University of St. Thomas
Minneapolis St. Paul
Residential Real Estate Index
January 2013
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.

January 2013

The housing data in January continues to exhibit many of the encouraging market trends that have been observed over the last 12 months. The median price of a traditional (non-distressed) home sale was recorded at $199,900, a decrease of 4.4% compared with December, yet it is a 3.6% increase over the January 2012 level. The volume of closed sales in January 2013 was 2,797. That is a 20% decrease from the 3,496 sales that closed in December; however it is 11% higher than the number recorded in January 2012.

The UST Traditional Sale Composite Index decreased again in January (down 1.6%) moving from 994 in December to 978 in January. The decrease is showing the continued effect of the seasonal decline in the median sale price of traditional homes that started in November. It should be noted that despite the fact that the index has decreased in the last several months, this January’s index of 978 is 9.1 % higher than what was recorded in January 2012 when it was 896.

The UST Residential Real Estate Short Sale Composite Market Health Index in January was 786, a 6.8% increase compared to one year ago.

The foreclosure market’s health as represented by the UST Residential Real Estate Foreclosure Composite Index recorded a slight increase in January, moving from 698 in December to 699, and it is up 13.8% compared to January 2012. The Foreclosure Index continues to show evidence of stabilization. During the previous six months it has fluctuated in a narrow range between 698 and 705.

The percentage of distressed sales, while historically high, continues to remain well below last year’s levels. In January 2013 the percentage of distressed sales was 42.9% compared with 54.8% in January 2012 and 60.9% in January 2011.

The inventory of homes for sale continues to decline. In January there were 11,977 homes for sale. This is the lowest number of homes for sale that has been recorded in the last 10 years. The inventory of homes for sale in January 2013 is 32% less than the 17,655 homes that were available for sale in January 2012. One measure of the health of the market is to examine the ratio of homes on the market for sale and the number of homes sold. In January there were only 4.28 homes for sale for every home sold. This is a very low level when compared to historical data. In January 2012 there were 6.8 homes for sale for every home sold. Historically, in a balanced market the ratio typically falls between 6 and 10 homes for sale for every one sold. The good news for sellers is that as we move into the spring market more potential buyers will find a limited number of homes for sale which will put upward pressure on prices.

The fact remains that many homeowners are still under water or have little equity in their homes; that, along with feelings of general economic uncertainty surrounding the federal government’s automatic tax increases and budget cuts (commonly called “sequester”) has kept many current and potential home owners on the sidelines. Assuming the sequester issue is resolved favorably, housing prices should begin to increase, causing homeowners’ equity positions to improve resulting in more sellers deciding to list their homes for sale.

<table>
<thead>
<tr>
<th>UST Residential Real Estate Indexes</th>
<th>January 2012</th>
<th>December 2012</th>
<th>January 2013</th>
<th>Year to Year Change</th>
</tr>
</thead>
<tbody>
<tr>
<td>Traditional Sale Index</td>
<td>896</td>
<td>994</td>
<td>978</td>
<td>9.15%</td>
</tr>
<tr>
<td>Short Sale Index</td>
<td>737</td>
<td>796</td>
<td>787</td>
<td>6.78%</td>
</tr>
<tr>
<td>Foreclosure Sale Index</td>
<td>607</td>
<td>698</td>
<td>699</td>
<td>15.16%</td>
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</tbody>
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January 2013
2013 – Where Do We Go From Here?

What do these events mean for 2013? Interest rates are expected to remain at current extremely low levels during 2013. Low interest rates, a shortage of homes for sale, and generally improving economic conditions will continue put upward pressure on median sale prices through the spring and summer. The median sale price of all types of homes should continue to show healthy year over year increases for the first half of the year. As home prices continue to increase, homeowner’s equity positions will continue to improve and more homes will be put on the market, increasing the supply of available homes. As the supply of homes increases and the shortage abates, the market should become more balanced. Once this happens prices will continue to increase, although at a slower rate. Look for annualized increases in median price of 2% to 3% in the second half of 2013. The number of foreclosures and distressed sales will continue to moderate in 2013. The percentage of distressed sales should fall into the 25% to 35% range in comparison with the 35% to 55% range that was observed in 2012. The shortage of homes for sale coupled with an increase in the rate of household formation that comes with an improving economy will continue to create opportunities for home builders. New construction of both multi-family and single family homes should continue to increase throughout the year with 2013 bringing much needed relief to home builders and the construction industry.
### January 2013 UST Composite Index Data

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</thead>
<tbody>
<tr>
<td>Traditional</td>
<td>$193,000</td>
<td>$209,000</td>
<td>$199,900</td>
<td>-4.35%</td>
<td>3.58%</td>
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<tr>
<td>Short Sale</td>
<td>$122,000</td>
<td>$134,250</td>
<td>$125,500</td>
<td>-6.52%</td>
<td>2.87%</td>
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<tr>
<td>Foreclosed</td>
<td>$102,000</td>
<td>$123,000</td>
<td>$124,900</td>
<td>1.54%</td>
<td>22.45%</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>2. Closed Sales</th>
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</tr>
</thead>
<tbody>
<tr>
<td>Traditional</td>
<td>2,519</td>
<td>3,496</td>
<td>2,797</td>
<td>-19.99%</td>
<td>11.04%</td>
</tr>
<tr>
<td>Short Sale</td>
<td>1,127</td>
<td>2,129</td>
<td>1,598</td>
<td>-24.94%</td>
<td>41.79%</td>
</tr>
<tr>
<td>Foreclosed</td>
<td>972</td>
<td>932</td>
<td>903</td>
<td>-3.11%</td>
<td>-7.10%</td>
</tr>
</tbody>
</table>

| 3. % Distressed Sales| 54.78%       | 39.07%        | 42.90%       | 9.80%            | -21.69%         |

| 4. Days on Market    | 141          | 108           | 107          | -0.93%           | -24.11%         |

| 5. Month's Supply    | 5.0          | 3.0           | 2.9          | -3.33%           | -42.00%         |

| 6. New Listings      | 5,114        | 2,855         | 4,799        | 68.09%           | -6.16%          |

| 7. Pending Sales     | 3,049        | 2,902         | 3,456        | 19.09%           | 13.35%          |

| 8. Homes for Sale    | 17,655       | 12,369        | 11,977       | -3.17%           | -32.16%         |

| 9. % of Original Price| 91.20%       | 93.80%        | 93.50%       | -0.32%           | 2.52%           |

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**Real Estate at the Opus College of Business**

**Shenehon Center for Real Estate** [www.StThomas.edu/Shenehon](http://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](http://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](http://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.
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 22%. Our analysis of traditional housing sales for the same period, with a three-month moving average, reveals a price decline of 2.9%. Short sales and foreclosure sales had price decreases of 19.1% and 20.9% respectively. The Case-Shiller Index also uses a three-month moving average.

About the Authors

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Herb is the director of the Shenehon Center for Real Estate and Master of Science degree in Real Estate at the University of St. Thomas Opus College of Business. His research specialties include housing studies, affordable housing and commercial market analysis. Herb received a Bachelor of Science degree in business from Colorado State University and an M.B.A. from the University of St. Thomas.

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Tom is an associate professor of Real Estate with the Department of Finance at the University of St. Thomas Opus College of Business. His research specialties include public utility valuation and real estate feasibility studies and investment analysis. He received a Bachelor of Science degree in natural resources from the University of Wisconsin and a Master of Science degree in Finance from the University of Wyoming. He received an M.B.A. and Ph.D in Urban Land Economics from the University of Wisconsin.
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.