



NEWS RELEASE

FOR FURTHER INFORMATION CONTACT:

Pamela Haggerty
Coldwell Banker Hunt Kennedy
646-442-7002

“Knowing what we know about real estate.”

By David M. Michonski

How we know what we know is an arcane epistemological question. Now it may be a matter of national economic security. Our entire financial system’s survival may now depend on how we “know” what we “know” about real estate markets.

What we “know” is that day after day the headlines tell us real estate markets in America are falling out of bed. Because homes are presumably falling in value, the mortgage markets have seized up and institutions are reluctant to lend against an asset declining in value.

The financial market’s reluctance to lend against this declining asset and the public’s reluctance to buy it, fuels a self-fulfilling cycle of falling prices that today threatens the very Wall Street firms who securitized and internationalized the once sleepy, local mortgage market. The failure of one or more of those firms could have a domino effect on our entire financial infrastructure and cause further panic in financial and real estate markets of epic proportions.

But what if the headlines are not quite accurate? What if what we know about the real estate markets is distorted and the distortions are being sensationalized?

Given the importance of the outcome, now might be a good time to ask how we know what we know before fiction becomes reality.

What we know today is largely courtesy of the S &P Case Shiller Index. This index has replaced two older indexes on the front page of American newspapers. One was the National Association of Realtors’ monthly price index and the other is the OFHEO index (Office of Federal Housing Economic Oversight). The latter two use rather different methodologies but over the years have reached remarkably similar conclusions about prices of homes in America. When different methodologies yield similar results, you get a good handle on reality.

Today we don’t hear much about either index. Instead, the Case Shiller index is everywhere with its ominous message. The index talks about a 15% price decline in Miami and 4.8% for the year in New York. Bloomberg quotes Shiller: “We are in an historic housing bust right now.”

Two weekends ago I opened my AOL account and saw a bold headline that home prices in 20 markets were falling rapidly with quotes from Shiller that prices nationally finished down 8.9%. “Wherever you look things look bleak” Shiller said.

The Wall Street Journal runs a headline “Home Prices Decline at Record Rates” quoting Shiller yet again.

Is Shiller right? The importance of the question forces us to look at the market through the other available lenses, NAR and OFHEO.

OFHEO has been keeping a national index for years and publishes monthly a one inch thick book on housing prices. It says that in 2007 the average price in America was down .3%. Yes, that is three tenths of one percent, not Shiller’s 8.9%. Compared to OFHEO Shiller’s index overstates the decline by 29 times or 2900%, not a small amount.

The National Association of Realtors index showed a median 1.4% decline nationally after 64 years of uninterrupted gains. Compared to NAR’s 1.4% median price decline, Shiller overstates the “freefall” by 6.3 times or over 600%.

When I pondered the 2007 OFHEO and NAR numbers a blasphemous thought came to mind, one contrary to today’s media dogma: the numbers showed not weakness in the real estate markets, but rather resiliency. Just my musing. Interpret as you will.

Recently, another report came out that was greatly at odds with Shiller’s shrillness. It came from the 2007 results for Realogy, the largest real estate brokerage company in the world. It owns the Century 21, Coldwell Banker, Coldwell Banker Commercial, Sotheby’s, ERA and Better Homes and Gardens brands, among others. They have over 300,000 agents under their franchised brands, or about one-fourth of the members of the National Association of Realtors. So these are real people doing real business everyday in the real marketplace, not in a Yale think tank.

Realogy reported that their average price in 2007 was down 1%, right in line with the NAR and OFHEO data. Again this is from a real real estate firm operating in the real world daily. This makes three out of four indexes point in one way and Shiller alone points to much more calamitous and foreboding results. Is there a reason why?

Some think it may have to do with methodology. Shiller and OFHEO’s are both repeat sales indexes whereas NAR’s data and that of Realogy take all sales volume and divide it by unit sales to get an average price and then figure out the median. Still, even using different methodologies, three out of four give one clear answer, that prices have fallen about 1%, while Shiller points to a 9 times greater fall.

Some additional notes. Shiller issues national press releases monthly but his index is anything but national unlike OFHEO, NAR and Realogy’s data. He covers completely only 8 states out of 50 and in part another 13. He has no data from 29 states.

The eight states completely covered are among the weakest in the nation. Coincidence? Even the Wall Street Journal said several weeks ago that Shiller’s index may be negatively biased.

