University of St. Thomas

Minneapolis St. Paul Residential Real Estate Index

July 2013

University of St. Thomas Minnesota

Real Estate

UST Opus College of Business

Welcome to the latest edition of the UST Minneapolis St. Paul Residential Real Estate Index.

The University of St Thomas Residential Real Estate Index has been developed by the Shenehon Center for Real Estate at the University of St. Thomas Opus College of Business to correct the overstatement of housing price decline reported by the S&P Case-Shiller Price Index for the Minneapolis–St. Paul metropolitan area. Rather than a single index or price representative of all homes, the UST Residential Real Estate Index includes the price of homes in three sub-markets: traditional sales, short sales and foreclosure sales as well as a nine variable composite index for measuring market health for each category based on a three-month moving average.

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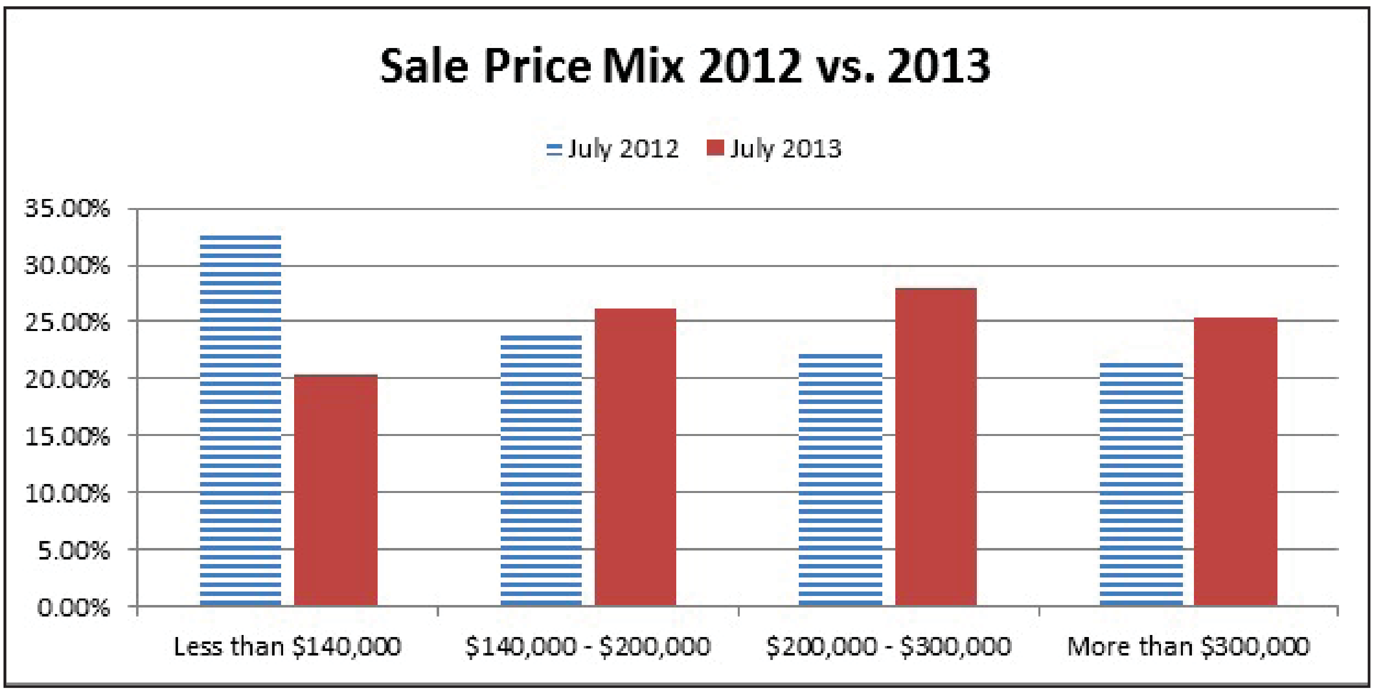
A Look Behind the Numbers - Median Prices and Inventory of Homes for Sale

