Economic Indicator — February 18, 2022

Existing Home Sales Surge Ahead of Rising Mortgage Rates

Summary

Existing Homes Sales Handily Top Expectations

Sales of existing homes jumped 6.7% in January to a 6.5 million-unit annual pace. Sales of single-family homes rose 6.5% to a 5.76 million-unit pace, while sales of condominiums and co-ops rose 8.8% to a 740,000 unit pace. Homes to continue to sell quickly, amidst record low inventories and strong demand from both individual and institutional investors. The median sales price fell slightly from the prior month on a non-seasonally adjusted basis to $350,300, but remains up 15.4% over the past year, with prices for single-family homes up 15.9% year-to-year and prices for condominiums and co-ops up 10.8%.

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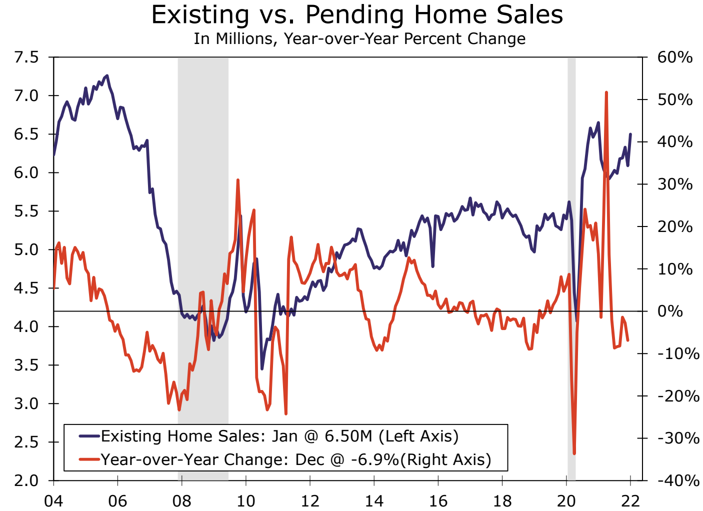
Buyers Strive to Keep a Step Ahead of Rising Rates

Existing home sales handily beat consensus expectations in January, with overall sales jumping 6.7% to a 6.5 million-unit pace. Sales rose solidly for both single-family homes (+6.7%) and sales of condominiums, townhomes and co-ops (+8.8%). We suspect that buyers rushed to close sales on homes ahead of rising mortgage rates. Pending home sales, which reflect purchase contracts, fell 3.8% in December, following a 2.3% drop in November. Existing home sales, which reflect closings, tend to lag closings by 30 to 60 days, which means January's stronger-than-expected rise must reflect many of that month's buyers speeding up the closing process in order to lock in lower mortgage rates. According to Freddie Mac, the average commitment rate of 30-year conventional mortgages was 3.45% in January, up from 3.10% in December but well below the current 3.92%.

Homes are clearly selling quickly. The average home remained on the market for just 19 days during January, which is the same as December but down from 21 days in January 2021. The National Association of Realtors noted that 79% of homes sold in January were on the market for less than a month. Another reason homes closed so quickly is that cash buyers accounted for a larger proportion of sales. Cash buyers accounted for 27% of sales in January, up from 23% in December and 19% in January 2021.



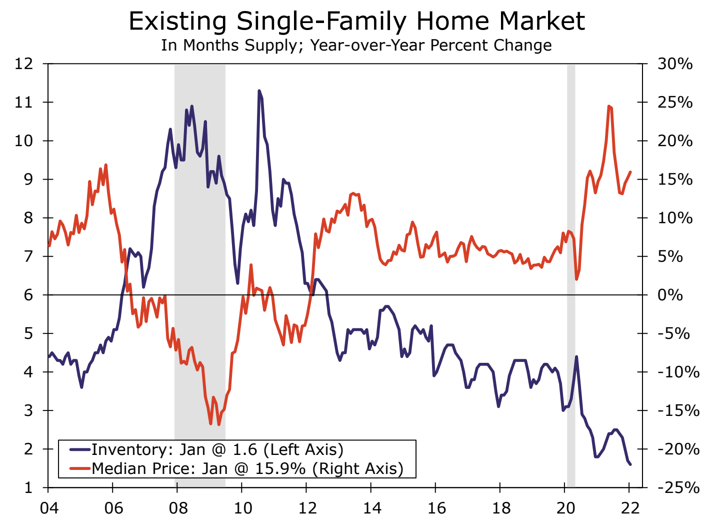
Source: National Association of Realtors and Wells Fargo Economics

