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THE ORANGE COUNTY HOUSING REPORT

HOUSING INSANITY

WHEN WILL IT END?

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THE RESIDENTIAL RESALE HOUSING MARKET HAS BEEN AT AN UNRELENTING, TORRID, INSANE PACE SINCE JULY OF LAST YEAR, AND, SEEMINGLY, NOTHING WILL SLOW IT DOWN.

INTEREST RATES JUICING THE MARKET

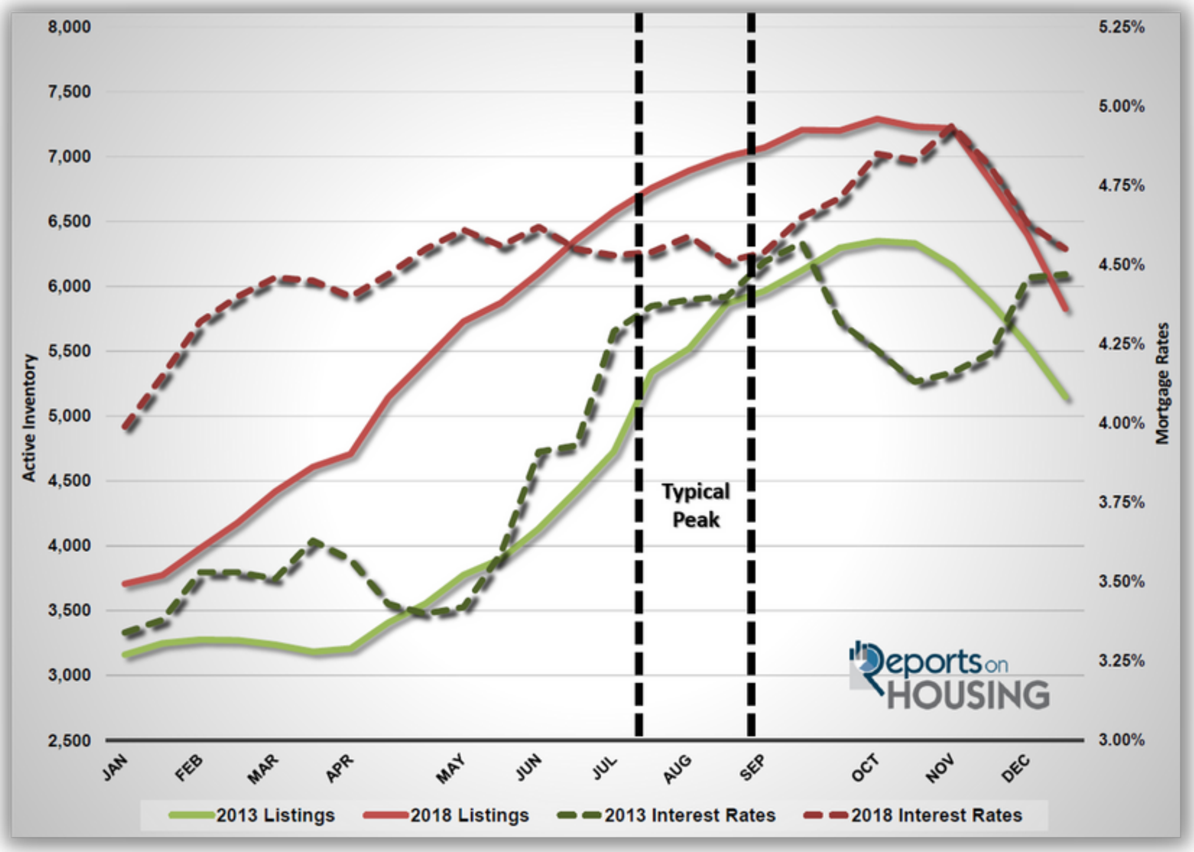
HISTORICALLY LOW RATES HAVE LED TO THE EXPECTED MARKET TIME DROPPING TO 23 DAYS, THE LOWEST LEVEL FOR THIS TIME OF YEAR SINCE TRACKING BEGAN IN 2004.

For Los Angeles Angels fans, prior to 2002, it seemed that their team would never make the World Series. The Major League Baseball franchise was founded in 1961, and it took them 41 years until they reached the pinnacle games. They had only earned 3 trips to the playoffs prior. As a fan, there were more losing games than winning games, so any vision of hoisting the World Series Commissioner's Trophy was more of a daydream. There was no light at the end of the tunnel, until the Angels made the playoffs with a wild card berth in 2002. They became only the second team ever to win their solo World Series appearance.

Similarly, for buyers waiting for the market to slow and turn more favorably towards the home shopper, there seems to be no light at the end of tunnel. Housing has lined up in favor of sellers since 2012. Many thought that the pandemic would slow housing, create a deep recession, and erode home values, giving buyers that much desired edge. Instead, rates plummeted to record lows, demand escalated, the inventory of homes available plummeted to unfathomable depths, and home values soared to unbelievable heights. The pandemic led economic recession lasted only two months, and it did not touch the housing industry.

Values have climbed more than 20% year-over-year and the pace of Orange County housing has not slowed much at all this year. The Expected Market Time (the amount of time between hammering in the FOR-SALE sign and opening escrow) is currently at 23 days, an unbelievably Hot Seller's Market. A Hot Seller's Market is defined as a market time below 60-days, the lower the level, the hotter the market. At 23-days, the market remains insane with plenty of showings, multiple offers, and sales prices above their list prices. At this point, what will decelerate the market enough to allow housing to transition away from a Hot Seller's Market to a Slight Seller's Market, Balanced Market, or even a Buyer's Market? Rising mortgage rates. That is precisely what occurred in 2013 and 2018.