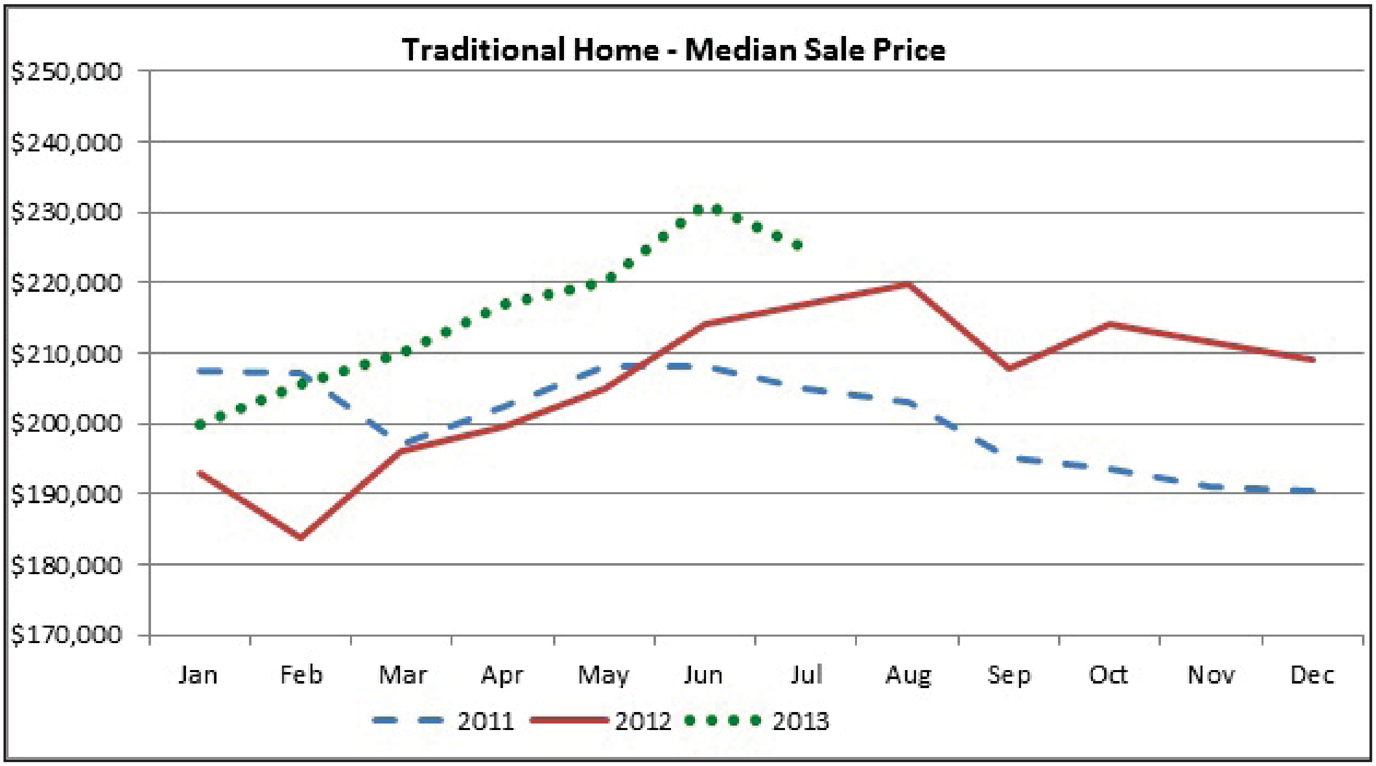
As we noted in our June report the normal seasonal slowdown in the Minneapolis / St. Paul housing market was beginning to take effect. That seasonal trend continued into July with the overall market showing its first month-to-month price decline of 2013. From June to July the median sale price went from $210,000 to $208,000, a decrease of .95%. Compared to last year, the median price for the market as a whole, including all categories of homes, is up a healthy 16.85%. The median price of a traditional (non-distressed) home sale in July 2013 was $224,950, a decrease of 2.66% from June of this year, yet it is an increase of 3.66% over the $217,000 reported in July 2012. Median sale prices have historically plateaued in June, July and August and declined in the 3rd and 4th quarter. Look for median sale prices to follow their normal pattern and decline moderately throughout the remainder of 2013.

