July CA home sales were so weak at down 20% MoM and 22% YoY, despite a CA-specific $10k tax-credit for new and first time buyers still being in place, this single month could go a long way in confirming that little to no fundamental improvement ever occurred over the past year. Rather, the massive stimulus and artificial lack of supply through pervasive foreclosure "prevention" initiatives temporarily suspended the true supply and demand fundamentals in the state allowing for a statistical 'recovery' completely undone in a month. And because CA likely outperformed most other influential housing regions in the country due to it's large stimulus program in place through mid-August, it bodes ill for tomorrow's BBG economist's consensus of 4.68mm national Existing Home Sales, down 12.9% from June's 5.37mm level.

M Hanson Advisors – Real Estate & Finance

***The Mortgage Pages** - August 23rd 2010*

- **July CA House Sales Drop Sharply - No Fundamental Recovery in Sight**

Our mission is to provide our clients a significant edge. This is done by turning the daily, market-moving real estate and mortgage news flow and events into old news by the time it makes headlines. - *Mark Hanson*

July House Sales - Terrible Weak
Get Ready for Inevitable Price Pressure

Despite a $10k CA specific first-timer and new home buyer tax credit running through mid-August, July CA house sales still tumbled 20% from June levels and 22% from last year to the worst levels for any July in years.

Through June, CA had dual stimuli in the $8k Federal and $10k CA specific credits. Yet still, sales during the national May and June tax-credit closing frenzy only passed 2009 levels by 1700 units in total. If all that the 2010 massive cash and interest rate stimuli could muster was 1700 incremental sales, what happens next?

The answer is simple - CA housing takes a hard double-dip unless a lot more foreclosures and short sale supply is introduced. If so, then it takes a moderately hard double-dip.

With investors and first timers continuing to rule the market due to epidemic effective negative equity, which prevents the majority of potential organic buyers from selling (paying a Realtor 6% and putting a 10% to 20% downpayment on the new property per new vintage loan guidelines), the organic buyer will not come back anytime soon. And among investors and first timers, distressed properties are what are in demand.

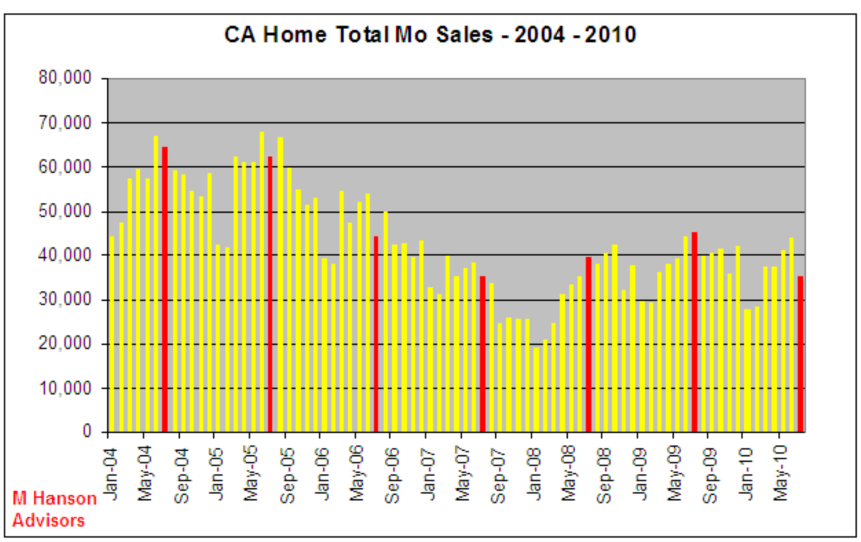
If there is demand, supply will find a way to occur. Yes, prices will suffer. But as prices fall more demand will occur as a result and the market will eventually find its footing over a number of years.

With respect to CA sales as a proxy to next weeks Existing Home Sales release, I addressed this last week:

> *CA can't be used as a proxy for anything 'housing' other than loan defaults relative to the other bubble states. It's not called the 'United States of CA' for nothing. Both Northern CA and Southern CA stand unilateral as fully independent housing regions. In fact, the largest few MSA's within CA contain dozens of micro-housing economic regions each containing completely unique housing market core fundamentals...the San Francisco MSA is so large it covers five counties and 4.4 million people. The population centers are so large and economically diverse, "distress mix-shift" was invented here. This is why John Paulson, who in part based his housing market recovery thesis, which led to his national recovery thesis, on early housing data from CA will ultimately be wrong at least about this input.*
>
> *Another extremely important fact to remember is that **CA had a $10k new-home and first-timer parallel tax-credit** for those that closed escrow after April 30th. A total of $100mm for each group (approx 30k sales total) was made available and when it is used up, the stimulus ends. This means if a buyer went into contract in March and April and closed May and June, they would have received BOTH the CA and national tax-credit for a maximum of $18k. As of July, both CA tax-credits were still on and just like with the national figures, they positively influenced sales. However, it was announced this week that the first-time buyer allotment was used up. Obviously, there are still plenty of available funds left for new home buyers but they are such a small percentage of total sales that **the days of tax-credit stimulus effecting sales are officially over.***

