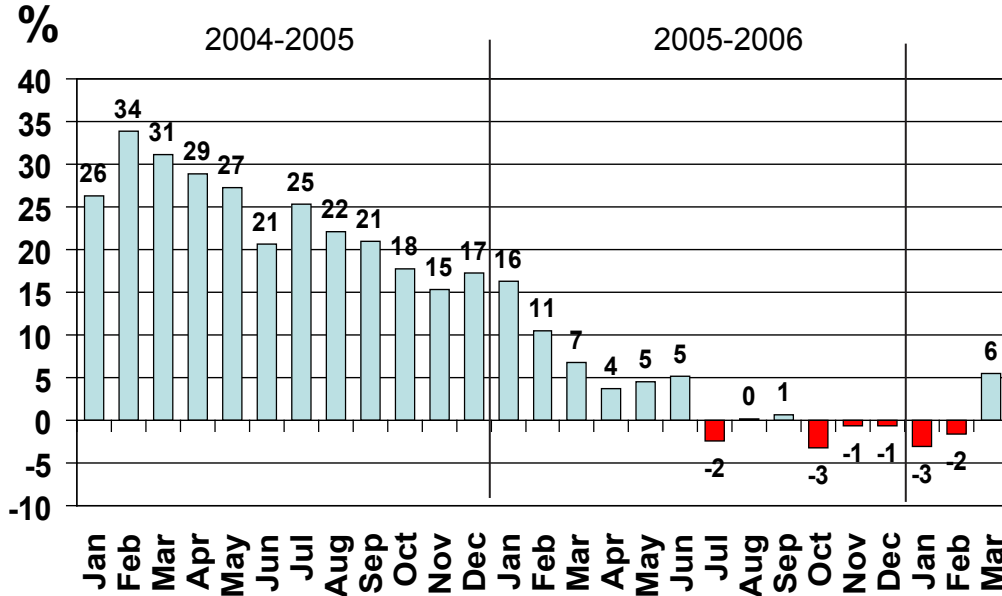
Washington MSA
 Single Family Detached



Source: MRIS, GMU

Figure 6
Average Sales Price Percent Change
Month-over-the-year, 2004 - 2007

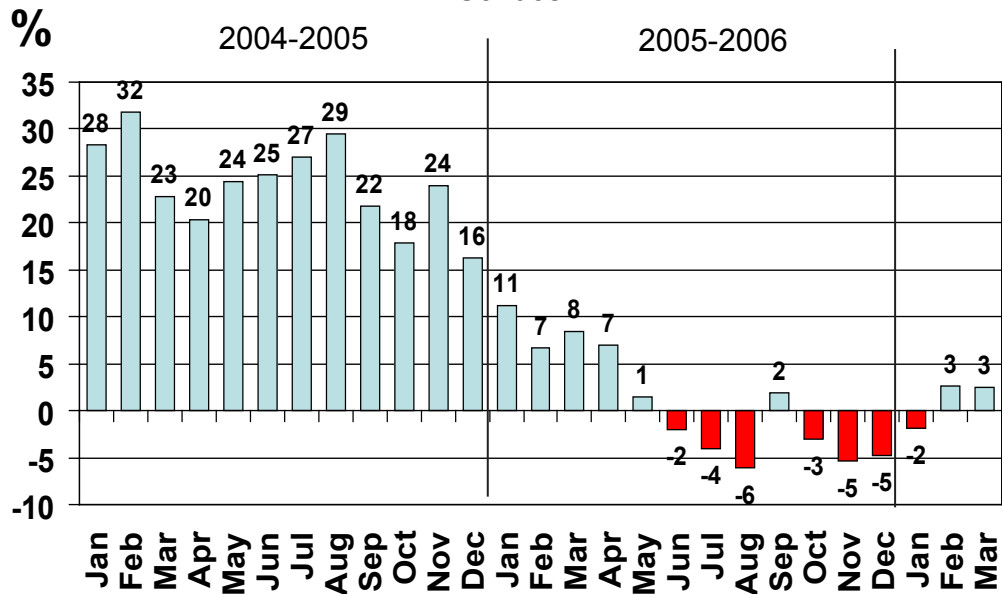
Washington MSA
 Single Family Attached



Source: MRIS, GMU

Figure 7
Average Sales Price Percent Change
Month-over-the-year, 2004 - 2005 - 2006

