CIO believes the size of the 25–39-year-old demographic represents a solid source of future housing demand. (UBS)

The state of the US housing market: Not a repeat of '08

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The significant jump in 30-year fixed mortgage rates, combined with the surge in home prices between July 2020 and July 2022, the retrenchment in single-family home sales, and the COVID pandemic had many prognosticators predicting a repeat of the 2008–09 housing debacle. CIO believe otherwise. Here's why.

Inventory, or lack thereof

The current housing cycle continues to experience an ongoing dearth of available for-sale supply. The existing home market (which represents the largest portion of the housing market) is suffering from significantly reduced supply whether measured on an absolute or months-of-supply (MOS) basis.

Regarding the new-home market, much has been made about the significant increase in the MOS of homes available for sale. We take into account housing in all stages: not started, in construction, and completed and available for sale. The MOS for homes actually completed and available for sale is extremely low. We credit the homebuilders for learning some important lessons from the housing bubble, and do not believe the builders will revert to the frenetic pace of speculative building of the housing bubble.

Additionally, in the existing-home market, people are aging in place longer. The homeownership rate for those over 65 years of age is up several hundred basis points from the early 1990s and has held relatively steady in the 78–79% range over the past decade or so.

In terms of the new-home market, the pandemic-induced supply chain and labor availability challenges have significantly increased the average cycle time to build a home.

Further exacerbating the ongoing housing shortage is the years of under-building of both single-family and multifamily residences in the years following the global financial crisis (GFC). The growth in the number of households far outpaced the total number of housing starts post-GFC. We believe it is unlikely that this gap will narrow anytime in the near future.

Demographics
There is a common misconception among many market participants that the biggest portion of the US population is over 65 years of age. In actuality, the single biggest cohort is between the ages of 25 and 39, at approximately 68 million people This is crucial because, despite a national homeownership rate of approximately 66%, the homeownership rate for those below 35 years of age is some 2,600 basis points below the national average.

Marriage and family formation are an essential contributor to homeownership, and the homeownership rate is much higher for married people between the ages of 25 and 39. As the trend of men and women getting married and women having children later in life continues, we believe the size of the 25–39-year-old demographic represents a solid source of future housing demand.

An additional potential source of housing demand (including rental demand) is the plethora of 25–34-year-olds still living at home. As the data indicates, almost 7 million people between the ages of 25 and 34 still live at home. It is likely that a number of these people who ultimately move out could rent an apartment of a single-family home; it is also possible that a portion of them are living at home to save for a down payment for a home purchase.

Lending standards substantially better in the current cycle
This is perhaps one of the great understatements of all time. The pre-GFC underwriting cycle featured such loans as no-doc, low-doc, stated-income (liar loans), and NINJA (no income, no job, no assets). Although there is undoubtedly some poor underwriting that has occurred post-GFC, the quality of underwriting has been much more conservative in the current cycle. This is evidenced by several data points including the Mortgage Bankers Association Mortgage Credit Availability Index, the Federal Reserve's Senior Loan Officer Opinion Survey (SLOOS), and the serious delinquency and foreclosure rate trends.

Equity and consumer balance sheets
As of 4Q22, homeowners were sitting on some USD 30 trillion of equity. Although this figure has likely declined by several trillions over the past several months, homeowners have a significantly larger equity cushion than they did leading up to the GFC.

In addition, it is estimated that homeowners are currently sitting on approximately USD 9.3 trillion in tappable equity, which is defined by Black Knight Financial Services as the amount available to homeowners with mortgages to borrow against while still maintaining at least 20% equity in their homes.

One other observation we would make is the composition of fixed versus floating-rate mortgages during the housing bubble and the current cycle. At the peak of the housing bubble, some 40% of the outstanding mortgages were floating-rate. We estimate that, at least prior to the recent spike in rates, floating-rate loans represented some 3% of outstanding mortgages. Although that figure has likely grown over the past several months, we believe the risk of a payment-reset shock is substantially lower than during the GFC.

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Read the full report, **US housing market update: Green grass and high tides** (14 April 2023), which also discusses challenges for the housing market.

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