SPRING MARKET SOURCE NEWSLETTER

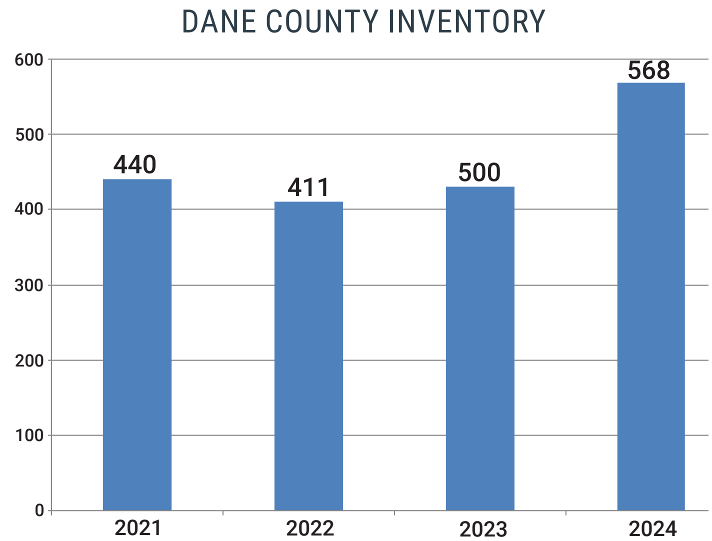
Written by President David Stark

THE SPRING MARKET is upon us, amid far less uncertainty about its direction than a year ago. Back then we were still digesting the effects of the unprecedented increase in mortgage rates manufactured by the Federal Reserve. Analysts remained confused about the direction of housing prices, predicting they would fall when it was clear they were rising, and erroneously believing demand would drop, when in fact the main effect was a decline in new listings. This confusion carried over to buyers and sellers, who were unclear as to the direction housing as an investment would take.

A year later, there is far less confusion. Analysts have figured out that housing prices are not falling, and there is even some chatter in the media about housing being a source of strength for the economy. The early indications are that demand is as strong as ever, while sellers seem at least a bit more willing to test the market.

In terms of sales, the first quarter of 2024 looked much like 2023. First quarter sales were essentially flat in Dane County, while they were up 7.7% in Sauk/Columbia. But underneath the raw sales numbers are some encouraging supports that are cause for optimism going forward. The most encouraging early sign is that new listings are up 15% in Dane County and 19% in Sauk/Columbia. Inventories are up 28% in Dane County and a whopping 67% in Sauk/Columbia. While months of inventory are still relatively low at 1.2 months in Dane County and 1.7 months in Sauk/Columbia, that's up by 50% and 70% respectively since last year. Two years ago, it seems hard to believe that we had only 0.5 months of inventory in Dane County and 0.6 months in Sauk/Columbia. So, while we still have a long way to go, the improvements are significant nonetheless.

With the weather finally warming up, many buyers and sellers are wondering what to think of this market. We'll give you our thoughts on the major variables, and how to attack them.



MORTGAGE RATES

The level of mortgage rates continues to captivate the media, leaving many buyers and sellers to conclude that they need to wait for them to fall before they act. This is a mistake, for two reasons.

First, we do not believe mortgage rates are going to fall all that much from their current levels. If you read our winter edition of this newsletter three months ago, you saw how the Fed's quantitative easing program manufactured a fourteen-year period when mortgage rates were lower than at any time in history. Outside of this unusual period, 30-year mortgage rates have historically averaged around 6-7%, or higher. The Fed ended quantitative easing in early 2022, when it finally started to cause unhealthy levels of inflation. Since then, mortgage rates have moved right back to their previous levels, currently standing around 7%. While they could drift a little lower over the next few months, we do not anticipate they will drop below 6% this year. If they do, it won't be by much. So, putting off a needed life change in the hopes that rates will drop is likely to be futile.

Second, housing prices are rising, as we'll explain below. This means that even if rates do come down, the savings will be offset by the appreciation you forgo and the higher price you pay. We illustrate nearby how this works. So, if mortgage rates are holding you back, think again.