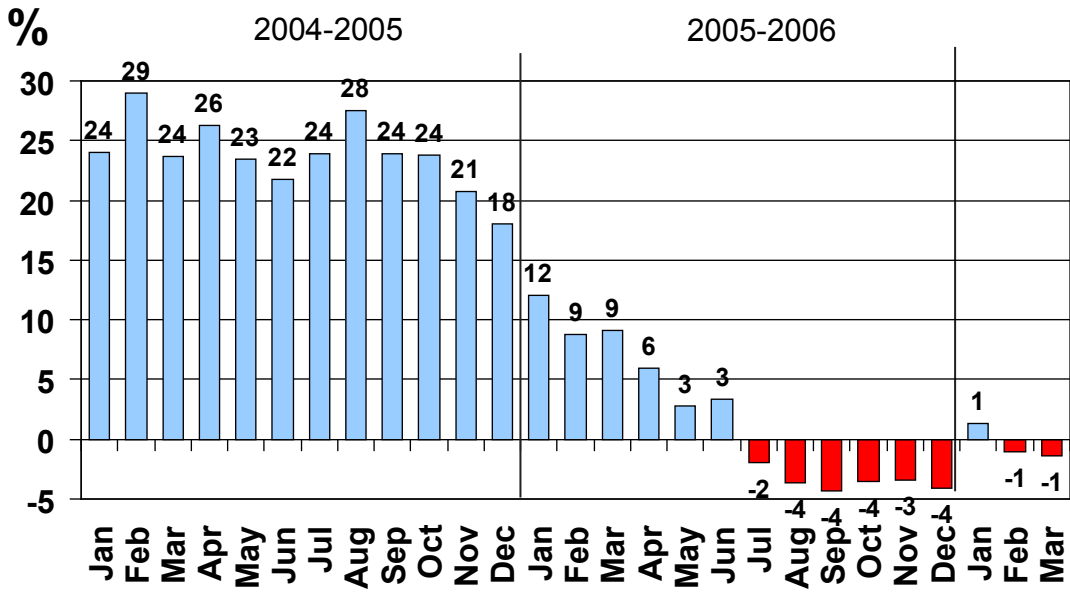
Washington MSA
 Condos



Source: MRIS, GMU

Figure 8
Average Sales Price Percent Change
Month-over-the-year, 2004 - 2007

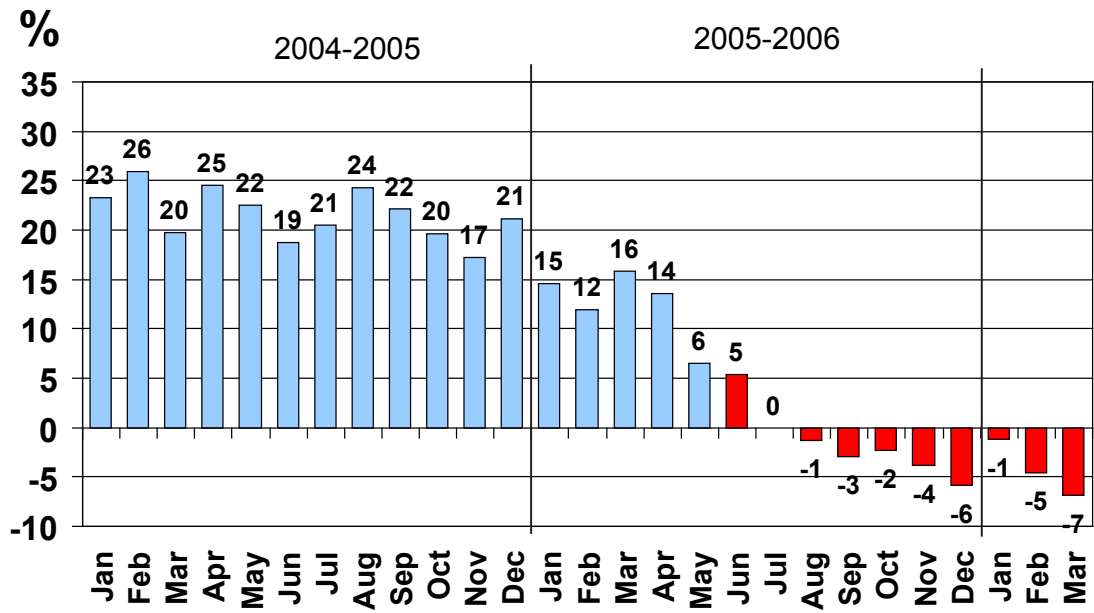
Northern Virginia
 All Housing Types



Source: MRIS, GMU

Figure 9
Average Sales Price Percent Change