Part of the recent rise in median sale prices can be explained by examining the prices of the homes being sold. The mix of home prices has changed over the past year. There are now a greater percentage of higher priced homes being sold compared to this time a year ago (see the chart below). This change in the proportion of more expensive homes being sold also helps to explain why the median sale price continues to show large increases compared to the same period last year. This is another sign of the market's return to good health since it indicates that there are fewer lower priced and distressed properties being sold.



In July 2013 the volume of closed sales was 5,671, virtually the same as the 5,610 recorded in June. The level recorded in July was 19.1% higher than the 4,761 recorded in July 2012. The proportion of distressed sales continues to decline. Compared to July 2012 traditional sales are up 42% and short sales and foreclosures are both down 27%. In July 2013 only 20.7% of the closed sales were distressed. That is the lowest percentage of distressed sales since January 2008. The number of new listings declined by 4.3% from June to July yet they remain 16.6% higher than last year at this time. The number of pending sales was unchanged between June and July.

The inventory of homes for sale continues to improve. In June and July there were about 15,900 homes available for sale. That is an improvement over the 12,000 to 13,000 homes that were available for sale earlier this year. However, due to the higher number of sales, the ratio of closed sales to homes available for sale remains very low in July at only 2.8 homes available for sale for every home sold. Typically this ratio ranges from 6 to 8 in a balanced market. As we move into fall look for a declining number new listings and a relatively higher number of sales to keep downward pressure on the number of homes available for sale through the fall and winter. Low numbers of homes for sale and stronger sales numbers will combine to keep upward pressure on prices. As prices continue to improve look for a much better inventory of homes for sale in the spring of 2014.



The UST Indices - Continued Movement in a Good Direction

The UST Traditional Sale Composite Index continued its upward momentum in July, moving from 1,072 in April to 1,083. The important news here is that this increase puts the index at a near record level that has not been seen since it was recorded at 1,084 in August 2005. This is a reflection of the sustained recovery of the traditional home median sale price and a number of other favorable market factors including favorable low levels of inventory, the decreasing percentage of distressed sales, and historically low interest rates. The index continues to remain well above the levels recorded in the previous year. July's Traditional Sale Composite Index of 1,083 is 8% higher than the 1,002 recorded in July 2012. .

The UST Residential Real Estate Short Sale Composite Market Health Index was 885 in July, an 11.3% increase compared to one year ago.

The foreclosure market's health as represented by the UST Residential Real Estate Foreclosure Composite Index increased slightly in July, moving from 785 in June to 789 in July, an increase of. 0.5%.The index is up 11.3% compared to June 2012 and continues to close the gap compared with the Traditional Sale Composite Index.

