

Housing Boom-Bust Revisited: Demand Shock Deepens

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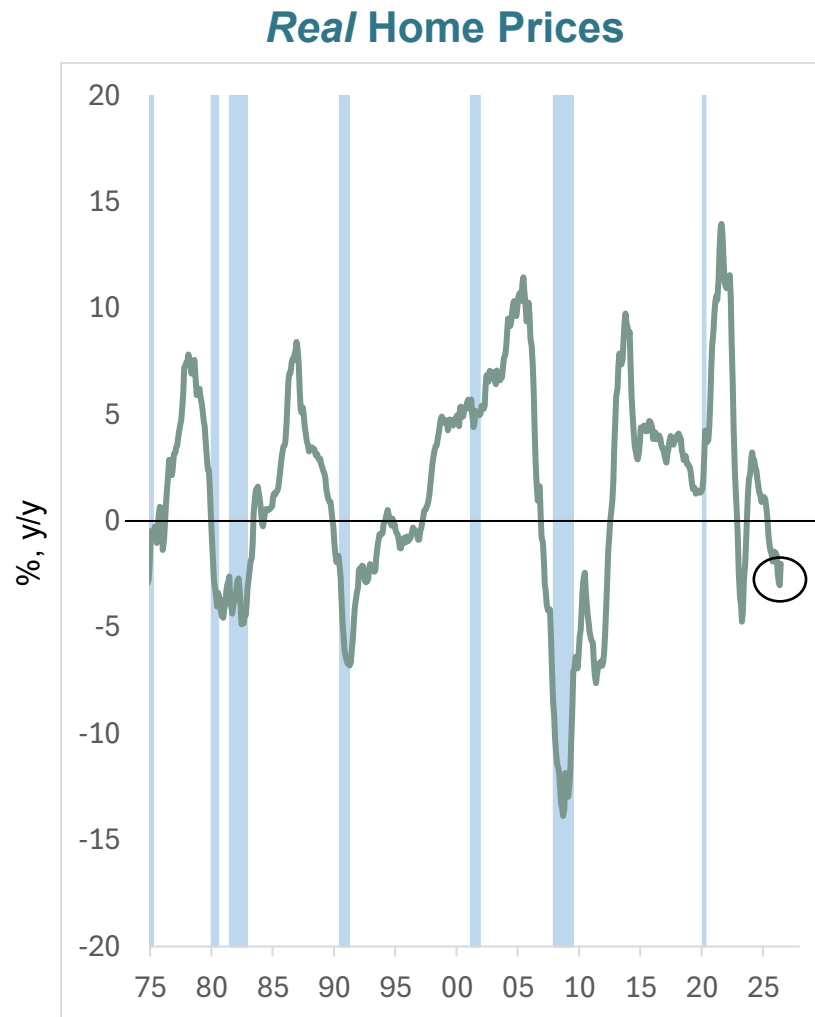
September 2026

House Views

- Home prices are likely to underperform the rate of inflation due to a dearth of credit and new people entering the asset class. We forecast a -5% decline in home prices nationally by yearend 2027, albeit with tremendous regional disparity. The global back up in sovereign bond yields reinforces our base case of lower demand and home prices.
- It is critical to distinguish between the *national* market and the thousands of *regional ones* that are dependent upon a community's demographics, net regional migration, labor market, infrastructure, geography, laws/codes/regulations, and tastes and preferences.
- Significant post-Covid home price growth led to record construction. Mortgage rates increased to ~8% in 2023 and have remained above 6% since. Home prices never adjusted.
- Builders are now pulling back on their investment. The lack of system leverage and existing home supply suggests that a “bust” is unlikely, but that a slow deflation is.
- The combination of high rates and prices has led to low affordability and demand. There is a scheduling effect too, where easy pandemic government policy moved future demand forward. The housing market is now experiencing demand *deficiency*.
- Newly built homes are being met with tepid demand, and for the first time on record are priced *below* existing homes (Census, NAR). Prices are under pressure. Real residential investment is down -3.9% YoY and our outlook remains negative, absent a material change in rates or prices.

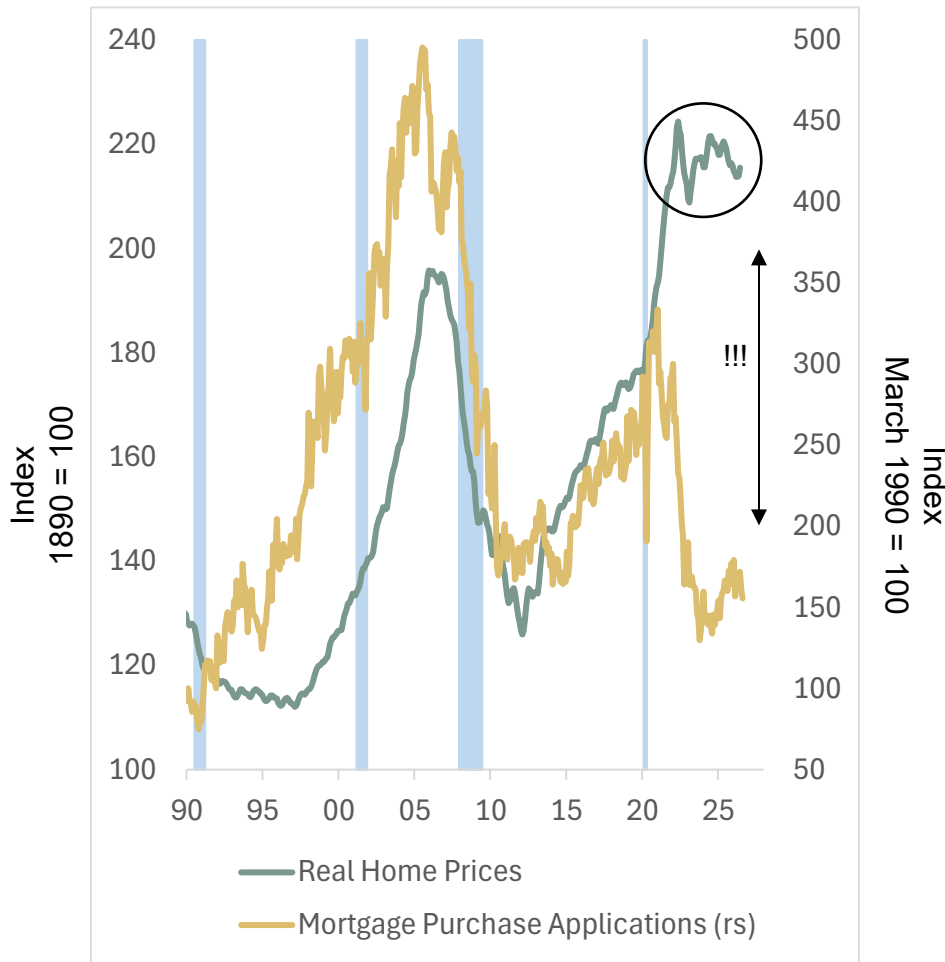
Home Prices are Weakening

- Weak demand from elevated mortgage rates and increased new home supply has led to price growth of just 1.5% year-over-year in June. Growth of this magnitude has typically only occurred in or around economic downturns.
- In the first six months of the year, Case Shiller national home prices have increased by just 0.2%.
- Home price weakness has been pronounced on an inflation-adjusted basis, having declined -2% y/y. This recession-like price behavior is likely to continue in the near term.



