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OF SOUTH CENTRAL WISCONSIN

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Dave Stark

As predicted in our last issue of the Market Source, closing activity for the second quarter continued its steady improvement over the same period in 2009. For the three months ended June 30, 2010, the closings in the combined Dane, Sauk and Columbia markets showed a strong 27% increase over Q2 2010. For the year to date, closings are up 25%. For the 12 month period from July 1, 2009 to June 30, 2010, all three counties turned in performances that are not far from what we estimate to be a normal pace of business, with 7,250 combined sales, up 23% from 5,888 a year ago.

That's the good news. As we also discussed in our last issue, the expiration of the federal government's home buyer tax credit was upon us, and we predicted that new offer activity would decline noticeably after the passing of the April 30 deadline by which offers had to be accepted to qualify for the credit. While data from the MLS on current offer activity is always spotty since offers are frequently not reported until they close, a look at May data is still highly suggestive. In Dane County, single family and condo offers in May of 2009 totaled 654. So far in May of 2010, only 282 offers have been reported. While that number will still go up as offers yet unreported close, it's unlikely we'll get anywhere near the 2009 total. June looks a little better, but is still far below the level of 2009, and below the pace of the year through April. Speaking of April, there have been a whopping 938 offers reported so far this

DANE COUNTY

	Single Family			Condominiums			Total Residential		
	2010	2009	2008	2010	2009	2008	2010	2009	2008
2nd Quarter Closings	1,651	1,270	1,399	510	364	426	2,161	1,634	1,825
Year-to-Date Closings	2,283	1,827	2,100	717	506	650	3,000	2,333	2,750
Active Inventory	3,036	2,734	3,053	1,661	2,182	2,388	4,697	4,731	5,235
Months of Inventory	6.9	8.1	8.2	12.3	20.7	19.3	8.2	10.9	10.8
3 Month Median	\$218,000	\$217,500	\$228,700	\$145,250	\$150,000	\$160,000	\$200,000	\$201,500	\$214,900
12 Month Median	\$219,000	\$223,750	\$234,266	\$147,900	\$160,900	\$165,550	\$200,000	\$210,000	\$217,900

SAUK COUNTY

	Single Family			Condominiums			Total Residential		
	2010	2009	2008	2010	2009	2008	2010	2009	2008
2nd Quarter Closings	138	156	138	21	17	25	159	173	163
Year-to-Date Closings	233	227	221	33	18	33	266	245	254
Active Inventory	767	724	684	221	239	219	988	963	903
Months of Inventory	21.0	17.5	18.7	39.7	53.0	33.0	23.4	21.0	20.9
3 Month Median	\$145,000	\$146,500	\$158,000	\$155,000	\$175,000	\$152,500	\$149,000	\$150,000	\$156,000
12 Month Median	\$135,000	\$142,800	\$162,500	\$148,000	\$157,750	\$161,900	\$136,500	\$145,000	\$162,500

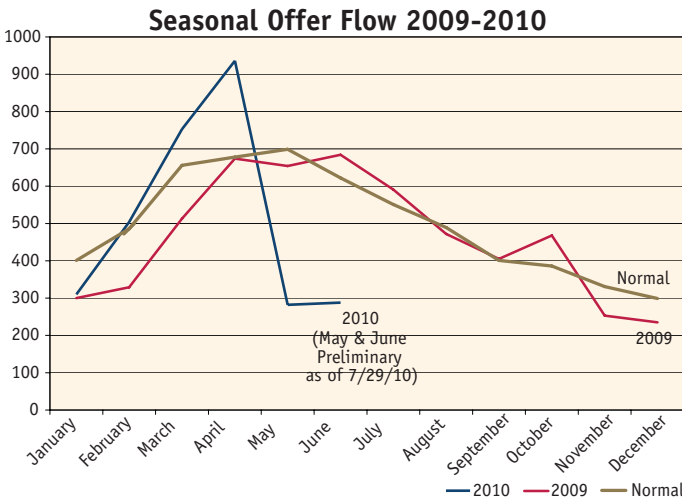
COLUMBIA COUNTY

	Single Family			Condominiums			Total Residential		
	2010	2009	2008	2010	2009	2008	2010	2009	2008
2nd Quarter Closings	171	146	126	9	11	12	180	157	138
Year-to-Date Closings	253	220	203	14	19	15	267	239	218
Active Inventory	735	725	657	132	117	177	867	842	834
Months of Inventory	16.2	18.7	19.7	55.3	40.1	55.6	18.2	20.2	22.8
3 Month Median	\$140,000	\$146,100	\$165,500	\$145,900	\$225,000	\$147,250	\$141,950	\$149,500	\$165,000
12 Month Median	\$142,000	\$145,000	\$162,000	\$128,500	\$173,000	\$145,000	\$140,000	\$149,900	\$159,450

* Closed sales reported to the SCW MLS between 4/01/10 and 6/30/10. Data for all years pulled between the 15th & 21st of the month following the end of quarter. "Months of Inventory" represents the number of months it would take to sell the entire active inventory at the pace of sales for the most recent quarter represented, adjusted to account for seasonal variations.