Shiller claims to cover 20 markets (some are in the same states and hence 20 markets but only 8 states are fully covered) . He labels those markets with the names of cities, not states. Hence New York, Miami, Seattle, etc. This gives the impression that the markets he is reporting on are in fact cities (what else would one think?)

In fact, Shiller does not report on cities but on MSA’s, short for Metropolitan Statistical Areas. This leads to some remarkable distortions. For instance, Shiller claims New York prices fell 5.6% in 2007 versus an index created by Manhattan based Miller Samuel that says the average Manhattan price rose 17.6%. The two are reporting apples and oranges but which gives the more correct impression?

Miller Samuel tracks coop and condo sales in Manhattan and Manhattan is what most people think of when they think of “New York.” Shiller’s index, expressly excludes condominiums and coops which account for 1/3 of New York City sales and 99% of Manhattan sales. Thus, Shiller gives the impression of reporting that prices have dropped 5.6% in a place where he does not cover 99% of the sales and where prices have not dropped but risen, substantially.

Even more perversely, Schiller’s MSA for “New York” tracks sales in Putnam County, two hours north, and single family home sales in Bergen County, New Jersey and home prices out on Long Island. Trailer park sales in Putnam County are in his “New York” index.

Criticisms of Shiller’s inaccuracies are growing. RealTrends, a national industry monthly, ran its January headline “Case Shiller Index Exposed” and ran a synopsis of a paper done by Andre Leventis of OFHEO in which it chronicles the “flaws in Case-Shiller that are traceable and have a huge impact on the variance between their reports and those of so many other reports, including NAR’s and our own.”

Lawrence Yun of the National Associations of Realtors (who was named by *USA Today* as one of the top ten economic forecasters for his accuracy) has ratcheted up his criticism of Shiller. Yun calls Shiller’s index a “total distortion of market conditions based upon a small selection of falling local metro coverage.”

OFHEO has also chimed in by indicating that 70% of markets nationwide are not falling but actually rising, a far cry from what Shiller is peddling to the press.

But something more sinister is coming to the fore which a responsible press cannot ignore. Shiller shrillness may be due to self interest and private gain.

The gospel according to Shiller is that national home prices are in a freefall of epic proportions and that 20% to 30% price drops are in order. How could that help Shiller?

Yun suggests that Shiller profits from creating fear. He creates fear so that people will want to hedge themselves against price declines by buying insurance against a free fall in prices. Where is such insurance available? Answer: on the S & P Case Shiller index traded on the Chicago Mercantile Exchange. According to Yun, Shiller has a “side business in Chicago. His index is used at the Chicago Mercantile Exchange for hedging housing futures values. The more hedging of bets that occur, the more profits go into Dr. Shiller’s bank account. And more hedging of the bets will take place if people believe there will be a crash in housing values. So naturally he has a financial incentive to ‘scare’ the market.”

I have no direct knowledge that he does so for profit although anecdotally I have been told this is true. I suggest it is time for the media to find out.

If the media does not look more deeply into the methodology being used today, Shiller may indeed scare America into depression or a Depression.

While asking for disclosure of Shiller’s self interest, allow me to disclose mine. I am indeed a REALTOR and make a better living when real estate markets are healthy than when they are sick. As a REALTOR I subscribe to something made clear in our Code of Ethics: we believe that upon “widely allocated ownership [of real estate] depend the survival and growth of free institutions and of our civilization.” No small thing. Our Code says this imposes on us “obligations beyond those of ordinary commerce.”

Today the commerce of real estate is being distorted, possibly for private gain. Widely allocated ownership and possibly the survival and growth of our free institutions is at stake. With it is something else at stake. It is called the American Dream.

While REALTORS work to make a living, most find a different satisfaction from the business. Ostensibly the business seems to be about selling homes, but really it is about selling the American Dream. We take some satisfaction out of trying to make sure as many people as possible can have that dream. We even think that promoting home ownership fosters better citizenship, because citizens who own a piece of America will want to take greater care of it.

So we feel there is a lot at stake here, both for REALTORS like me, as well as the rest of America. Is it not time to start some background checks?

David M. Michonski is Chairman and CEO of Coldwell Banker Hunt Kennedy in New York City

Contact: 212-326-0301

Cell: 203-570-5477