High Home Prices Inconsistent with Paltry Demand

Real Home Prices vs. Mortgage Applications for Home Purchase

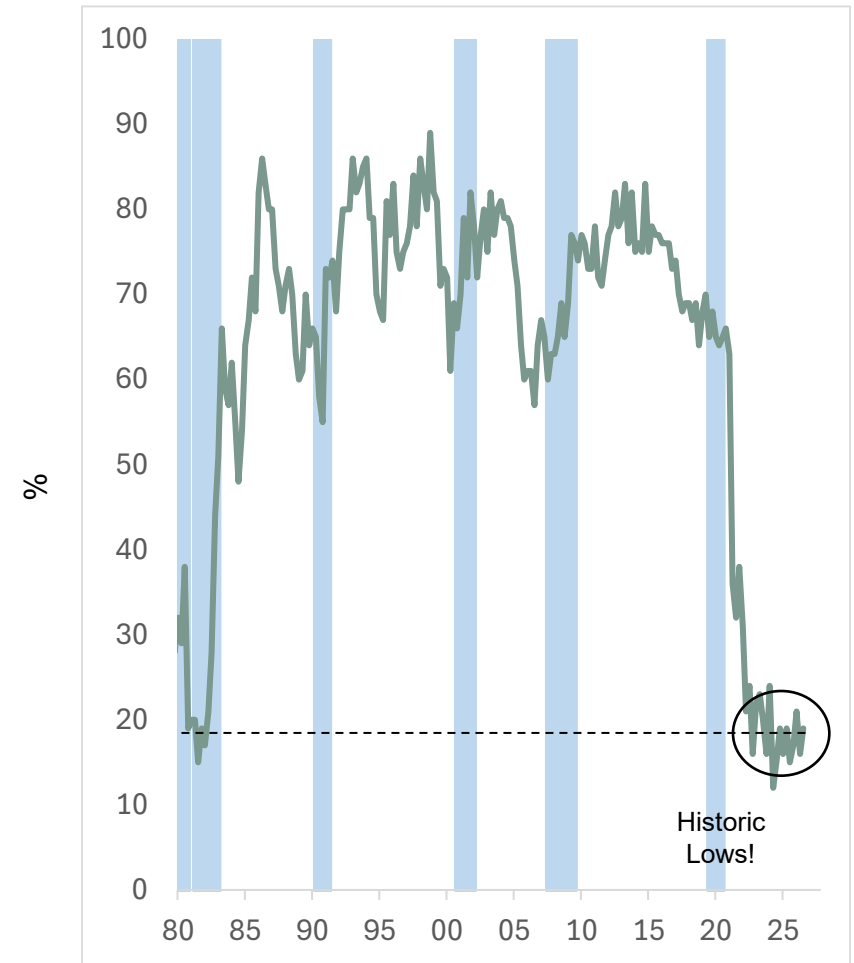


- There is little demand for homes from rate sensitive buyers.
- This is critical because real homes prices tend to move with mortgage lending.
- But, in 2022, real home prices continued to climb while marginal inflows of capital from the bank lending channel (mortgages) fell to multidecade lows (1995).

No More Home Buying Euphoria

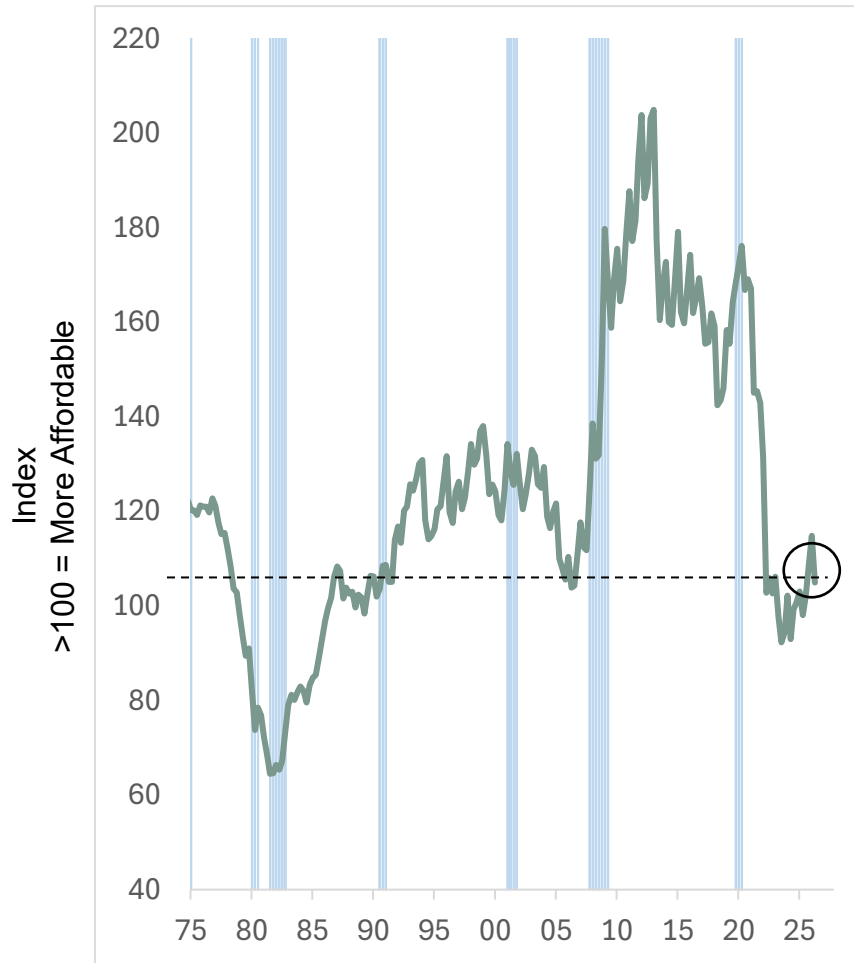
- Sentiment toward housing has deteriorated significantly post pandemic, as the percentage of those saying 'now is a good time to buy a home' is at historic lows.

Good Time to Buy a House?



Ultra Low Housing Affordability

Housing Affordability Index

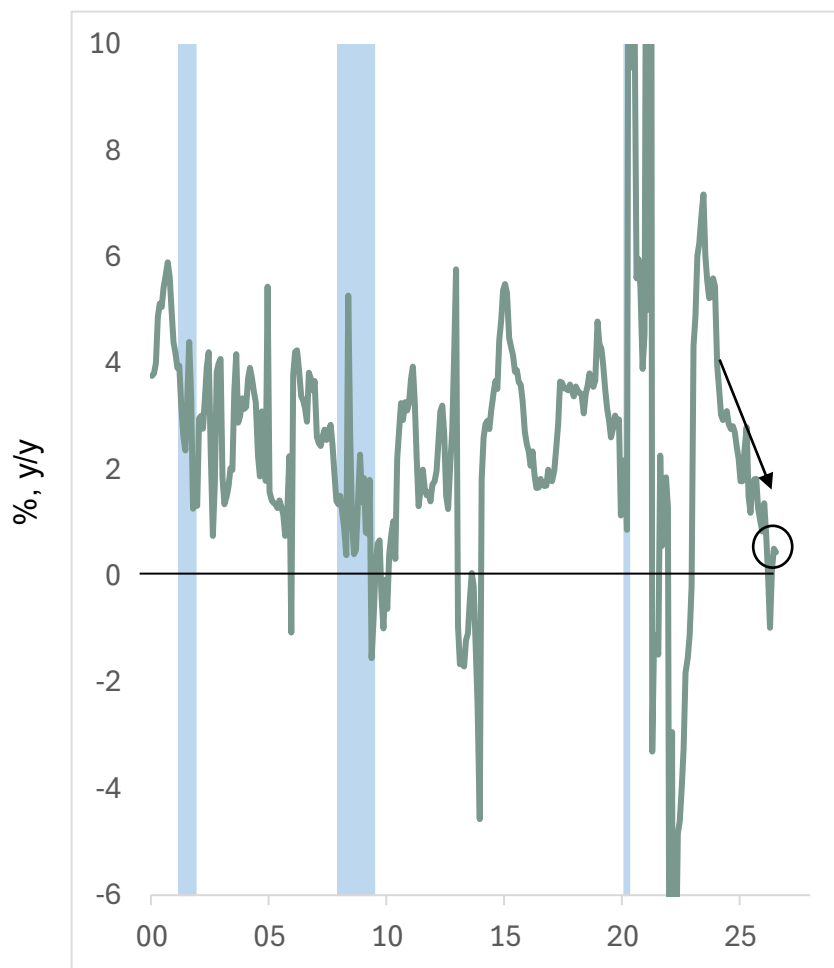


- Home affordability — which measures median household income relative to the payment required to buy a median priced home at current mortgage rates with a 20% down payment — is showing the lowest readings since 1990 and 2006!

