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# Spec Houses Rise as Builders Bet On Buyers Before Tax Credit Ends

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By DAWN WOTAPKA

Home builders are ramping up speculative construction to attract last-minute home buyers who want to tap a soon-to-expire tax credit.

The strategy is risky. If the buyers don't materialize, builders could be saddled with unsold homes that will require heavy discounting to sell, hurting profits and slowing the housing recovery. New homes may also continue to lose market share to lower-priced foreclosed houses. Indeed, some economists expect an avalanche of foreclosures in the months ahead as lenders release homes they have been keeping off the market.

But that's a chance the industry is willing to take. "We know that we're going to have more people out now," says Lance Wright, co-owner of CastleRock Communities in Houston, Texas. "Buying is an emotional decision. Seeing the actual product that you're moving into will certainly make it easier."

Ken Campbell, chief executive of California-based Standard Pacific Corp., agrees. Buyers trying to beat the tax credit's expiration "will buy a house somewhere," he says. "It does make a difference if the home is ready, available to go."

Late last year, builders lost sales because they didn't have enough houses to satisfy a flurry of demand from buyers looking to take advantage of a federal tax credit for first-time buyers before they expired on Nov. 30.

Some experts believe that those credits have satisfied the urge of potential buyers to jump into the market.

"They did the job," says Christopher Thornberg, a principal at Beacon Economics, a Los Angeles-based research firm. "They stabilized the market. Now, let the program go."

But that hasn't happened. Instead, the tax credit has been extended and expanded. The current credit, which offers first-time buyers up to \$8,000 and repeat purchasers up to \$6,500, applies only to deals signed by April 30 and closed by June 30.

Builders expect buyers will wait until the last minute. "As we roll into March and April, more people are going to become aware of the fact that there's a deadline, and it's for real," says Rob Bowman, president of Lancaster, Pa.-based Charter Homes & Neighborhoods.

Houses typically take between four and six months to build, so the window to start construction is closing quickly. And current inventory is low. At the end of 2009, there were 234,000 homes for sale, the lowest level since April 1971, according to the National Association of Home Builders.

It's difficult to measure the total number of spec homes nationwide. But according to a survey conducted by John Burns Real Estate Consulting, based in Irvine, Calif., home builders have about three finished homes with no buyer per community. That's up slightly from 2.8 finished

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homes in November but much lower than the peak of six finished homes in July 2008.

"Every builder I talk to around the county is starting a spec home or two [per community] for the spring season, provided they have the cash to do it," said Jody Kahn, a John Burns vice president.

But not everyone. [Pulte Homes Inc.](#), the nation's largest builder, has 2,800 spec homes in inventory and doesn't plan to add more, even if it has to "sacrifice a few sign-ups and closings in the short term," Chief Executive [Richard Dugas](#) said in an earnings conference call Tuesday.

"We got caught with a lot of inventory at a bad time in the market, it depressed our margins dramatically, and we're not going back there, God willing," he said.

[KB Home](#), the nation's fifth-largest builder by annual closings, has been among the most vocal proponents of not building on spec. Like all builders, the company was hurt during the housing bust, which left them with too many high-priced homes that had to be sold at a discount.

But even KB has said it will now build a limited number of spec homes in select markets and communities. It plans to build the houses about half way through, to the drywall phase, allowing enough time for buyers to personalize finishes, such as cabinet and carpet colors, and still close in time for the credit.

Charter Homes also considers itself a build-to-order builder, but it is currently building some 20 speculative homes, about 8% of this year's expected deliveries. It is selecting the most popular colors and upgrades, and every home will include a natural stone countertop on the kitchen island.

"No matter how tough times are, that's still a luxury that most people look at and say, 'That's something I really want,'" says Mr. Bowman, the company's president.

Builders say they're being careful, studying each community to determine demand and what price point and bedroom count will sell most quickly. And they're building just a few spec houses per neighborhood. [Meritage Homes Corp.](#)'s average in its 153 communities is 3.4, down from 4.3 a year ago, Brent Anderson, vice president of investor relations, says. Additional starts still require corporate review from the Scottsdale, Ariz., home office.

During the housing frenzy, builders quickly sold everything they built. But when the bubble popped, they were overwhelmed with a glut of speculative homes, as well as with cancellations. The homes were oversized with too many features that didn't match downsized buying preferences, forcing steep price cuts.

Builders responded by scaling back construction, building simpler homes and switching to a build-to-order strategy. Now, with many public and regional private builders increasing construction, inventory should climb during a "spring selling season on steroids," says Ms. Kahn.

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