Month-over-the-year, 2004 - 2007

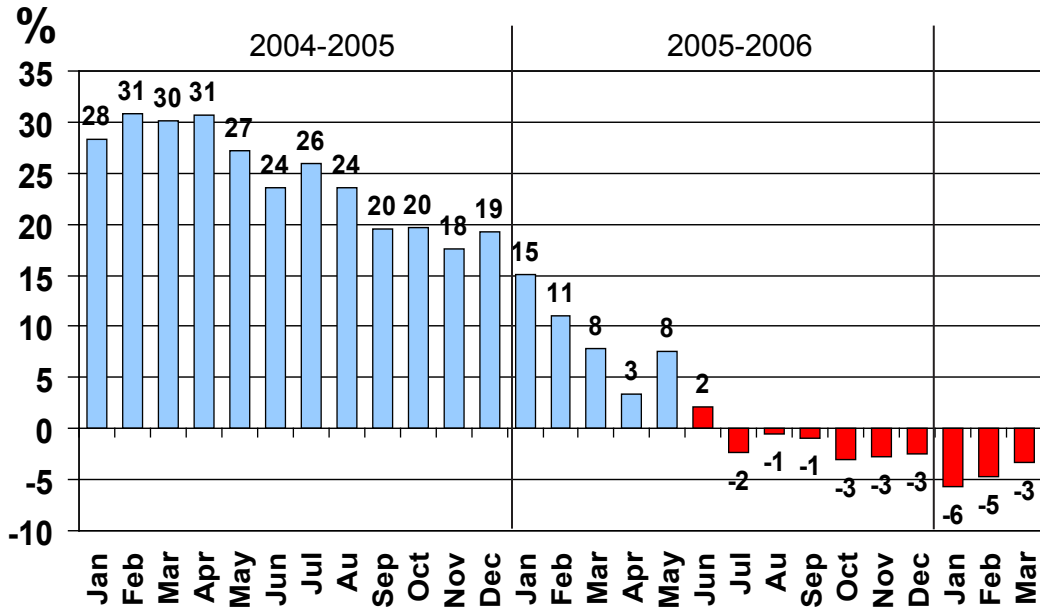
Northern Virginia
 Single-Family Detached



Source: MRIS, GMU

Figure 10
Average Sales Price Percent Change
Month-over-the-year, 2004 - 2007

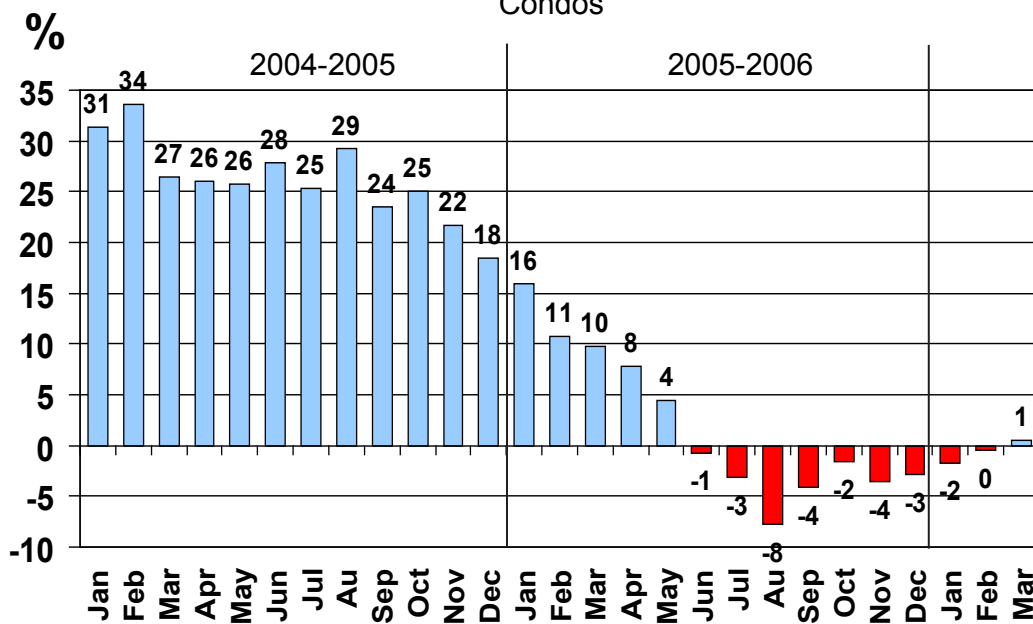
Northern Virginia
 Single-Family Attached