Inventories Continue to Drop

One reason homes are selling so quickly is there are so few homes on the market. Total housing inventory at the end of January totaled just 860,000, which is a record low, down 2.3% from December and 16.5% below its level from last January. At the current sales pace, there is just a 1.6 month supply of homes available for sale, which is down from 1.7 months in December and 1.9 months in January 2021. Homes priced below $500,000 are particularly scarce, while there are slightly more homes available for sale priced above $500,000 than a year ago.

While inventories normally decline this time of year, the most recent drop comes from extraordinarily low levels and continues a long-running trend. The lack of inventory of lower priced homes appears to be feeding upon itself, with homeowners increasingly reluctant to put their homes on the market because they fear they will not be able to find another home they can afford. That is an issue that will be compounded in coming months with higher inflation slowing real income growth and driving interest rates higher.

With a larger share of existing home inventories priced above $500,000, we would expect the median sales prices of an existing home to rise faster in coming months and look for more buyers to opt for condominiums and townhomes, which are often more affordable options.

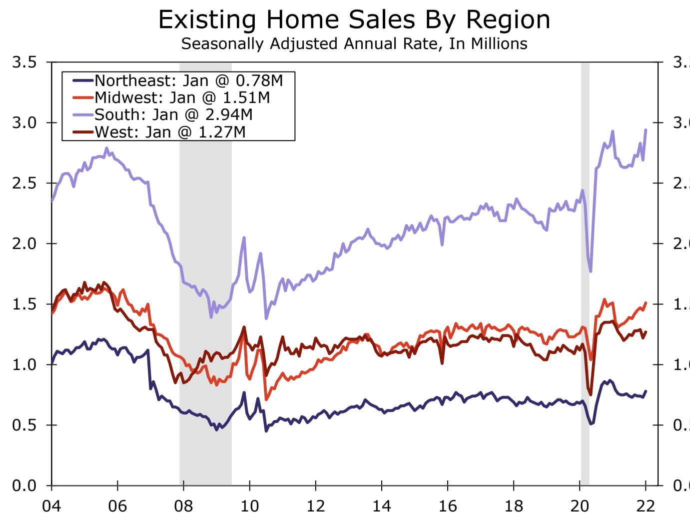


Source: National Association of Realtors and Wells Fargo Economics

Affordability Is a Growing Challenge for Traditional Buyers

Rising home prices and higher mortgage rates are further eroding affordability. The impact is most apparent among first-time home buyers who do not have the benefit of rising equity in their current home to help offset the surge in home prices seen over the past couple of years. First-time buyers accounted for just 27% of existing home sales in January, which is down from 30% in December and 33% in January 2021. With mortgage rates up a half a percentage point over the past months, some buyers are now likely to be priced out of the market. The impact will likely be most apparent in higher priced home markets, where the rise in mortgage rates will translate into substantially higher monthly payments

We expect existing home sales to moderate in coming months but look for the median price of homes sold to edge higher, as higher-priced homes account for a larger proportion of sales. The housing market is still riding some powerful tailwinds, with a wave of Millennials reaching a point in their lives when they are marrying, having children and purchasing their first homes. Moreover, we continue to see a massive affordability migration to the suburbs and outer suburbs of the nation's largest metro areas, as well as an accelerated migration to smaller, although still substantial, metro areas in the South and Mountain West.



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