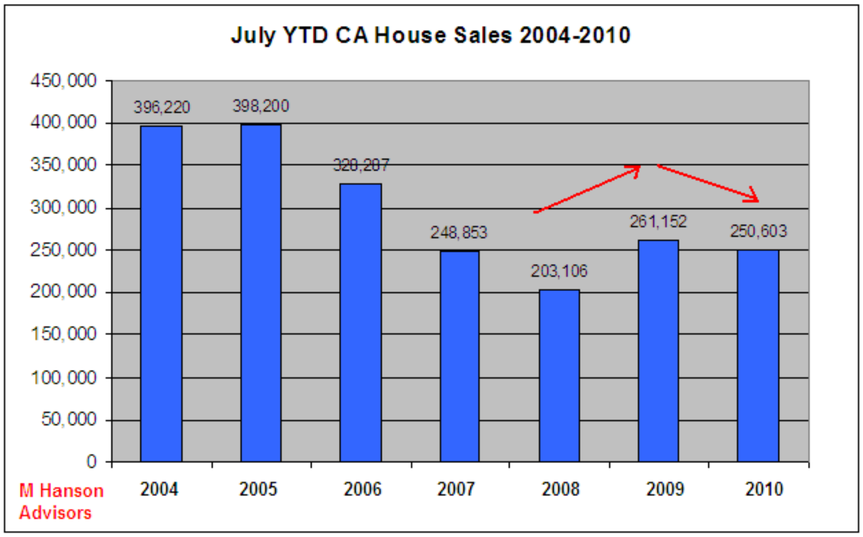
CA sales dropped 20% MoM and 22% YoY- Bodes ill for Tomorrow Existing Home Sales

With a $10k CA-specific tax credit in place in July for first-timer and new home buyers, CA likely outperformed most other states at down 20% from June levels and 22% YoY. If so, tomorrow's BBG national Existing Home Sales consensus of 4.68mm seasonally adjusted, down 12.9% from June's 5.37mm, should be at least a 10% miss.



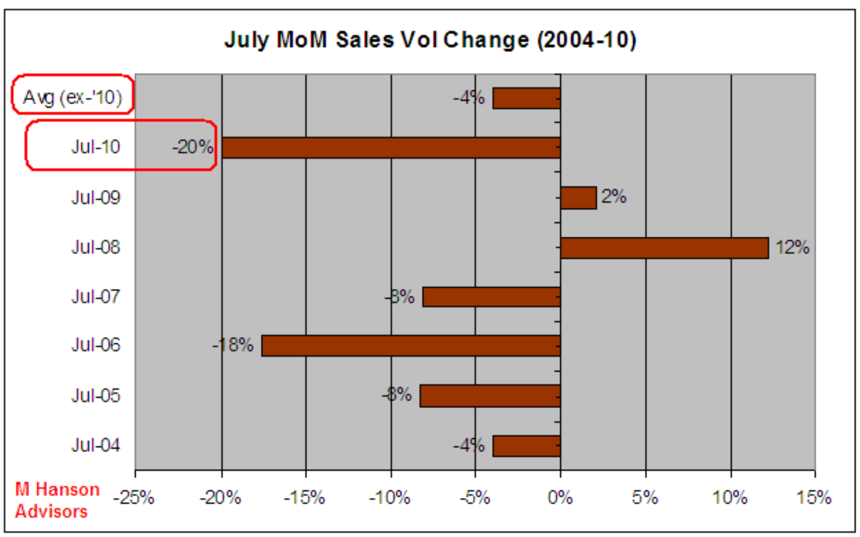
July 2010 YTD CA Sales Lower Than Last Year's Anemic *Non-Tax Credit* Levels

What's most amazing is that despite the rush to buy in the first half of the year due to the tax credit, **sales are still lower July year-to-date than last year when there was no tax credit impact.** The reason is because there were far more foreclosures on the market, as this was before the massive mortgage mod can-kicking experiment time period suggesting that the free market was in fact working to some extent before the interference.



