

BUSINESS FIRST

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Home building market in metro Louisville area has dried up

Building permit volume continues to drop as builders grapple with excess inventory

**Business First of Louisville - by [Sarah Jeffords Pister](#) Business First Staff
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This is the time of year when home builders typically are at their busiest.

But this year, the frenzied pace of construction has slowed to a crawl.

Building permits for the first quarter of 2008 are down across the region, continuing a steady decline since 2005.

Jefferson County saw a 25 percent drop in building permits for detached single-family homes in the first quarter, compared with a year earlier.

Surrounding counties on both sides of the river saw an even greater decline during the same period.

Single-family building permits dropped 47 percent in Shelby County, 47.5 percent in Bullitt County and 51 percent in Oldham County.

In Indiana, single-family building permits dropped 59 percent in Floyd County and 60 percent in Clark County.

Construction affected by overall decline

The downturn in new home construction comes as no surprise in light of challenges the residential real estate market has faced in the past year.

Nationwide, the industry has been hit by a record number of foreclosures, sluggish sales and price depreciation.

Louisville has not been as hard hit as other parts of the country, but the city has felt the pinch of the real estate crisis.

For instance, there were 3,089 foreclosure judgments and sales scheduled in Jefferson County in 2007, and 2,093 sales resulted. (Some foreclosures were settled before homes were auctioned.)

This was a 13.3 percent increase from 2006, according to an April report released by the Jefferson County Property Valuation Administrator's Office.

On the real estate sales front, 2,695 homes were sold in the first quarter of this year, down nearly 16 percent from the same period a year ago.

The average sales price was \$163,015, reflecting a 1.4 percent drop, and the median sales price fell 2.2 percent to \$132,000.

Sales figures for April and May show similar percentage decreases compared with the same period in 2007, said Lisa Stephenson, executive vice president of the [Greater Louisville Association of Realtors](#).

Inventories are double what is needed

The stagnant sales environment follows a building boom that peaked in 2005, a combination that has led to high levels of excess housing inventory.

Chuck Kavanaugh, executive vice president of the [Home Builders Association of Louisville](#), estimated that there is an available housing inventory of nine to 11 months, which translates into about 500 to 600 homes for sale in an eight-county area.

That's about twice the level of a healthy inventory, he said.

The drop in building permits is largely related to a decrease in speculative home building, which needed to happen anyway, Kavanaugh said, because the housing inventory includes an oversupply of spec houses that builders now are unable to sell.

Some spec building is good, even necessary, said Russ Lohan, a partner in the local franchise of MarketGraphics of Louisville, a market research firm that gathers data on residential construction for eight counties in Kentucky and Indiana.

Lohan said the Louisville area had become overbuilt. Healthy levels of spec housing average about 20 percent of home sales, but spec housing locally has made up 40 percent or more of housing sales.

So Lohan said it was time for new home starts to taper off.

As of April, the number of homes under construction in the eight-county region was 1,429, according to MarketGraphics data.

In comparison, there were 1,892 homes under construction in April 2007 and 2,742 under construction in April 2006.

That data was based on visits to area subdivisions in which MarketGraphics counted the number of homes under construction.

The firm also keeps a tally of closings, Lohan said, which he defines as an unoccupied home that has become occupied since the company conducted its previous subdivision audit.

From April 2007 to April 2008, there were 3,950 closings. In comparison, there were 4,306 closings from April 2006 to April 2007 and 6,088 closings from April 2005 to April 2006.

The decline in sales means that it will take longer for the levels of inventory to balance out, Lohan said.

Builder moving speculative starter homes

Despite the numbers, some home builders have not been deterred from building spec houses.

Scott Thomas, manager of [Lynn Homes](#) LLC, said the New Albany development and construction firm continues to build about 30 spec homes per year, the majority of which are priced between \$120,000 and \$170,000.

Spec homes represent about 60 percent of Lynn Homes' business, down from previous years, when the company was building about 90 percent spec homes.

Lynn Homes has shifted to contract work because that is where the demand has been, Thomas said, not because of an inability to sell spec homes. He said the company sold 46 homes in 2007, and it is on target to generate the same level of sales this year.

Most of the homes his firm is building are in the Southern Indiana communities of Meyer Manor, Glenwood Springs and Liberty Pointe, all of which Lynn Homes is also developing.

The developer/exclusive builder combination has worked to his company's advantage, Thomas said. Another plus is that the "starter home market is still very strong. Very few are competing within this price range."

Though Lynn Homes has not reduced its building activity, Thomas admitted that it is becoming more difficult to close a deal because the mortgage restrictions have tightened.

"We're still moving product. ... It is down, no doubt about it. But it could be worse," he said. "I'm still fairly optimistic."

Focus is on contract homes

Lynn Homes' situation is more of an anomaly than the norm.

Kavanaugh said he believes about the only houses getting built these days are contract homes.

Developer Lawren Just, whose projects include Persimmon Ridge and the Overlook at Persimmon Ridge, can vouch for that.

She said builders who have purchased lots in Persimmon Ridge, a 328-lot golf course community in Shelby County, have shifted toward contract work.