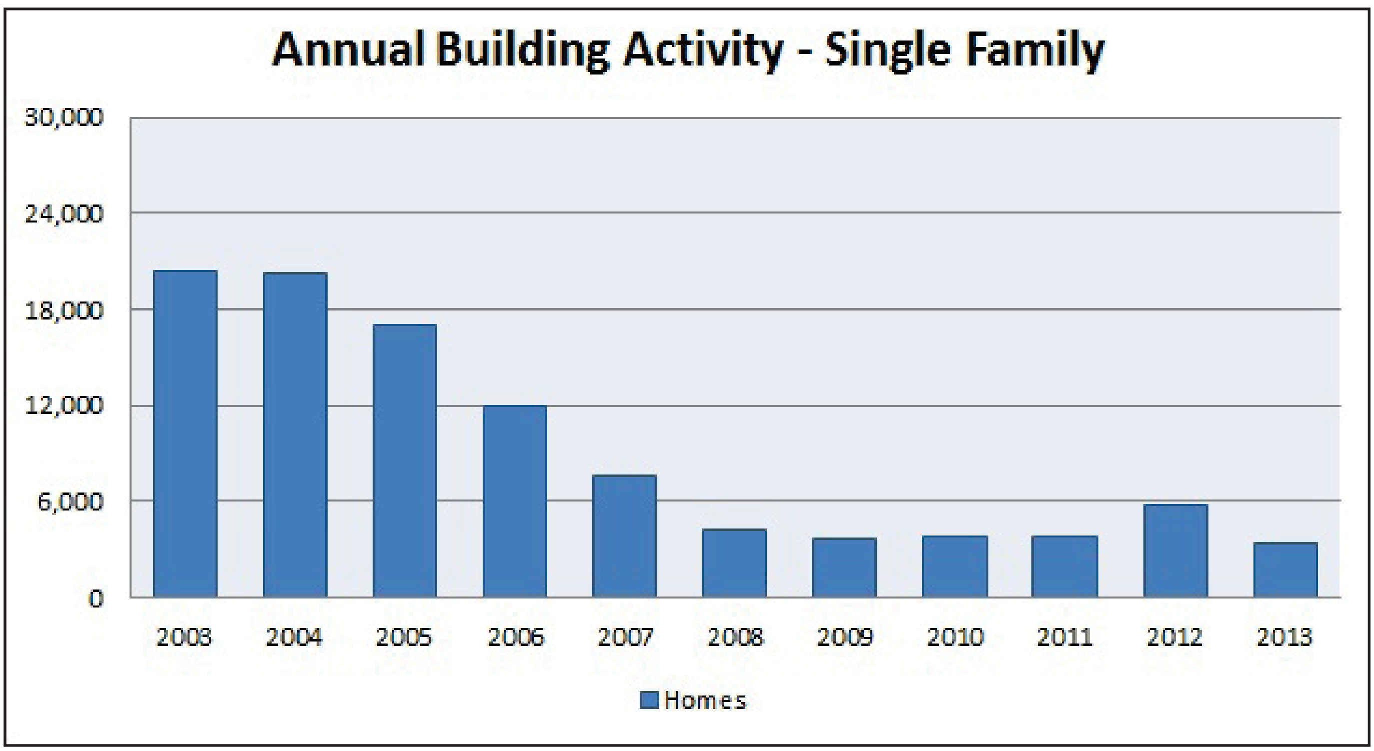
New Home Construction Continues to Increase

Homebuilders continued to be busy adding to the supply of new homes for sale in the metro market in July. According to the Keystone Report single family new construction permits continue to run about 30% ahead of last year's levels through the first seven months of the year. According to the U.S. Census Bureau there were 5,750 new home starts in the Minneapolis / St. Paul metro area in 2012. The chart to the right shows that in 2012 Minneapolis / St. Paul was one of the top 20 metro areas in the country in terms of the number of new housing starts.

The number of new home starts is expected to show an increase of 15% - 18% by the end of 2013, reflecting a seasonal slowdown slow in new home starts in the late fall and winter. While the number of permits issued is running far behind the levels seen in the early 2000's, homebuilders in the Twin Cities are in the midst of a third year of steady growth.

Rank	Market	Annual Starts
1	Houston	26,074
2	Dallas / Ft. Worth	20,384
3	Central Florida	15,786
4	Phoenix / Tucson	14,381
5	Denver / Co. Springs	11,751
6	Southern California	11,691
7	Northern California	11,511
8	Atlanta	11,027
9	Austin	9,826
10	Suburban Maryland	8,729
11	Northern Virginia	8,456
12	San Antonio	8,445
13	Raleigh/Durham	8,279
14	Charlotte	7,812
15	Salt Lake City	7,715
16	Las Vegas	7,119
17	South Florida	6,380
18	Tampa	6,159
19	Central California	6,148
20	Twin Cities	5,767

