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Most over- and under-valued housing markets

Low prices bring investors back into many markets.

By Les Christie (CNNMoney.com)
Last Updated: June 4, 2009: 12:58 PM ET

NEW YORK (CNNMoney.com) -- Home price declines have sent affordability soaring. Prices have fallen so far that the average U.S. home is now undervalued by 12.2%, according to a new report from IHS Global Insight.

"The good news is that the declines are happening as consumer confidence is rising and housing sales and [building] starts seem to be bottoming out," said Jeannine Cataldi, senior economist for IHS in a statement accompanying the study.

"The bad news is that job losses continue at high rates, housing inventories are still elevated and consumers, while becoming somewhat more confident, are still wary in the face of economic uncertainty."

Prices still falling

The IHS study, *House Prices in America*, reported that, of the 330 markets it tracked, homes are under-priced in 248. That contrasts sharply with four years ago when only 108 markets were undervalued.

One-time bubble markets are now going through sales renaissances, according to Cataldi. "In Las Vegas and Phoenix, people are going in and snapping up foreclosures," she said. "They often rent them back to the former owners."

The report claimed the most undervalued metro area in the nation is Vero Beach, Fla., where the median home price has fallen 29.7% since the first quarter of 2005 to $125,400. That is 42.5% below the expectation. Houma, La., prices, at a median of $113,500, are undervalued by 41.4%. Las Vegas prices have dropped more than 46% since 2005, and the city is now undervalued by 40.9%.

To arrive at these figures, the analysis focused on three key factors of home affordability: income, housing densities and historical prices. IHS used that to define statistically normal house values for a given area and then compared them with the actual prices. The difference between those two figures determines how much a place is under - or over - valued.

And there are still some over-valued areas. Atlantic City, N.J., for example. Here the median price is $243,600, an overvaluation of 44.1%, the most of any metro area. The Ocean City, N.J., median price of $302,100 is the second most overvalued, at 33.8%. In third place is Wenatchee, Wash., which at $247,100, is 29.3% above normal.

In the biggest metro area, New York City, the price is just about right, with a median at $469,400, an under-valuation of just 3.3%. Los Angeles ($357,100) is a bit further off, undervalued by 6.6% and Chicago ($220,800) is down 13.2%.

One may presume that the undervalued cities should return to their natural equilibrium and astute real estate investors and homebuyers could pounce on bargains and make a profit later. But Cataldi thinks that could take a long time. "Price declines are slowing but we're still cautious," she said. "We're predicting stagnant prices through 2011."

Bottom fishing

In Florida, there are many condo developments with listings ripe for plucking, either in bunches or individually, according to Matt Martinez, who represents a private equity group that is investing hundreds of millions of dollars there. He reports that investors are able to make profits of 7% to 8% a year, after all expenses, by buying condos and then renting them at market rates.

"Even higher [profits] exist on some highly distressed fractured condo deals where the lenders are selling the notes," he said.

In California, sales of deeply discounted distressed properties are flourishing, according to the California Association of Realtors. Inventory of homes priced under $500,000 has shrunk to a three-month supply at current rates of sale while the supply of million-dollar homes has expanded to 17 months.

"The dramatic difference in inventory exemplifies how the low end of the market is attracting more first-time buyers and investors, creating a shortage of distressed properties for sale," said James Liptak, president of CAR, in a statement accompanying the sales data.

Even the battered Michigan market is attracting investors, according to the CEO of the Michigan Association of Realtors, Bill Martin.

"It tends to be in the low-to-middle price range that is moving," he said. "There has been investment buying, mostly concentrated in Detroit. People are buying up bundles of 100 to 200 homes."

The median single-family home in the Detroit metro area -- where layoffs may threaten any recovery -- sold for $77,700 during the first three months of 2009, according to the IHS report, but many repossessed homes in the city itself are packaged and sold as bundles and can be had for under $10,000 apiece.

These markets may be in the forefront of a market recovery but, according to the IHS report, it's too early to call a bottom.

"More observations through the spring will be needed to support this trend," it said. ■

First Published: June 4, 2009: 12:19 PM ET