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The Housing Market: Will It Crash or Boom in 2021?

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In this issue of the ***Hibbs Brief***, we discuss some facts and statistics regarding the United States housing market in 2020 and early 2021. Then, we present current home sales figures and potential scenarios for 2021 for the nation and Tyler, Texas.

How it Works

The housing market, essentially, consists of buyers and sellers. When you see more sellers than buyers in a geographic location, the number of houses available (home inventory) rises, and the prices are pushed down (lower prices). This is known as a *buyer's market*. When you see more buyers than sellers, the number of houses available drops, and prices are pulled up (higher prices). This is known as a *seller's market*.

An indicator often used by the real estate professionals to measure the state of the housing market is the *months of inventory*.[1] If this indicator is around 6.5 months, the housing market is balanced. While more than seven months is considered a buyer's market, less than six months is considered as a seller's market. See **Figure 1**. Like any other market, the housing market is cyclical, from seller's market to buyer's market, again and again, with several factors influencing the length of each cycle.

Figure 1. Months of Inventory: Buyer's, Seller's and Balanced Markets

Source: Hibbs Institute using Real Estate Center at Texas A&M University information.

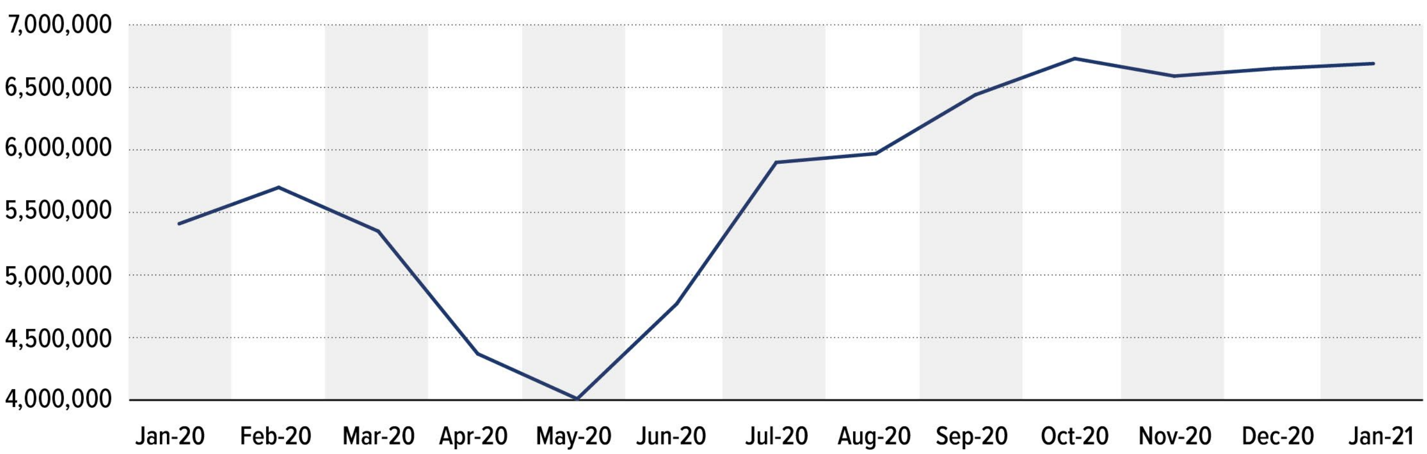
When you are buying a home, you look at two main things: the mortgage interest rates and the price of a home. For simplicity, we can say that the Federal Reserve Bank (FED) determines the interest rates, which are used by commercial banks to set the mortgage interest rates available to individuals.[2] On the other hand, the home prices are determined by the number of buyers and sellers (demand and supply) in the market. The number of buyers and sellers can be influenced by many factors, such as the construction of new housing, migration, public policy measures and other factors.