Source: Metrostudy



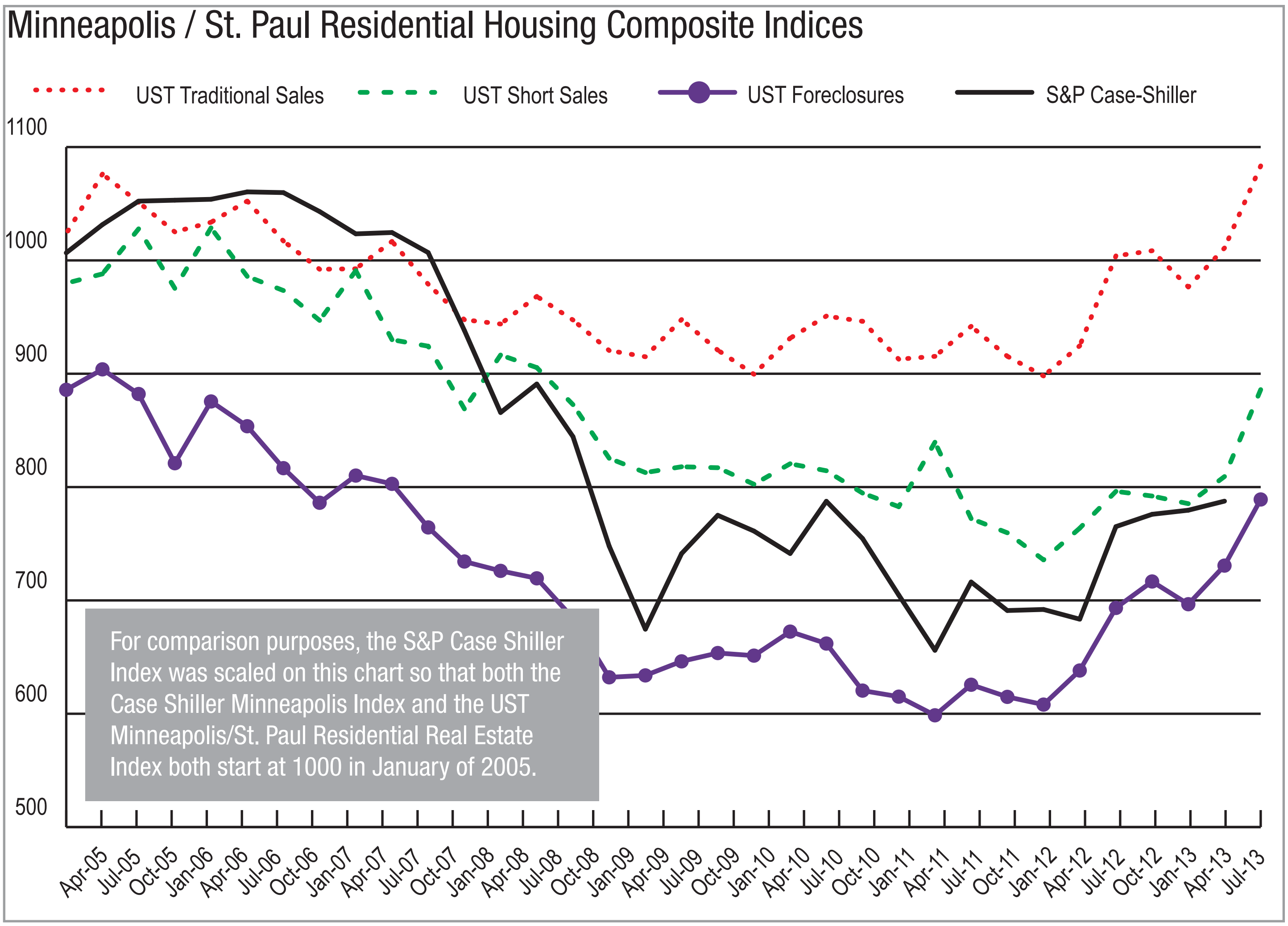
Data Source: U.S. Census Bureau, Building Permits Survey

Note: Data for 2013 is preliminary, through June 2013

UST Residential Real Estate Indexes	July 2012	June 2013	July 2013	Year to Year Change
Traditional Sale Index	1003	1072	1083	7.98%
Short Sale Index	796	863	886	11.31%
Foreclosure Sale Index	692	785	789	14.02%

Return of the Condo - Coming Soon to a Neighborhood Near You?