Source: MRIS, GMU

Figure 11
Average Sales Price Percent Change
Month-over-the-year, 2004 - 2007

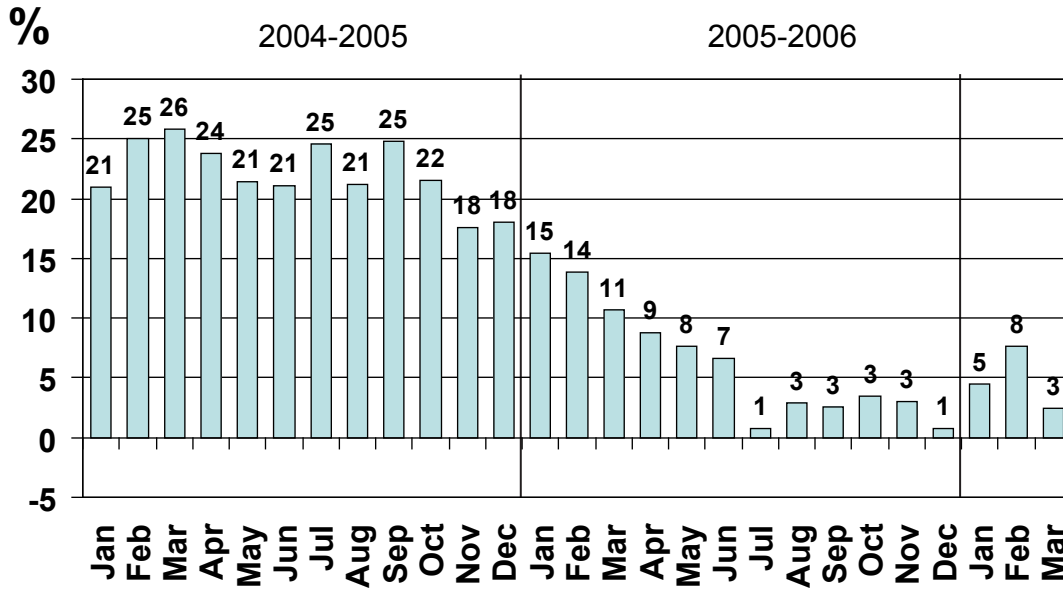
Northern Virginia
 Condos



Source: MRIS, GMU

Figure 12
Average Sales Price Percent Change
Month-over-the-year, 2004 - 2007

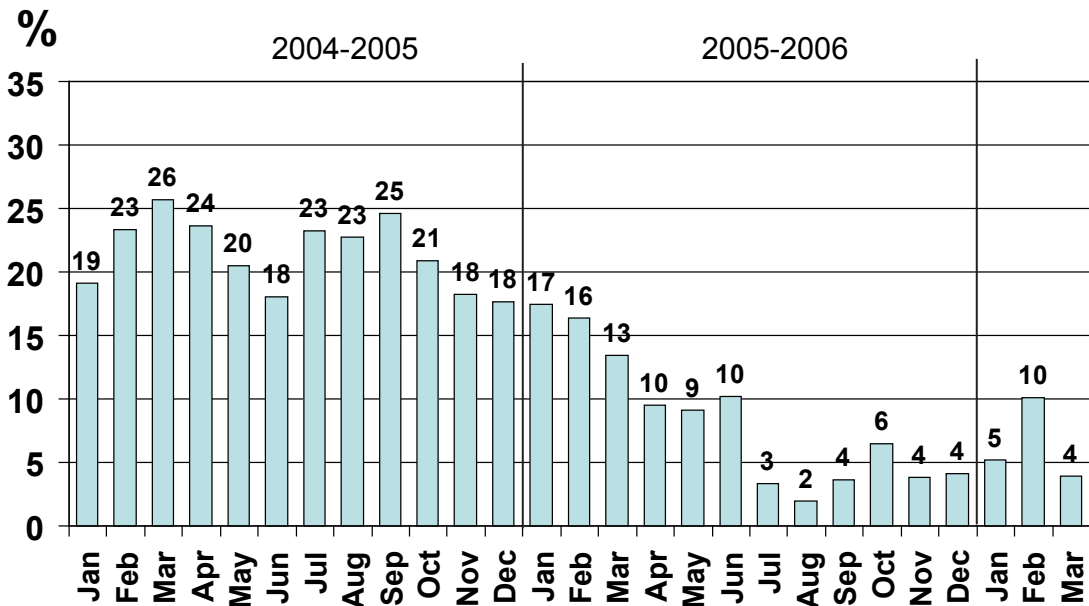
Suburban Maryland
 All Housing Types



Source: MRIS, GMU

Figure 13
Average Sales Price Percent Change
Month-over-the-year, 2004 - 2007

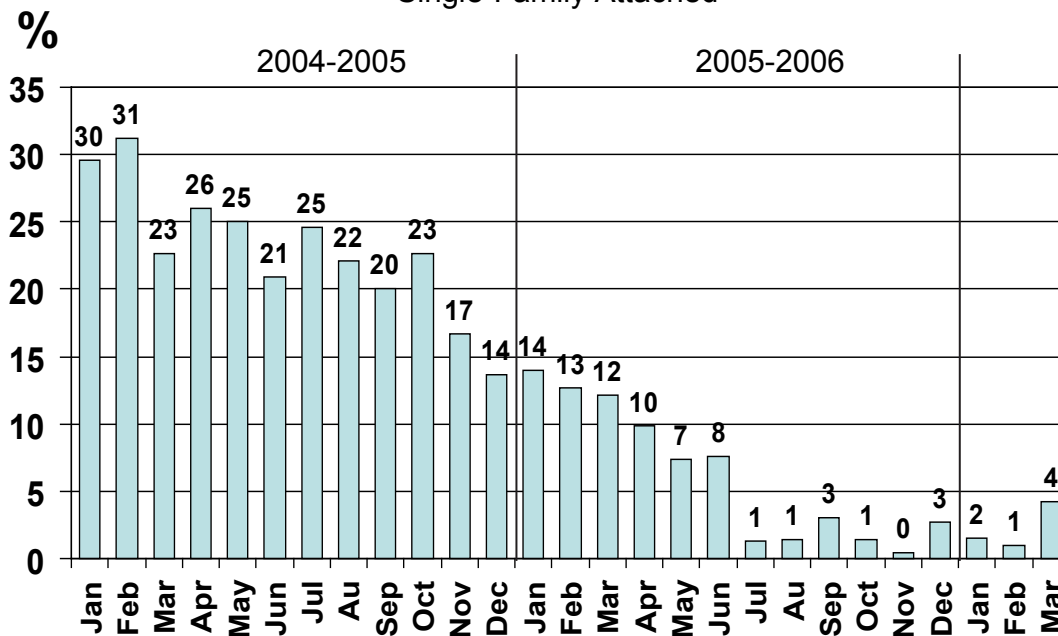
Suburban Maryland
 Single-Family Detached



