# Monthly Market Views

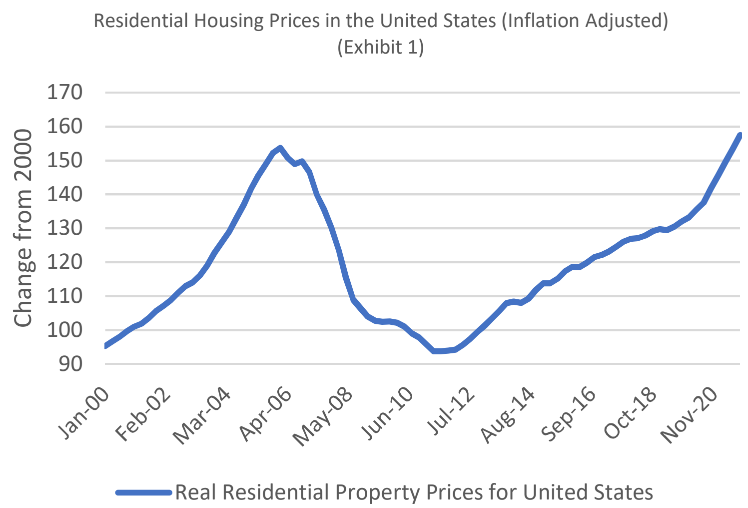
**International Private Banking Division**

**JUNE 2022**

## For investors considering investments public or private market real estate, what can be gathered about the likely path forward for today's housing market?

The housing market in the United States tends to be a significant driver of the overall economy. It is the sector of the economy that has historically both led the economy into recessions and pulled it out of them. It is also the sector of the economy that is specifically targeted by the US Federal Reserve when adjusting interest rates with a goal of affecting economic activity. Since the start of the Covid-19 pandemic in March 2020, the housing market has experienced a sustained and significant price increase. Looking ahead to 2022-23, while keeping in mind the housing bubble that burst during the 2007-2009 Great Financial Crisis (GFC), what should investors consider when thinking about housing today?

**Home Prices** - The housing market in the United States went through a significant adjustment following the bursting of the housing price bubble in 2006. In the years leading up to that peak, prices of real estate skyrocketed. At the height of the frenzy, inflation-adjusted housing prices had risen around 60% on average in a six-year period from 2000 to 2006, a rate far above historical norms (Exhibit 1[1]). This rise in prices also led to a simultaneous boom in construction; a lot of it for the purpose of real estate speculation, without consideration for underlying regional fundamentals. The bursting of this bubble was a catalyst for the GFC, which caused enormous wealth destruction. The unraveling of the GFC and resulting decline in home prices also led to an abrupt decline of home construction.



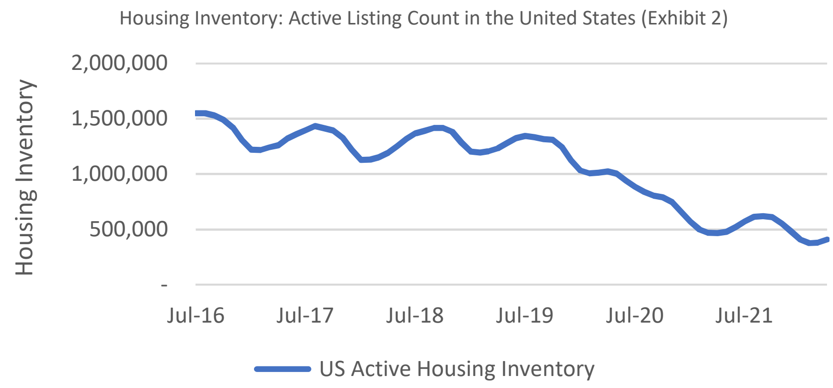

Today's housing price levels (inflation-adjusted) have recently surpassed their 2006 high's, fueled by low-interest rates and a Covid-19 induced migration. However, unlike the period leading up to the GFC, lending standards have remained conservative; and mortgage activity has largely involved 30-year fixed loans, diminishing the risk of refinancing risk.

