Economics

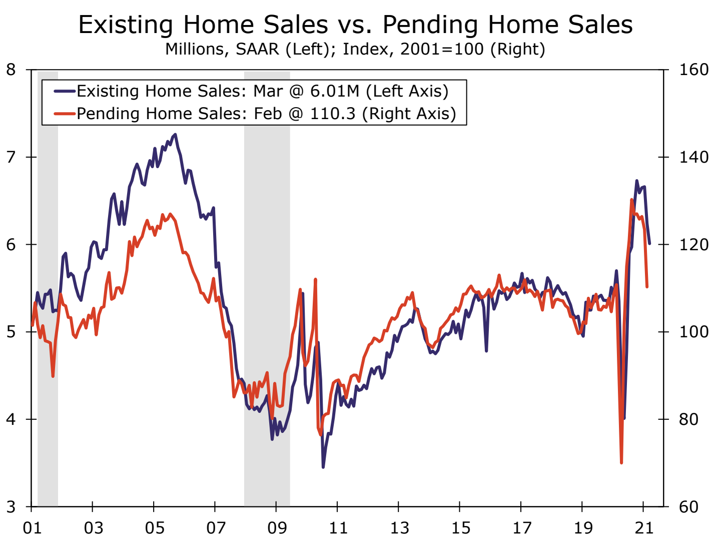
Economic Indicator — April 22, 2021

Existing Home Sales Slip 3.7% in March

Summary

Home Prices Surge Amid Strong Demand and Low Inventories

Existing home sales fell 3.7% in March to a 6.01-million unit pace. The decline was slightly larger than expected and comes one month after extreme weather severely cut into economic activity in Texas and other parts of the South and Midwest. Existing home sales reflect closings, which tend to occur four-to-six weeks after a purchase contract, captured by pending home sales, is signed. The drop closely follows the trend in pending homes sales. Sales fell in all four regions of the country, and would have likely been higher if there were more homes available for sale. Higher home prices are also likely pushing some buyers to the sidelines. The median price of an existing home has risen 17.2% over the past year to $329,100. Prices for single-family homes surged 18.4% over the past year to $334,500, both marking new historic highs.



Source: National Association of Realtors and Wells Fargo Securities

Economist(s)

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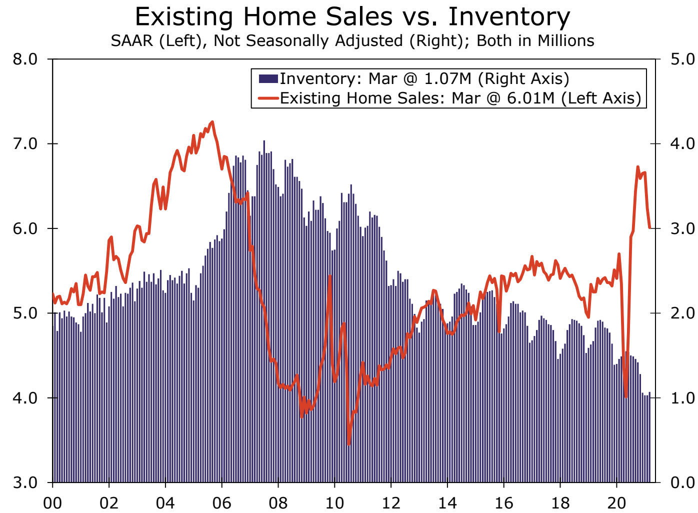
Too Hot, Too Soon

The March existing home sales data confirm what anecdotal reports have suggested for some time—the housing market heated up well ahead of the rest of the economy, and prices have surged to record levels. The surge in home prices over the past year is the key takeaway from the March data. The median price of an existing home, which includes condominiums, co-ops and townhomes, has risen 17.2% since last March and prices for single-family homes have surged an even higher 18.4%. The increase in home prices has rekindled fears of a housing bubble, reflected partly by reports of a surge in Google searches for "When Will the Housing Bubble Burst?"

We still feel that bubble talk is premature. The surge in home prices reflects a historic imbalance in the supply and demand for housing. Home sales turned up well before the economy began to improve, with record low mortgage rates and the transition to remote work and schooling setting off a race for more living space. The surge in demand came at a time that existing home inventories were already extraordinarily low, which set off bidding wars for what few listings were available. Eighty-three percent of homes sold in March were on the market for a month or less, and properties typically were on the market for just 18 days, down from 20 in February.