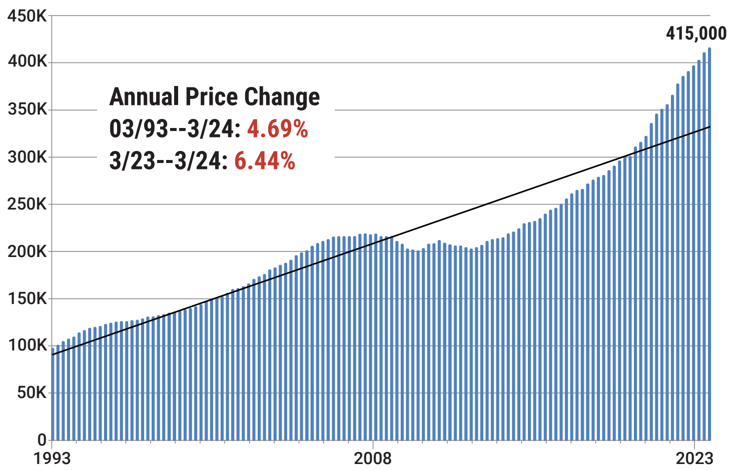
▶ PRICES

There is absolutely no evidence that housing prices will be falling. Over the 12 months from March of 2023 to March of 2024, the median residential price in Dane County (single family and condo combined) rose 6.44%. In Sauk/Columbia, it rose 8.91%. While we've seen a slight increase in the number of new listings, and in the level of inventory on hand, prices are already being bid up again at a rate similar to last year. For example, March closings in Dane County sold for an average of $5,605 over the list price, compared to an average overbid of $4,456 in March of 2023. So far this year, the Dane County 12-month median is already up 1.24%, and we're heading into spring when prices rise the most and overbids are the highest.

The fact is that with rare and temporary exceptions, housing prices rise pretty much every year. For perspective, consider that over the past 31 years (as long as we've been keeping the data), Dane County prices have risen an average of 4.69% per year. Over the past five years, the Dane County median price has increased 48.75%, or an average of 9.75% per year. Certainly, this is higher than the long-term trend. However, it's also important to note that over the entire 31-year period, we only saw prices actually decrease between December of 2007 and December of 2012, when they fell a total of 7.34% over the five year period of the great recession. They have risen steadily ever since, far outpacing the highs before the recession. Outside of very unusual circumstances, housing prices rise at a steady pace, usually at or slightly above the underlying rate of inflation. It has really only been since the pandemic that our price increases have exceeded the long-term average.

Does this mean prices could fall sometime in the future? That's always possible, of course, under the right set of circumstances, such as what we saw 17 years ago. But those circumstances are very rare, and nowhere in sight presently. As we've reminded our readers many times, inventories were over 10 times higher in 2007 than they are now, the only time we know of that prices started to decline. And mortgage loans were being underwritten very poorly back then, unlike now. We dug back through our archives and were astonished to be reminded that in 2007 we had around 10 months of inventory on the market, compared to barely one month today. Certainly, if we ever got back to a "balanced" market, which most observers believe is 6 months of inventory (we think it's lower), price increases would moderate, probably to about the rate of inflation. But we're years, maybe decades, away from that.

DANE COUNTY MEDIAN PRICE CHANGE, 1993-2023



The point of all this is that waiting for the market to "correct" is a fool's errand. We've been making the case for the last two years that today's mortgage rates are not too high. They were too low for the decade before this. Likewise, the demand for housing in our region pretty much guarantees that prices will continue to rise, although we believe that higher rates will moderate the rate of increase. In fact, they already have; prices rose 6.44% over the past 12 months, compared to the aforementioned 9.75% average increase over the past five years. But no matter how you slice it, the cost to buy will only go up year after year.

ADVICE FOR BUYERS AND SELLERS

IF YOU'RE BUYING

It's important to let go of the notion that mortgage rates are "too high," or that housing is "unaffordable." The question should be, "can I find a house I can afford and want to own?" Inventory is still low, and depending on where you want to live, competition can still be fierce. For that reason, a good buyer agent is a must. We can't stress enough the importance of spending time upfront with your agent to agree on exactly what your parameters, needs, and wants are. Set objectives and limits, and then stick with them. If you're in competition, you'll probably have to overbid, so be very clear on how high you're willing to go and listen to your agent's advice. If you're a first-time buyer, you might not be buying your dream home as your first home, but that's ok. Find one you can live in, and start getting appreciation to work for you, not against you. And don't be afraid to look farther out if you have to. There are more choices and lower prices the further from Madison you go.

▶ PRICES MATTER MORE THAN RATES

We're reprinting here an updated version of an illustration we first published in our Fall 2023 newsletter. Let's assume that 30-year mortgage rates do in fact fall from 7% all the way to 5% by next April, and that prices rise 4% during that time. Let's use, as our example, a home that you can buy today for $400,000 with a 20% down payment. Should you buy it now, or wait until next April? By waiting a year and seeing rates fall by two full percentage points, your purchase price will have risen to $416,000, but due to lower rates your monthly payment will decline from $2,129 today to $1,787, saving you $342 dollars a month, or a total of $4,109 over the twelve months. But, you missed out on the $16,000 of appreciation. In other words, you sacrificed $16,000 in appreciation for $4,100 of payment savings. And this estimate is extremely conservative. A far more likely scenario is that rates fall by 1% and prices increase by 6%. Under this scenario, you would save only $95 a month, or $1,144 a year in monthly payments while foregoing $24,000 of appreciation at 6%.