Source: MRIS, GMU

Figure 14
Average Sales Price Percent Change
Month-over-the-year, 2004 - 2007

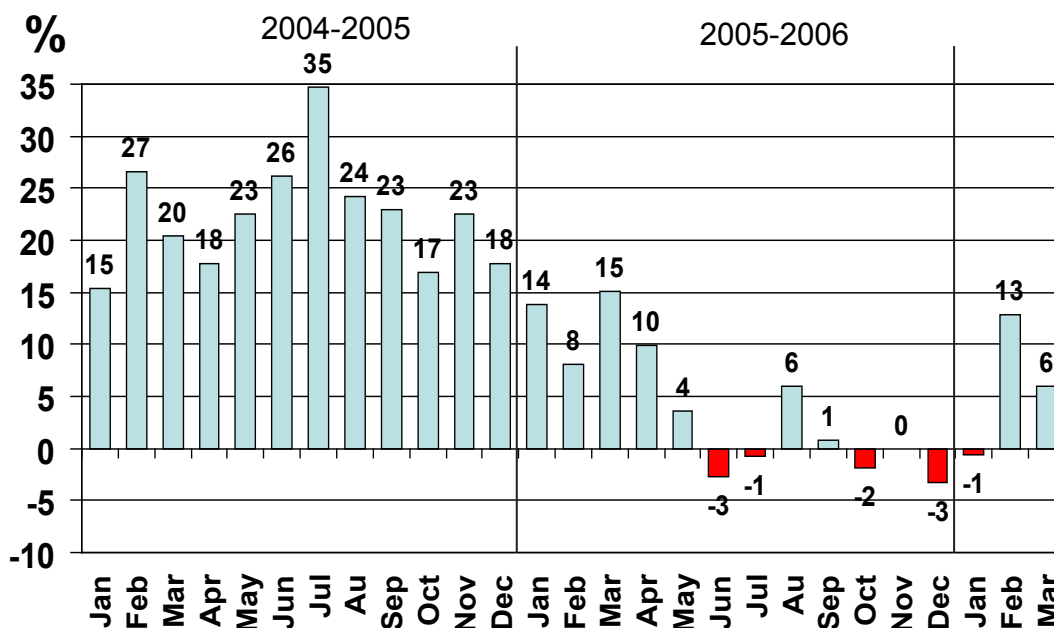
Suburban Maryland
 Single-Family Attached



Source: MRIS, GMU

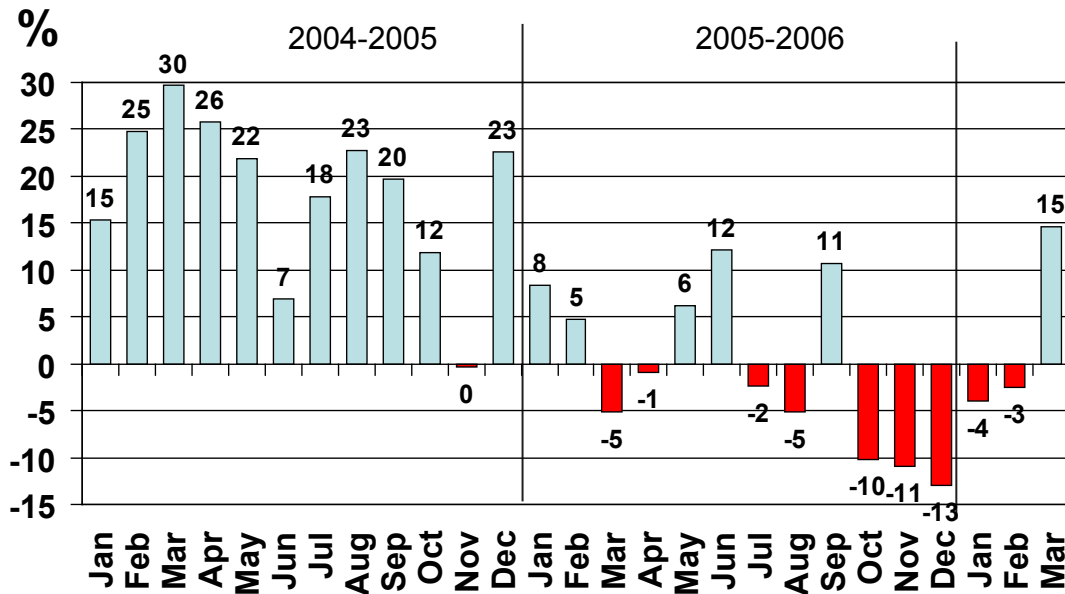
Figure 15
Average Sales Price Percent Change
Month-over-the-year, 2004 - 2007