The Pandemic Effect

In March 2020, the COVID-19 pandemic in the U.S. slowed the entire economy, which caused a significant recession. Many sectors of the economy (the deemed non-essential businesses) shut down in March and April in many states. In response to the adverse conditions, the FED used its full range of tools, such as cutting interest rates, to support and stimulate the economy.[3]

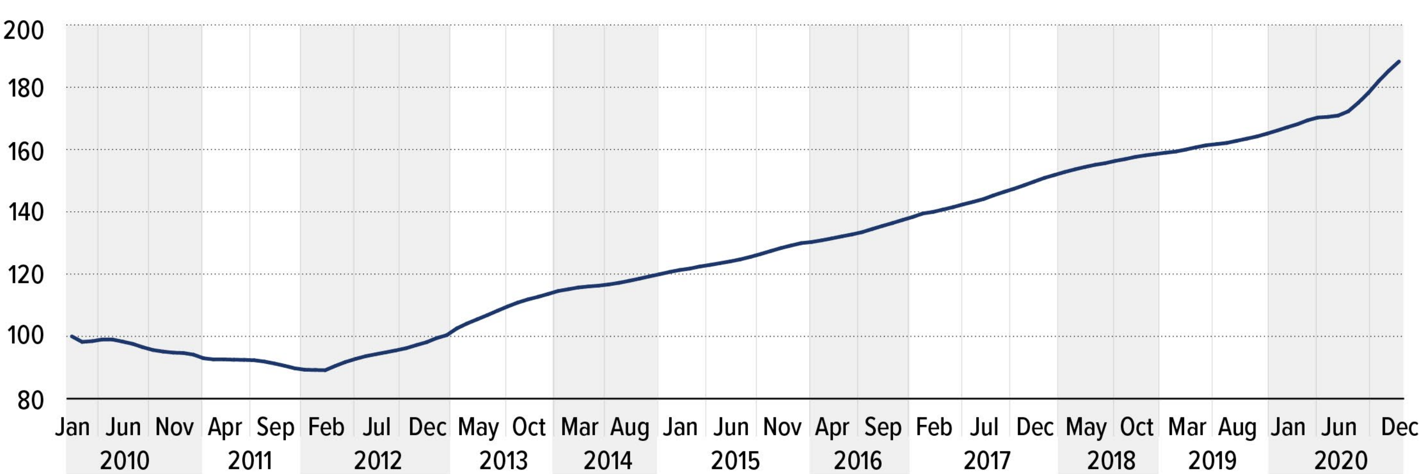
After a deep downturn early after and during the business shutdown in spring, home sales unexpectedly rebounded in the summer (**Figure 2**). People looking for a new work-life environment, larger homes or migrating to suburban areas, in combination with low mortgage interest rates, increased the demand for homes. At the same time, pandemic uncertainties affected construction companies, which slowed down new house construction. With fewer new homes and a reduced number of people trying to sell their homes due to the pandemic, a limited number of homes were available to the selling lists. Large demand and limited supply of housing naturally pushed up home prices (**Figure 3**).

Figure 2. Existing Home Sales in the U.S. (January 2020–January 2021)



Note: Number of Units; Seasonally Adjusted Annual Rate. Source: National Association of Realtors, provided by FED.

Figure 3. S&P / Case Shiller U.S. National Home Price Index (January 2005–December 2020)



Note: Index January 2005 = 100; Seasonally Adjusted. Source: S&P Dow Jones Indices, LLC, provided by FED.

The Housing Market in 2021

The key factor that will keep raising the housing market prices or would cause the market prices to plummet is the available inventory. As more buyers keep entering the market with not enough homes available, prices will continue to increase for many more months. Alternatively, if the number of buyers stagnates or is reduced, and the number of houses available grows (sellers) in a relatively short period of time, we may see a substantial drop in home prices.

The housing inventory will be influenced by several factors in the following months:

a. ***Mortgage rates.*** The 30-year fixed mortgage rates went below 3% in July 2020 and reached their historic low mark in late December (2.66%).[4] Moreover, the FED announced that interest rates are to be kept very low (near zero) at least through 2023.[5] Thus, we expect mortgage rates to stay below or near 3% for several months.

b. ***New construction***. While new construction of private housing units increased considerably during the third and fourth quarters of 2020 (22.5% for the same period in 2019),[6] most of these new homes will not be available until summer 2021. The completion time of building a new single-family home is around nine months (once the permit is ready).[7] Although some new homes will be available later in 2021 (increasing the housing supply), new homes represent only a small portion of average sales. The ratio of existing homes to new homes is 6 to 1; 14% of sales are new homes.[8]

c. ***Jobs***. The COVID-19 pandemic struck the U.S. economy by the end of the first quarter of 2020. More than 25 million jobs were lost in April and May combined. The unemployment rate went from a historically low rate of 3.5% in February to 14.7% in April.[9] Although both measures (the unemployment rate and the number of unemployed individuals) have improved substantially over the past 10 months (after the April highs), they remain well above the pre-pandemic numbers of February 2020.[10] The sooner unemployed people find a job and reach economic stability, the less the risk of them falling into mortgage delinquency. The longer it takes to reach economic recovery, the higher the risk to have some of the unemployed falling into mortgage delinquency, and eventually, in housing foreclosures.

