U.S. foreclosure 'crisis' is overblown

Sure, there are pockets of pain around the U.S., but it's not as if most Americans are losing their homes. More than 99% of homes aren't in foreclosure.

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A recent list of year-end mortgage foreclosure rates in 100 top U.S. metropolitan areas drew a lot of attention. Released by RealtyTrac, a company that compiles data on home foreclosures, the list showed the number of foreclosure filings in each metro area, the percentage of homes being foreclosed and the percentage change from the previous year.

- Though the report had some dismal news -- such as the nearly 4.9% foreclosure rate in the Stockton, Calif., area -- a close look at the data also provides some reassuring information. It tells me, for instance, that the foreclosure crisis is a regional problem, not a systemic one. It could become a systemic problem, of course, but we're a long way from that now.

- This news will disappoint the gloom-and-doom crew and all those seeking the excitement of financial upheaval. But it may be time to temper our worry and take a closer look at some of the year-over-year foreclosure statistics:

- Though the U.S. rate of foreclosure increased by a whopping 79% between December 2006 and December 2007, the rate was still only 1.033%. Because about 30% of all homes are owned mortgage-free, this means that for all the noise about a crisis, only seven-tenths of 1% of all homes were in foreclosure.

In the top 100 U.S. housing markets, the average foreclosure rate was somewhat higher -- 1.38% -- and it was up 78% over the previous year. But if you rank-ordered the list of the top 100 areas, only 34 had foreclosure rates above the group average. Fifty-one areas had rates of 1% or less.

Foreclosure rates actually fell in 14 of the 100 areas. More important, many of the areas with the highest increases in foreclosure rates were rising off rates that were tiny. The Bethesda, Md., area, to offer the most extreme case, saw foreclosures rise 1,288% -- to a rate of 0.682%. In other words, foreclosures there were virtually nonexistent the year before. Today they are still well below the national average. The same can be said for the Albany, N.Y., area (up 638% to 0.25%), the Baltimore area (up 544% to 0.73%) and the Providence, R.I., area (up 354% to 0.41%).

Another pattern emerges if you cross the foreclosure rates with the U.S. Office of Federal Housing Enterprise Oversight (OFHEO) index of home prices. It shows that the top 10 foreclosure areas in America are areas of extreme price change -- changes far from the U.S. average of 46.92% over the past five years. (See the table below.)

Seven of the top 10 foreclosure areas had experienced major price spikes in the past five years. Three of the top 10 foreclosure areas had experienced price increases that were dramatically lower than the U.S. average. That pattern continues when you examine the top 25 foreclosure areas.

A tale of two extremes: Metro area Foreclosure rate, December 2007

Metro area	Foreclosure rate, December 2007	Year-over-year increase of foreclosures	5-year home-appreciation rate
Detroit/Livonia/Dearborn, Mich.	4.92%	68.15%	-0.92%
Stockton, Calif.	4.87%	271.30%	65.07%
Las Vegas/Paradise, Nev.	4.23%	169.11%	88.33%
Riverside/San Bernardino, Calif.	3.83%	186.14%	107.80%
Sacramento, Calif.	3.12%	272.54%	56.90%
Cleveland/Lorain/Elyria/Mentor, Ohio	2.97%	112.43%	9.36%
Bakersfield, Calif.	2.96%	244.82%	113.82%
Miami	2.72%	106.13%	114.98%
Denver/Aurora, Colo.	2.64%	27.19%	10.83%
Fort Lauderdale, Fla.	2.63%	110.05%	94.29%
National average	1.03%	79.21%	46.92%
Average of top 100 metro areas	1.38%	78.23%	Not available
Sources: RealtyTrac, OFHEO			

The seven areas with the top price appreciation for the past five years averaged a stunning 91.6% increase, nearly double the U.S. average. The U.S. average, in turn, was about triple the inflation rate for the period.

Small wonder the foreclosure rate is booming as well. Anyone who bought in the past few years with a 5% or 10% down payment has a good chance of being upside down as froth comes off the market. In those areas the problem is about irrational price spikes and the hazards they bring to homeownership.

Some would call this "a Cadillac problem" -- a great problem to have, like having more boats than you have water-skiers. Though 5% of the homeowners may be losing their homes, most of the other 95% probably feel significantly richer.

How much richer? Try this. Suppose you paid three times your income for a house and it nearly doubled in value over five years. What does that mean? It means your net worth grew by nearly three years of income. Try achieving that with your retirement plan. Even if you bought halfway through the surge, your gain is likely to be well more than one year of income. However you cut it, the change compares quite favourably with working and saving.

The three metro areas with low price appreciations are a different matter. Homeowners in Detroit have actually lost money on their homes over the past five years. That, in turn, has limited their ability to make up for income shortfalls by borrowing against home equity. Add a shrinking job market, and places such as Detroit are coping with a perpetual surplus of sellers over buyers.

One indication is the cost of renting a U-Haul truck. It recently cost $1,447 to rent a 26-foot truck to move from Detroit to Dallas but only $521 to rent the same truck to move from Dallas to Detroit. The real economic problem, for the most people, isn't the price-spike states. It's the deflation states.

Questions about personal finance and investments may be e-mailed to scott@scottburns.com. Questions of general interest may be answered in future columns.