The Short View: US housing

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To have a house of your own is the essence of the American Dream. The problem is that that dream shows signs of turning into a nightmare. And all of the world now shares it.

Risk aversion returned on Tuesday, with stocks in the US and Europe falling more than
2 per cent, volatility spiking, a flight to Treasuries, and a fall in the dollar against the yen.

The trigger was concern for the US homeowner. The Case-Shiller housing indices, seen as the most statistically robust measure of US house prices, on Tuesday painted a gloomier picture than many had expected. Home prices in the 20 biggest metropolitan markets fell 3.2 per cent in the second quarter - the biggest such fall yet recorded. Only five of the 20 cities avoided falls in prices.

Following Monday's news that the overhang of unsold apartments in condominiums and co-operatives is now equivalent to a year's worth of supply, the message was clear: US housing could still get worse. Publication of minutes for the Federal Open Markets Committee's meeting this month, showing that Fed governors thought the housing slump would be "deeper and more prolonged " than earlier expected, confirmed the gloom.

The problem is no longer restricted to subprime lenders. Anthony Sanders, of Ohio State University's business school, points out that median house prices have fallen less than the mean, showing that the most expensive houses are suffering the fastest drops. The rates for "jumbo " mortgages (too big to be covered by the federal mortgage agencies) exceed standard fixed mortgages by the highest spread ever.

These borrowers could be most affected by the resetting of adjustable-rate mortgages later this year, which will see a sharp increase in borrowing costs.

The Case-Shiller is only 3.6 per cent below its record high. Tuesday's rout may well be an overreaction. But markets needed a reminder that there are still reasons for concern.

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