New condominium development is showing early hints of a comeback. After 5 years of declining values, excess units, and no new development, certain areas of the metro area are showing positive signs of development activity. Two recent projects illustrate this point. The second phase of the Stonebridge Lofts now under construction in Minneapolis has sold nearly half of its 164 units almost one year before its expected completion date. Parkside Condominiums in St. Louis Park has already sold 17 of its 22 units while still under construction. The supply of new condos on the market is very low after a long period of oversupply. In downtown Minneapolis there is only a 2.4 month supply of condos available for sale. The recovery of the housing market and rising rental rates are having two effects. First, increasing prices, low interest rates, and rising rental rates are causing more people to consider a condo purchase. Secondly, rising prices are making new condo development financially feasible for developers. The condo market will be slow coming back but don't be surprised to see more condos being built in select locations over the next several years.



July 2013 UST Index Data					
1. Median Sale Price	**July 2012**	**June 2013**	**July 2013**	**Monthly % Change**	**Annual % Change**
Traditional	$217,000	$231,100	$224,950	-2.66%	3.66%
Short Sale	$129,000	$145,000	$150,000	3.45%	16.28%
Foreclosed	$121,000	$145,000	$135,000	-6.90%	11.57%
2. Closed Sales	4,761	5,610	5,671	1.09%	19.11%
Traditional	3,149	4,392	4,494	2.32%	42.71%
Short Sale	444	338	323	-4.44%	-27.25%
Foreclosed	1,169	887	850	-4.17%	-27.29%
3. % Distressed Sales	33.88%	21.84%	20.68%	-5.27%	-38.95%
4. Days on Market	105	74	72	-2.70%	-31.43%
5. Month's Supply	4.6	3.7	3.6	-2.70%	-21.74%
6. New Listings	5,856	7,631	7,300	-4.34%	24.66%
7. Pending Sales	4,585	5,316	5,349	0.62%	16.66%
8. Homes for Sale	18,019	15,797	15,768	-0.18%	-12.49%
9. % of Original Price	95.00%	97.50%	97.50%	0.00%	2.63%

Real Estate at the Opus College of Business

Shenehon Center for Real Estate www.StThomas.edu/Shenehon

The Shenehon Center for Real Estate serves as a resource to the commercial, industrial, residential and corporate segments of the real estate industry and the community to advance the public interest in real estate issues. For more than 15 years, the center has supported improvement in real estate leadership and management by creating and developing real estate leadership and management programs for undergraduate and graduate degree programs and professional development, providing a neutral forum to convene real estate professionals to share best practices, supporting and working with local real estate industry organizations, conducting real estate research, and developing mechanisms to transfer leading edge business practices to the real estate industry.

Master of Science Degree in Real Estate www.StThomas.edu/RealEstate

The Master of Science Degree in Real Estate is one of seven graduate business degree programs offered through the Opus College of Business. This part-time, evening program provides students with a comprehensive understanding of real estate financial and quantitative decision making processes, and advanced issues in valuation and land economics, knowledge of critical legal issues, and techniques for market and feasibility studies and real estate investment analysis. Students in the UST MSRE program come from a variety of different backgrounds including appraisal, brokerage, property management, finance, development, engineering, design, facilities management and corporate real estate. The program produces alumni with strong leadership abilities, aptitude for sound decision making, focus on ethics and social responsibility, and a solid network of real estate professionals.

Bachelor of Science Degree in Real Estate www.StThomas.edu/business/BSRealEstate

The Bachelor of Science Degree in Real Estate is one of 13 undergraduate concentration areas in the Opus College of Business. This four-year degree program provides students with a background in general business and real estate theory and practice. Students study the many factors involved in property assessment and sales, how they change and how these changes affect real estate and individuals. Recent graduates hold positions in the government, nonprofit, construction and private business sectors, including leadership positions in real estate brokerage, investment management, property management, appraisal, construction management, land-use planning and land development.

