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Inter-Departmental Memo

To: Hon. Judy Jacobs, Chairperson
All Members of the Budget Review Committee

From: Eric C. Naughton, Director
Legislative Budget Review

Date: May 15, 2008

Re: Economic Outlook Reports

This report on the residential housing market is the first of a series of "Economic Outlook Reports" targeting leading sectors of Nassau County's economy and how they impact County residents. These categories include the real estate market, consumption, tourism, consumer prices, employment and the residential housing market. We also forecast for several regional and national economic variables, to assist the County with its multi-year projections for several major revenue and expense categories. The forecasted data are obtained from Moody's Economy.com, a leading independent provider of economic, financial, country, and industry research.

cc: Hon. Howard Weitzman, County Comptroller
Martha Wong, Acting Director, OMB
Chumi Diamond, Clerk of the Legislature
Edgar Campbell, Chief of Staff
Eric Eichenlaub, Majority Counsel
Roseann D'Alleva, Majority Finance
Christopher Ostuni, Minority Counsel
Evan Cohen, Executive Director, NIFA
Dan McCloy, Special Assistant Minority
Tom Stokes, Deputy County Executive
Charo Ezdrin, Director of Legislative Affairs

**THE IMPACT OF CURRENT ECONOMIC CONDITIONS
ON THE REAL ESTATE MARKET IN NASSAU COUNTY
MAY 2008**

**NASSAU COUNTY
OFFICE OF LEGISLATIVE BUDGET REVIEW**

As we move into the second quarter of 2008, the economic outlook of Nassau County mirrors the uncertainty and recessionary environment of the entire nation. Most recently in its ongoing attempt to spur the economy, the Federal Reserve continued cutting its target for the federal funds rate to 2 percent. This was the seventh reduction in a campaign that has brought rates down by 3.25 percentage points since mid-September when the Fed began its expansionary approach.¹

According to USA Today's quarterly survey of leading economists, two-thirds of the 52 economists polled believe the economy is already in recession, while others believe that the economy will contract at some point in 2008.² The good news is that these economists further believe the recession will be short and shallow, with unemployment rising to about 6%, a rather low percent for a recession. Nonetheless, we are reminded by Allen Sinai, chief global economist for Decision Economics that many things, such as inflation and consequently the prices of food and oil (due to the high demand for food and energy by India and China) are forces that are outside the Fed's control. The other big worry: real estate. "Given the drop in home prices, there's a big risk that foreclosures will go up more than expected," David Berson, leading economist for the PMI Group asserts.³

Keith Hembre, chief economist for First American Funds, believes further weakening of the U.S. economy could cause the central bank to start cutting once again later this year or early in 2009. On the other hand, Rich Yamarone, director of economic research at Argus Research, believes the Fed's next move will be to raise rates to combat building inflationary pressures. He points out that the real fed funds rate, which is the fed funds rate minus the inflation rate, is now negative 1.27%. Adjusted for the increase in the consumer price index, the real federal funds rate has averaged positive 1.75% since 1956.

The question remains for the nation in general, and Nassau County in particular, whether the financial system is back on track from the fallout of the sub-prime mortgage debacle and credit market turmoil, or if the threat of further weakening remains. Recently, Federal Reserve Chairman Ben Bernanke

¹ The fed funds rate, as it is more commonly known, is a benchmark for home equity lines of credit, credit cards and other consumer loans as well as the prime rate used for short-term business loans.

² Waggoner, J. and Hansen, B. "USA TODAY survey: We're in recession, economists say", [USA Today.com](http://www.usatoday.com) April 28, 2008

³ Ibid.