**Housing Inventory** - As the Covid-19 pandemic took hold in early 2020, the demand for single-family housing increased sharply. At the same time the inventory of available homes for sale; due to a combination of people not wanting to leave their homes, and years of underbuilding, causing a housing shortage across many parts of the United States (Exhibit 2). These factors combined with a low interest rate environment, ushered in a significant appreciation in home prices.

*"By raising or lowering short-term interest rates, monetary policy affects the housing market, and in turn the overall economy, directly or indirectly through at least six channels: through the direct effects of interest rates on (1) the user cost of capital, (2) expectations of future house-price movements, and (3) housing supply; and indirectly through (4) standard wealth effects from house prices, (5) balance sheet, credit-channel effects on consumer spending, and (6) balance sheet, credit-channel effects on housing demand." – Fred Mishkin, Ex. Board of Governors of the Federal Reserve*

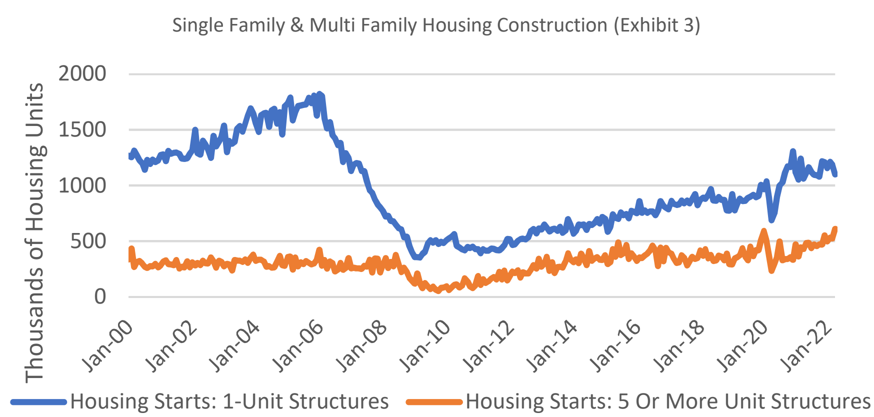
[1] Real Residential Property Prices for United States, Index Q1 2000=100, Quarterly, Not Seasonally Adjusted https://fred.stlouisfed.org/series/QUSR628BIS#0

**Housing Inventory** (Continued) Focusing on the path of available homes for sale will be an integral part of determining the path of the housing market in 2022-2023. With rising mortgage rates there is likely to be an increase in housing inventories, but based on current construction trends it is unlikely that there will be enough new supply to return inventories to pre-pandemic levels in the near future. If that turns out to be the case, the low level of inventories is likely to put a floor under average housing prices.

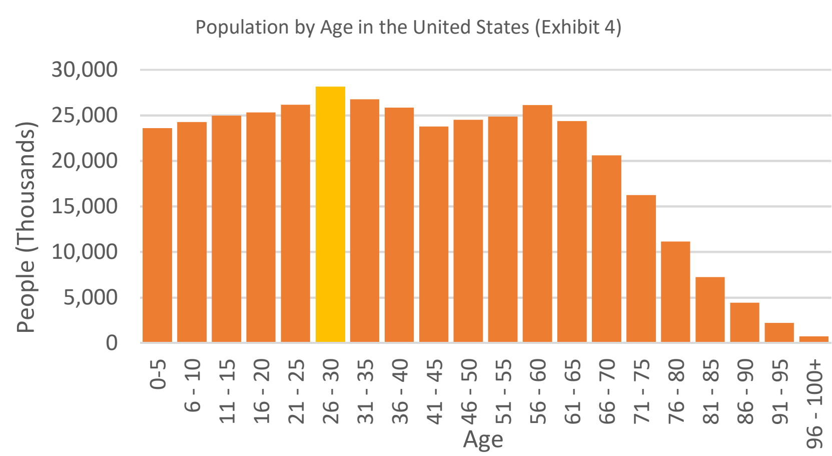



**Home Construction** - The pace of single-family home construction was almost certainly growing faster than the US population from 2000 to 2006 (Exhibit 3[2]). Since 2006 however, while the US population has grown around 11%, from 298 Million to 333 Million, the pace of home construction has lagged far behind (Exhibit 2 – Blue line).