Suburban Maryland
 Condos



Source: MRIS, GMU

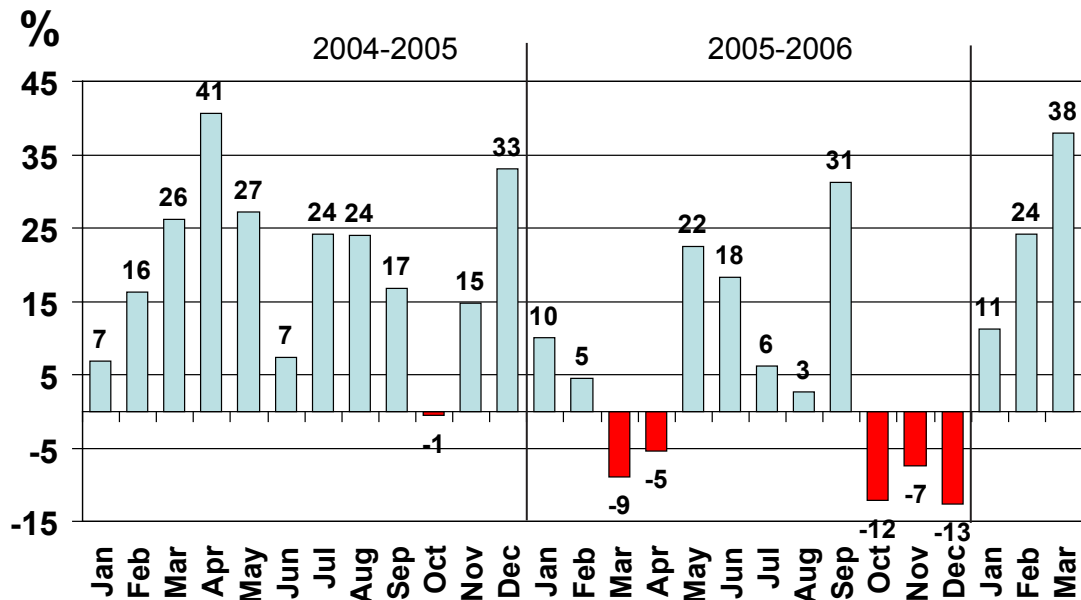
Figure 16
Average Sales Price Percent Change
Month-over-the-year, 2004 - 2007
 District of Columbia
 All Housing Types



Source: MRIS, GMU

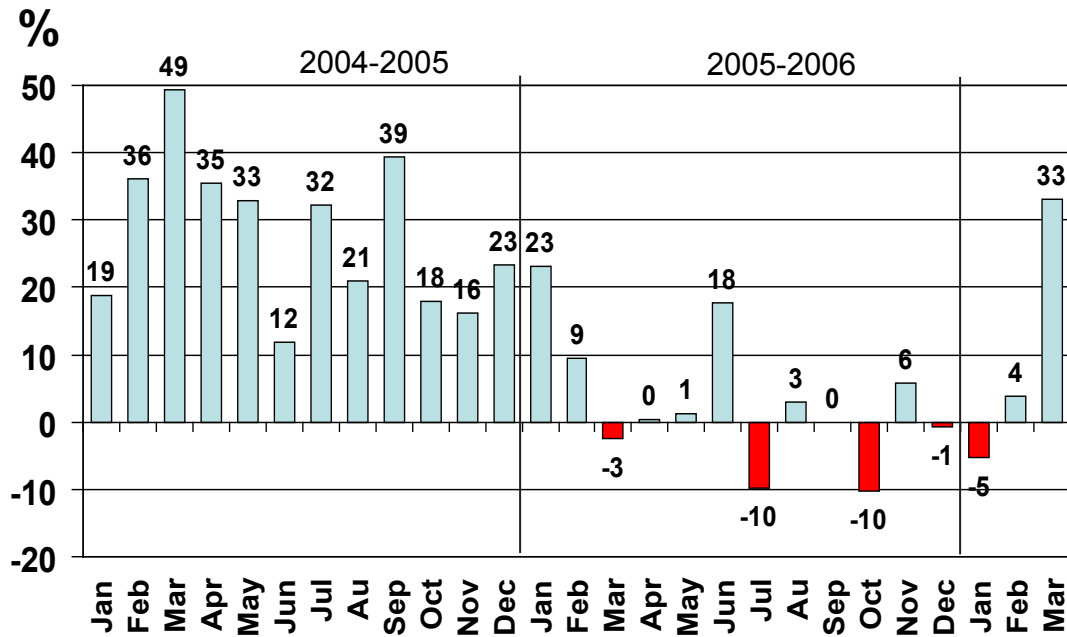
Figure 17
Average Sales Price Percent Change
Month-over-the-year, 2004 - 2007

