



## The Impact of The Pandemic on Residential Real Estate

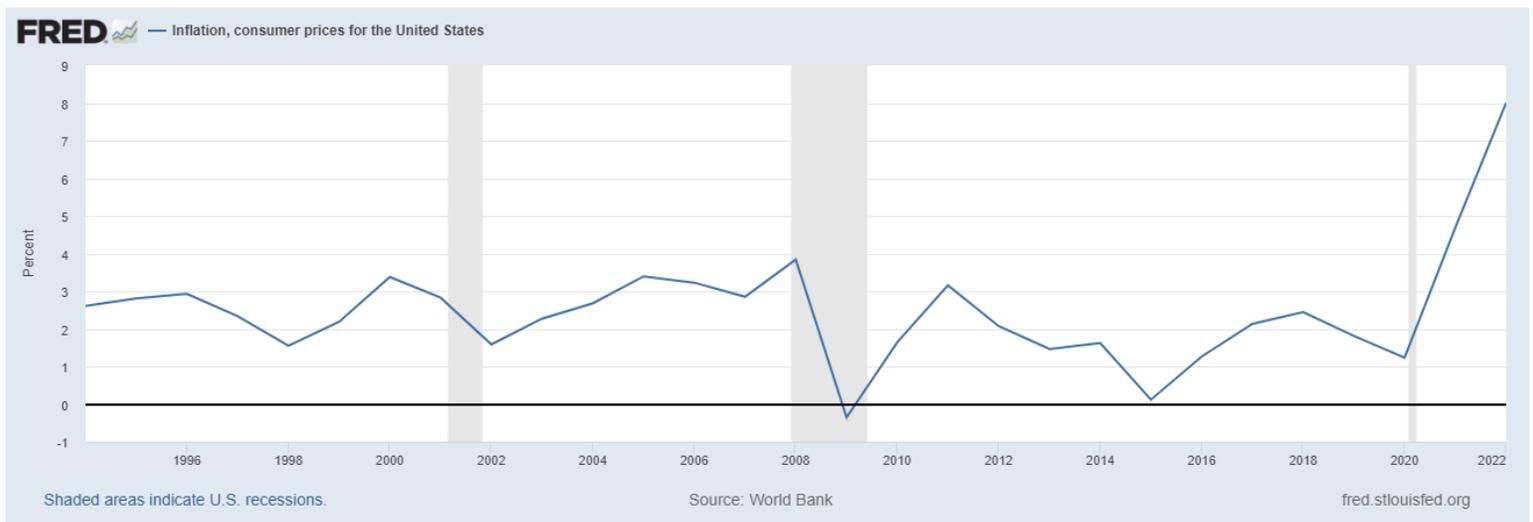
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Since the pandemic started in 2020, home affordability has suffered a triple whammy from three key factors – high inflation, skyrocketing home prices, and sharply rising mortgage rates. This has resulted in homes moving out of reach for the average American in almost every state, including Virginia.

### The first shock: High inflation

Americans had become accustomed to low inflation for the past 30-years. Inflation stayed around 3% from 1992, reaching a low of 1.2% in January 2020.

This rosy picture changed suddenly with the pandemic. In just two years (2020 - 2022), inflation jumped from 1.2% to over 8%. Meanwhile wages stayed the same or even declined. Consequently, real wages adjusted for inflation fell, resulting in Americans working more hours for less real pay each passing month.



Income adjusted for inflation is nearly 20% lower in Virginia today compared to January 2020. In other words, a household earning \$85,000 annually in January 2020 had the same buying power as a household earning \$100,000 annually in July 2023, according to BLS CPI data.

### The second shock: High Mortgage rates

Americans enjoyed steadily declining mortgage rates for almost 16 years. The 30-year fixed Mortgage rates fell from 6.74% in June 2007, to a low of 2.65% in January 2021.

However, things changed rapidly for the worse starting January 2021. Mortgage rates began to rise quickly, and continued rising, reaching 7.5% in October 2023.

