

In forecasting home prices, the last housing cycle is a poor guide for this one

The post-pandemic demand and supply backdrop has strong and stable underpinnings

As the US housing market transitions to its post-pandemic phase, it faces major headwinds including a historically rapid increase in mortgage rates. With negative headlines growing and memories of the Great Financial Crisis still fresh in investors' minds, fears of a major home price correction have grown. In comparing this cycle to the last, Pretium believes that housing's risk profile is dramatically different in 2022 than it was in 2006. The risk to home prices was underappreciated by many investors in 2006 because home prices hadn't seen a significant national decline since the Great Depression; conversely, the current perceived risk to home prices may be overstated because home prices experienced a major correction just 10 years ago. Fundamentals matter, and the demand and supply backdrop for the post-pandemic period is solidly grounded especially relative to the mid-2000s housing boom. Looking ahead, the supply-demand imbalance that propelled housing during the pandemic is still likely to remain an important dynamic in the post-pandemic housing market. While home prices may not emerge unscathed from adverse economic scenarios, Pretium expects downside risk to be limited compared to the last cycle. Overall, housing's unresolved supply-demand imbalance underpins a favorable risk-reward profile for residential housing investment, particularly for single-family rental homes.

The strong demand backdrop for housing is most clearly illustrated by the increase in rents alongside home prices the past few years, as shown in Exhibit 1. Both single-family and multifamily rents grew at a double-digit pace and are up more than 20% in the two years ending June 2022.¹ This compares to the roughly 7% increase that rents experienced during 2004-05 period. Easing mortgage lending standards amplified housing demand mostly in the purchase market during the mid-2000s whereas mortgage lending standards tightened during the pandemic. Rental markets don't experience speculative excess as the home purchase market does, so the meaningful increase in rents during the pandemic argues that housing demand is well-grounded fundamentally. Pretium believes that the pandemic structurally increased housing demand as reflected in trends such as work-from-home, increased migration and greater consumer prioritization of space & wellbeing.

Exhibit 2 illustrates the strong relationship between home prices and months supply of resale inventories. The historically low levels of resale inventories during the pandemic (more than two-thirds below pre-pandemic levels) anchored home price growth. For sustained home price pressure to emerge in the post-pandemic period, inventory levels would have to increase substantially from current levels as they did in 2006-07. This seems unlikely given low levels of mortgage distress, a reluctance by existing homeowners to give up their low fixed rate mortgages, aging-in-place and long-term underbuilding since the last cycle. These factors appear to have already begun to limit inventory growth even as the housing market transitions – in recent weeks, the volume of new resale listings has fallen 15-20% below pandemic levels and overall resale inventory levels have begun to flatten.²

EXHIBIT 1

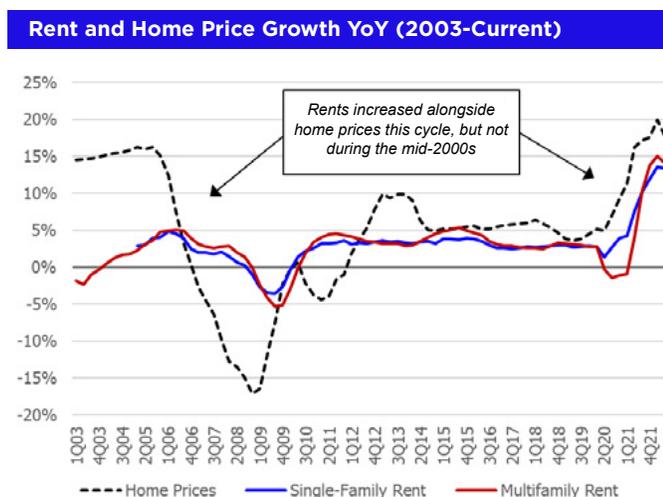
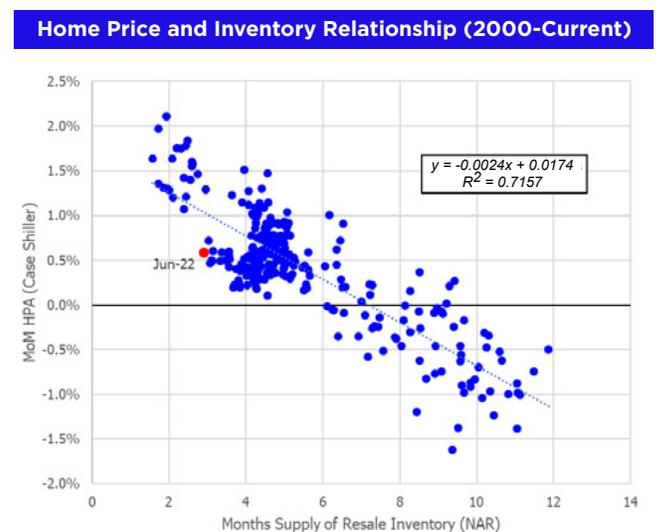


EXHIBIT 2



Source: CoreLogic Single-Family Rent, S&P Case-Shiller and Home Price Indices, all as of September 2022; RealPage Axiometrics Quarterly Market Performance Trend, as of September 2022; National Association of Realtors Existing-Home Sales retrieved via Bloomberg, as of September 2022.

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1. CoreLogic Single-Family Rent Index, RealPage Axiometrics Quarterly Market Performance Trend, both as of September 2022.
2. Redfin Weekly Housing Market Data, as of September 4, 2022.