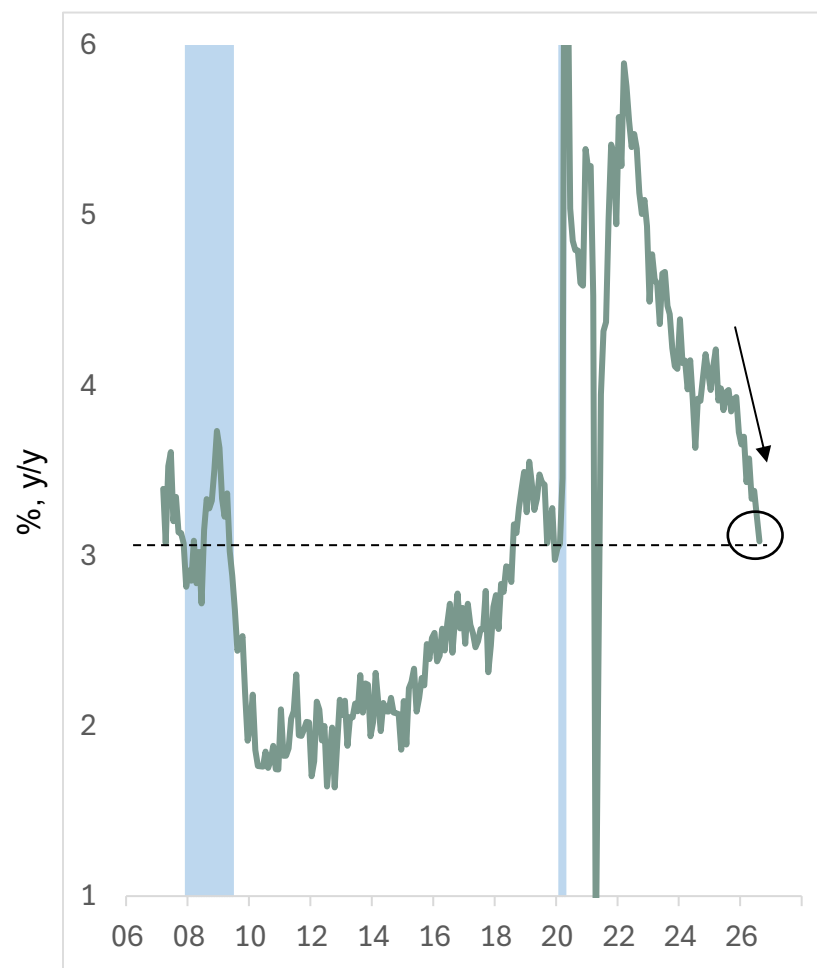
Labor Market Not Helping Affordability

The labor market is failing to help the housing market's affordability issue, as incomes on both an inflation-adjusted and nominal basis are deteriorating.

Real Disposable Personal Income



Average Hourly Earnings (Nominal)

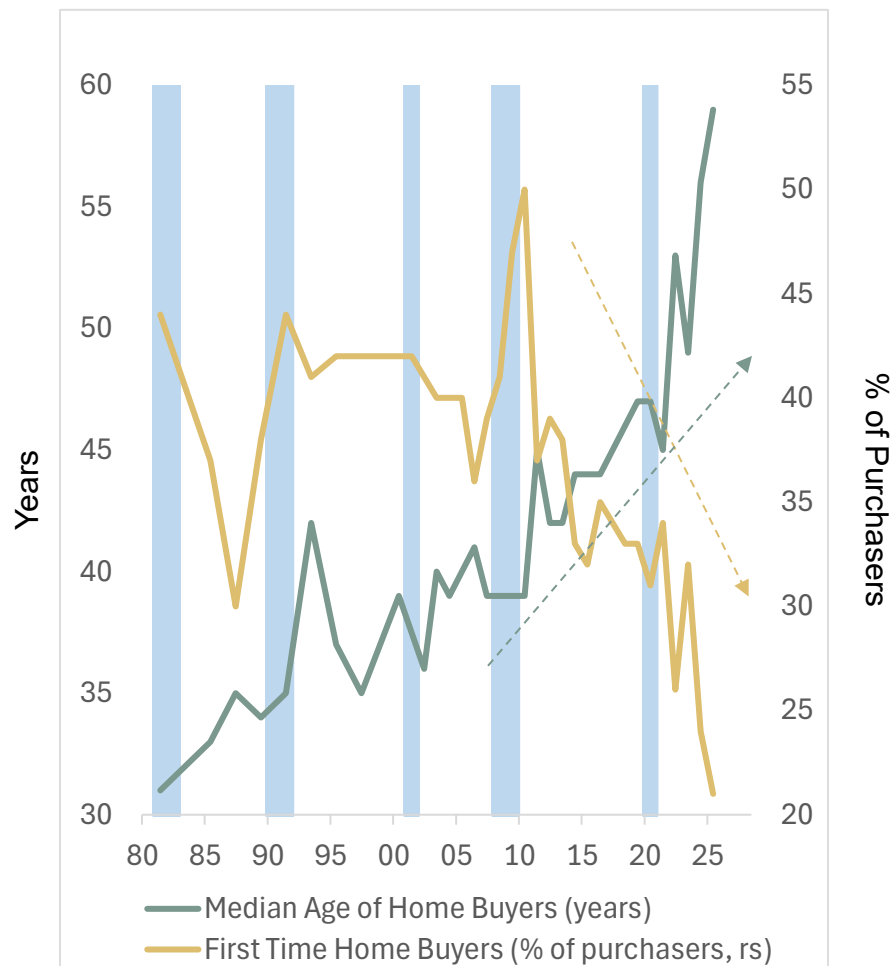


Sources: Census, Haver, SMBC Nikko

Merely Being Traded Back and Forth

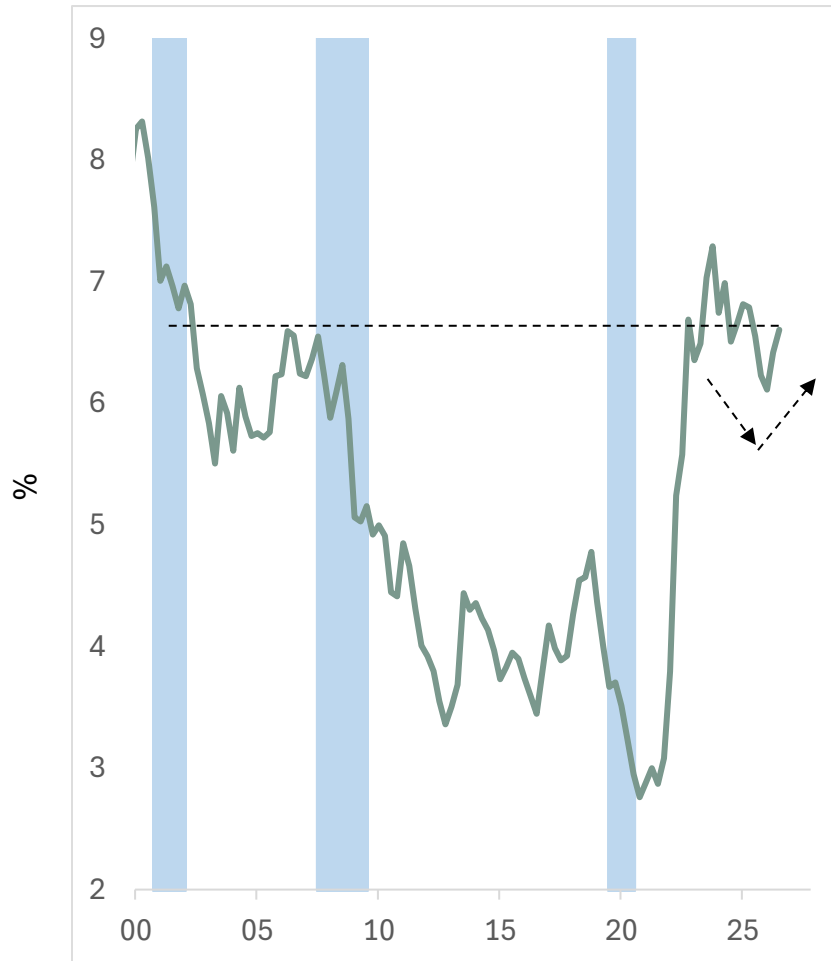
- Because mortgage-inflows have withered, new first-time buyers (more broadly) have fallen to a record low 21% of sales.
- With few new entrants into the asset, the deck of cards is simply being shuffled — not conducive to price appreciation!

First Time Buyers Disappearing



High Mortgage Rates

30-Year Fixed Rate Mortgage



- Mortgage rates have reversed their early year declines and are back above their pre-GFC levels (~6.6%). Absent additional intervention from the GSEs, the global rise in long end yields will pressure mortgage rates higher.

Poor ROI on *Mortgage-Financed* Home Ownership

A mortgage-financed home purchase is a leveraged bet on home prices. Previously, a home's price needed to increase by 60% to cover interest expense. Now it needs to appreciate 103%! This pushes "breakeven" back by nearly five years, assuming prices increase at their historic 5.1% pace.