	2024	2025	Difference
Rate	7%	5%	
Purchase Price	$400,000	$416,000	$16,000
Mortgage	$320,000	$332,800	
Payment	$2,129	$1,787	$342.43

Annual Payment Savings	$4,109
Lost Appreciation	$16,000
Net Loss	($11,891)

We understand that appreciation isn't realized until you sell, while monthly payments are paid out every month. But if you're taking a long term investment oriented view, buying now is clearly the better move, even if your monthly payments are a little higher. And don't forget, you can always refinance if rates come down. Waiting only makes buying more expensive. We don't think rates will fall nearly enough to change that reality.

▶ WHERE THIS IS ALL GOING

In 2022, the Fed ended once and for all (we hope) its 14-year experiment with quantitative easing. The housing market lurched suddenly from a period of abnormally low mortgage rates to one with historically normal rates. The market is now going through the process of adapting to the new reality. While it might take a couple more years to fully settle into the new equilibrium, the market will adapt, because markets always do if you let them.

What does this mean for 2024? As we write this, the picture is not yet fully clear, but there are positive signs.

For starters, the Fed has signaled that they are done raising interest rates, along with a desire to cut them if they can. What remains unclear is when, or even if, they actually can lower rates this year. The current market expectation seems to be that the Fed will make 1-3 cuts this year of a quarter point each, perhaps starting this summer. But even that prediction is starting to seem more uncertain. Our view is that, even if the Fed does cut a couple times this year, the effect on long-term mortgage rates will be minimal. For that reason, we think both buyers and sellers should simply ignore mortgage rates and get on with the business of moving to the housing they want or need.

The good news is that it appears buyers and sellers alike are starting to accept the new rate environment. As we write this in early April, activity is picking up very nicely after a sluggish March. Sellers are coming on the market in greater numbers than a year ago, which will lead to more transactions if it continues. We predicted about a 15% increase in total transactions in 2024, and we are so far on track to meet that target. Inventories are creeping upward, leading to more choices for buyers and marginally less upward pressure on prices. Prices rose by about 6% last year, and they are on pace to do so again this year.

It's a fundamental truth of real estate that people move because of changes in their lives. Those changes are ongoing for all of us, regardless of mortgage rates, housing prices, or inflationary pressures. While it may not seem like it, we are in a better place for the long-term health of our housing market than we were a couple years ago. The sooner we accept that fact and get back to the business of finding housing, the better off we'll all be.

IF YOU'RE SELLING

If you'd like to move but are waiting for rates to come down, you have a dilemma. If you've read the rest of this newsletter, you now know that rates are not likely to come down, at least not by more than 1% or so. So, you must ask yourself, how much longer can I tolerate my current living conditions, or put off the dream I have of living elsewhere? And what do you gain by waiting? Your current home will appreciate, but so will the home you want to buy. You'll be faced with essentially the same situation a few years from now. The math won't be the same for everyone, but it might help to speak to an agent to at least see how the situation really looks. If you are selling this year, it's still a seller's market, but perhaps not quite as strong as the last couple years. Pricing and condition remain critically important, so listen to your agent and be sure you're ready to compete. It could take a couple weeks to sell now, so don't be discouraged if you don't get 20 offers the first day. You'll get there eventually.

Charts represent sales reported to the South Central Wisconsin Multiple Listing Service (SCWMLS) with closing dates on or before March 31, 2024. Data for all years was pulled between the 6th-10th of the month following the end of the quarter. †Months of Inventory represents the number of months it would take to sell the entire active inventory at the pace of sales for the most recent 12 months. A six-month inventory is considered balanced. ‡When all properties sold during the period are ranked in order of price, the median is the price of the home in the exact middle. The above sales figures herein are based on data supplied to the SCWMLS Corporation by its Participants. The MLS does not guarantee and is not responsible for its accuracy. Data maintained by the MLS does not reflect all real estate activity in the market. Data presented here was generated from the SCWMLS on or before 4/11/24. This is not intended to solicit existing listings.

Stark

Real People. Real Success.

DANE COUNTY REAL ESTATE AT-A-GLANCE

Q1 2024

568

ACTIVE INVENTORY

1.2

MONTHS OF INVENTORY

New listings are up 15% in Dane County.

$415K

12 MONTH MEDIAN PRICE

1,065

YEAR-TO-DATE CLOSINGS

Prices rose by about 6% last year, and they are on pace to do so again this year.