ORANGE COUNTY ACTIVE LISTING INVENTORY AND RATES (2013 & 2018)



Like today, in 2013 there was a very limited supply of available homes to purchase, a supply crisis with less than 4,000 homes available. Market time was at a very low, insane level, below 40-days to start the year. The inventory remained at a low level until it started to climb in April. It continued to climb until reaching a late peak in October at 6,350 homes, doubling from the low 3,183 level in March. What changed? Mortgage rates. They started 2013 at just over 3.25%, eclipsed 4% in June, and surpassed 4.5% in September.

When rates rise, many buyers turn their collective noses away from pursuing a home because monthly mortgage payments rise, and affordability diminishes. As a result, the inventory rises with fewer buyers in the marketplace, and the Expected Market Time rises as well. It takes longer to sell with increased seller competition. In 2013, demand dropped by 27% from its peak in June to October, the inventory doubled from its March lows, and the market time increased from 33 days in March to 82 days in October, a Slight Seller's Market. That is a market with an Expected Market Time between 60 and 90 days, there are fewer showings than a Hot Seller's Market, far fewer multiple offer situations, sellers still get to call the shots, and home values are not appreciating much at all. It is not a buyer's market, but a market where buyers are not kicking and clawing their way to home ownership.

Similarly, in 2018 there was a supply crisis to start the year with less than 4,000 homes available. Yet, this time interest rates rose rapidly from 4% at the start of January to nearly 4.5% by March. It did not stop there either, making its way to almost 5% by November. With rapidly rising rates, demand was muted during the Spring Market, off by 12% compared to the prior 3-year average. Demand dropped by 28% from its peak in May to October, the inventory doubled from the start of the year to its peak in October, and the market time increased from 51 days in February to 110 days in October, a Balanced Market. A Balanced Market has an Expected Market Time between 90 and 120 days, does not favor buyers or sellers, and values do not change much at all.

This year there really has been no relief in the relentless pace of real estate due to the historically low mortgage rate environment. According to Freddie Mac's Primary Mortgage Market Survey®, mortgage rates have risen to 3.14% the highest level since March. For proper perspective, after the start of the pandemic, rates reached 17 record lows, the 17th was during the first week of January of this year at 2.65%. Yes, rates have risen from there, but keep in mind that prior to the pandemic, today's 3.14% rate would be an all-time low. They remain at very low levels, which is why the active listing inventory is 67% below the 3-year average between 2017 and 2019, prior to the pandemic, demand is 11% higher, and the market time is stuck well below 40-days.

For the market to noticeably slow, mortgage rates would need to rise considerably. At 3.5%, it would afford a little bit of relief, but not much. Rates would need to climb to 4% for the market to slow from an insanely Hot Seller's Market to just a Hot Seller's Market with market times closer to 60-days. Very few economists project rates to climb above 4%. That is what it would take for the market to move more towards a Buyer's Market. The market needs to transition first to a Slight Seller's Market, between 60 and 90 days, then to a Balanced Market, between 90 and 120 days, next to a Slight Buyer's Market, between 120 and 150 days, and finally, to a Deep Buyer's Market, greater than 150 days. A Deep Buyer's Market is one where there are very few showings, a glut of homes available to purchase, very few offers to purchase, buyers get to call all the shots and take their time, and values tumble. That would take a rise in rates to over 4.5%, which is not anticipated to occur anytime on the horizon.

The light at the end of the tunnel with a shift in the market will not occur until mortgage rates rise substantially. Freddie Mac forecasted a couple of weeks ago that mortgage rates will rise to 3.5% in a year from now. That is not quite enough to slow housing meaningfully. Either rates eventually climb to slow housing, or values will climb to the point that they soften demand. The Orange County housing market is just not there yet.

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ACTIVE LISTINGS

THE CURRENT ACTIVE INVENTORY PLUNGED BY 9% IN THE PAST TWO WEEKS.

The active listing inventory shed 178 homes in the past couple of weeks, down 9%, and now sits at 1,864 homes, the lowest level since tracking began in 2004. That's a huge drop and has plunged the inventory to uncharted territories with a record low number of homes to start November. Last year at this time it reached a record low level for a start to November at 3,944 homes, 111% more than today, more than double, or an extra 2,080 homes available to purchase. There are only a few more weeks until housing transitions to the Holiday Market, from the week prior to Thanksgiving through the first couple of weeks of the New Year. Fewer homes will enter the fray and many unsuccessful sellers will throw in the towel. It is hard to believe, but 43% of the inventory has been on the market for over 30-days, the most likely sellers to pull their homes off the market during the holidays and wait until next year to try again. Expect the inventory to continue to drop in the next couple of weeks before plunging to its lowest levels of the year upon celebrating ringing in 2022.

The 3-year average from 2017 to 2019 (intentionally omitting 2020 due to COVID skewing the data) is 6,010, an extra 4,146 homes, or 222% more, triple compared to today. There were a lot more choices back then. The inventory typically drops 5% at this time of the year, not quite as high at the 9% drop realized in the past couple of weeks.

ORANGE COUNTY ACTIVE LISTINGS YEAR-OVER-YEAR (2018-2021)