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Home Builders Sound Retreat on Land Deals

As Housing Sector Remains Weak, Some Firms Back Out of Contracts, Forfeiting Deposits; 'Holy Cow! Our Sales Are Down'

By DAWN WOTAPKA

The weakening of the housing sector is having repercussions in the land-speculation market, which enjoyed a miniboom earlier this year when it appeared that the worst of the housing crisis was over.

With sales volume falling and home buyers retreating, home builders are re-examining land contracts, asking land sellers for lower prices or abandoning deals entirely. Land brokers said several of the nation's builders, including [D.R. Horton Inc.](#) and [M.D.C. Holdings Inc.](#), have walked away from deals. In some cases, they forfeited the deposit: [KB Home](#) walked away from the option to purchase 90 lots, and a \$500,000 deposit, in Roseville, Calif.

D.R. Horton and M.D.C. didn't respond to requests for comment.

This summer, builder [Standard Pacific Corp.](#) signed a letter of intent to buy an option on 451 ready-to-build lots in the Inland Empire, a Southern California market where builders have ramped up construction in recent months. But in August, Standard Pacific decided to pass on the deal.

"The market is definitely doing worse now than at the beginning of the year," said Standard Pacific Chief Executive Ken Campbell. "It's a weaker home-sale environment than people had expected, which means land is less valuable."

This marks a change from earlier this year, when builders competed to boost their land supplies to have inventory ready for an improved market. Finished-lot prices in Phoenix and California's Riverside-San Bernardino area, two of the markets hardest hit by the housing crisis, soared more than 40% above the bottom hit in the first quarter of 2009.

Prices in other hard-hit markets such as Las Vegas and Tampa, Fla., rose between 21% and 40%, according to housing-research firm [Zelman & Associates](#).

"They obviously got pretty aggressive in terms of their assumptions in the first half of the year," said Alan Ratner, a Zelman vice president. "They were bidding up deals at prices that current home prices could not support."

Builders are trying not to overpay for land, which got them into trouble when the market slumped and land values plunged. These days, builders buy options rather than purchasing the land outright whenever possible. Options give builders the right to buy land at a later date at a set price.

Land speculators had been buoyed by improving home sales in the first half. But since the federal home-buyer tax credit expired April 30, sales volume has deteriorated. The Commerce Department said July's new-home sales level was the lowest since it began keeping track in 1963.

Some builders even have halted land acquisitions until the downturn's extent is more clear. Just three-fourths of builders were actively looking to buy or option finished lots in July, the latest month available, well below January's 94% peak, according to Zelman.

"The builders are looking at sales in the last three months and they're saying, 'Holy cow! Our sales are down,' " said Richard Gollis, co-founder of the Concord Group, a real-estate consulting firm. "They're slowing down on their lot buys coming into the fall season."

According to Zelman's latest report, nearly 40% of industry executives surveyed reported builders walking away from deals under contract. Also, fewer builders are participating in bidding wars: Just 8% of land buyers in July increased bid prices, down from April's 54%. Such weakness is expected to continue when the firm releases its latest land survey this month, Zelman's Mr. Ratner said.

To be sure, land transactions still are happening. Builders remain interested in large parcels, which are hard to come by, and raw or partially developed sites that will be ready for development down the road. Standard Pacific remains committed to the 468 acres of undeveloped land that it recently optioned in northern San Diego County.

But in many markets, the run-up in prices has stopped, and there even is a risk that prices will begin to slide, industry watchers said. Builder confidence remains low while high unemployment, poor consumer confidence, competition from foreclosed homes and other headwinds dog the sector. Industry watchers don't expect improvement this year, and some have low expectations for 2011.

"A lot of them got nervous that maybe they pulled the trigger a little early or got too aggressive," Mr. Ratner said.

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