Home Purchase Before & After Fed Hiking Cycle			
Item	March 2022	July 2026	Change (%)
Median Home Price	\$ 394,865.15	\$ 421,864.31	6.8
20% Down Payment	\$ 78,973.03	\$ 84,372.86	
Mortgage Amount	\$ 315,892.12	\$ 337,491.44	
30-year Fixed Rate	4.17	6.54	2.37
Monthly Payment	\$ 1,539.24	\$ 2,142.06	39
Total Interest Expense	\$ 238,234.49	\$ 433,650.62	82
Total House Cost w/ Mortgage	\$ 633,099.64	\$ 855,514.93	35
Disposable Personal Income per Capita	\$ 55,126.00	\$ 69,198.00	26
Mortgage vs. Cash Purchase Price	1.60x → 2.03x		
Years to Breakeven (assuming avg. 5.1% Price Growth)*	9.4 → 14.2		51
* 5.1% = Annualized national home price growth since 1975 (S&P)			

High Mortgage Rates Are Incompatible with Current Prices

- Mortgage rates tend to lead home prices by 7-months and imply a -5% decline in home prices.

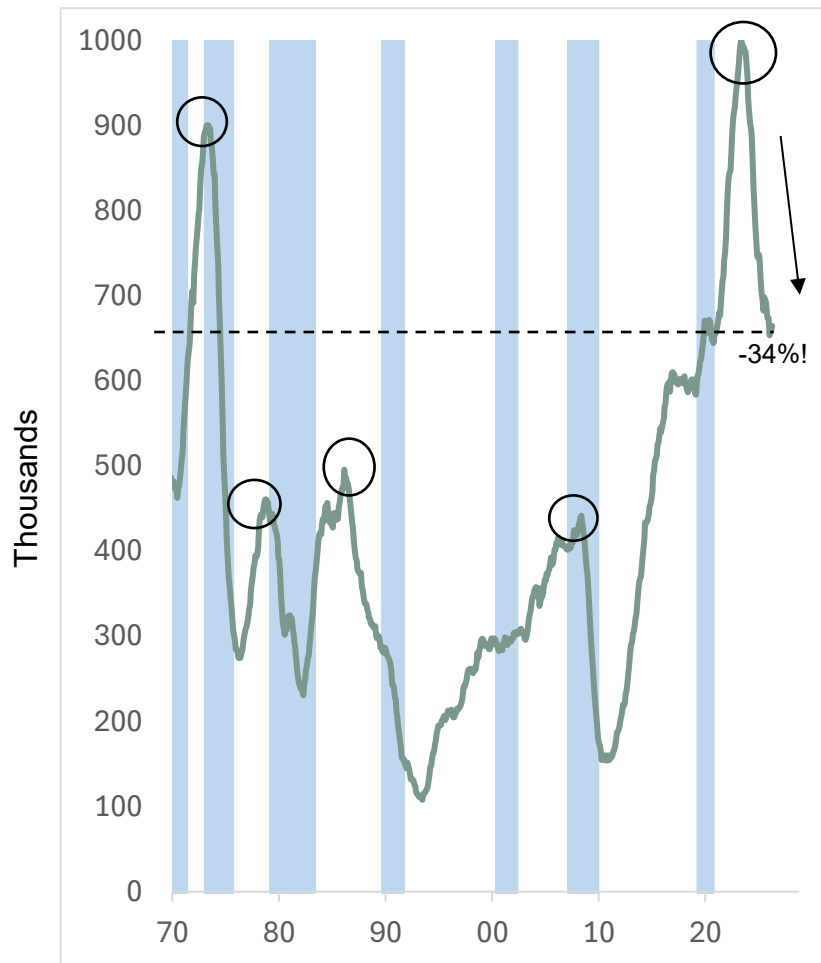
Mortgage Rates and Home Prices



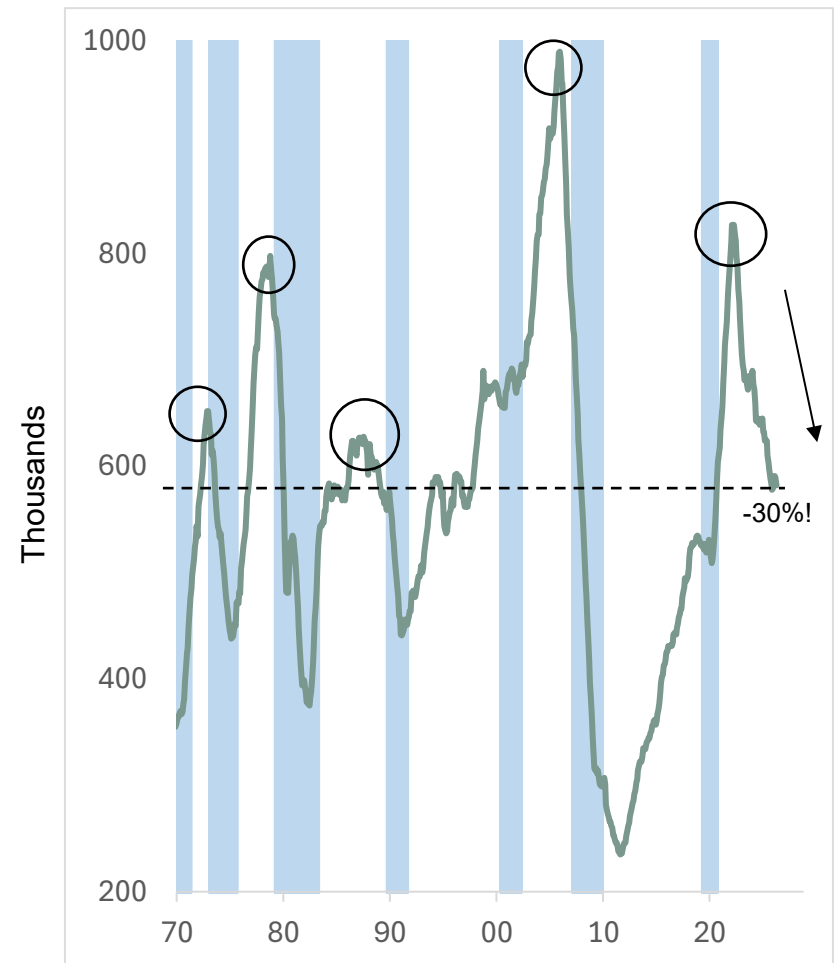
Home Building Boom-Bust?

Overbuilding is broad-based, but particularly acute for multifamily housing (5+ units). Even after a sharp pullback, it is still at the highest since the early 1970s. Single family is back to historic averages (571k).

Multi-Family Home Construction



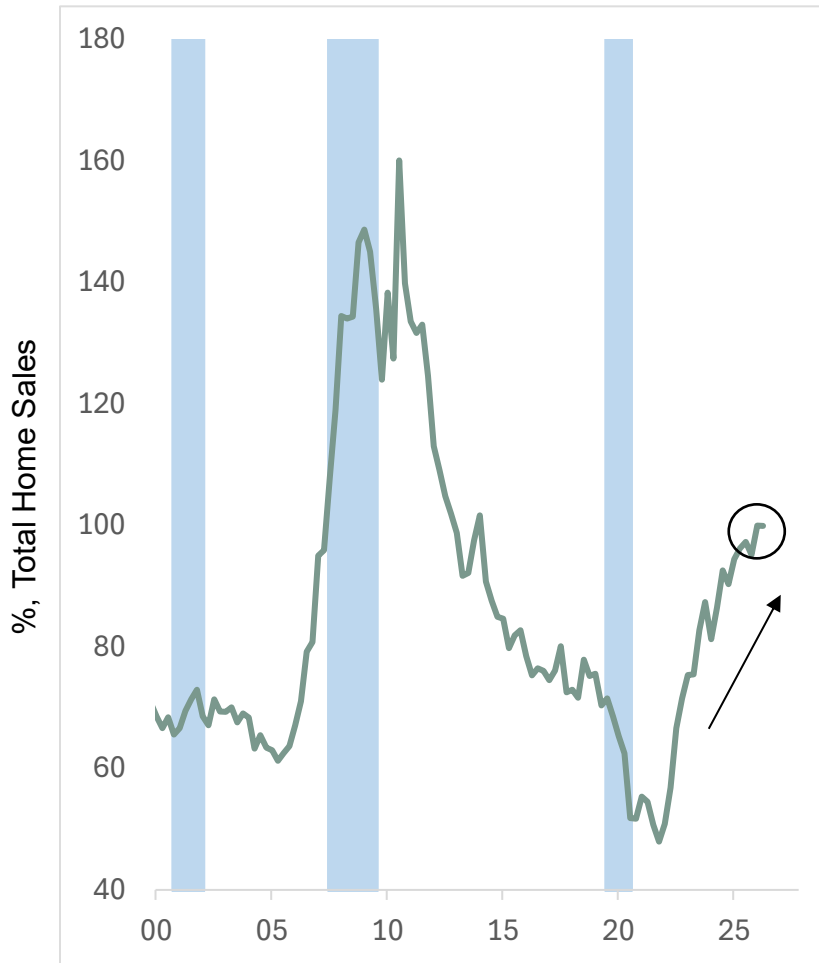
Single-Family Home Construction



Sources: Census, Haver, SMBC Nikko

Vacancies Rising

Vacant Housing Units Available for Sale or Rent



- Robust residential building (particularly for apartment buildings) over the last six years is not being met with commensurate demand. As a result, vacancies are rising.