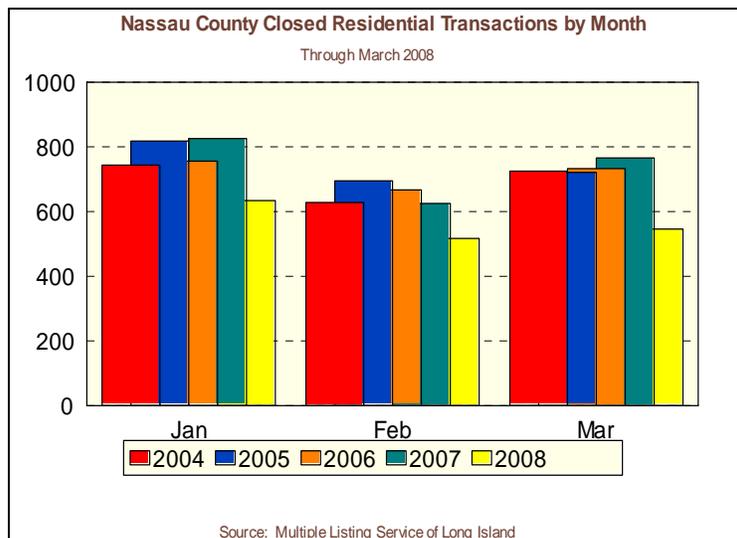
warned that some 1.5 million U.S. homes entered into the foreclosure process last year, up from 53% from 2006, further suggesting that new foreclosures look likely to be even higher this year.⁴

For Nassau County in particular, Newsday reports that foreclosure-related filings last month were 113% higher than from April 2007, compared to the 65% year to year jump at the national level.⁵ Furthermore, there have been growing complaints that the Fed's aggressive rate cuts this year have been a key to why food and oil prices have skyrocketed lately. The fact that the Fed has cut rates while central banks in Europe and Asia have mostly kept rates steady has led to a weakening of the dollar. That, in turn, has driven up commodity prices.

Residential Housing Market

According to the latest home figures, March 2008 was a disappointing albeit not unexpected month for Nassau's residential housing market.

- From an annual perspective, average closed sale prices decreased roughly 1.4% and median closed sale prices decreased 5.4%.
- Residential inventory levels were up roughly 6.5%, from 9,260 units in 2007 to 9,862 units available in March 2008.
- Although the number of closed residential transactions through March 2008 has increased by 5.61% from February, on an annual basis closed residential transactions have decreased from 766 units last year to 546, showing a 28.7% year to year decrease.



- Closed median home prices for Nassau County were reported at \$445,000 in March 2008, or 5.3% less than the \$470,000 last year.

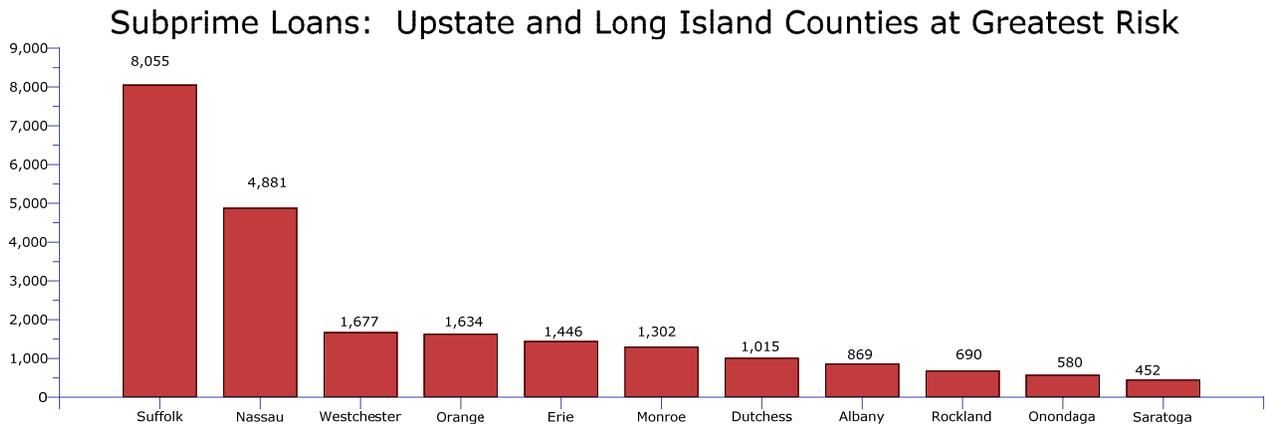
⁴ Aversa, J. "Bernanke urges more action to stem home foreclosure crisis", news.yahoo.com May 6, 2008

