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Quarterly Market Insights

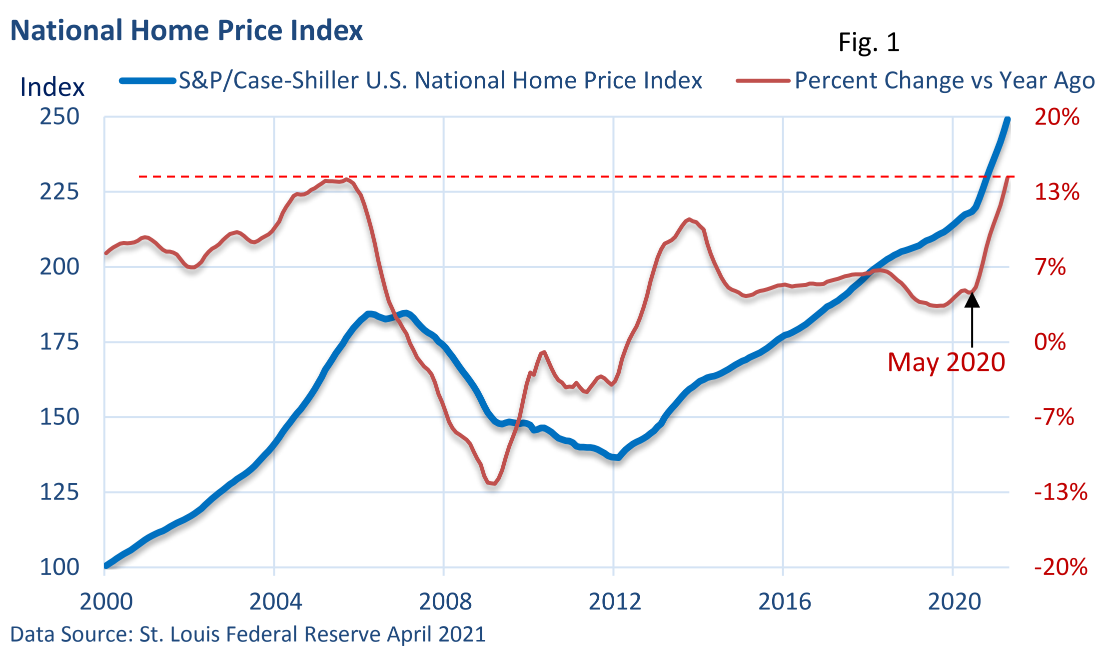
House Price Explosion

The pandemic has created long-lasting distortions in the economy. Fiscal stimulus checks and generous jobless benefits have left many folks with extra cash. We have seen that play out in strong sales for home improvement and autos.

While distancing restrictions that had been in place have devastated the travel industry, that may change amid pent-up demand and falling Covid cases. A shortage of rental cars has sent prices into the stratosphere in some locales.

One industry that has been met with unexpected demand is housing. Surging sales and the lack of supply have created bidding wars around the nation.

According to the National Home Price Index, prices are at a record level (blue/dark line showing an increase of approximately 250% since 2000)—Figure 1. In addition, the acceleration in prices, which began in the middle of 2020, is up at the fastest pace on record (red/light line; up 13% from a year ago through April 30). The survey began in 1987.



In a separate survey, the National Association of Realtors said that the median price of an existing home hit a record $350,300 this May, up 23.6% from May 2020. The median price of a new home in May is up 18% versus one year ago to a record $374,400, according to the U.S. Census.

Yet, as any realtor will tell you, the three most important things in real estate are location, location, location. What is happening in one neighborhood may not be mirrored in another, but nationally prices have soared amid a shortage of inventory.

Making sense out of the madness

Rising prices can't be pinned on one thing. There is plenty going on including:

1. **Mortgage rates fell to record lows**. The 30-year fixed mortgage fell below 3% last July, according to Freddie Mac's weekly survey. It held below 3% until March and has hovered near that mark since.