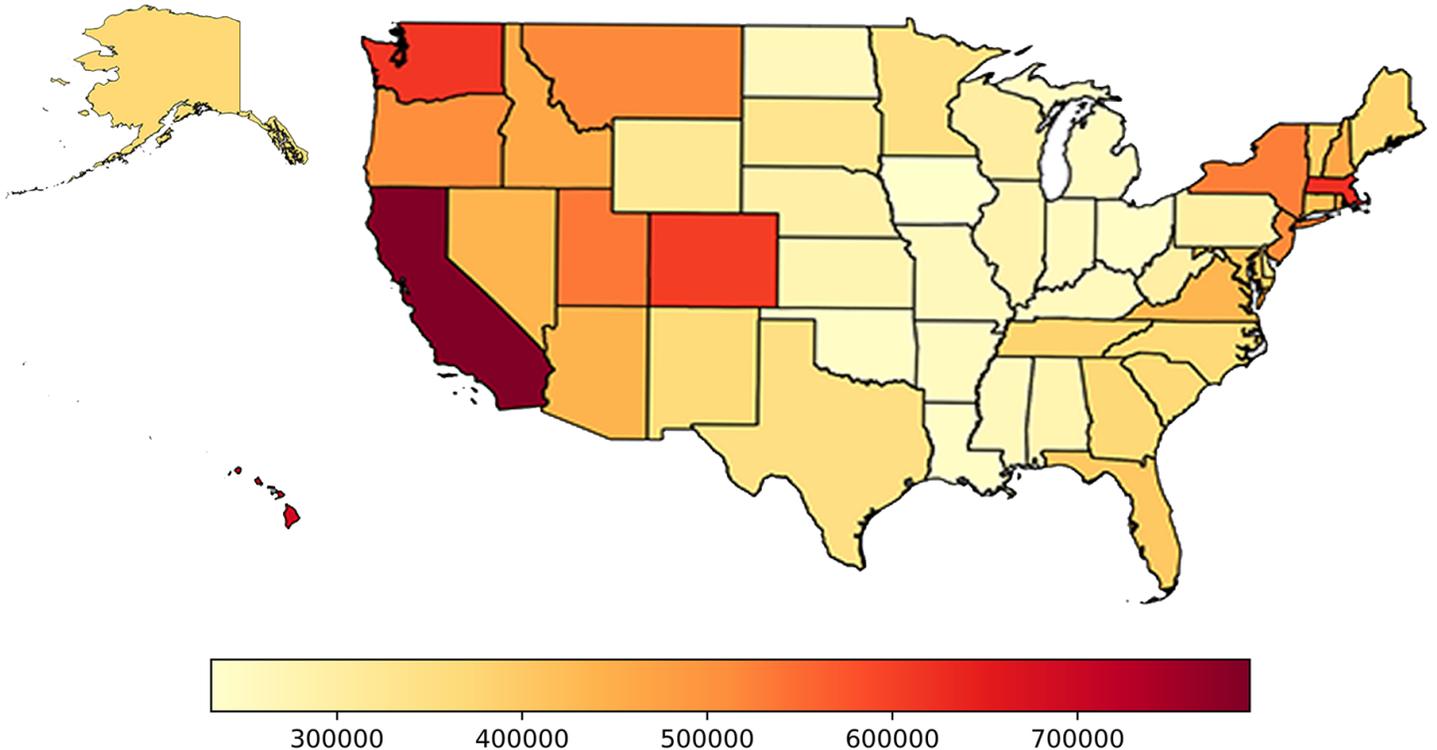


### The third shock: Rapidly rising home prices

Because Americans had become accustomed to declining mortgage rates for over 15 years, they believed they could afford bigger homes for the same monthly payment. Builders began building larger homes each year to earn higher profits, and as a result home prices rose steadily nationwide. Buyers were not too affected since the declining mortgage rates kept the overall monthly payments fairly steady.

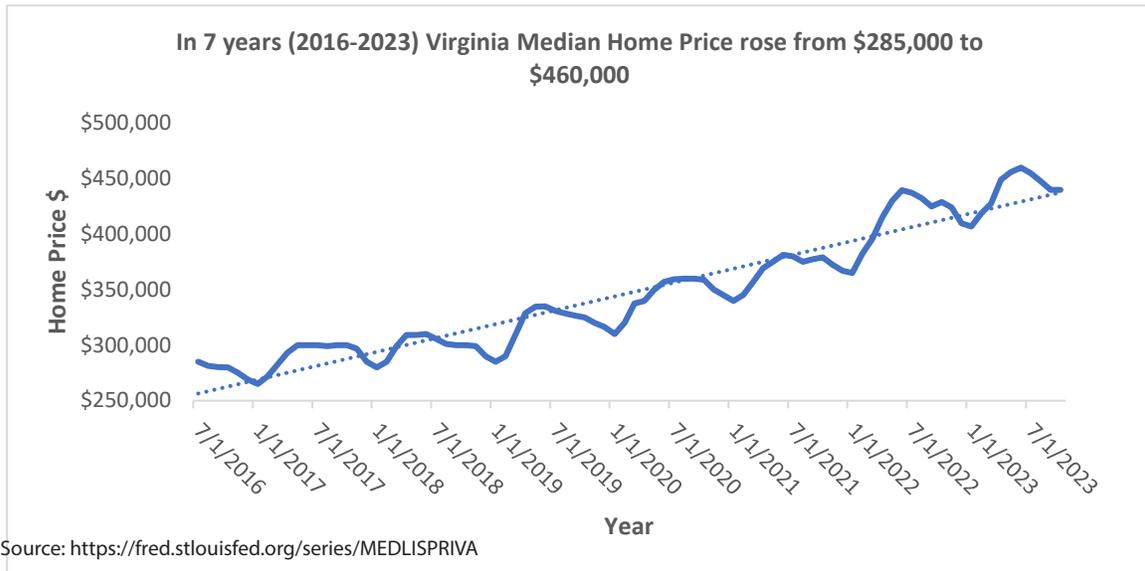
However, this party ended abruptly starting January 2021. Homes prices began to rise at a rapid rate, and continued rising in every state. As of August 2023, the highest median home price was in California (\$793,000).