About the Index

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One of the problems with the S&P Case-Shiller Price Index is that the matched pairs selected to develop the index do not make a distinction between a traditional, normal market sale and a distressed (short or foreclosure) sale. A property purchased at the peak of the market in 2006 and then foreclosed in 2010 and subsequently sold by the lender is considered by the Case-Shiller Index as a "normal, arms-length," transaction. The UST Residential Real Estate Index does not consider the transaction to have occurred at "arms-length" because the seller (the bank as the lender) is not a typically motivated seller. In many cases foreclosed properties are sold at distressed, discount prices because the lender wishes to recover as much of their investment as possible and get the property off their books. Further foreclosed homes have often fallen into disrepair and require a significant amount of work to become habitable.

Traditional sales of homes include those properties not subject to the threat of foreclosure or to a sales price which is less than the balance of the outstanding mortgage. Short sales are sales of homes sold for a price less than the outstanding mortgage balance and relieve the seller of the burden of continued payment for a home worth less than the outstanding debt. A short sale also eliminates the threat of future foreclosure. Foreclosure sales are sales of those properties whose owners have defaulted on their mortgage payment obligations and have lost their home to their lender. Title is held by the lender and the home is vacant.

Combining foreclosure and short sales of real estate with traditional property sales skews any single composite price index, such as the S&P Case-Shiller Index, and creates a downward bias when foreclosure sales and short sales represent a significant part of total housing sales. In a normal housing market less than 5% of properties sold would be classified as distressed. During last few years foreclosure and short sales have comprised between 35-60% of all housing sales. This unusually high disproportionality of distressed sales causes the reported decline in a single, overall housing price index to be overstated.

Analysis of these three submarkets for MSP Metro Area since 2005 has revealed that the S&P Case-Shiller Price Index has significantly overstated the price decline for the traditional housing market while understating the loss of value for homes subject to a foreclosure sale. Since the first quarter of 2005 Case-Shiller has reported an overall decline in market price of 20.1%. Our analysis of traditional housing sales for the same period, with a three-month moving average, reveals a price decline of 1.5%. Short sales and foreclosure sales had price decreases of 14.6% and 13.5% respectively. The Case-Shiller Index also uses a three-month moving average.

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Why Another Real Estate Index?

How does the UST Residential Real Estate Index differ from the S&P Case-Shiller Price Index for the Twin Cities market?

The Case-Shiller Index is an aggregate price index only and is based on sales data from matched pairs of residential properties. Matched pair analysis compares the recent sale of a property with a previous sale at some point in the past. The difference in sale prices of the property over the time interval between sales is used to calculate the price change and the Case-Shiller Index for a particular month. As many matched pairs property sales as possible for the Twin Cities market are identified and used to calculate each month's index value.

The University of St Thomas Residential Real Estate Index for Minneapolis St. Paul metropolitan area has been developed by the Shenehon Center for Real Estate to provide a broad measure of the health and strength of the local residential housing market covering the 13 county Twin Cities metro area. The health of a housing market is more than just the current reported price for housing. Therefore the UST index incorporates other variables that together provide a better picture of the residential real estate market's health; it takes into account supply and demand factors that are indicators of market velocity and vitality, as well as their effect on housing prices.

The index is comprised of nine different elements that together reflect the residential real estate market health and include the following:

1. Selling prices for traditional, short and foreclosure sales;
2. Number of closed sales;
3. Proportion of traditional, short and foreclosed sales;
4. Time on the market;
5. Months' supply of homes for sale;
6. Number of pending sales;
7. Number of new listings;
8. Number of homes for sale; and
9. Sale price as a percentage of the asking price.

These factors are synthesized and used to calculate a numerical index reflecting overall health of the Twin Cities real estate housing market each month. Another element of the index is using a three month moving average for each of the variables. The use of a smoothing average eliminates many irregularities and distortions that can occur on a month to month basis. The UST Residential Real Estate Index reports a composite value for the total market—after accounting for distressed sales—as well as individual indices for traditional, short and foreclosed sales.

The baseline for the index is the three-month period January through March of 2005, which was assigned a value of 1000. The January through March 2005 period was selected because that was near the apex of the residential real estate housing market. Each month's index can be compared to the previous month, year or market peak to understand the relative strength, direction and momentum of the Twin Cities housing market.

The raw data we use in our research originates from the Northstar MLS in co-operation with the Minneapolis Area Association of Realtors.