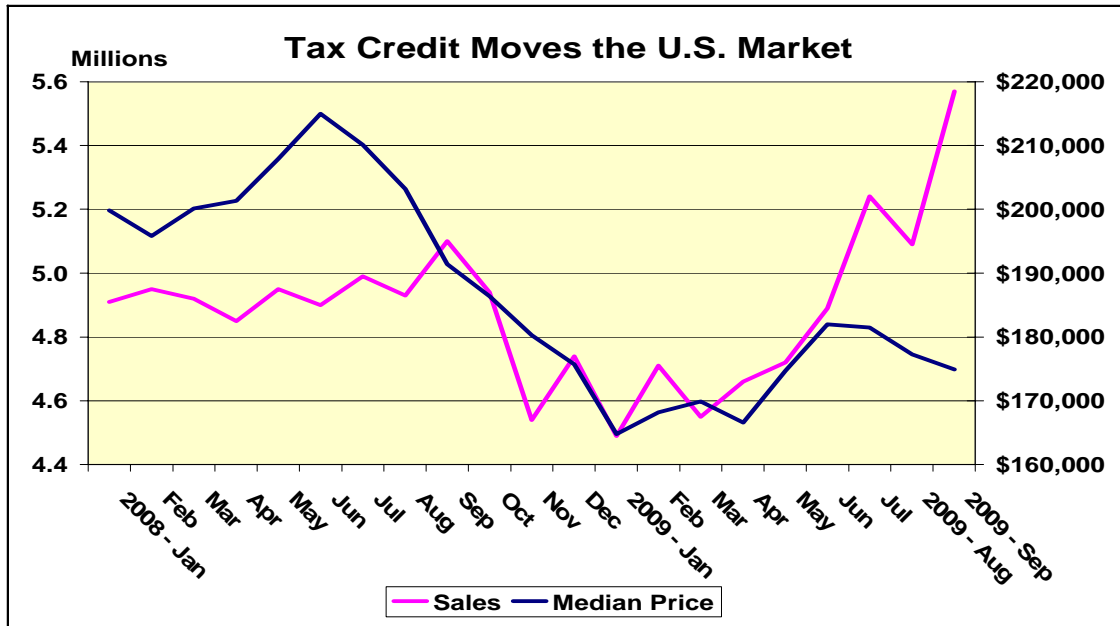


What's Driving Your Market?

By Ken Fears
Manger, Regional Economics

We all know that this is one of the strongest buyers' markets in years, possibly decades. But there is a lot of confusion about what is driving it; the \$8,000 first-time home buyer tax credit, falling prices, record low mortgage rates, or improved confidence?



It is hard to say which factor sparked this summer's up-tick. By most accounts, though, the majority of first-time home buyers who purchased knew about the first-time home buyer tax credit and were eager to take advantage of it. Given that the share of first time buyers is at its highest levels in years, it's fair to assume that the recent improvement is owed in large part to this credit. However, the current tax credit is far from perfect and what's more, it is set to expire in November.

The first-time homebuyer tax credit allows a new buyer a refund of \$8,000 in their taxes if they purchase a home. However, since the only way to get the money from the credit is to file with the IRS after the purchase, a buyer cannot use the \$8,000 for closing. The Treasury and HUD have made efforts to get state governments to create programs that would enable buyers to use the credit money at the time of purchase. In effect, the HUD suggested that state governments make zero-interest loans to first-time buyers for \$8,000. The first time buyers would then pay back these loans when they receive their credit from the IRS. Unfortunately, given the current environment of tight budgets, few state governments created such programs. Thus, the \$8,000 may help new buyers to afford improvements and new appliances after a purchase, an added economic boost, but it doesn't help to facilitate the transaction.

A second issue with the current tax credit is that it is relatively small. Here in the market covered by MRIS, the average selling price is \$327,919. Even though this credit money cannot be used at close, it could be used to reduce the principal by 3.0% for the average mortgage (assuming a down payment of 20%) or 2.5% of the average mortgage insured by the FHA (assuming a 3.5% down payment). This translates to a reduction of a buyer's monthly payment from \$1,473 to \$1,437 under the private financing situation or from \$1,777 to \$1,734 under the FHA situation.

Even if your buyer doesn't qualify to use the first time buyer tax credit, your buyer will still benefit. Purchases by first-time buyers unlock equity for trade up buyers to make their purchase. Furthermore, the sheer volume of sales stimulated by this tax credit helps to stabilize prices, boosting buyer confidence and easing access to PMI.

By most accounts, the current first-time homebuyer tax credit has helped stimulate demand in the housing market at a time when it was necessary to bring down high inventory levels and stabilize prices. But the program suffers from two big problems. With the tax credit expiring in November and calls for its renewal, there is also the opportunity for improvement.