d. ***Housing foreclosures***. The number of loan accounts in delinquency status (30, 60, 90+)[11] increased 130% in two months (from the end of March to the end of May 2020). However, the number of housing foreclosures remains low. Both foreclosure-starts and foreclosure-sales (completions) reached a record low in 2020, as forbearance and moratorium plans protected homeowners from experiencing foreclosures in the wake of the COVID-19 pandemic.[12]

   The CARES Act[13] provides a mortgage payment forbearance option for borrowers who suffer financial distress due to the COVID-19 national emergency. The CARES Act forbearance program is a temporary reduction or postponement of mortgage payments. Borrowers are entitled to an initial forbearance period of up to 180 days if requested. This forbearance may be extended (if requested) for up to an additional 180 days.[14] Furthermore, this program has been recently extended by President Biden. A six-month period of additional mortgage payment forbearance, in three-month increments, is available for borrowers who entered the program on or before June 30, 2020.[15]

The following months will be crucial to the housing market. First, homeowners who entered the forbearance program in April and May (about 625,000 and 355,000, respectively) will see the end of the mortgage payment support by the end of October 2021 (if still supported). Second, the economic rebound and the COVID-19 vaccination campaign will likely help unemployed individuals to find a job (as the economic recovery continues and the pandemic slowly becomes under control). Some people in forbearance or delinquency status may be able to resume their mortgage payments as both the pandemic and economic conditions improve. But, if the recovery and controlling the pandemic is slower than expected, a large number of foreclosures may occur and will likely result in a rise of the housing supply.

Markets are cyclical. The housing market will correct itself from a seller's market (as we have today), reach balance and will eventually turn into a buyer's market. When the cycle will start and end is nearly impossible to predict exactly. Yet, if the correction results in an unsubtle change, suddenly overflowing the market with sellers (excess supply), we may see home prices crash.

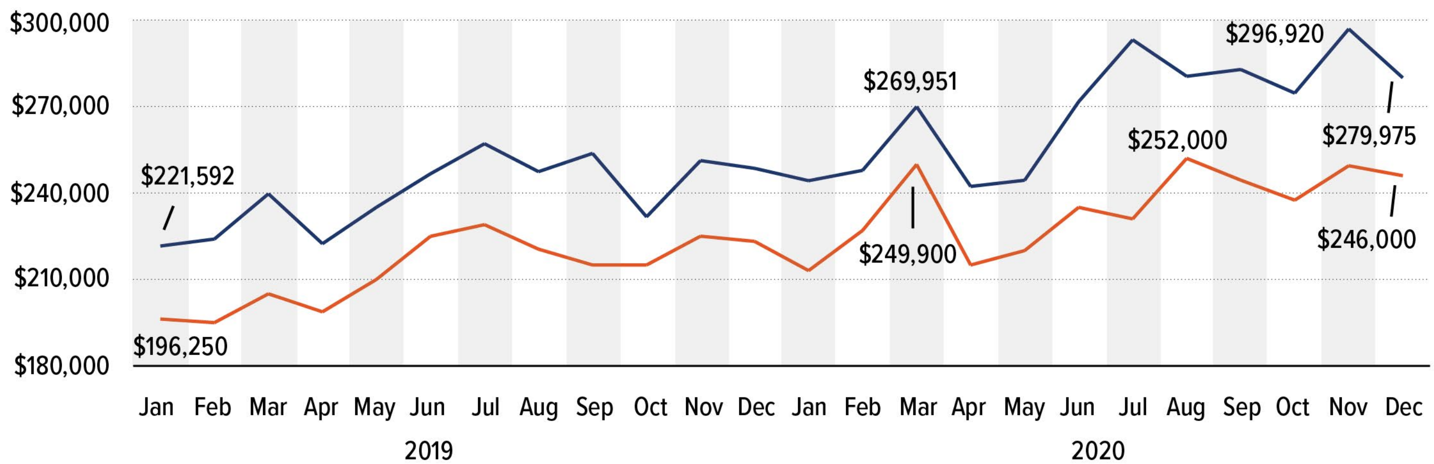
The Housing Market in Tyler

Although we track national figures, we need to understand that the U.S. is not one large housing market, but many different markets. Each city in every state within the nation has its own conditions that determine its housing market. The Tyler housing market does not necessarily follow the national figures or all determinants.