The demand for housing has been met partially through an increase in rentals of single-family homes and multi-family apartments. Even with the recent increase in building activity, single-family home construction has yet to fully recover to pre-GFC levels. Meanwhile multi-family construction activity (e.g. apartment buildings) had fully recovered by 2013, and has continued at or above pre- GFC levels for the past eight years (Exhibit 3 – Orange line).




**Demographics** - In addition to the near-term fundamentals mentioned previously, there is another significant change taking place in the age distribution of the United States population. The millennial generation, which represents the largest age cohort among the US population, is entering their 30s (Exhibit 4[3]). This age group has traditionally been the front end of the peek home buying demographic, as increasing family size tends to lead to a demand for larger living quarters. This demographic shift is likely to be a tail wind for demand in the coming years.




Today's housing environment should be a looked at in terms of a combination of factors. On one hand, the low level of inventories and generally positive demographic trends are positive for housing prices. On the other hand, the rapid increase in mortgage rates, significant price appreciation since 2020, and record levels of units under construction are negative for housing prices. **Taking these factors together, our outlook for 2022-23 is an environment where housing appreciation reverts to longer-term single-digit trends, from the rapid-growth of the last few years.**

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2 Privately Owned Housing Starts: 1-Unit Structures, Thousands of Units, Monthly, Seasonally Adjusted Annual Rate, Privately Owned Housing Starts: 1-Unit Structures, Thousands of Units, Monthly, Seasonally Adjusted Annual Ratehttps://fred.stlouisfed.org/series/HOUST1F#0

3 US Census https://www.census.gov/newsroom/press-kits/2020/population-estimates-detailed.html

**Economic Overview**

| | GDP Forecast (2022) | GDP Forecast (2023) | Inflation Forecast (2022) | Inflation Forecast (2023) | Currency vs. USD | IG Credit Downgrade |
|---|---|---|---|---|---|---|
| Argentina | 2.7% | 2% | 56% | 48% | -13.7% | N/A |
| Brazil | 0.6% | 2% | 9% | 5% | 14.9% | N/A |
| Chile | 2.1% | 1% | 8% | 4% | 1.9% | Low |
| Mexico | 2.0% | 2% | 7% | 5% | 3.4% | Medium |
| Peru | 2.8% | 3% | 6% | 3% | 8.6% | Low |
| Uruguay | 4.2% | 3% | 9% | 7% | 11.6% | High |
| Israel | 5.0% | 4% | 3% | 2% | -7.2% | Very Low |
| USA | 2.7% | 2% | 7% | 3% | 6.8% | Very Low |

**COVID-19 Overview**

| | Vaccine Doses / Population | Total Cases | Total Cases/ Population | Last 30 Day Growth Rate |
|---|---|---|---|---|
| Argentina | 214% | 9,178,795 | 19.28% | 1% |
| Brazil | 202% | 30,836,815 | 14.24% | 1% |
| Chile | 278% | 3,651,076 | 18.26% | 2% |
| Mexico | 158% | 5,759,773 | 4.38% | 0% |
| Peru | 219% | 3,576,640 | 10.52% | 0% |
| Uruguay | 233% | 916,388 | 25.61% | 1% |
| Israel | 211% | 4,127,018 | 47.99% | 1% |
| USA | 178% | 83,501,457 | 25.46% | 2% |

*Data Source: Bloomberg Terminal, as of May 31, 2022*

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**IMPORTANT DISCLOSURES**

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