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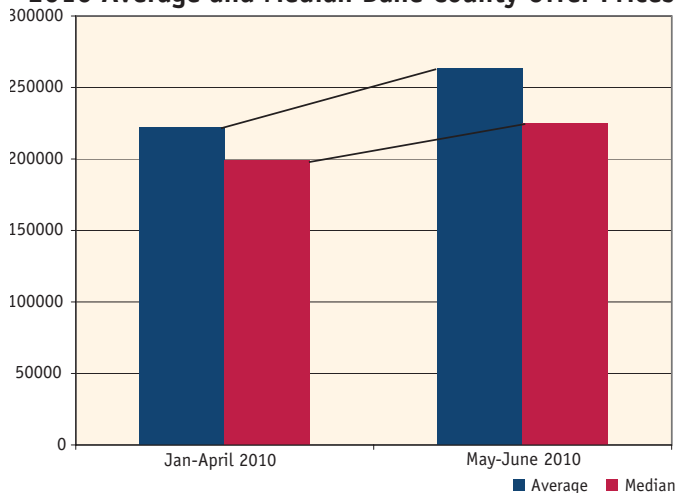
year. Last year, there were 674. The chart below shows how monthly offer activity for 2009 and 2010 so far compares with a “normal” seasonal curve at 6000 sales, about what we did in the most recent 12 months.



Obviously, going from 938 offers in April to 282 in May is a little bit of a shock to the system. Normally, those two months are fairly similar in the volume they generate. April was one of the best offer months we’ve ever seen. May was one of the worst. However, if you add the two together and average them out, you get pretty close to normal for each. Through April, reported offers year to date were up 38% over last year. When we get everything reported through June, we’ll probably be back to even with last year. Obviously, a great many buyers accelerated their offers into April to preserve their eligibility for the credit. The passing of the deadline has created a sizeable vacuum in demand that is still being refilled as we write this edition. How offer activity rebounds from here will determine what kind of year this is going to be.

Frankly, this is a very confusing time in the marketplace for buyers, sellers, and real estate professionals. We’ve been saying for some time now that the tax credit has had a very distorting effect on the market, making it hard for all involved to plan and make good decisions. We know with certainty now that July and August closings will underperform last year, probably by sizeable amounts. That should not in and of itself be taken as a sign that the market is slowing again, and in fact, we fully expected this to happen. Rather, it means that this year will not follow the normal seasonal pattern, and we probably won’t know until the very end just how good it will be. It also means that we won’t know for a while yet, perhaps not until next year, what the current sustainable, un-subsidized sales rate is for our market. Our best guess

2010 Average and Median Dane County Offer Prices



is that the total for this year will be a good indicator of what we can expect next year.

Here’s one more good, and very interesting, piece of news. Our readers will recall we’ve been saying for some time that the first time homebuyer tax credit has had the effect of reducing the median prices in our market by skewing activity to the lower end of the range. From January through April, the median was \$199,000. For offers reported so far in May and June, the median is back up to \$225,000. Anecdotally, we’ve been hearing that activity in the upper ranges is starting to pick up again. This tells us two things. First, we were absolutely correct that the reductions we were seeing in overall median prices were influenced heavily by the stimulus to the lower end of the market. And second, once the stimulus was removed, the averages bounced right back up, which tells us that our overall price levels remain largely intact. While we think prices will continue to be fairly flat for the balance of this year at least, the fundamental value of our market is still strong.

THE EUROPEAN INTEREST RATE GIFT

Nearly all forecasters, including yours truly, have been predicting for some time that interest rates are about to rise. There were two main reasons for the consensus. First and probably foremost, the Federal Reserve recently stopped a massive 1.25 trillion dollar program to buy mortgage backed securities. The program expired on schedule on March 31, and most observers reasoned that the void in demand when the Fed exited the stage would cause rates to rise (the whole purpose of the Fed program, after all, was to keep rates low). The second, tangentially related reason was that the combination of Fed buying and federal government stimulus (TARP, and the 800 billion dollar stimulus plan) would ultimately spark inflation fears, which generally cause interest rates to rise.

