Today, in lieu of my usual economics and investing news and commentary, Iâ€™d like to briefly expound a bit on my view of the collapsing real estate market in the United States.

Iâ€™ll begin by mentioning something published in Investment Watchblog that I found linked over at the Whatfinger.com news aggregation site: US Median Home Price Drops 12% in Six Months â€“ Largest Drop Since 2009. Please take the time to read that article.

Now take a look at an ominous figure that was neatly buried down in the ninth paragraph of an article with a cheery headline over at the webâ€™s Perpetual Cheering Section, CNBC, on January 26th:

â€œA 26.7% plunge in residential fixed investment, reflecting a sharp slide in housing, served as a drag on the growth numberâ€¦â€•

People are now recognizing that the tide has turned. See: 41% Of Americans Expect A Housing Crash In 2023. Here is a pericope from that article:

â€œ41% of Americans, according to the survey that was originally reported by the New York Post, believe that the housing market will collapse within the next 12 months.

Comparatively speaking, only 25% of respondents said they believed the industry would escape a crash, and 34% said they were unsure.

74% of those anticipating a crash think it will be as catastrophic as, or worse than, the housing market collapse that occurred in 2008 during the Great Recession.â€•

Those articles confirm something that Iâ€™ve been warning folks about in SurvivalBlog, for many months.

With the Federal Open Market Committee (FOMC) likely to continue to raise interest rates, we can expect house prices to decline in most markets, and simply crater in the most over-priced markets.

I hope that my readers took my advice and have already shed themselves of any speculative investment (â€œspecâ€•) houses or under-used vacation homes.

To back up a bit, I should point out that the real estate market in the UnIted States has been highly cyclical, since 1945. This article at Investopedia provides some solid background information: Four Key Factors That Drive the Real Estate Market.

Weâ€™ve Seen The Top

I can foresee that the currently unfolding real estate market rout will differ from previous market busts. In my estimation, this in part will be because

government debt has reached extreme proportions. Presently, paying just the interest on the national debt now consumes nearly as much of the annual Federal budget as all defense spending, combined. Ponder that for a moment. Because of compounding interest, the mountain of government debt simply cannot be repaid without destroying the Dollar as a currency unit, via mass inflation. Absent mass inflation, paying down the debt is mathematically impossible. Letâ€™s resign ourselves to that fact.

Interest rates were held artificially low by the Federal Reserveâ€™s FOMC for at least five years too long. These low rates fueled a boom in the real estate market that enlarged market demand and grossly inflated house prices. Traditionally, the price of a typical three-bedroom suburban house (with interest) equated to about 10 years of income for the average buyer. Thus, when putting one-third of a middle-class income toward mortgage payments, a 30-year mortgage was feasible. But in recent years, with ballooning house prices, that now equates to something closer to 20 years of income. The only reason that anyone other than cash buyers could afford to buy a house is because the artificially-low interest rates made monthly mortgage payments smaller. But, now, with interest rates normalizing to their traditional average levels, very few middle-class families can afford to buy a home.

Houses Are Too Expensive

Here is an excerpt from a 2018 article published by Curbed:

â€œTo understand just how unaffordable owning a home can be in American cities today, look at the case of a teacher in San Francisco seeking his or her first house.

Educators in the City by the Bay earn a median salary of $72,340. But, according to a new Trulia report, they can afford less than one percent of the homes currently on the market.

Despite making roughly $18,000 more than their peers in other states, many California teachersâ€”like legions of other public servants, middle-class workers, and medical staffâ€”need to resign themselves to finding roommates or enduring lengthy commutes. Some school districts, facing a brain drain due to rising real estate prices, are even developing affordable teacher housing so they can retain talent.

This housing math is brutal. With the average cost of a home in San Francisco hovering at $1.61 million, a typical 30-year mortgageâ€”with a 20 percent down payment at todayâ€™s 4.55 percent interest rateâ€”would require a monthly payment of $7,900 (more than double the $3,333 median monthly rent for a one-bedroom apartment last year).

Over the course of a year, thatâ€™s $94,800 in mortgage payments alone, clearly impossible on the aforementioned single teacherâ€™s salary, even if you somehow put away enough for a down payment (that would be $322,000, if youâ€™re aiming for 20 percent).â€•

Well, guess what, folks? House prices continued to climb, and now, most recently, interest rates have risen a lot. As of January 25, 2023, the prevailing 30-year fixed mortgage rate is 6.49%. Meanwhile, the â€œjumboâ€• 30-year fixed rate is 5.52%, the 30-year fixed rate is 6.66%, and the Veteranâ€™s Administration (VA) loan 30-year fixed rate is 6.85%. In effect, the increase in interest rates by just 3% has pushed nearly half of would-be buyers out of the market. They simply canâ€™t afford the monthly payments. That sad fact has rapidly turned the real estate market around.

Here is a â€œscrawled on the back of paper napkinâ€• example for you: A typical suburban home in a Blue State is now $420,000. In early 2022, with a 3% interest rate mortgage, the monthly payment was $1,800. But now, in January 2023, at a 6.5% interest rate, that same $420,000 home will require a $3,000 monthly payment.

The Roof Just Fell In

Instead of a super-heated sellerâ€™s market, we are starting to see a buyerâ€™s market. Folks realize the market shifted, so they are trying to sell their â€œextraâ€• houses (rentals, spec buys, vacation homes, and whatever), before house prices drop even further. We will soon witness a nationwide fire sale.

Some prices for existing listings on the coastline towns near Los Angeles and on the San Francisco Peninsula have already been reduced by 20% to 40%. Granted, those were particularly over-heated markets, but this shows us the direction that the market is heading. This will get quite ugly. I predict that if the Fed raises another 50 basis points (read: 1/2 of one percent), then it will trigger some panic selling.

The hardest hit areas will be the places that were recently overvalued. These include:

Austin, Texas

Phoenix, Arizona

San Jose, California

San Diego, California

Lakeland, Florida.

We probably wonâ€™t see the bottom for at least a couple of years â€” or perhaps even five or more years, if this turns into a general market depression.

But, On The Bright Sideâ€¦

Keep in mind that every market collapse has a bottom, and every bottom has some buying opportunities. And the really good news is that by buying real estate at the bottom of the market, you will be obtaining something for your familyâ€™s future that is quite tangible. This will become quite important when the Almighty Dollar inevitably collapses. Fiat currencies come and go, but the Earth abides, in 40-acre parcels.

As always: Sell high, and buy low.

And thatâ€™s all that I have to say about that.- JWR

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Reference

30 Essential Skills for the Qualitative Researcher

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