University of St. Thomas

Minneapolis St. Paul Residential Real Estate Index

April 2014

UNIVERSITY of ST. THOMAS
MINNESOTA

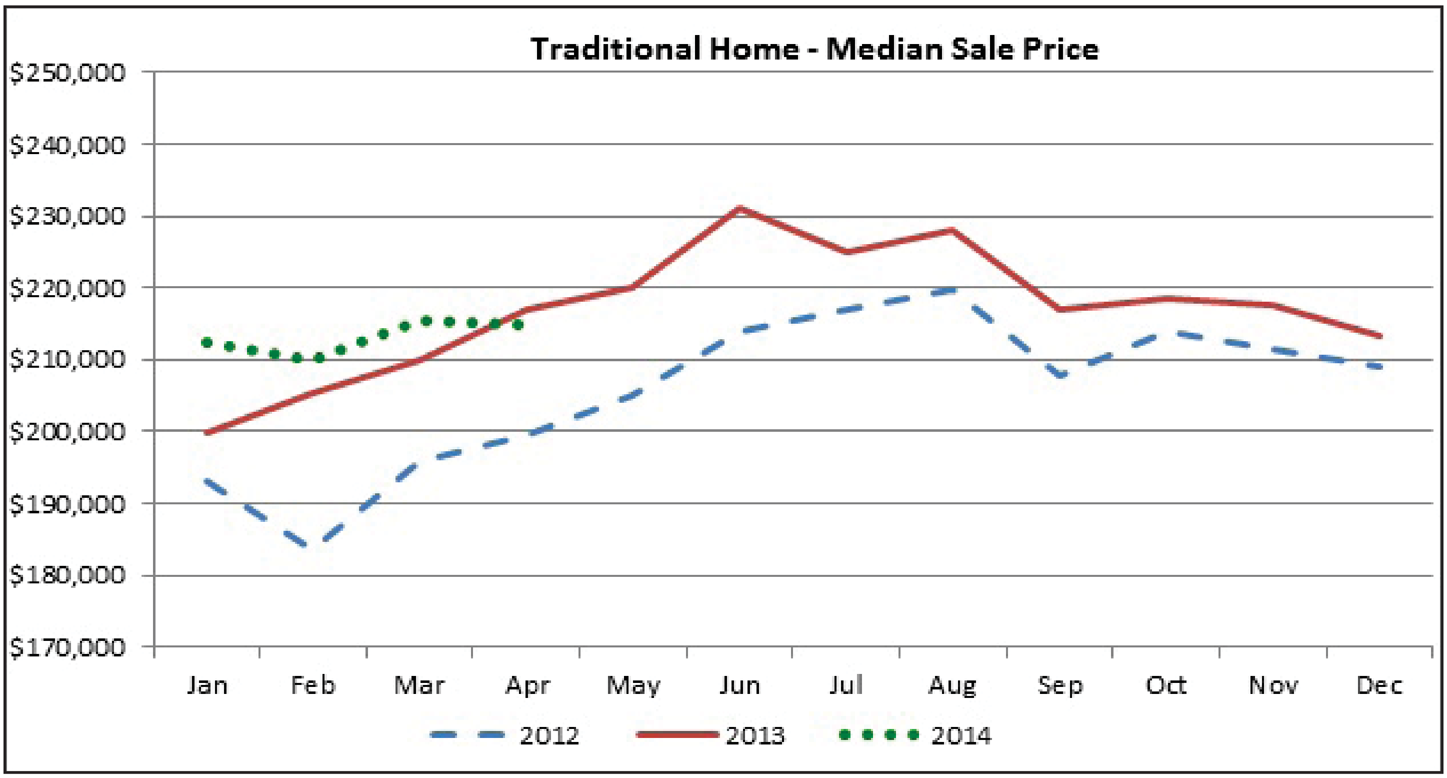
Real Estate
UST OPUS COLLEGE OF BUSINESS

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.

April 2014

The housing market in the Twin Cities continues to show mixed signals as we move into the 2nd quarter of 2014. Single family housing starts have rebounded in April, but year-to-date numbers remain barely ahead of last year at this time. Mortgage rates have touched a seven month low but the volume of closed sales remains below last year's levels. Median sale prices overall have increased but the median sale price of a non-distressed home in the Twin Cities has decreased compared to April 2013. The news is not all bad. The inventory of homes for sale has increased, the number of new listings has increased sharply, and the percentage of distressed sales and new foreclosures continues to fall.