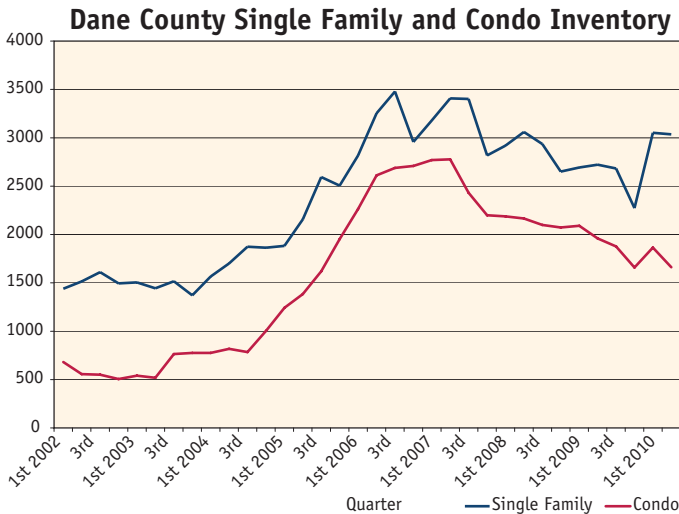
In defiance of these two powerful drivers, mortgage rates have fallen to record lows. How can this be? Part of the answer, in somewhat over-simplified terms, is the European sovereign debt crisis, and the subsequent fall of the Euro against the Dollar. In essence, investors worried about the risk of default in Greece and elsewhere went on a classic “flight to quality”, buying dollar denominated assets, including US Treasury securities. At this writing (July 19th), yields on 10 year Treasury Securities, which heavily influence 30 year mortgage rates, remain at an historic low 2.95%. 30 year rates themselves are currently being quoted at around 4.5%. To be sure, there are other related influences, not least of which are some disinflationary fears, and a choppy stock market, both of which also tend to push investors to safer bonds. While rates will indeed some day have to rise, the current environment is an unexpected opportunity that should not be missed.

A rule of thumb you can use to see how powerful this is we call the “10% rule.” Roughly speaking, a 1% increase in interest rates translates into a 10% decrease in the amount of house you can buy for the same monthly payment. If nothing else, if you can save 1% or so on your current mortgage rate, you should definitely look into refinancing. While we fear we’re starting to sound like a broken record, the fact remains this environment won’t last forever. If you miss it, don’t say you weren’t warned.

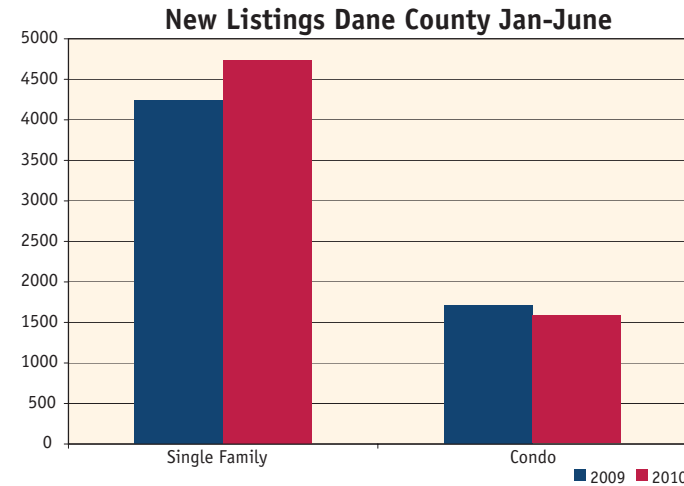
INVENTORIES IMPROVE

In our last issue, we expressed surprise at the sudden spike in inventories we were seeing, particularly in single family. At the time, we guessed they would come back down with the heavy closings expected in May and June. This has happened to some extent, but most of the improvement, oddly, has been in condominium inventories. Single family inventories remain somewhat elevated from a year ago. See the chart that leads off the next column for an illustration of how this trend is unfolding.

The improvement in condo inventories can be viewed two ways. Condo sales are up more in percentage terms than single family home sales are, which is bringing inventories down. Most condos are less



expensive than single family homes, making them perfect for first time home buyers. Also, there have been fewer new condo listings to the market than last year, while there were more single family listings taken through June of 2010 (see the chart below). On the other hand, most condo listings are marketed new by the developer, and one wonders if some units are being held off the market until conditions improve. We know some developers have rented their units rather than carry them empty much longer. And, not surprisingly, it's been a while since any new condo projects have been announced.



Single family inventories remain a puzzle. The influx of new listings has certainly been a factor. What's drawing those listings in is the question. In all likelihood, there are many who would like to be buyers, if they can first be successful sellers. Many were probably attracted by the active spring market, some perhaps relisting after giving it a rest from last year. The big drop in the fourth quarter of last year, followed by the spike back

in Q1 of this year, suggests that many sellers may have withdrawn when the first tax credit expired, then came back in the spring trying to catch the second. Now that the credits are gone for good, it will be interesting to see how sellers respond as we move into the fall.