Regional Breakdown

- Home prices in New England, the New York Metropolitan area, and the Great Lakes continue to outperform. Meanwhile, the Western and South Atlantic markets are underperforming. Housing supply growth and in-office work are key dynamics.

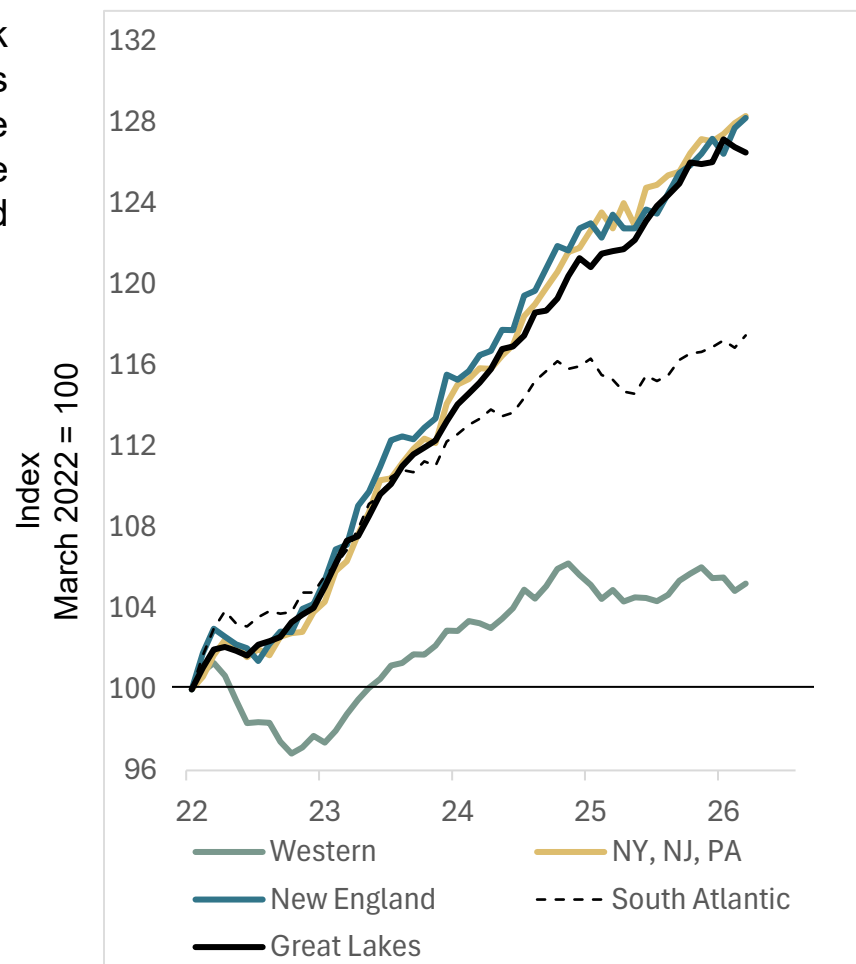
*Western = California, Oregon, Washington, Alaska, Hawaii, Arizona, Colorado, Utah, Nevada, Wyoming, Montana, Idaho, New Mexico

**New England = Connecticut, Massachusetts, Rhode Island, New Hampshire, Vermont, Maine

***Great Lakes = Illinois, Ohio, Michigan, Wisconsin, Indiana

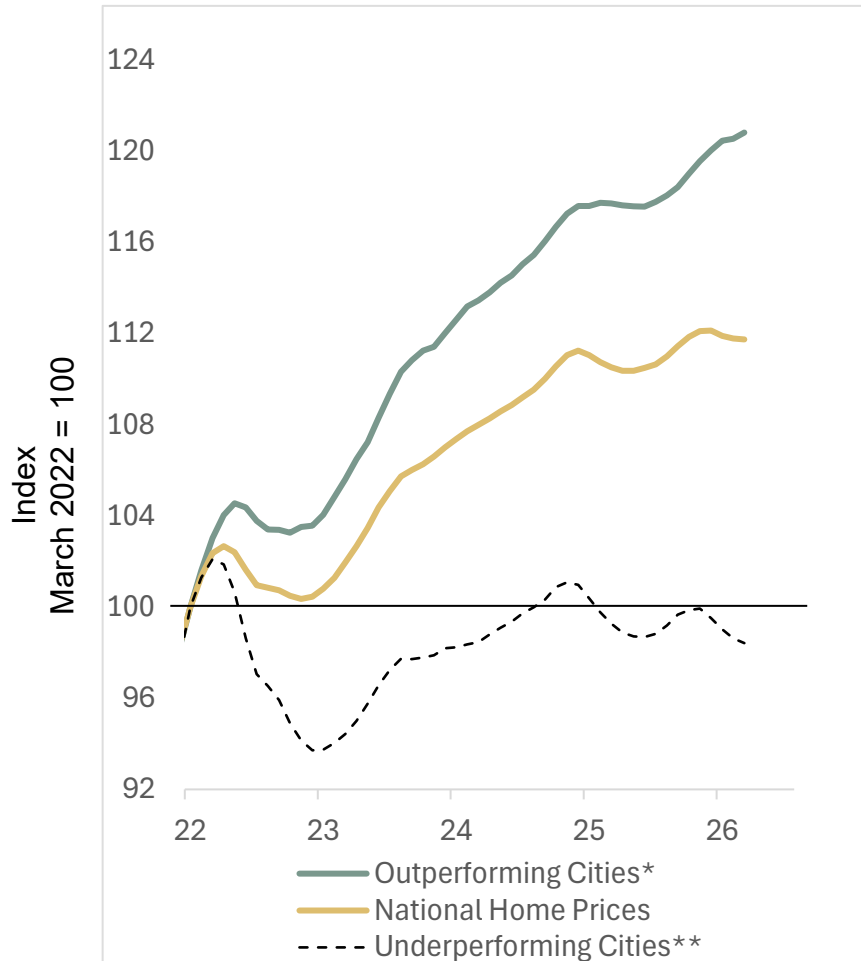
****South Atlantic = Florida, Georgia, North Carolina, South Carolina, Washington D.C., Maryland, Virginia, Delaware, West Virginia

Home Prices by Region (FHFA)



Which Cities are Demonstrating Alpha?

Home Prices by City (Case Shiller)



- In line with the FHFA data, Western cities are underperforming notably according to Case Shiller data. Office vacancies and regional migration trends are key drivers.
- Most underperforming cities have technology sector driven regional economies and are experiencing office vacancy rates above the national average (20%). Phoenix is the exception where office vacancy rates are in line with the national average.
- Atlanta, Boston, Charlotte, Miami, New York, and the Great Lakes region (Chicago, Cleveland, Detroit) are outperforming!