⁵ Yan, E. "Nassau County's foreclosure filings rise 113%" Newsday.com, May 15, 2008

- Suffolk County reported a closed median home price in March 2008 of \$365,000, which represents a 7.4% decrease from a year prior, when the closed median price was \$394,000.
- The housing market slowdown will continue to negatively impact County Clerk fee revenues, of which roughly 70% are attributable to housing market transactions.

On Long Island, 0.973% of houses are in some state of foreclosure, which is less than the national average of 1.033%.⁶ However, according to [Newsday.com](http://www.newsday.com), between the months of January and February, Nassau’s foreclosure-related filings jumped 47%, the biggest percentage hike of any downstate county.⁷ As shown below according to the Empire Justice Center, a nonprofit firm that advocates for low-income families, Long Island accounted for 33 percent of New York State subprime loans, or 12,936 loans made in 2006 that are now in foreclosure. Aggressive mortgage sales and the over-inflated prices paid by home buyers, who believed property values would continue to rise, are blamed for the high foreclosure rate.⁸

The data suggest that the almost 32,000 mortgages with resets, that may increase monthly payments by 20% or more, are much more likely to go into default and foreclosure than loans without resets.⁹ As of October 2007 of the total 16,581 subprime loans in the County, 30% were already in jeopardy (20% were 30 or more days late and 10% were already in foreclosure). In addition, 24% of these subprime mortgages have interest rates that will reset by October 1, 2009.



Source: Empire Justice Center

The charts and map that follow show the areas of Nassau County that face the greatest challenges. The data, provided by the Empire Justice Center, are based upon statistics for subprime loans generated by the Federal Reserve Bank of New York in January 2008, and reflect loan totals as of October 2007. Please note that as the interest rates on Adjustable Rate Mortgages (ARMs) increase, or “reset” in the coming months, there is also the possibility that the situation may worsen. Although the Fed’s

⁶ Phillips, T. “Wall Street Woes Outdo the Mortgage Mess” [The Bond Buyer Online](http://www.thebondbuyer.com) April 15, 2008

⁷ Yan, E. “Foreclosure filings up 47 percent in Nassau” [Newsday.com](http://www.newsday.com) March 13, 2008

⁸ Maker, R. “Curbing the Mortgage Meltdown: The Impact of Foreclosures on New York’s Economy and on Upstate and Long Island Communities: An Analysis of Securitized Subprime Loans at Risk” [Empire Justice Center](http://www.empirejusticecenter.org) March, 2008

⁹ Ibid.

lowering interest rate helps existing homeowners to some extent, for those homeowners holding ARMs, interest rate reductions will only be beneficial if they don't have to adjust upwards.

NASSAU COUNTY Delinquencies, Foreclosures and Resets As of October 2007	
Total number of subprime loans	16,408
30 or more days late	3,232
In Foreclosure	1,649
Number of Resets by 10/1/09	1,171

Source: Empire Justice Center

NASSAU COUNTY Villages Most Impacteted by Foreclosures		
Villages	Number of Loans in Foreclosure	% of County's African American Homeowners
Hempstead	475	18%
Freeport	417	12%
Elmont	12	12%

Source: Empire Justice Center

In addition, the foreclosures in Nassau County, according to data prepared by the Empire Justice Center, reflect a staggering impact on African American homeowners.

