

# How Will Home Boom End?

**Even If Prices Don't Collapse,  
Some Owners Will Feel Pain;  
Big Mortgages, Little Equity**

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When America's housing boom finally ends, don't expect a loud pop.

"It's not going to be a big dramatic event," says William Apgar, senior scholar at Harvard University's Joint Center for Housing Studies.

Unlike stock prices, the housing market can't collapse in a few days. People can dump their stocks almost instantly, but it often takes months to sell a house.

In past housing busts in California, New England and elsewhere, many owners who couldn't get what they considered a reasonable price yanked their houses off the market. The number of transactions plunged but prices fell only gradually, often over several years.

Still, that's little reassurance for Americans who are worried that they bought at the top of the market or for those waiting for prices to ease before jumping in. And the end of the boom is likely to be painful for many people. Among the most vulnerable: people who may have to sell in a weak market because of a job loss or transfer; those with little or no equity in their homes and big mortgages; and those counting on big gains in home equity to make up for a lack of retirement savings.

The housing boom has been an enormous boost to the economy, spurring construction, increasing the net worth of millions of families and allowing Americans to borrow against the rising value of their homes. Mark Zandi, chief economist at Economy.com, a forecasting firm in West Chester, Pa., says the housing surge accounts for nearly 40% of the four million jobs created by the U.S. economy over the past two years.

Economists disagree about how much damage a housing downturn would inflict on the economy. Mr. Zandi hopes that strong job growth in other parts of the economy will cushion any blow from housing. But, he says, the risks of harm to the economy will grow if house prices keep surging for another year or two.

Predictions that the housing market would falter soon have proved premature repeatedly. Still, many economists believe the boom is now peaking or will do so within a year or so. Few expect a sharp fall in prices nationwide but lots of economists think prices will decline at least modestly in some of the cities along the East and West coasts, where buying has been most frenzied.

The housing market has been unusually hot for the past five years largely because low interest rates have allowed Americans to borrow and spend more. The National Association of Realtors forecasts that sales of new and previously owned homes will

total 8.2 million in 2005, setting a record for the fifth year in a row. That would be nearly twice the 4.2 million sales recorded in 1995.

In the five years through June, the nation's median house price grew at an inflation-adjusted average annual rate of 4.9%, according to the Realtors. That's triple the annual average since the real-estate trade group began compiling the data in 1968. In some places, the rise has been far greater. The median price (not adjusted for inflation) shot up 47% to \$243,400 in the Phoenix area over the past 12 months, the Realtors say.

How bad could the next downturn be? Optimists say that the pace of price increases will merely slow to a more sustainable level. Many economists say past drops in house prices have been recorded only in places where lots of jobs have been lost. One example is Los Angeles, hit by a rapid shrinkage of the aerospace industry in the early 1990s. In cities with strong job markets, home prices have tended to keep rising, albeit at a slower rate, when the market cooled.

Even so, history shows that house-price declines are less rare than many Realtors suggest in their sales spiels. Richard J. DeKaser, chief economist at National City Corp., a Cleveland-based banking concern, recently studied home prices in 299 metropolitan areas over the past 20 years. He found that 63 of them at some point suffered declines of 10% or more over periods of at least two years. The worst hit was Lafayette, La., where prices fell 39% in the late 1980s amid a slump in the oil industry. Honolulu, hurt by a decline in Japanese tourism, sank 20% in the late 1990s. The median decline in those 63 markets was 17%.

The end of the boom isn't likely to cause a recession, however, says Mr. DeKaser of National City. He expects prices to erode in some overheated markets. But because the housing market depends so much on local conditions, prices probably will continue to rise in some places as they fall in others, diluting the effect on the national economy, he says.

Unless interest rates rise much more sharply than expected, there is no reason to expect a national housing crash, says Allen Sinai, chief global economist at Decision Economics Inc. in Boston. "I don't think this is a situation of boom-bust," he says.

But Edward Leamer, an economics professor at the University of California Los Angeles, thinks a housing downturn could "kick the economy into slow growth and possibly an outright recession." He counts 10 declines in residential investment since World War II. Eight of them, he says, provided the early warnings for recessions.

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