*Outperforming = Atlanta, Boston, Charlotte, Chicago, Cleveland, Detroit, Miami, New York City

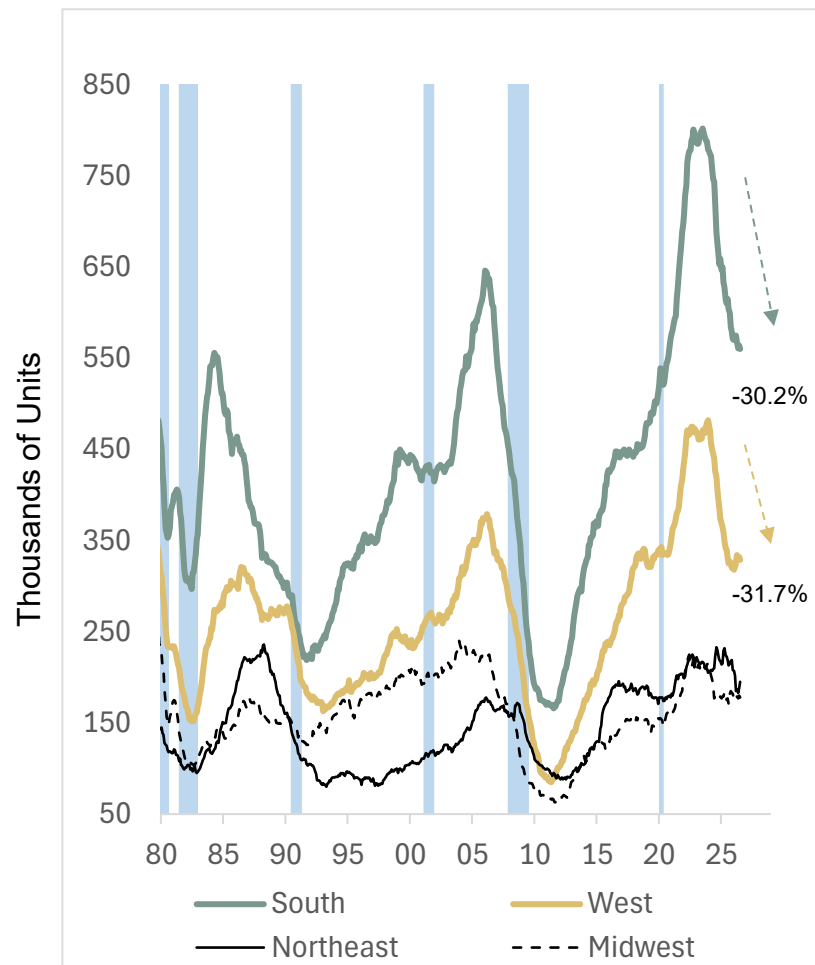
**Underperforming = Dallas, Denver, Phoenix, Portland, Seattle, San Francisco

*** Neutral = Las Vegas, Los Angeles, Minneapolis, San Diego, Tampa, Washington DC

Regional Overbuilding

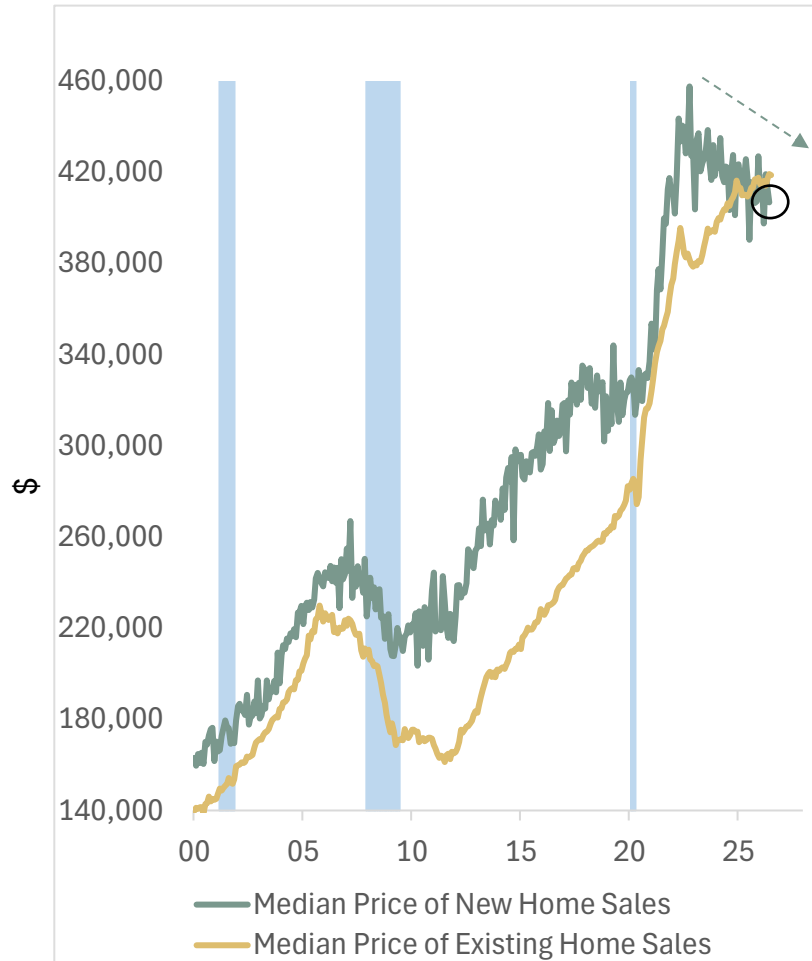
- While some areas are more overbuilt than others, building is broadly in decline. The pace of drawdown reflects homebuilders' deteriorating expectations. This is most pronounced in the West and South.
- The Northeast and Midwest are seeing more modest pull backs, for now. This reflects the relatively tight regional supply-demand dynamics.

Regional Home Construction



Homebuilders Capitulating

Median Price of New vs Existing Homes

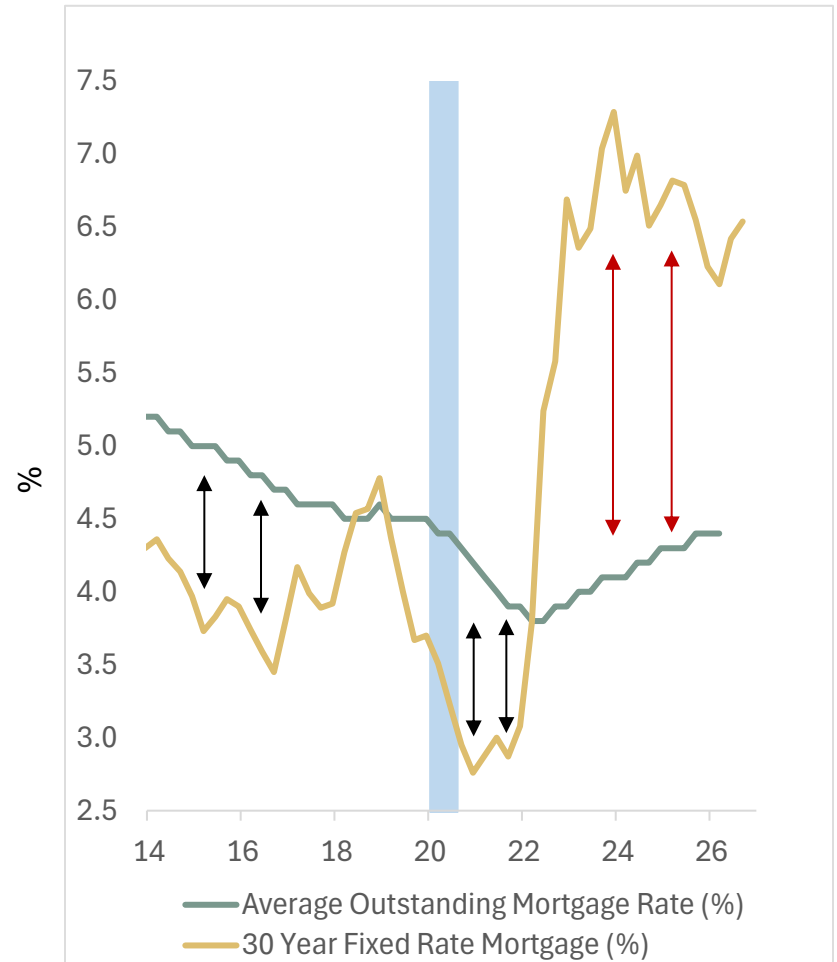


- For the first time on record, the price of newly built homes (\$407K) has fallen below that of existing homes (\$419k)!
- Supply of the former is positive, while supply of the latter is constrained. The marginal seller of homes is lowering prices!

The Rate Lock-in Effect?

