

JANUARY 1, 2010, 1:25 PM ET

Five Key Housing Issues to Watch in 2010

The housing market, which brought the economy to its knees in 2008, struggled to recover in 2009. The modest gains of the past year can be credited in many ways to federal support that will be removed at some point in 2010.

That makes for an uncertain outlook for the year ahead, one filled with questions about what policymakers will choose to do and how markets will react to those decisions. "The can has been kicked down the road," says Ivy Zelman, chief executive of Zelman & Associates, a housing-research firm.

Here's our list of five big issues to keep an eye on in 2010:

Mortgage rates: The Federal Reserve has kept mortgage rates low for most of 2009 by committing to purchase up to \$1.25 trillion in mortgage-backed securities. Mortgage rates stayed at or below 5% for much of 2009 thanks to the Fed's purchases, which have already been [extended](#) once, to March 31. Whether the private market is ready to fill the gap when the Fed exits is one of the hottest debates between economists, investors and analysts. The Mortgage Bankers' Association says that it expects rates to rise by around one-quarter of a percentage point, but others say rates could jump by as much as a full percentage point. Low mortgage rates helped ignite a fragile recovery in home sales in 2009, and they allowed millions of homeowners ([including](#) Federal Reserve Chairman Ben Bernanke) to refinance out of mortgages that might have increased to higher rates.

Fannie, Freddie and the FHA: Nearly nine in 10 mortgages are now being backed by Fannie Mae and Freddie Mac, the mortgage-finance giants taken over by the government, or government agencies such as the Federal Housing Administration. The future of Fannie and Freddie remains nearly as uncertain now as it was one year ago, but the White House has said it will offer its recommendations on how to remake the U.S. housing-finance infrastructure early this year. The FHA, meanwhile, has suffered from [heavy losses](#) that could lead to a taxpayer bailout, and it is set to announce a series of [measures](#) in the next few weeks to tighten its standards. The New Deal-era agency, which offers loans with minimum 3.5% down payments, backed half of all sales to first time home buyers during the peak April-June buying period. Needless to say, builders are anxious about the prospect of any tightening of loan standards.

Loan modifications: The Obama administration launched the most ambitious government effort to date in February to modify loans for troubled borrowers. That program, however, has been off to an [underwhelming start](#) because loan servicers, which collect loan payments, have had to rapidly build staff and systems to administer the program. Borrowers who complete three reduced loan payments are eligible for a permanent modification that reduces their monthly payment for up to five years. Through November, some 728,000 borrowers have signed up for trial modifications, but just 31,000 have moved into permanent workouts, or fewer than 5% of those eligible. Loan modification efforts have helped to hold back the supply of foreclosures for sale. The number of seriously delinquent loans continues to climb, so it's reasonable to expect a pick up this year in distressed sales and foreclosures that hit the market.

More loan resets: Analysts and pundits have been warning for years about the coming wave of option adjustable-rate mortgages that will jump to sharply higher payments beginning this year. Those loan recasts are concentrated particularly in high-cost housing markets, such as coastal California and other areas where homes became increasingly unaffordable at the height of the housing boom. Meanwhile, more interest-only loans that allowed borrowers to avoid making principle payments for three, five, or seven years will reset to higher payments. Those loans became especially popular among borrowers of jumbo loans, which are too large for government backing and range from \$417,000 in most parts of the country to as high as \$729,750 in the most expensive housing markets. Many of these borrowers [owe more](#) than their homes are worth, leaving them particularly vulnerable to default if they can't afford the higher payments. That could cause more pain for mid-to-upper end housing markets that began to show more [signs of stress](#) in 2009.

Tax credit and home sales: Sales were fueled in the late summer and early fall in part due to an \$8,000 tax credit that had been set to expire in November. Congress has extended that through the first half of next year, but some economists say that the tax credit will steal demand from future months. The tax credit led first-time buyers to compete with investors on lower-priced homes, and prices posted [six straight months](#) of modest gains through October, according to the Case-Shiller index, which measures home prices in 20 cities. While it wouldn't be surprising to see prices tick down again during the winter, when home sales are normally cooler, there's still a good deal of debate between housing economists and analysts over whether a "double-dip" could lead home prices to fall below the bottom that was set last April. Meanwhile, housing analysts expect to see an uptick in short sales, where lenders allow homeowners to sell for less than they owe on the mortgage.

Readers, what else about the housing market keeps you up at night?

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