One more note on inventories. Each quarter, we publish a "months of inventory" calculation (on the first page) that measures how many months it would take to sell the entire current inventory at the pace of sales for the most recent quarter, seasonally adjusted. 6 months of inventory is considered a "balanced market." In Dane County at least, we approached that number in single family, and made big progress in condos. Sauk and Columbia Counties still have a way to go. However, we need to prepare our readers for this number to go back up, at least for the third quarter, based on the closing decline we will certainly see. Again, this is something we fully expected, and you should not be surprised when you see it in our next edition, due in November. We'll analyze it in more detail then, when we have more data on how the market is adapting, and give you a better read at that time on how sales and inventories are truly relating to each other.

INVESTMENT IN REAL ESTATE GOING FORWARD

We'd like to close this issue by referring back to a prior issue of the Market Source, where we outlined how real estate works as an investment (please go to www.starkhomes.com, click on "Market Source Newsletter and Published Articles", and go to the 4th Quarter 2008 issue). There, you'll find a discussion of "How Real Estate Works", and a section on "Why to Buy in Our Market Now." The principles laid out there are every bit as valid today as they were then. In fact, they may be more so now. In a healthy market, real estate has always been a "get rich slow" investment. Everyone needs a place to live, and owning your own home, "paying rent to yourself," is one of the smartest long term investments you can make. We emphasize "long term," because real estate has always been a long term store of value, a fundamental, bedrock asset, not a financial asset that rises and falls with the short term whims of speculators. That's what started to happen in the early part of this decade, and look where it got us. Ideally, real estate should be held for a minimum of five years (the longer the better,) for the benefits of owning to start to show, and appreciation should be slow. With the economy slowly improving, interest rates at record lows, prices more reasonable than they've been in years, what would you wait for? The heavy demand fueled by the tax credit tells us that people still want to own their own home. Taking the long view, it shouldn't take a tax credit to induce you to make that investment. Do it because it makes the kind of life you want to live possible. That's the best reason to buy real estate.

NEWS FLASH

Our regular readers know that we are not fans of national real estate indexes, the S&P Case-Shiller Index in particular. We nonetheless find it ironic, since so much attention was paid to this index during the period when prices were falling in the 20 markets it measures (none in Wisconsin), that it seemed to have gone unnoticed, as we go to print, when the May 2010 Case-Shiller Index was released showing a 4.6% increase in housing prices over May of 2009. Just thought you'd like to know.

ADVICE FOR BUYERS AND SELLERS

BUYERS

The previous paragraph said it all. If you're looking for a place to put down your roots and pursue the life you've always wanted, the window of opportunity keeps being pushed back open. Look for a place you love, buy it with a fixed rate mortgage, put some money down, make sure you're comfortable with the monthly payment, and live there for 5 years or more. Over the long run, your equity will grow, and your lifestyle will improve. With record low rates and inventories still ample, it's hard to see your cost of ownership ever being any cheaper.

SELLERS

It's clear that many buyers accelerated their purchases into April. Since then, demand has been very soft. If you listed in the spring hoping to catch that wave, you've missed it. While record low interest rates should eventually shake smart buyers out of the trees, they haven't yet overcome the vacuum created by the tax credit expiration, and it's not clear how quickly demand will return to normal. If you don't need to sell now, our advice would be to withdraw from the market and try again next spring. If you do need to sell, you'll have no choice but to position your home as attractively as you possibly can.

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TREND WATCH

Likely direction next 6 months

Number of homes sold (12 Months)

	Dane	Sauk	Columbia
12 mo. ended, 6/30/10	6,075	590	585
12 mo. ended, 3/31/10	5,603	606	561
12 mo. ended, 6/30/09	4,941	509	438



Comments

We hate to draw this arrow but the tax credit vacuum will be big in Q3.

30 Year Mortgage Rates

June 2010	4.74%		
March 2010	4.97%		
June 2009	5.42%		

Source: Freddie Mac



European debt crisis was a wild card sending rates lower. Money is on sale - get it!

Median Sales Price – Single-Family & Condos (12 Months)

	Dane	Sauk	Columbia
12 mo. ended, 6/30/10	\$200,000	\$136,500	\$140,000
12 mo. ended, 3/31/10	\$201,000	\$138,250	\$144,000
12 mo. ended, 6/30/09	\$210,000	\$145,000	\$149,500



The tax credit is gone, so the lower end will no longer dominate.

Building Permits – Dane County Single-Family

	2nd Quarter	Year-to-Date
2010	164	336
2009	172	281
2008	216	380

Source: MTD Marketing Services



Hard to see improvement with tax credit gone, inventories still high

Inventories – Single Family & Condo

	Dane	Sauk	Columbia
June 2010	4,697	988	867
March 2010	4,916	968	839
June 2009	4,731	963	842



They are down a little, as predicted. Hard to see improvement for next 6 months.

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