District of Columbia
 Single-Family Detached



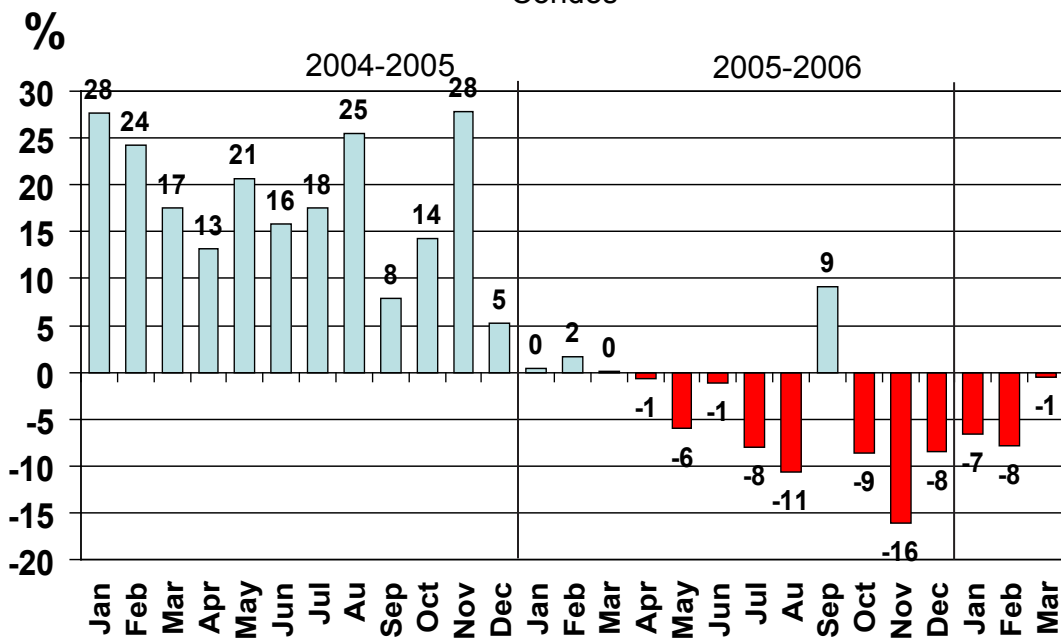
Source: MRIS, GMU

Figure 18
Average Sales Price Percent Change
Month-over-the-year, 2004 - 2007
 District of Columbia
 Single-Family Attached



Source: MRIS, GMU

Figure 19
Average Sales Price Percent Change
Month-over-the-year, 2004 - 2007
 District of Columbia
 Condos



Source: MRIS, GMU

average prices were up 14.6%. This marks a change from the negative price growth that has occurred in the District in each month since October (See Figures 16 through 19.)

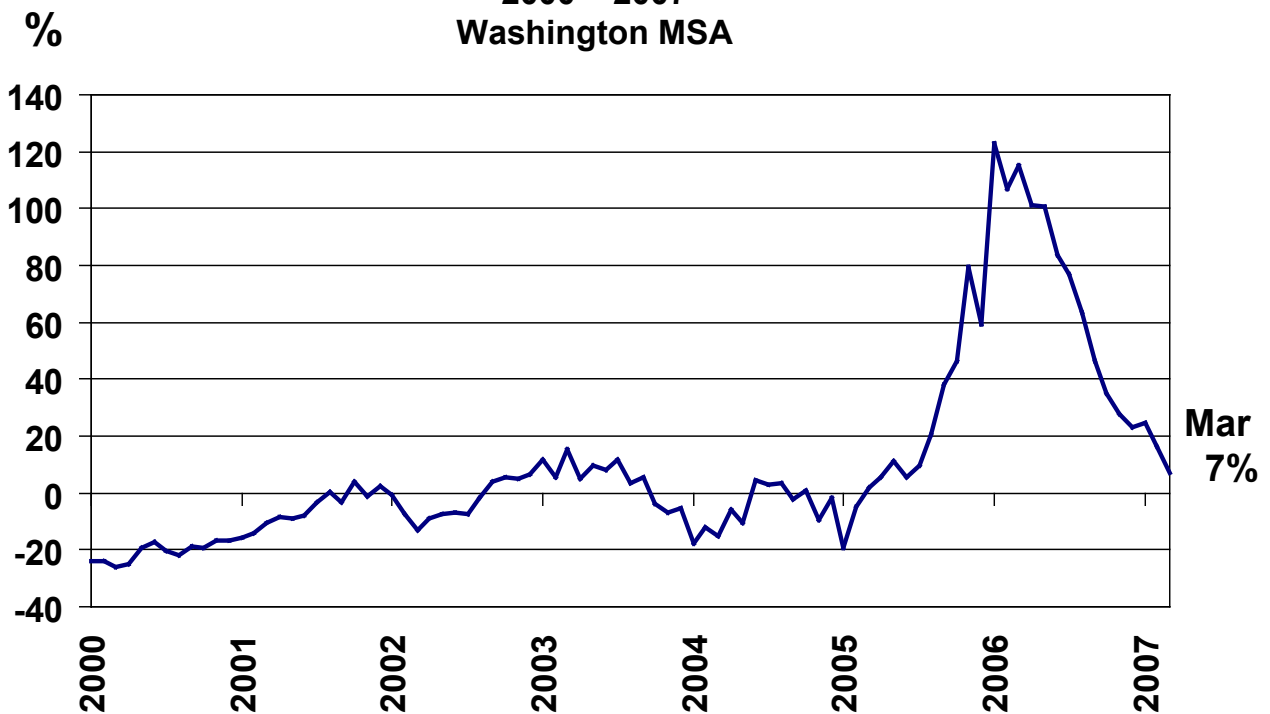
Closer-in suburban jurisdictions with higher priced housing (e.g., Alexandria, Arlington, Fairfax) experienced moderate month-over-the-year price declines in the 2nd half of 2006. Prices of existing homes also have declined in Loudoun and Prince William counties where there is competition with new construction. However, several jurisdictions with more moderately priced housing are still experiencing price growth. Home prices continue to rise each month in Prince George's County, Maryland. Even some more expensive jurisdictions saw positive price appreciation in March, reflecting their desirable location and amenities. For example, home prices were up 7.6% in March 2007 in Montgomery County, where the average home sold for over \$520,000.