Existing Homes

In April we observed something that we have not seen in over two years. While overall median sale prices for all sale categories in the Twin Cities metro increased moderately compared to last April, the median sale price of non-distressed homes sold in April of 2014 was actually slightly less than the median sale price in April 2013. In the chart above you can see where the dotted line has crossed the solid line. If this phenomenon were to continue into the late spring and summer months we will have to seriously re-examine our expectations of price increases for non-distressed homes for the remainder of the year.

On a positive note the number of closed sales was down compared to a year ago, however the decrease was mainly due to a reduction in the number of distressed sales as traditional non-distressed sales were up slightly compared to a year ago. The change in the proportion of non-distressed sales is also reflected in the fact that the percentage of distressed sales dropped from 26.8% in March to 21.1 % in April. In comparison, the April 2013 the percentage of distressed sales was 31.5%. We expect the percentage of distressed sales to continue to moderate, falling below 20% in the second quarter of 2014.

The inventory of existing homes for sale is improving slightly. At the end of April there were 14,675 homes for sale. This is a 3.25% increase over the number of homes available in April 2013. This is the second month in a row and the first time since the summer of 2012 that we have seen a year over year increase in the number of homes for sale. Another encouraging sign is the number of new listings increased sharply this month. In April there were 7,777 new listings, which is a 19.7% increase from March and is 10.2% higher than March of 2013. This is a healthy development as a continued increase in the number of homes for sale will lead to a better balance between the supply of homes for sale and the demand in the market.

New Home Construction

During April of 2014 the number of single family home permits reported by Keystone Report increased significantly over both the March and April 2013 levels. In April single family home permits were up 37.5%. This verifies our expectation that the spring construction season will see a flurry of new construction activity as home builders seek to make up for time lost due to harsh weather conditions in January and February. Year to date the number of single family permits is only up 0.65% compared to the same period in 2013. Look for the year-to-date increase in permitted single family homes to improve as the construction season moves into its peak months this summer.

Affordability

As we mentioned above mortgage rates have decreased to the lowest rates seen in the last seven months. The 30 year fixed rate is near 4.2% and the 15 year rate is under 3.5%. Recently the Federal regulators have instructed Fannie Mae and Freddie Mac to direct their focus to making more credit available to more homeowners. That is a major change in direction from previous directives to pull back from the mortgage market. Policy makers at the Federal Reserve have expressed worries that the housing sector, which in the past has been a key driver of an economic recovery, is struggling to shift into a higher gear. They are also concerned that first time home buyers will be unable enter the housing market due to high levels of student debt.

Expectations are that in order to sustain the economic recovery mortgage rates may not increase as much this year as was originally expected. Originally rates were expected to increase to around 5% by year end, however, if the recovery begins to falter during the year rates may not increase by quite that much.

UST Residential Real Estate Indexes	April 2013	March 2014	April 2014	Year to Year Change
Traditional Sale Index	1,009	1,005	1,021	1.19%
Short Sale Index	806	865	887	10.05%
Foreclosure Sale Index	730	738	757	3.70%

