The Residential Real Estate Market Is Slipping. Is it 2008 Deja Vu?

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There are troubling numbers but most factors indicate we are not heading for another housing bubble burst.

We had seen these real estate signs before. By the summer of 2020, homes are selling at record prices. Owners are getting multiple offers for above the asking price within hours after putting their houses on the market. Agents are unable to sign contracts fast enough. But then the decline begins. Single-family and condo/co-op sales go down 3.6% between April and May 2022 with an overall drop of 7.7% since April 2021. Houses remain on the market longer and longer.[1]

Are we spiraling toward a repeat of the burst of the residential real estate market bubble of 2008?

Not likely, even though some of the numbers are troubling.

An explosion in construction precipitated the residential real estate boom of the mid-2000s. Builders were raising subdivisions at record rates, fueled by easy money from lenders and suspect qualifications for buyers. Then it all crashed. Homes sat on the market for months, "underwater," as they were valued less than the amount owed on their mortgages.

In contrast, this latest housing boom was an unexpected by-product of the COVID-19 virus that infected the country and the world.

After the initial economic pause from COVID in March 2020, housing trends changed. People stuck working in their apartments desired more space. Millennials, a huge population group, aged into their prime buying years. Interest rates were low. Inflation was not a factor. Home prices were considered reasonable. So investment took off.

As the health crisis began to abate toward the end of 2020, it seemed as if the residential real estate market might return to normal. However, available inventory remained low in many parts of the country because folks hunkered down during COVID and improved their properties. Real-estate values also continued to soar because of supply chain issues, higher costs for construction material and a shortage of laborers.

So what happened?

As we reached the halfway point of 2022, a number of economic factors have begun to depress the real estate market again:

- Inflation remains elevated and has reached the highest level in four decades. As a result, the Federal Reserve (the Fed) has raised interest rates multiple times with more hikes to come, causing mortgage interest rates to exceed 5% for the first time in years.
- A bear market, down more than 20% at times, has put a big dent in the portfolios of many investors.
- Higher mortgage interest rates coupled with the higher home prices – the national median price of existing and new homes is now over $400,000 – has increased the average cost to purchase a home by 10.8% from 2021 to 2022 and it is expected to continue to rise further by an additional 3.2% going into 2023.[2]

All of this has led potential buyers to balk before investing in residential real estate.

But is it really that bad?

Many factors indicate what is happening now is not a repeat of 2008, such as:

- The excess home supply from the construction boom before 2008, plus the wave of foreclosures, led to the real estate bust. Today, supply remains short and demand is still strong.
- We have tighter lending guidelines and standards for mortgages compared to the loose credit of the early 2000s. The mortgage delinquency rates are only around 3%, compared with a peak of 9.3% during the housing crisis.[3] Presently, there are only 2.5 million adjustable-rate mortgages outstanding now; there were 13.1 million in 2007, just before the crash.[4]
- Savings rates are stronger as a result of the COVID Economic Stimulus and Relief Bill, which may help cushion any anticipated uptick in unemployment if we have another recession.

The unemployment rate remains at a low 3.6%, half of what it was in December 2008, when more than 11 million people were out of work. And we think many of those folks who might be vulnerable to unemployment today are already out of the hunt because the labor force participation rate at 62.3% is lower than it was in February 2020 at 63.4% (the Fed defines the labor force participation rate as "the percentage of the [civilian] population that is either working or actively looking for work").

We should note that the current housing slide has not equally affected all areas of the country.

The Sun Belt states, in particular, remain a strong market. According to seasonally adjusted federal data, almost 90% of the new homes sold in May were either in the South or the West. Median sales prices have increased in all sectors of the country year-over-year. But in the Northeast, median sales price has moderated. Still, the region has the highest median sales price in the US at $563,000, up about 10% year-over-year. In the Midwest, the median sales price in Q1 was $406,800, up from $320,600 the previous year, the largest increase of any of the four sections of the country.[5]

Key takeaways

Recessions affect every aspect of the economy, and real estate and housing are not exceptions. However we believe prices will continue to increase/appreciate, though at a much smaller pace because of the inventory situation and number of buyers. Most price declines during a recession are minimal.

As we move into 2023, we believe we will experience a leveling off and return to normal appreciation. Residential real estate is still a worthy investment.

To learn more, please contact your advisor.

About the Author

Emily Mogen specializes in fiduciary property management, helping individuals, families, professionals, business owners, foundations, and executives navigate the complexities of Trust Real Estate. With more than 22 years of experience, she provides advice and services for real estate investments, sales, purchases, inspections, ADA compliance, environmental issues, rent collection, renovations, management of mineral, oil, and gas assets, and property management. She attended the University of Akron, holds the Accredited Commercial Manager and Certified Property Manager designations from the Institute of Real Estate Management, and holds an Ohio real estate license. Emily is Treasurer and past President of the Northern Ohio Chapter of the Institute of Real Estate Management (IREM), President of the National Trust Real Estate Association (NTREA), a Member of the Commercial Committee at the Akron Cleveland Association of Realtors® (ACAR), and a Member of the National Association of Realtors.

[1]Existing-Home Sales Fell 3.4% in May; Median Sales Price (globenewswire.com)
[2]Homes Sales & Residential Lending Forecast by Fannie Mae & The MBA -- May 2022 | Stewart Title
[3]U.S. mortgage delinquency rate 2000-2022 | Statista
[4]Here's why this housing downturn is nothing like the last one (cnbc.com)
[5]Q1 2022, Quarterly New One-Family Home Sales by Price and Financing: Median and Average Sales Price of Houses Sold by Region

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