Is this the right time to be buying a home?

The "super hot" housing market in the Washington area began to normalize in mid-2005. Housing supply increased rapidly as investors dumped their units onto the market in an effort to capture the value gained in the preceding years. Simultaneously, demand conditions softened temporarily during the second half of 2005 in response to higher energy costs, interest rate fears and media-fueled concerns over the housing market's gradual slowdown.

This normalization process continued in 2006 and was accelerated by further energy price increases during the year's second quarter. The excess units on the market should be largely taken down by the first quarter of 2007 with price stability occurring during the first half of 2007 as demand solidifies in response to interest rate stability, declining energy costs, rising consumer confidence and positive seasonal factors associated with spring housing market activity. Annual appreciation for 2006 is 1.96%, lower than the long-term average of 7% gain, but a sign of a return to a health long-run condition.

Figure 20
Percent Change in
Inventories of Existing Homes
Month-Over-the-Year-Change
2000 – 2007
Washington MSA



Source: MRIS, GMU Center for Regional Analysis

Also indicative of the housing market's normalization process is the relationship between the supply of available units (total active listings) and sales each month. For the first seven years of the 1990s, about 10% of active listings were sold each month in the region. In 2003 and 2004, when the housing market was over heated and experiencing dramatic price acceleration, between 40 and 50 percent of the active listings sold each month. However, the number of total listings was only 50% of its normal level. By December 2005—six months after the summer 2005 peak—the ratio of sales to listings had dropped to 26%. In March 2007, the ratio of sales to listings was 14%.

Figure 20 shows how the rapid run up in inventories has slowed dramatically in the Washington DC metropolitan area, indicating a transition to a better balance between buyers and sellers. In early 2006, the total number of monthly listings was more than double the number in the same period a year earlier. In contrast, the number of total active listings in March 2007 was just 7% higher than March 2006. Eventually, the month-over-the-year change in the total number of listings will approach zero. This ratio indicates that the imbalance between supply and demand is being reduced and that the prospects for the area's housing market are good. A normal market is good for both buyers and sellers.

Housing prices are projected to stabilize in spring 2007 and maintain a rate of appreciation ranging around their long-term average of 7% over the remainder of this decade. With the region's above-average job growth projected to continue through at least the end of the decade and with the supply of new housing units limited, an annual short fall of approximately 15,000 housing units is forecast through 2010.

This pattern of pent-up demand is shown in Figure 21. The resulting housing price pressures will persist for all types of housing over this period. And, given the growing number of one- and two-person households (young professionals, baby-boomers and older empty-nesters), the demand for smaller units located close to public transportation and major employment centers will command the greatest price growth going forward. This trend is now being reinforced by gasoline prices that remain historically high and traffic congestion that will only get worse in coming years.

Why is buying a house now a good long-term investment?

The 7% average annual housing price growth trend for the Washington area is a good guide for judging the investment value of housing. An annual 7% compounded rate of price increase over 10 years doubles the initial value; that is, a \$250,000 investment will increase to \$500,000 in 10 years and \$1.0 million in 20 years. This has been the experience of the Washington housing market for the last three decades.

In addition to its long-term rate of gain being more than double the rate of inflation and at least 50% better than US Treasury Bonds, you can live in and enjoy your house or condo while its value is appreciating. No other investment can claim this dual benefit. With the small equity requirement needed to leverage a mortgage and the tax benefits resulting from the favorable treatment of housing ownership, housing remains the least risky of all investment options available today as it has been for decades.