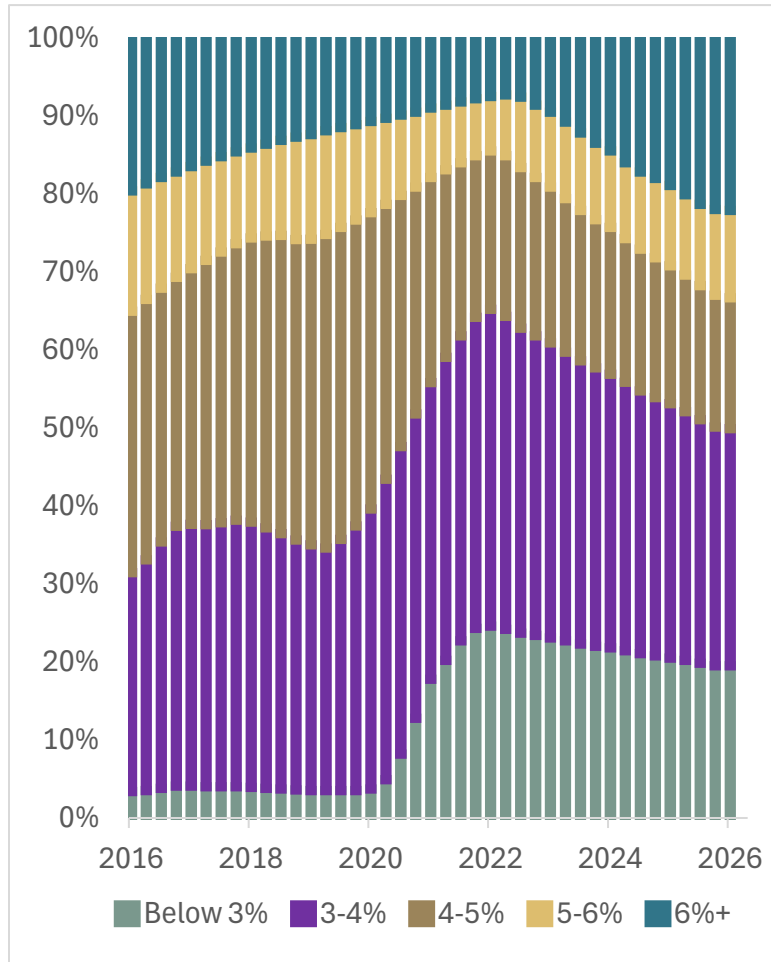
- The average outstanding mortgage rate is 4.3%, while the rate on a new mortgage is 6.8%. This imbalance discourages home sales. Keep in mind that this rate differential applies to roughly 60% of the 87 million US owner-occupied homes, as a record ~40% of homeowners are mortgage free.

Mortgage Market Disconnect



High Rates Slowly Altering the Composition of Mortgage Holders

Composition of Outstanding Mortgages by Interest Rate (%)

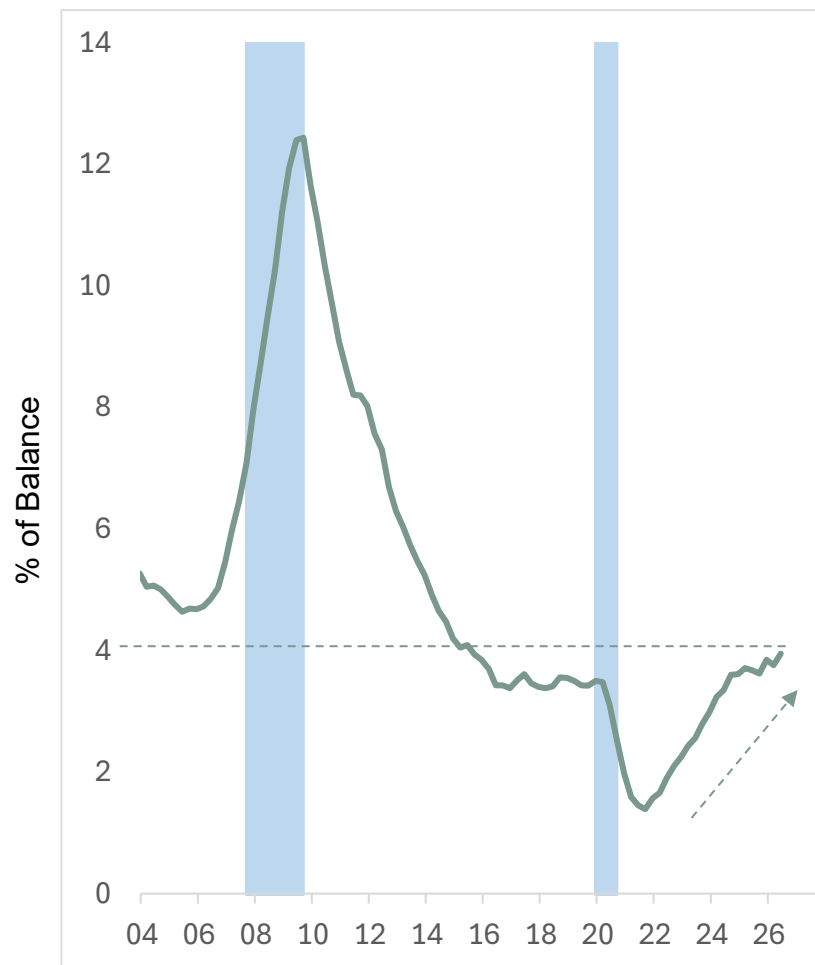


- The “lock in effect” is diminishing, as 33.3% of mortgages outstanding now have a rate above 5%. 22% have a rate above 6%.
- The percentage of mortgages with a 5% rate or less peaked at 65.2% in Q1 2022. This is down to 49.9%.

Consumer Credit Universe is Weakening

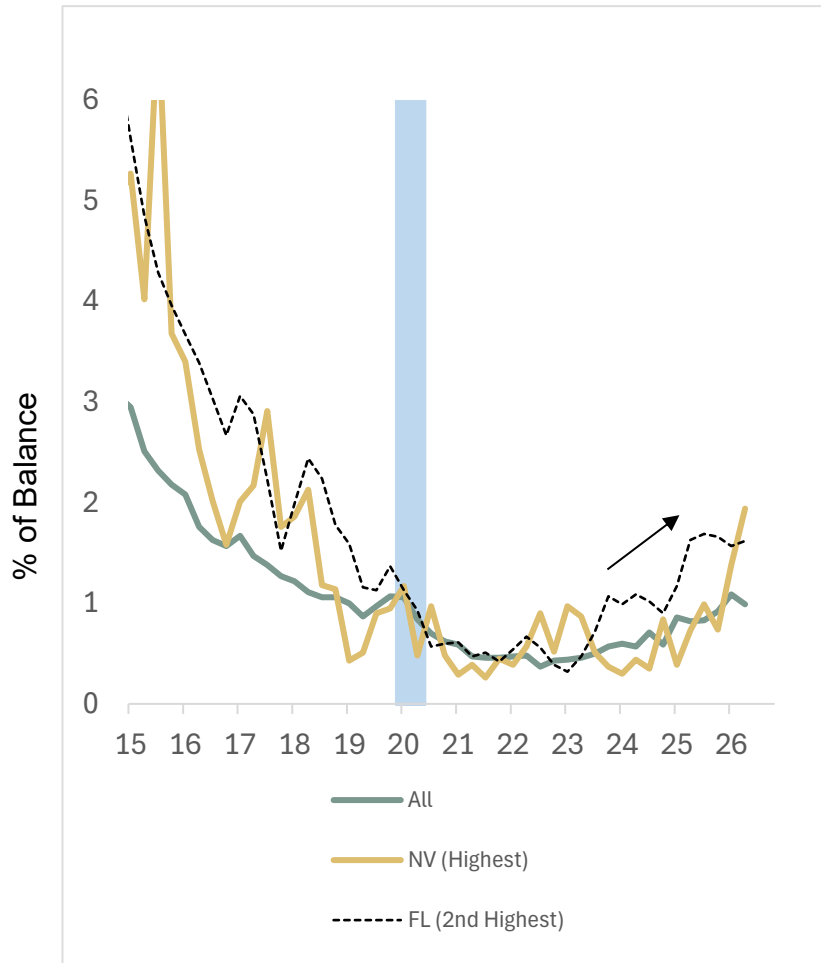
- Mortgages have followed delinquencies in the rest of the consumer credit universe higher, rising to 4.0% — the highest since 2015.
- Auto loans have risen to 7.9%, their highest since 2010.
- Credit cards have risen to 8.7%, their highest since 2011.
- The percentage of total loans 30 days+ delinquent sits at 5.0%.