The demand for homes in Tyler was high before the pandemic hit in April 2020. The *months of inventory* indicator was below 6.5 months (a balanced market) in 2019 and early 2020. (**Figure 4**). Although the structure of Tyler's business economy mitigated the negative impacts of the pandemic (Tyler was not hit as severely as other cities in the nation), the local housing market has been affected by factors that made the national demand for homes to rise in 2020. Sales have increased substantially since July 2020. Similarly, average and median prices have grown consistently during the same period. The *months of inventory* indicator is currently at 2.2, which implies a strong seller's market.

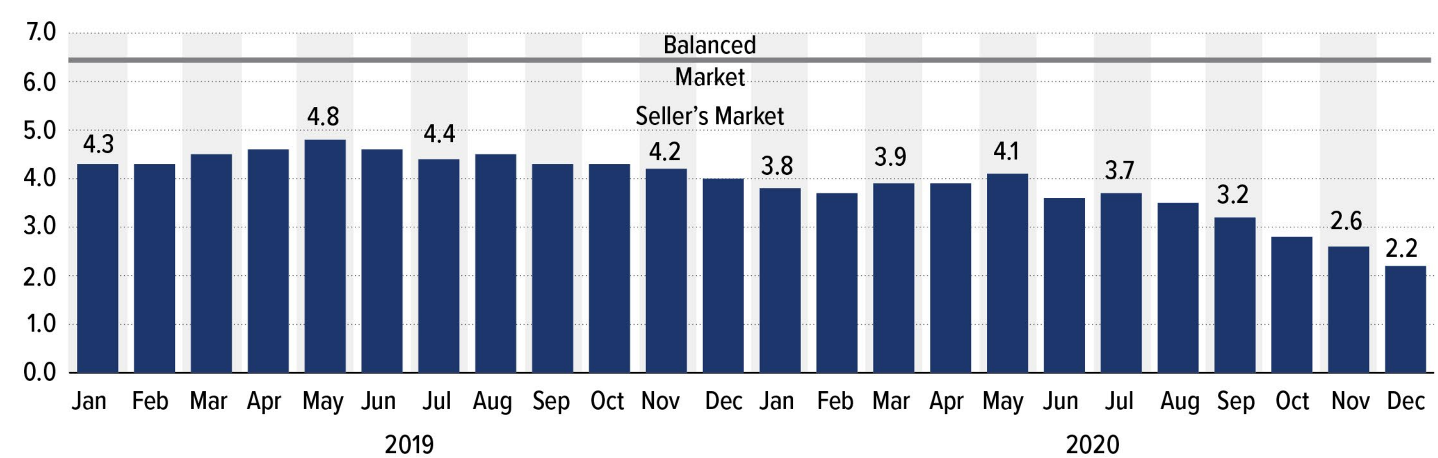
Unemployment and foreclosures are the two key factors that could cause the housing market to crash in the nation if economic conditions do not to improve in 2021. Tyler is doing well and moving toward a complete economic recovery. Therefore, we expect the Tyler housing market to do better than the national average during the post-pandemic economic recovery in 2021.

Figure 4. Average and Median Prices in Tyler, TX (January 2019–December 2020)



Source: Greater Tyler Association of REALTORS®, Inc.

Figure 5. Months of Inventory in Tyler, TX (January 2019–December 2020)



Source: Greater Tyler Association of REALTORS®, Inc.

