HOME PRICES FALL AND MORTGAGE RATES RISE, OUR OUTLOOK ON HOUSING MARKET

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(01Dec2022) … As home price decline over the next year and mortgage rates stabilize or even possibly rise, the risk exposure to prevailing well-concentrated mortgage portfolios can be properly positioned to minimize credit risk exposure - even should recessionary pressures return in 2023.

Lower Prices - Higher Rates - Higher Monthly Payments

Data shows that November's median home list price was $416,000, down 18% (annualized) from June's record peak of $449,000. However, high mortgage rates—which, as of Wednesday, hover at 6.58% for a 30-year fixed-rate loan—are a stark reminder that many potential buyers might still struggle on the affordability front.Prices remain double digits higher from a year ago and with mortgage rates also higher, buying a home is more expensive than last year. As of Thursday, average 30-year fixed mortgage rates hovered at 6.58% - pushing the industry's affordability index significantly more adverse for buyers. Combined, elevated prices and higher rates are now sending monthly payments about 75% higher, or $900 higher, than they were just one year earlier.

Falling Demand - Higher Prices - Growing Inventory

Subsequent to the COVID pandemic-fueled home buying, the number of homes on the market fell to all-time levels. More recently, the inventory of homes has since rebounded with more than 47% more homes for sale in November - or 240,000 more homes from a year ago.

But the interesting trend is that new listings are down -17% from last year. This means that potential sellers have decided to stay put rather than list their homes - all because of higher mortgage rates and cash-strapped buyers who aren't making offers like they did a couple of months ago.

The median monthly supply of new homes - based on current sales - is 8.9 months. For existing homes, the supply is 3.3 months. This compares with supply level of 5.7mos and 1.5mos, respectively, at the beginning of 2022. It is even more greater than the most recent low in September 2020 of 3.3mos and 1.6mos, respectively.

Falling Prices to Continue - More Stability in Mortgage Rates

Home prices declined for a third straight month in September amid a cooling housing market. This was the longest streak of monthly declines in more than a decade as mortgage rates have risen from 3.50% to as high as 7.00% in 2022. The S&P CoreLogic Case-Shiller National Home Price Index fell another 1% in September from August and now has lost 2.6% over the past three months.

The slowdown in the housing market continues but is it not as broad-based as some believe. In fact, six out of 9 regions of the country experienced higher prices in September from August and all continue to see year-over-year increases. But higher prices and surging mortgage rates have led to a big pullback in home construction and sales which in turn affect inventory.

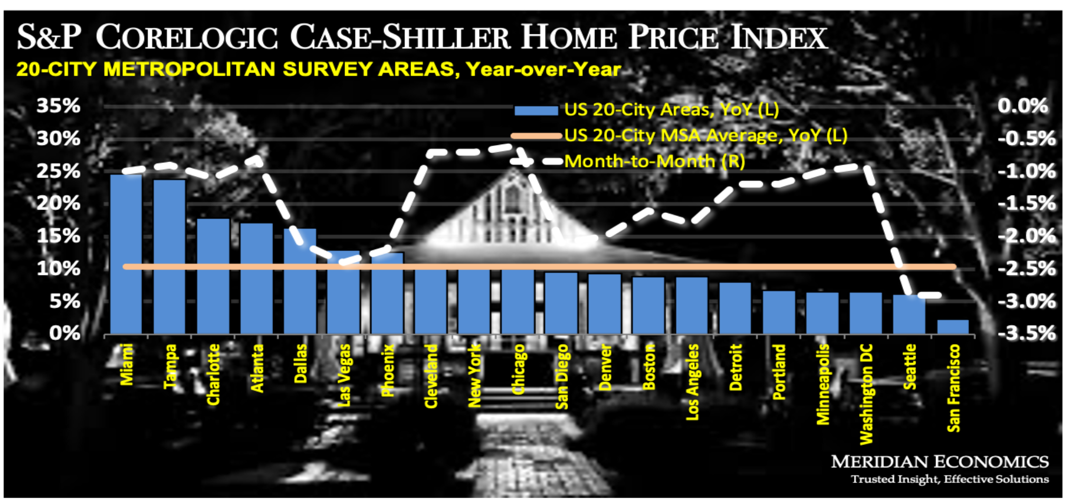
We anticipate that over the next 18 months, housing values will decline between 10-15%. This is still less of a correction than the 27% price decline between 2006 and 2012 - the last housing correction characterized by high unemployment, low affordability, questionable lending practices and rising mortgage rates.

Watch Your Ps & Qs - And your LTVs

As mortgage rates decline, affordability should increase and, if inflation slows and financial conditions improve, demand will begin to increase - hopefully with adequate inventory to support. But during the interim, there might be an impact to industry loan-to-value metrics - not only for mortgages but all secured consumer loans as well - especially considering the growth in mortgage originations this past summer when home values increased 4-times the mass of consumer inflation and mortgage rate almost doubled.

The best credit mitigation plan is to set marginal caps for the amount of originations made between now and next spring, Mortgages issues during the past summer will most likely not experience a significant level of refinancing in the future decline in mortgage rates will not bring enough incentive. And if they do bring refinancing requests, the refi rate will still most likely be higher than current portfolio yields.

With the prospect of rising LTVs - due to decline values - most institutions have more than adequate loss reserves in place to accommodate expected defaults - even if a recession does present itself in 2023.



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