Of the 4,881 loans in Nassau County that are in foreclosure, or 30 or more days late:

- 60% (2,916) are concentrated in 10 out of 67 zip codes
- 85% of Nassau County's African American homeowners live in these 10 zip codes
- 42% of Nassau County's African American homeowners live in the 3 neighborhoods most impacted by the foreclosures –

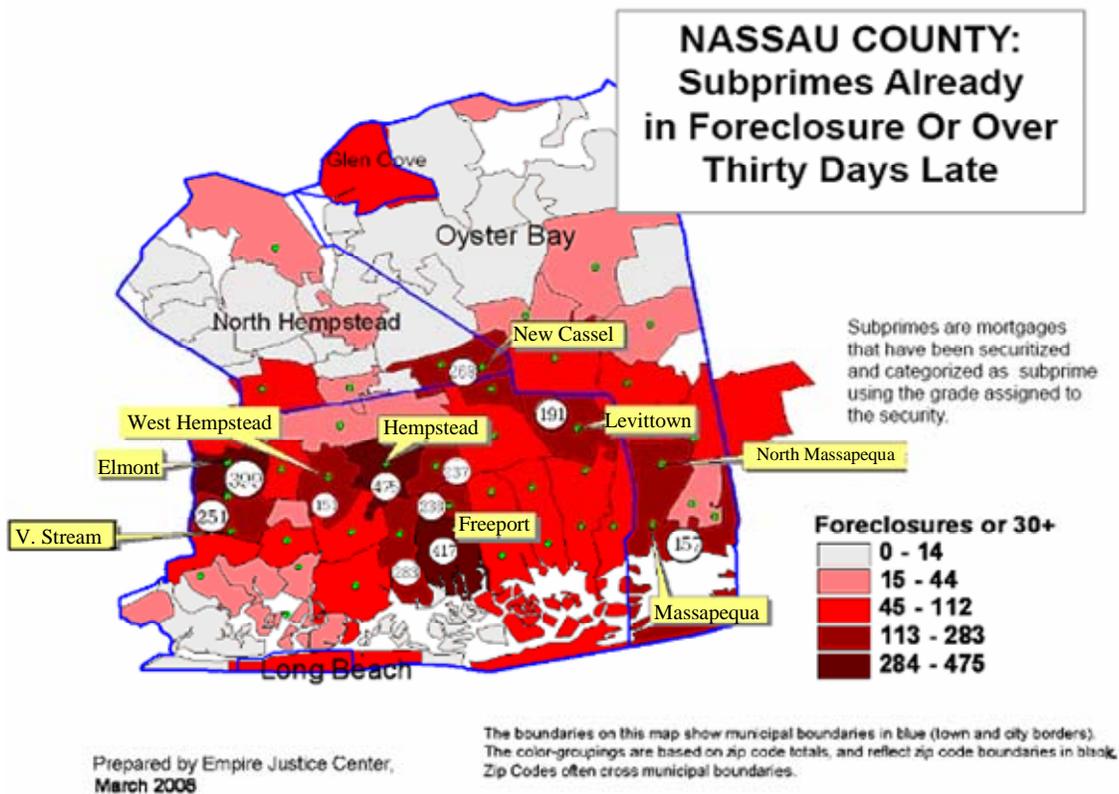
According to the Federal Reserve data set, out of the zip codes that had more than 100 subprime loans in New York State, the Village of Freeport in Nassau County was among the areas having the highest percentage of subprime loans already in foreclosure or over 30 days late, as of October 2007. Of the 1,094 subprime loans, 38.1% or nearly 42 homes in Freeport are already foreclosed or at risk of foreclosure. The zip codes in New York State with the highest percentage of subprime loans that are already in foreclosure or over 30 days late are shown below.