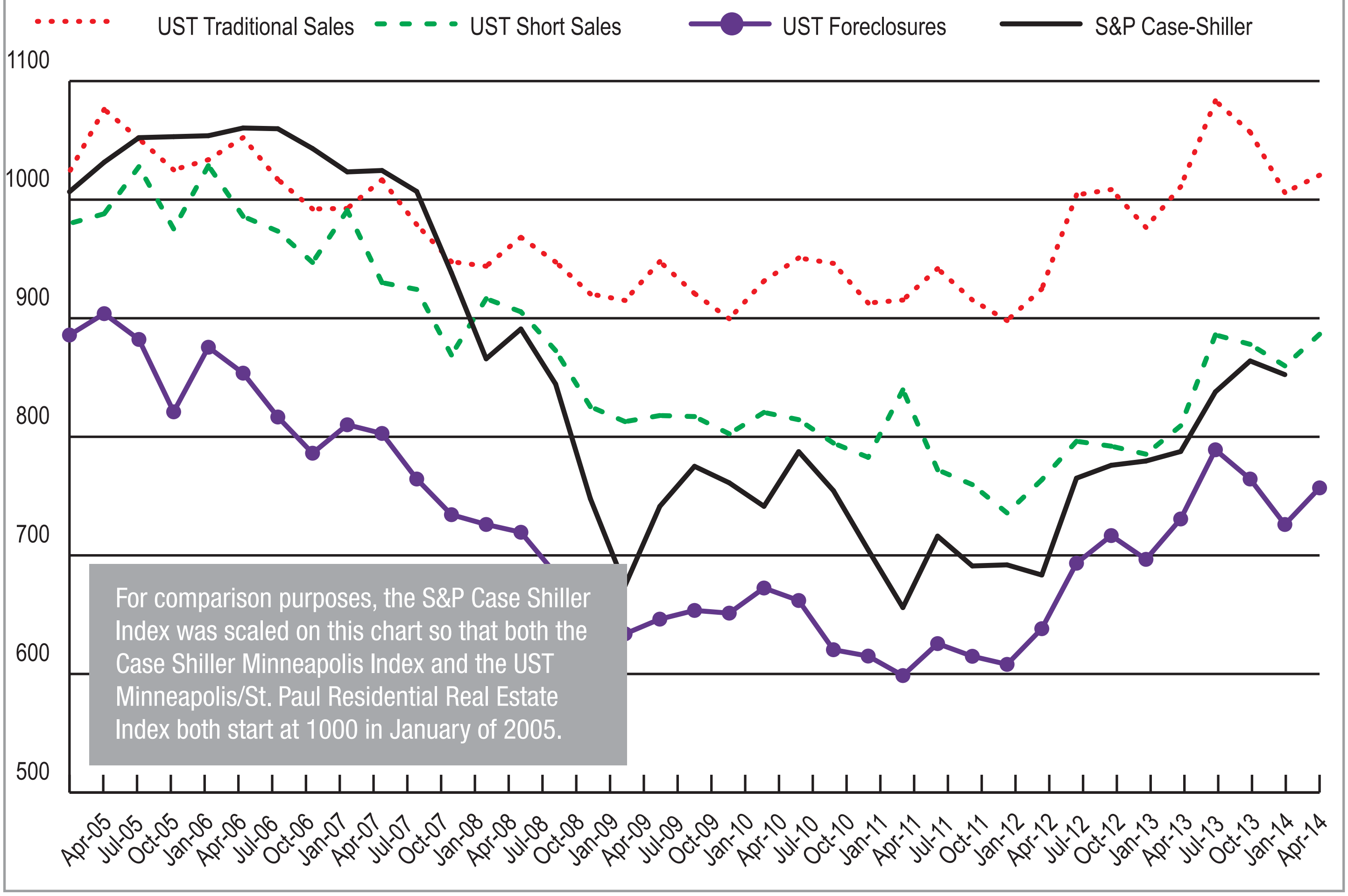
The UST Indices

The UST Traditional Sale Composite Index continued its upward trend in April, moving from 1,005 in March to 1,021 in March, a 1.6% increase. The index is 1.2% above the level recorded in April 2013.

The UST Residential Real Estate Short Sale Composite Market Health Index was 887 in April, up 23 points from the 864 recorded in March, a 10.05% increase compared to one year ago.

The foreclosure market's health as represented by the UST Residential Real Estate Foreclosure Composite Index increased in April, moving from 738 in March to 757 in April, an increase of 2.5%. The index remains 3.7% higher when compared to March 2013.

Minneapolis / St. Paul Residential Housing Composite Indices



April 2014 UST Index Data					
1. Median Sale Price	**April 2013**	**March 2014**	**April 2014**	**Monthly % Change**	**Annual % Change**
Traditional	$217,000	$215,400	$215,000	-0.19%	-0.92%
Short Sale	$135,000	$155,000	$147,000	-5.16%	8.89%
Foreclosed	$134,000	$136,550	$138,050	1.10%	3.02%
2. Closed Sales	4,322	3,211	3,847	19.81%	-10.99%
Traditional	2,962	2,346	3,026	28.99%	2.16%
Short Sale	321	156	195	25.00%	-39.25%
Foreclosed	1,039	706	619	-12.32%	-40.42%
3. % Distressed Sales	31.47%	26.85%	21.16%	-21.18%	-32.76%
4. Days on Market	97	95	89	-6.32%	-8.25%
5. Month's Supply	3.4	3.2	3.4	6.25%	0.00%
6. New Listings	7,059	6,494	7,777	19.76%	10.17%
7. Pending Sales	5,337	4,091	5,074	24.03%	-4.93%
8. Homes for Sale	14,210	13,601	14,675	7.90%	3.27%
9. % of Original Price	96.00%	95.00%	95.90%	0.95%	-0.10%

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

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.

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 15.3%. Our analysis of traditional housing sales for the same period, with a three-month moving average, reveals a price decline of 2%. Short sales and foreclosure sales had price decreases of 12.6% and 18.3% 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.