At one time, all builders in Persimmon Ridge built only homes under contract, but the housing boom prompted spec building to pick up steam.

Two years ago, Just said, there were 12 spec houses under construction in Persimmon Ridge. Now, the development has one completed spec home that is for sale. Seven spec houses have sold since December.

Plus, a second home that a builder started as spec construction now is under contract.

Just said she believes that one factor that has contributed to the decrease in spec building is the inability to secure financing.

Progress slows at Heritage Hill

Paul Dries, managing member of Heritage Hill Properties LLC, agreed.

He is developing Heritage Hill, an 840-acre, golf course community in Bullitt County that will have a total of 1,000 homes sites when completed.

"Spec construction has slowed down considerably," Dries said. He added that builders often are afraid they might not be able to sell their product, plus "financing is little more difficult to obtain for some builders."

At Heritage Hill, five spec homes are under construction, and another four spec homes are completed and remain on the market.

That is in addition to 31 single-family homes that have been built and sold since the development got under way in 2005.

There also are two lots that have sold to individuals who are waiting to build until they sell their current residences.

And the first of about 90 patio homes has been built, Dries said. Heritage Hill sold a portion of the property to Buddie Jaha and Steve Cox, who are developing the patio homes.

So Heritage Hill is taking shape but not as quickly as the developers would like.

Dries said he expected to have 30 more lots sold at this point.

He projected that these slow times could add a couple of years to what started as a 10- to 12-year project.

Economic uncertainty

In Kavanaugh's opinion, the real driver behind the decline in new home construction is increased housing inventories, not credit restrictions.

To rectify the situation, levels of inventory are going to have to be reduced, which will happen when the economy turns the corner and job growth begins.

The challenge is the "uncertainty in the marketplace," Kavanaugh said. "Our economy has people a little bit freaked."

Consumer confidence has been eroded by national news reports on the mortgage crisis as well as skyrocketing energy and food costs.

"People are being very cautious," Just said. She does not expect to see any sort of rebound prior to the presidential election and probably not until 2009. "It's going to be a rough year."

Kavanaugh is looking at a similar time frame.

"This isn't something that going to turn around next month," he said. And even when it does start to bounce back, "it's going to be a gradual uptick."

Adapting to the changing conditions

But some builders are feeling the financial squeeze now from the inability to sell existing product and the lack of demand for new home construction.

For instance, Prospect firm Hartung Builders recently filed for Chapter 7 liquidation in U.S. Bankruptcy Court for the Western District of Kentucky, Louisville Division. The company listed \$1.6 million in assets and \$2.19 million in debts.

Builder Stephen Hartung declined to comment on the bankruptcy filing or circumstances leading to the current situation.

Although Hartung is one of the few Louisville builders who have filed bankruptcy, Kavanaugh said that is happening frequently in other cities.

He acknowledged that local builders are "struggling."

But Kavanaugh said banks have tried to work with home builders to resolve financial situations.

Plus, builders are switching gears and tackling smaller projects, such as remodeling jobs and basement finishes that they might have turned down three or four years ago.

"That's why we haven't seen a lot of bankruptcies," Kavanaugh said. "Folks are figuring out how to work through this kind of downtown."

Diversification is key

One builder's answer was to move into additional price points and geographic areas.

Prior to the shift in the market, Louisville firm [Olympia Homes](#) LLC began to develop and build in nearby Hardin County, which is home to Fort Knox.

Mike Peterson, partner and executive vice president of Olympia Homes LLC, said the move into that market has opened new opportunities.

For instance, there is a lot of relocation activity with new jobs at Fort Knox as well as local companies bringing in employees.

So even though construction activity and the number of relocations have slowed in Oldham and Jefferson counties, where the company primarily had been building, Olympia Homes has seen a steady volume of business in the Fort Knox area.

The company has signed 10 contracts in the past three months for homes in The Cedars, an Olympia Homes community that is developing residences in three different price ranges.

The company also plans to start a new development, Arlington Park, in Hardin County next year.

For Will Prifogle, president of New Albany firm Will'Z New Construction Inc., it made sense to shift his focus to remodeling jobs. The transition has kept his nine crews with a total of 18 workers hopping.

Originally a handyman/remodeler, Prifogle moved into new home construction about six years ago. He launched a sister company, TEEM Builders Inc., that started out doing a lot of spec construction.

Then, about three years ago, Prifogle saw the signs of a slowing market.

He said it used to be that a spec home would sell by the time it was framed. But when he had a home sit on the market for six months, it became too difficult to turn a profit.

So Prifogle began to reduce his spec inventory before he was hit hard by the downturn. Now, he has only one spec house yet to sell -- a \$355,000 home in Heritage Place subdivision in Charlestown, Ind.

His current business model calls for four to five contract homes per year along with remodel jobs.

In addition, Prifogle has a third company, [Restrotech Disaster Services](#), that offers fire and water restoration and related services.

Typically, insurance companies contract with Restrotech to provide services to clients following a fire or severe weather damage.

Employees with Will'Z Construction handle work for all three companies.

The diversification has been his saving grace. "Financially, we're very stable -- probably more so than we have been in 10 years."

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