Subprime Loans in Foreclosure or Greater Than 30 Days Late by Zip Codes as of October 2007 (*)			
Zip Code	Town	County	Percent
11798	Wyandanch	Suffolk	43.4% of 581
11951	Mastic Beach	Suffolk	43.0% of 532
11961	Ridge	Suffolk	40.8% of 201
12182	Troy	Rensselaer	39.5% of 167
11738	Farmingville	Suffolk	39.4% of 287
10930	Highland Mill	Orange	39.3% of 107
12549	Montgomery	Orange	38.8% of 129
11950	Mastic Beach	Suffolk	38.4% of 557
11967	Shirley	Suffolk	38.4% of 813
11520	Freeport	Nassau	38.1% of 1,094

(*) Outside of New York City

Source: Empire Justice Center

The following map depicts subprimes already in foreclosure or over 30 days late by municipal boundary in Nassau County. As noted, the boundaries show municipal boundaries in blue (town and city borders). The color-groupings are based on zip codes, and reflect zip code boundaries in black. Zip codes often cross municipal boundaries.

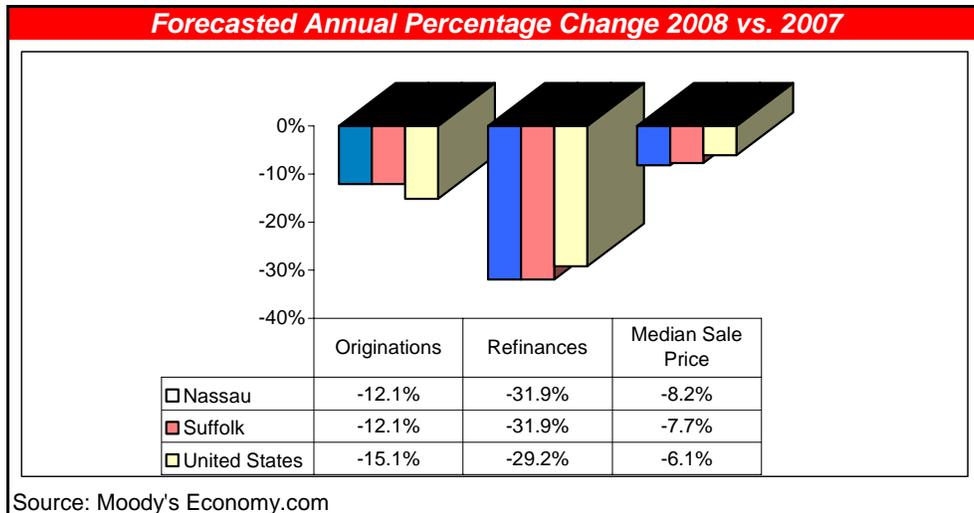


Similar data were reported by researchers at New York University’s Furman Center for Real Estate and Urban Policy. Statistics suggest that in 2006, homebuyers in predominantly black and Hispanic neighborhoods in New York City were more likely to have received mortgages from subprime lenders than homeowners in white neighborhoods even with similar income levels.¹⁰ The study focused on mortgages issued by 210 lenders identified by federal housing officials as subprime specialists in 2005, including HSBC Mortgage Services and CitiFinancial.

Forecast

The following chart details the forecasted annual percentage change from 2007 to 2008. Since 2007, mortgage purchases, mortgage refinancing and median home sale prices in Nassau County, Suffolk County and the United States have shown a dramatic decrease. Since 2007, refinancing in both Suffolk and Nassau Counties has decreased by nearly 32%, slightly ahead of the nation’s 29.2% refinancing decline.

¹⁰ Fernandez, J. “Study Finds Disparities in Mortgages by Race” *The New York Times*, October 15, 2007



In addition, the following growth forecast illustrates year-end 2008 and annual 2009 projections for mortgage purchases, mortgage refinancing and median home sale prices in Nassau County, Suffolk County and the United States.