Median Home Sale Price in USA - August 2023



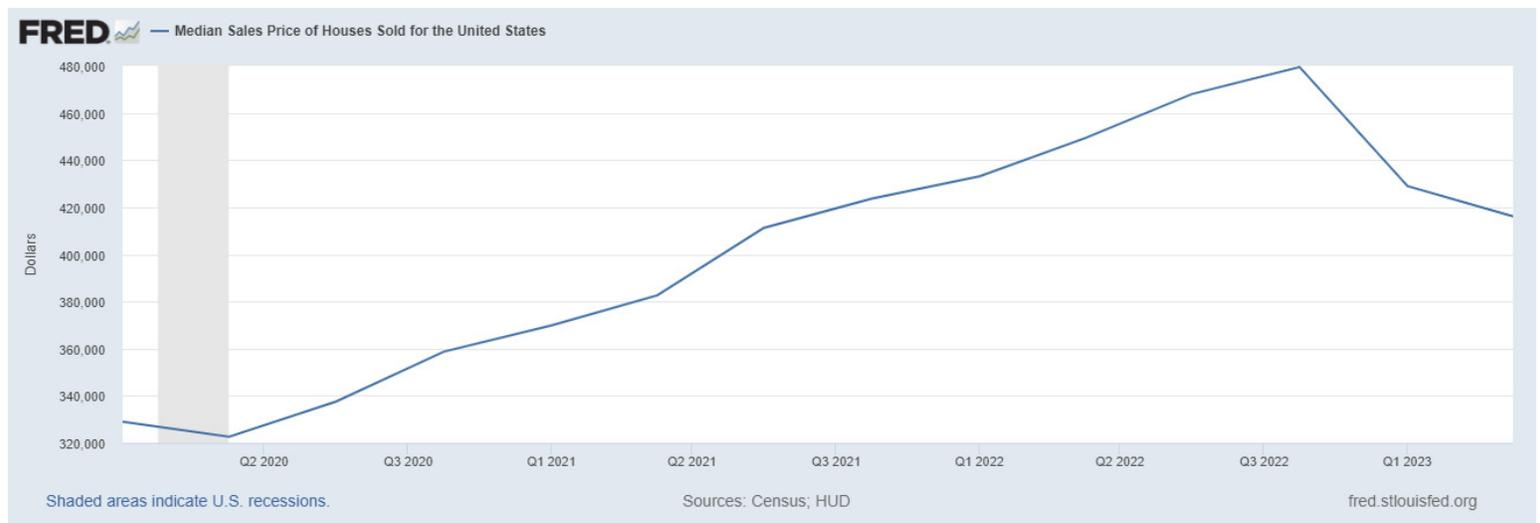
Source: Data provided by Redfin, a national real estate brokerage

Virginia was no exception to this steep increase. The median list price in Virginia increased by 61% from 2016-2023.



### The anomaly of rising mortgage rates and rising home prices:

If past history were any guide, rising mortgage rates should have resulted in a corresponding decline in home prices. However, that did not happen. Both mortgage rates *and* home prices rose together sharply starting 2021.



## How has this anomaly impacted monthly payments?

In July 2016, a median home's list price in Virginia was \$285,000, the 30-year mortgage rate was 3.41%, and the monthly payment (not including property taxes, insurance, other fees) was \$1,252.

By January 2022, the median home list price had shot up by \$80,000 to \$365,000. However, since the 30-year mortgage had dropped slightly to 3.22%, the monthly payment was \$1,582 – a modest increase considering the big jump in the home price.

In other words, from 2016 to January 2022, Virginians enjoyed fairly stable monthly mortgage payments between \$1,300-\$1,500 for a median home despite rising home values during this period, thanks to a low and declining mortgage rate.

And then the bottom fell out.



In the next 20 months, both home prices and mortgage rates rose steeply. In October 2023, a median home's list price in Virginia was \$440,000, the 30-year mortgage rose to 7.5%, and as a result the monthly payment jumped to an all time high of \$3,074 (an increase of 95% from January 2022).

In other words, monthly payments for a median home in Virginia have nearly doubled within 20 months, while incomes have stagnated and even declined after taking overall inflation into account.

## When will this situation improve?

No amount of new home construction can fix this situation quickly because an overwhelming majority (approx. 90%) of homes sold each year are existing home sales. However, homeowners are reluctant to sell, since the mortgage when they purchased the home was between 2-4%, whereas today's rate is closer to 8%. The profit they might make from their home sale will be negated by the inflated purchase price of another home, and additionally, their new mortgage monthly payment would be nearly double or more than their old payment.

Although inflation is now back down to a reasonable 3.7%, and Virginia's median home prices have declined by about \$20,000 from their peak of \$460,000 in the past three months, mortgage rates have risen by another percentage point during this period to 7.5%. As a result, the monthly payment for a median home has actually increased by an additional \$100.

Unfortunately, the situation is unlikely to improve until mortgage rates drop back to pre-pandemic levels.