[1] The *months of inventory* measures the current supply of homes offered for sale relative to the number of homes being purchased. The result indicates the number of months it would take to sell all properties currently for sale at the average monthly sales pace. It is calculated by dividing the number of active listings in the Multiple Listings Service (MLS) by the average number of sales per month during the prior 12 months. Real Estate Center at Texas A&M University. https://assets.recenter.tamu.edu/documents/articles/2046-7.pdf

[2] For a more detailed explanation on the interest rates determination, please refer to a past issue of the Hibbs Brief:
"The Federal Reserve Lowered their Rate... Why do I care?"
https://www.uttyler.edu/hibbs-institute/files/briefs/2019/hibbs-brief-federal-reserve-lowered-their-rate-why-do-we-care.pdf.pdf

[3] On March 15, the Federal Open Market Committee (FOMC), in an emergency meeting, agreed to lower the rate between 0 and 0.25%, and reactivated the quantitative easing program promising to purchase at least $500 billion in U.S. Treasury securities, and at least $200 billion in mortgage-backed securities. Additional tools were then put in effect in another emergency meeting on March 23.
https://www.federalreserve.gov/newsevents/pressreleases/monetary20200315a1.htm

[4] On December 24, 2020, the primary mortgage market survey, weekly gathered by Freddie Mac, reached its lowest point, 2.66%, since it was first gathered in April 1971.
http://www.freddiemac.com/pmms/

[5] The New York Times (Economy); "Fed Pledges Low Rates for Years, and Until Inflation Picks Up." September 16, 2020.
https://www.nytimes.com/2020/09/16/business/economy/federal-reserve-interest-rates.html

[6] Office of Policy Development and Research; U.S. Housing Market Conditions. National Housing Market Summary and Data (Supply Data – Single and Multifamily Construction).
https://www.huduser.gov/portal/ushmc/hs_sfm.html

[7] National Association of Home Builders (Economics, Trends); "How Long Does it Take to Build a Single-Family Home?" September 30, 2020.
https://nahbnow.com/2020/09/how-long-does-it-take-to-build-a-single-family-home-2/#:~:text=The%20average%20completion%20time%20 of,SOC)%20from%20the%20Census%20 Bureau.

[8] Office of Policy Development and Research; U.S. Housing Market Conditions. "Quarterly National Housing Market Summary: 3rd Quarter 2020."
https://www.huduser.gov/portal/sites/default/files/pdf/NationalSummary_3Q20.pdf

[9] U.S. Bureau of Labor Statistics; Labor Force Statistics from the Current Population Survey (Databases, Tables & Calculators by Subject).
https://www.bls.gov/cps/

[10] In February 2021, the unemployment rate was 6.2%, while the number of unemployed was of 10 million. Although both measures are much lower than their April 2020 highs, they remain well above their pre-pandemic levels in February 2020 (3.5 percent and 5.7 million, respectively). U.S. Bureau of Labor Statistics; Economic News Release. "Employment Situation Summary – February 2021." https://www.bls.gov/news.release/empsit.nr0.htm

[11] The number of delinquent accounts is defined by the Mortgage Banker Association (MBA) methodology. This method considers a mortgage loan delinquent if a monthly payment has not been received by the end of the day immediately preceding the loan's next due date. For instance, assuming a cut-off date of the end of the month, a loan with a due date of September 1, with no payment received by the close of business on September 30, would have been reported as delinquent on the next statement. Law Insider; Dictionary.
https://www.lawinsider.com/dictionary/mba-methodology

[12] Black Knight; "Mortgage Monitor – December 2020 Report."
https://cdn.blackknightinc.com/wp-content/uploads/2021/01/BKI_MM_Dec2020_Report.pdf

[13] The Coronavirus Aid, Relief, and Economic Security Act (CARES Act) is a bill passed by the U.S. Congress and signed into law by President Donald Trump in response to the economic fallout of the COVID-19 pandemic affecting the United States. The Act included $2.2 trillion economic stimulus distributed in different plans and programs when signed on March 27, 2020. AP News; "Trump signs $2.2T stimulus after swift congressional votes." March 27, 2020.
https://apnews.com/article/2099a53bb8adf2def7ee7329ea322f9d

[14] U.S. Department of Housing and Urban Development; "CARES Act Forbearance Fact Sheet for Borrowers with FHA, VA or USDA Loans."
https://www.hud.gov/sites/dfiles/SFH/documents/IACOVID19FBFactSheetConsumer.pdf

[15] The White House – Briefing Room; "Fact Sheet: Biden Administration Announces Extension of COVID-19 Forbearance and Foreclosure Protections for Homeowners." February 16, 2021.
https://www.whitehouse.gov/briefing-room/statements-releases/2021/02/16/fact-sheet-biden-administration-announces-extension-of-covid-19-forbearance-and-foreclosure-protections-for-homeowners/