Growth Forecast: Local and National Housing Market			
Year-end 2008 Growth Projections			
	Mortgage Originations		Median
	Purchase	Refinance	Sales Price
Nassau County	-21.1%	-21.1%	-14.6%
Suffolk County	-21.6%	-3.9%	-14.0%
United States	-18.3%	4.8%	-10.9%
Annual 2009 Growth Projections			
	Mortgage Originations		Median
	Purchase	Refinance	Sales Price
Nassau County	5.0%	-7.5%	-14.6%
Suffolk County	4.6%	-7.4%	-13.2%
United States	-0.3%	3.7%	-8.9%

Source: Moody's Economy.com

Based on the forecasted data, all areas surveyed suggest a decrease in median home prices. On Long Island, both mortgage purchases and mortgage refinancing are expected to decline throughout the rest of 2008. On the other hand, as we look at the estimated data for 2009, a brighter picture begins to unravel as new mortgages begin to increase by 4.6% in Nassau County and 4.0% in Suffolk County. Refinancings will continue to decrease in FY 2009, but at a lower rate than the projected decrease for 2008.

Two areas in particular that these forecasted declines will impact are Nassau County Clerk fee revenues and County sales tax collections. The forecasted declines will have an immediate and direct impact on Nassau County Clerk fee revenues which are closely aligned with mortgage refinancing and the number of closed transactions. OLBR is currently forecasting 2008 County Clerk fee revenue to come in at \$9.9 million, nearly \$4.0 million less than budgeted for 2008.

The continued forecasted mortgage refinancing decline is also expected to have an impact on County sales tax collections since home equity lines are tied to the prime rate. According to the Federal Reserve, as of March 2008, home equity, which is equal to the percentage of a home's market value minus mortgage-related debt, has fallen below 50 percent for the first time on record since 1945.¹¹ Some economists suggest that this figure will drop even further as declining home prices eat into the value of most Americans' single largest asset. With tighter credit markets, homeowners will no longer have as great an opportunity to borrow against the value in their homes to make purchases. Further, residents who have been utilizing their home equity to finance major purchases will make fewer purchases and the County will collect less sales tax revenue.

The Multiple Listing Service of Long Island reports that the median closing prices on homes on Long Island actually increased in April on a month to month basis due for the most part to the low interest rate environment.¹² However, as we look to the remainder of 2008 and beyond, although the practice of easy lending has abated, Federal Reserve Chairman Bernanke reports "High rates of delinquency and foreclosure can have substantial spillover effects on the housing market, the financial market and the broader economy".¹³ In terms of the real estate market, most economists would agree that the housing implosion is nowhere near over on either the national or regional levels. In 75 of the 100 top U.S. cities, prices are expected to fall in the next 12 months.

The S&P Case/Shiller Home Price Index, which tracks 20 of the largest housing markets, showed prices plummeting by 12.7% in the 12 months ending February. That's the biggest fall since the index began tracking prices in 2000. In addition, foreclosure filings more than doubled in the first three months of 2008, spiking to 112%. So far this year 156,463 families have lost their homes to repossessions. Many markets won't hit bottom till late 2009 or even 2010.¹⁴

On a final note, the discouraging prospects for a quick turn around in the real estate market will undoubtedly have an adverse impact on revenues at both the State and County levels. However, the Empire Justice Center emphasizes that if we rely on lender efforts alone, even more borrowers will lose their homes and more communities will be impacted.¹⁵ In Nassau County alone, the study suggests, even if we are able to prevent 75% of the subprime loans that are delinquent or already in foreclosure from being foreclosed, the harsh reality is that over 1,200 home remain in jeopardy.¹⁶

*Prepared by: Dr. Helisse Levine, Budget Analyst
Office of Legislative Budget Review
May 15, 2008*

¹¹ "Home equity slips below 50%" [CNN.Money.com](#) March 3, 2008

¹² Yan, E. "Closing prices on homes on Long Island, Queens are up", [Newsday.com](#) May 8, 2008

¹³ Aversa, J. "Bernanke urges more action to stem home foreclosure crisis" [Yahoo.News](#) May 6, 2008

¹⁴ [CNNMoney.com](#) May 7, 2008

¹⁵ Maker, R. "Curbing the Mortgage Meltdown: The Impact of Foreclosures on New York's Economy and on Upstate and Long Island Communities: An Analysis of Securitized Subprime Loans at Risk" [Empire Justice Center](#) March, 2008

¹⁶ Ibid.