Mortgages Transitioning into Delinquency (30 Days+)



Ultra Low Delinquencies are Slowly Increasing

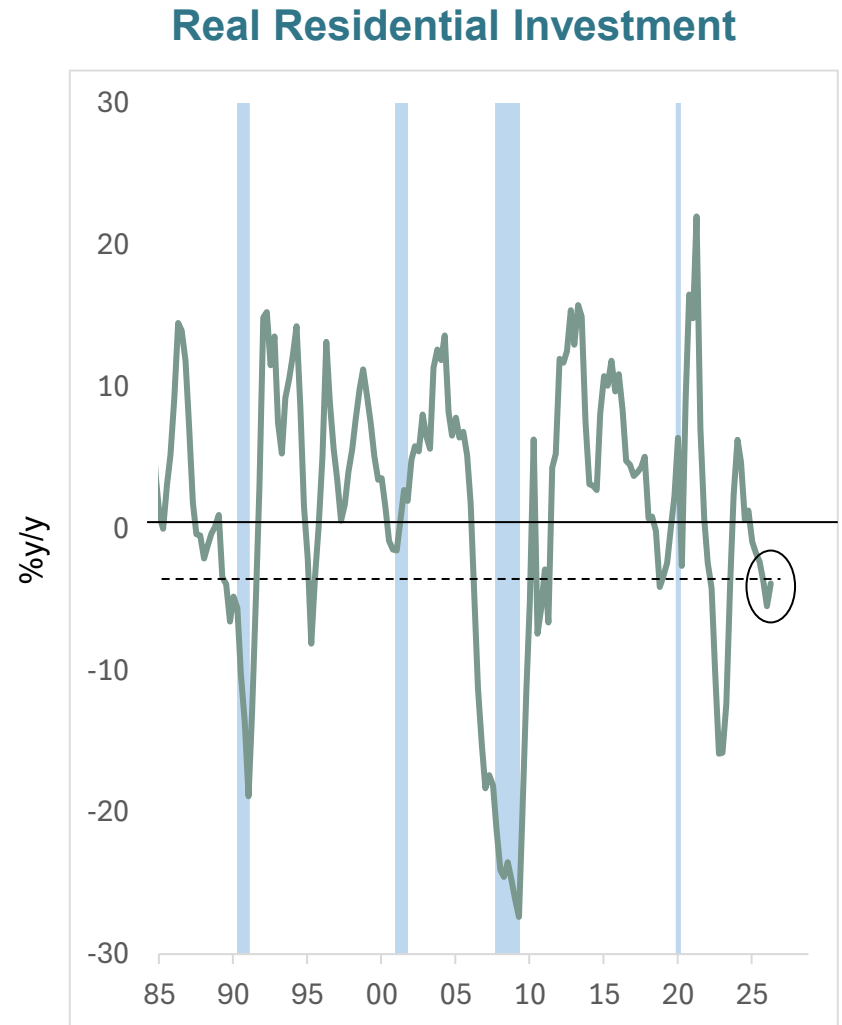
Mortgage Balance 90+ Days Late



- Mortgage delinquencies, those 90+ days late, have exhibited a slow increase to 1.0%, since bottoming at 0.4% in Q3 2022. Nevada and Florida have the highest rates at 1.9% and 1.6% respectively.

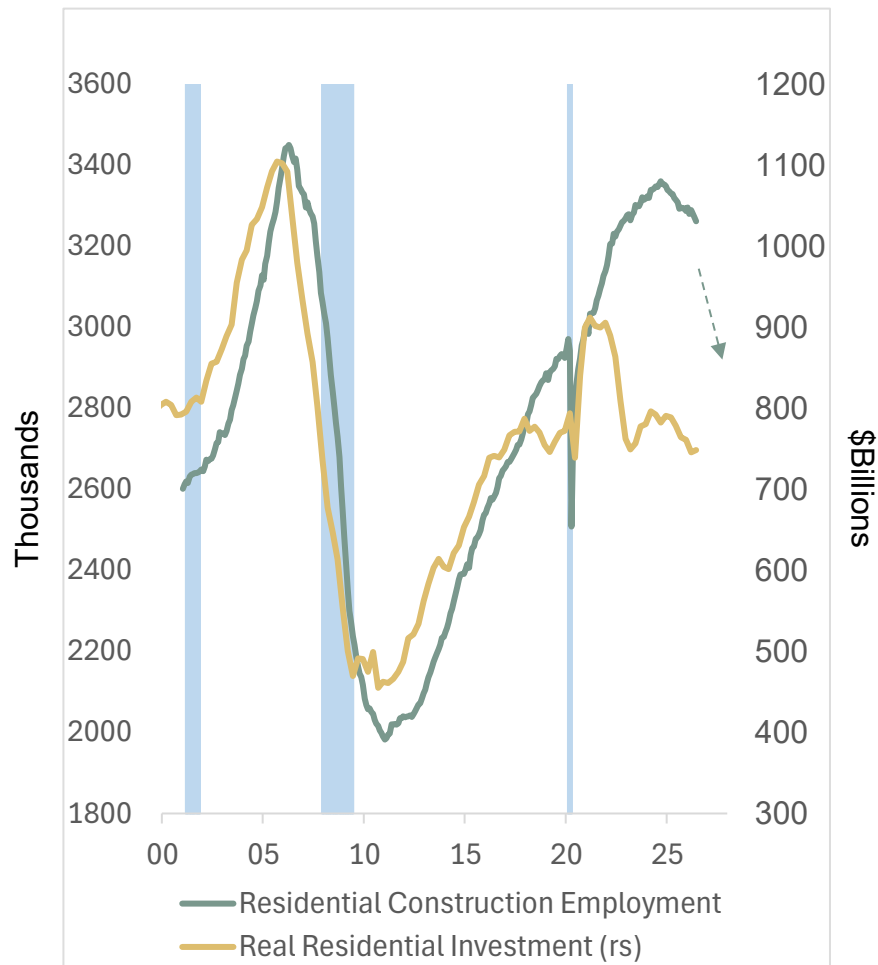
Beginning to Turn Lower (Again)

- Economy wide residential investment has declined -3.9% YoY.



Not Enough Investment to Justify Headcount

Real Residential Investment vs. Residential Construction Workers

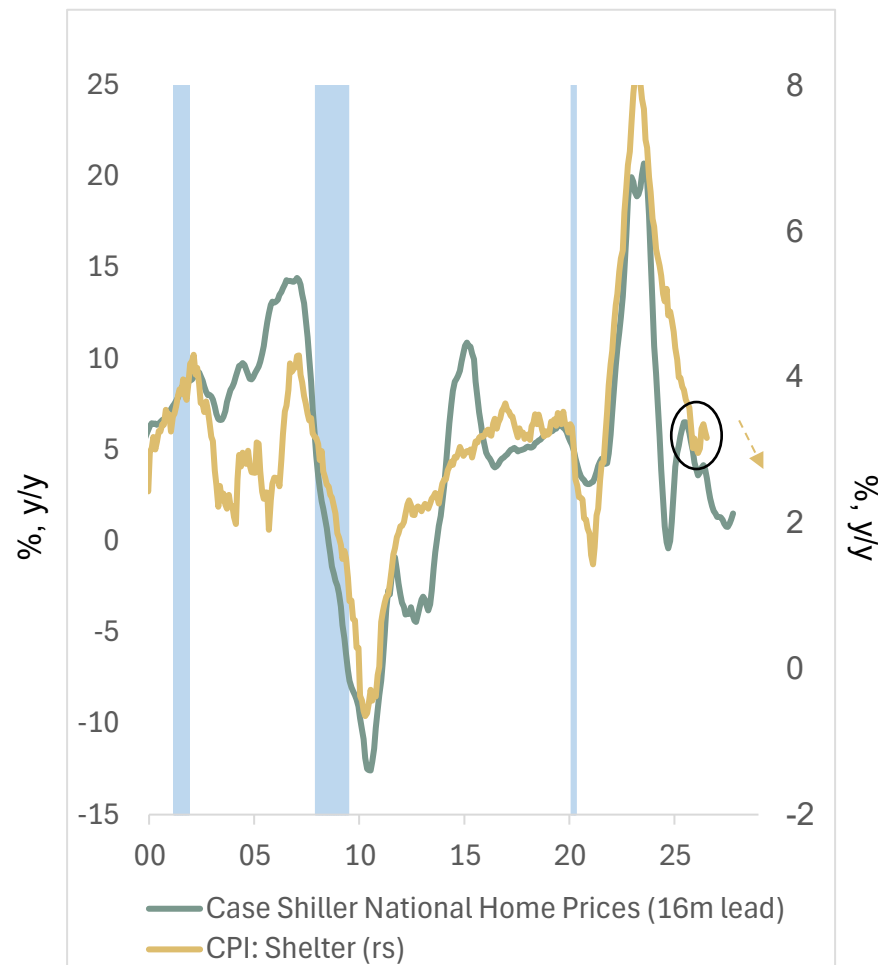


- Residential investment continues to weaken after reaching its cyclical peak in 2021, and residential construction employment has begun to follow after topping at the end of 2024.

Lower Inflation Ahead

- Home prices lead CPI shelter by 16-months. The trajectory of home prices statistically implies that shelter inflation should slow to 2.8% YoY by yearend (from July's 3.2% rate) and to 2.5% by October 2027.
- Because shelter is over 35% of the CPI, this would subtract another -25 bps from overall inflation!

Home Prices Lead CPI Shelter Costs



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