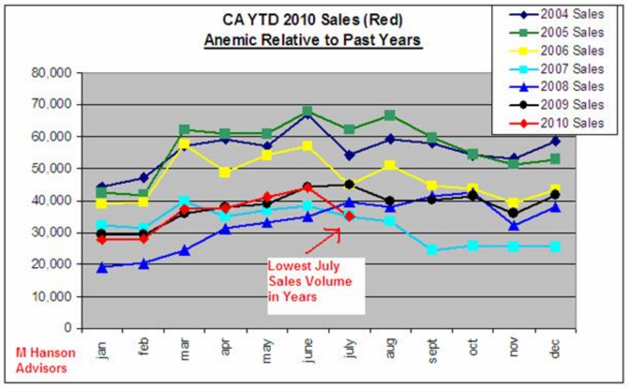
Worst MoM Performance in Years

This was the worst July month-on-month performance in years. The average June to July change is -4% not including 2010.



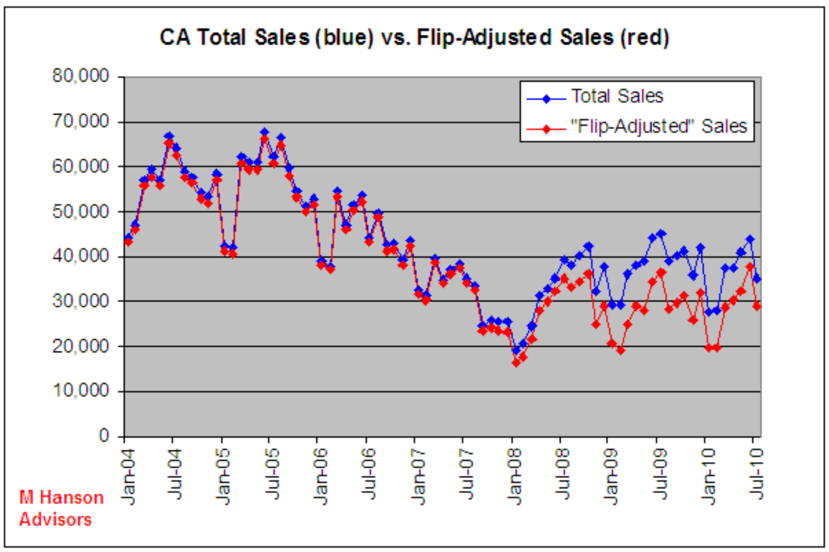
Sales Lower Than 2007 During the Great Crash

Shown another way, **2010 sales (red line) volume is nowhere near the bubble years and at the worst July on recent record for housing.**



Flip-Adjusted Sales **Reveal Fundamental Market Weakness**

When backing out likely flip-resales, which are abundant and lead to double counting of existing home sales in bother region and NAR's national, July CA "flip-adjusted" sales were below the 30k market, which is depression level.

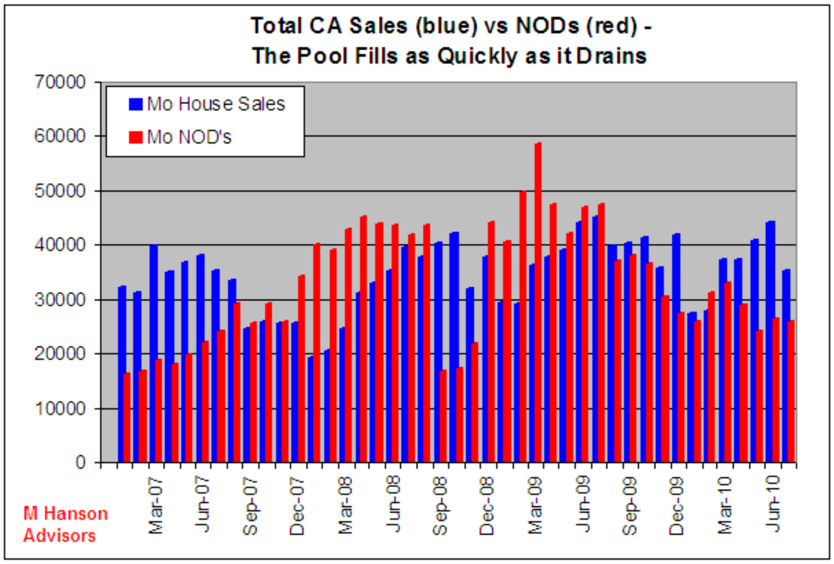


Shadow Inventory Levels Make Clear…No Fundamental CA Recovery in Sight

Last but not least, Notice-of-Defaults (red) as a percentage of CA sales jumped sharply in July to 73%. While this metric has been improving recently due to pervasive can-kicking through modifications, ultimately most NODs will end up as foreclosures.

The bottom line is that as long as you have shadow inventory filling the pool as quickly as sales drain the pool no fundamental improvement can ever occur. **<u>Thus, as evidenced by this chart little to no fundamental improvement has yet occurred in CA real estate.</u>**

When factoring in the **skyrocketing short sale inventory** (not shown here), it should be obvious even to the data deprived that the real 'bottom' is a long way off.



Best Regards,
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***Data for this report provided by M Hanson and DataQuick**