Housing Market in 2013: What to Expect

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When the housing market imploded in 2007 and took the economy with it, experts said the real estate market would never look the same again. Now, nearly six years after the crash, the dust has finally cleared and we have a true picture of the new housing landscape.

While investors may still be leery of hopping back into the market, housing starts, prices and confidence are on an upward trend and the tide may be turning this year to favor homesellers.

Homebuyers can expect a more competitive market in 2013, and should start the mortgage lending process at least three months before they plan to start seriously looking because experts expect the process to take several months under new lending standards. House hunters should be ready to deal right away as inventory is expected to remain at low levels throughout the year.

Homesellers are shifting into the driver’s seat with experts expecting bidding wars to break out in certain markets due to the low inventory. While homes will sell quicker this year, they still have to be priced right.

“The mobility rate has been at a very low rate, meaning that people really did not move during the recessionary years, so there is pent up demand -- but sellers need to price correctly,” says Lawrence Yun, chief economist at the National Association of Realtors.

Here's a rundown of what experts expect from the market:

Mortgage Rates and New Rules

The Federal Reserve has held interest rates steady at near-record lows over the last several years in an effort to entice buyers into the market, and experts don’t expect significant jumps in the rate this year. In fact, the central bank said it would not raise short-term interest rates until the unemployment rate drops below 6.5%.

“Mortgage rates were essentially at a generational low last year -- they could move modestly higher this year, but it will be the second-lowest [rate] in 40-plus years,” says Yun. “I anticipate by year end that mortgage rates may be close to 4%, but still one of the lowest in a generation.”

In early 2012 the nation’s largest banks agreed to put aside $25 billion in the robo-signing settlement to help fund loan and foreclosure modifications and compensate homeowners who claimed they were given unfair lending terms. Experts expect more mortgage rules to be handed down this year to help prevent reckless lending that led to the meltdown.

The Consumer Financial Protection Bureau issued new qualified mortgage standards last week that detail criteria lenders must use to determine if a borrower qualifies for a loan.

The rule states a qualified mortgage cannot include risky features such as extending beyond 30 years or include exotic terms like interest-only payments or negative-amortization payments, where the principal amount increases. Loans can’t carry fees and points above 3% of the total mortgage and limits the total debt-to-income ratio at 43% -- which some worry will restrict credit and discourage homebuyers at the lower-end of the income scale from seeking a mortgage.

Additional mortgage rules are aimed at curbing over-borrowing, but could make the process longer for potential homebuyers and could prevent some potential buyers from being able to qualify for a loan.

“The mortgage rates are very low, but only a few people are able to access that low rate,” says Yun. "A modest increase in mortgage rates may not be harmful, provided that there is a return to more normal underwriting standards.”

Housing Prices

Over the last two years the big question hanging over the market was how much lower home prices could drop, but home pricing indexes started to rise last year and are expected to continue the upward trajectory in 2013.

Increasing home prices will bring reluctant homeowners off the sidelines and will encourage homebuyers waiting for rock-bottom prices to jump in. According to the Mortgage Bankers Association, applications for new-home loans are expected to increase 55% this year.

Earlier this week CoreLogic reported it expects home prices to jump 6% this year compared to 7.5% in 2012. Markets experiencing a stronger labor market will seeing prices increase even more.

Housing Inventories

In reaction to the housing oversupply, housing inventories fell more than 40% across the nation since 2007 and experts say below-normal inventory will hold back sales and impede the market's recovery in 2013 if not corrected.

If home prices continue to rise it will help increase inventories, which will bolster the housing market even more, according to Jed Kolko, chief economist from Truilia, who says housing construction is up 60% in the last two years, but is still far from normal levels.

"Rising prices… encourage developers to build more and also lift more borrowers back above water and encourage some of them to sell," he says. "They've wanted to sell and haven't been able to, but now they will start thinking about it. The biggest question is whether it means inventory will expand or shrink less than last year, this could be the year."

In 2012, the total number of units constructed stood at 600,000, far less than what's necessary to keep up with the demand. This year experts forecast around 750,000 units to be constructed, far less than the 1.4-1.6 million units needed.

"In many markets sellers are in the driver's seat because of low inventories," says Kolko. "With inventories falling so dramatically in the last year, buyers are competing for a fairly small inventory of for-sale homes and that helps sellers."

The Fate of the Interest Rate Deduction?

This popular incentive to attract consumers to become homeowners may be on the chopping block as both Democratic and Republican lawmakers continue to look for ways to close the ballooning federal deficit and budget.

The mortgage interest deduction costs Uncle Sam nearly $100 million in revenue a year, but eliminating it could weigh on housing activity.

"Over the years one of the advantages of buying is getting that interest deduction," says Sam Davis, a real estate agent in Washington, D.C. "When we are trying to convince renters to purchase a home we can say: 'If you pay $1,500 a month on rent and you buy a home with a $2,000 mortgage, if you got that interest rate that would basically make the spending even, yet you aren't getting the advantage of appreciation and the right to own your own home."

Foreclosure Activity

According to Kolko, there are currently more than a million homes in the foreclosure process across the country, but the crisis on a nation level is over. However, he says foreclosures in the most-battered markets including Florida, Illinois, New Jersey and New York are still high, and regulators have been considering state-level foreclosure reform.

He adds that the housing price rebound is stronger in states with a quicker foreclosure process and less of a backlog, while states with a hefty backlog are holding back the price recovery.

As investors become increasingly more comfortable with the real estate market, Chris Boston, mortgage banker with the Fitz Gerald Financial Group Division of Monarch Bank, says he is seeing more people taking advantage of foreclosures and short sales. "Investors are taking advantage of the market, they are buying homes at 50 cents on the dollar and they are renovating them to where they should be, which will help the market this year."

Refinancing Activity

Low interest rates caused a wave of refinancing in 2012, but experts forecast a much slower pace in 2013.

"Refinancing is less about helping the housing market and more about boosting the economy by reducing payments and giving homeowners more money to spend," explains Kolko. He adds that only if rates drop further, or the eligibility requirements expand, will refi activity pick up this year.