2. **The pandemic discouraged potential buyers from listing homes last year.** As a result, inventories fell sharply, limiting choices for buyers at a time that low mortgage rates were encouraging fence sitters to start looking.

3. **New home builders were caught flat-footed** by surging demand and have struggled to catch up. Moreover, soaring lumber prices have caused added delays. Notably, the price of lumber fell sharply in June but remains about double the pre-pandemic price.

4. The Wall Street Journal reported in April that **the pandemic set in motion a furious scramble to buy vacation homes**. In January 2020, 9% of mortgage applications came from investors and those wanting a second home. That rose to 14% last February.

5. On a related note, **investors chasing yield have snapped up houses**, renting them and nibbling away at supply. These investors aren't simply mom and pop landlords. The Wall Street Journal said pension funds are also buying homes they plan to rent.

6. **Mortgage forbearance** has helped keep people in their home, preventing a flood of foreclosures.

7. **Potential sellers who want to move fear** a quick house sale could leave them without a home to buy; therefore, they choose to stay put, further limiting the supply of houses.

Surging prices bring up the next question: are we in a bubble as we were in the 2000s?

We are seeing sales come off the early 2021 peak simply because high prices are discouraging some buyers. Limited inventories, however, seem likely to support prices in the short term, even if today's outsized gains are unsustainable.

Still, unlike the bubble during the 2000s, we are not seeing a building boom with large numbers of speculators driving up prices. Just the opposite, there are not enough homes to satisfy demand.

Moody's Analytics noted last month, "Stress lines are developing as… house prices have substantially outstripped household incomes, effective rents, and construction costs."

Moody's stated, however, that "A bubble develops when there is speculation, or when buyers are purchasing homes with the intent of selling quickly for a profit. This isn't what is happening in today's housing market," as house flipping remains low.

Nonetheless, the bubble question is tough to answer simply because forecasting the future involves inputting unknown future variables into an imperfect forecasting model.

Stock, Bond, and Commodity Markets

Index	2nd Qtr. 2021 Return %*	YTD Return %**
S&P 500 (large)	+8.55%	+15.25%
S&P 400 (midsize)	+3.64%	+17.59%
Russell 2000 (small)	+4.29%	+17.54%
MSCI EAFE (intl.)	+5.17%	+8.83%
Bond Yields	**Jun 30 Yield & Qtr. Change**	**Dec 31, 2020 Yield**
3-month T-bill	0.05% (+0.02%)	0.09%
2-year Treasury	0.25% (+0.09%)	0.13%
10-year Treasury	1.45% (-0.29%)	0.93%
30-year Treasury	2.06% (-0.35%)	1.65%
Commodities	**June 30 Price & Qtr. Change**	**Year end 2020**
Oil per barrel	$73.47 (+$14.31)	$48.52
Gold per ounce	$1,771.60 (+57.80)	$1,895.10

*Stock indices include reinvested dividends for the period 4/1/2021-6/30/2021 and are not annualized
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The table of returns highlights the major market averages added to gains in the second quarter, as strong economic growth, strong profit growth, low interest rates, Fed bond buys, falling daily Covid cases, and the reopening of the economy aided stocks.

Notably, long-term Treasury yields fell in Q2, which suggests that investors may be accepting the Fed's line that the recent burst in inflation is temporary. It could also suggest that economic growth is set to peak soon, as fiscal stimulus wanes.

Final Thoughts

It is hard to believe that Hopwood Financial will have been in business for **18 years** this August. We can not thank each and every one of you enough for all your support through the years. When we say we could not do this without you, we truly mean it.

You have allowed us to prudently grow so we can continue to add the talented team members that we have today. With 9 highly skilled employees and a vibrant financial planning and investment management practice, we can provide a full assortment of financial services to each of our clients. We believe that this holistic approach allows us to better understand your situation and provide the best solutions to any issues that arise in your lives. When you add this technical knowledge with a staff that truly cares about our clients, we believe this is a winning combination.

Thank you for letting us serve you.

Hopwood Financial Services, Inc.