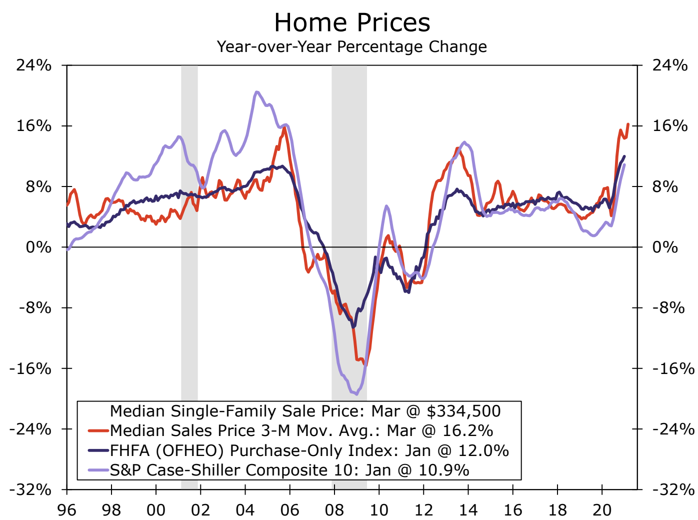
Source: National Association of Realtors and Wells Fargo Securities

Prices Are Up, But Speculation Has Not Returned Yet

There is no question that year-over-year home price appreciation in the high teens is unsustainable. Wages and salaries are only set to rise by a fraction of that pace, and higher prices are likely sending some would-be buyers to the sidelines. That said, first-time buyers accounted for 32% of March sales, up from 31% the prior month but down from 34% one year ago. The overwhelming majority of first-time buyers are Millennials, who are now forming households and seeking more living space.

Higher prices are also fueling a migration to more affordable parts of the country. For most markets, buyers are migrating to the suburbs or adjacent metropolitan areas. Realtor.com's Market Hotness Index noted that the nation's hottest housing markets in March were Manchester and Concord, New Hampshire—outside Boston; Vallejo, California—part of the Greater San Francisco area and Burlington, North Carolina, which is adjacent to the booming Durham metropolitan area and Research Triangle Park.

The one thing that has not returned is speculation in the housing market. Individual investors or second-home buyers accounted for just 15% of sales in March, down from 17% the prior month. Credit underwriting also remains relatively strict, with most of the growth in mortgages occurring among borrowers with high FICO scores. Existing homeowners are also sitting on a record amount of home equity.

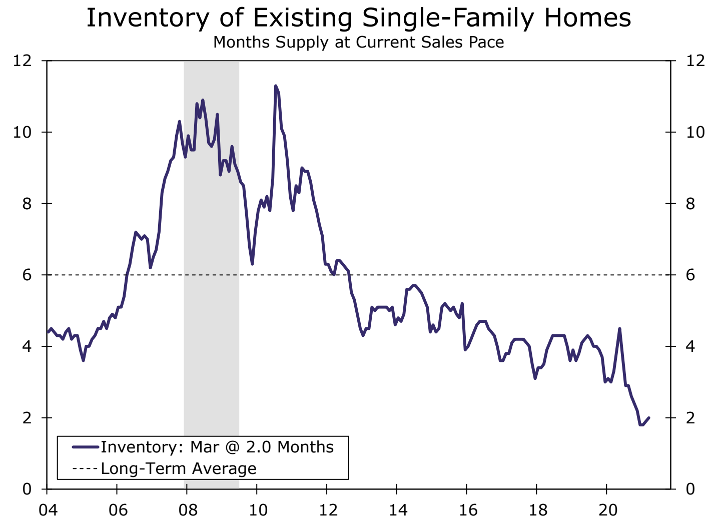


Source: NAR, FHFA, S&P CoreLogic and Wells Fargo Securities

The Best Solution to Higher Prices is Higher Prices

The surge in home prices is beginning to bring out sellers. Baby Boomers make up a disproportion share of existing homeowners, and many were understandably reluctant to put their homes on the market during the pandemic. Now that more than half of the U.S. population has been vaccinated, we expect to see more homes come on the market. The inventory of homes available for sale at the end of March rose 3.9% from the prior month to 1.07 million homes. Even with the increase, inventories remain at historic lows and are 28.2% lower than they were a year ago. The current inventory translates into just a 2.1-month supply at the current sales pace, up from two months in February. The long-time norm for inventories has been thought to be around six months, a level not seen consistently in years. Given the rise in cash buyers, pre-approvals of mortgages and third-party buyers, we believe this old benchmark is no longer relevant. The new normal for inventories is probably close to 3.5 to 4 months.

The strength in home prices will boost realtor's commissions, which is the key way that existing home sales influence quarterly GDP. The latest sales and home prices data are other variables pointing to exceptionally strong GDP growth in Q1 and Q2.



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