Housing Prices and Affordability

By: James A. Wood, Ivory-Boyer Senior Fellow

In 2022, higher home prices and a doubling of the mortgage rate combined to erode housing affordability. Thus, homeownership has become more difficult for many of Utah’s 333,000 renter households. However, for the 770,000 homeowners, rising prices in 2022 added over $50 billion in increased equity (wealth). Current homeowners can comfortably weather the affordability threat, aware that higher prices add to their wealth. But for renters and future generations of homeowners, declining affordability thwarts housing and wealth opportunities.

A Sharp Increase in Interest Rates

In the wake of the pandemic’s historically low mortgage rates, 30-year conventional mortgage rates reached their highest level in 20 years (see Figure 26.1). The pandemic led to a historic level of federal fiscal stimulus ($5.2 trillion) and disrupted global supply chains. Both led to accelerating inflation rates. From June 2021 to June 2022, the inflation rate increased from 5.3% to 9.0%.

In response to rapidly rising prices, the Federal Reserve raised the federal funds rate seven times from March to December, an increase of four percentage points. Interest rate increases are an often-used tool by the Federal Reserve to manage monetary policy. However, the Federal Reserve’s tightening (including for mortgages) and aggressive rate increases since early 2022 caused the most abrupt and sharpest nine-month increase in mortgage rates in over fifty years. The 30-year mortgage rate average doubled from 3.5% in January 2022 to over 7.0% by late October and early November 2022. However, rates have since dropped to about 6.3% as of mid-December 2022.

Housing Price Increases Slow Down in 2022

Utah has a long history of volatile but generally increasing housing prices (see Figure 26.2). Typically, the rate of increase accelerates over several quarters, establishing a peak followed by a period of slower increases.

In the price cycles of the 1990s and 2000s, Utah led the country in housing price increases for a few quarters. Year-over prices seldom decline. However, declines have occurred, most notably during the Great Recession when year-over prices fell for 15 consecutive quarters. The current cycle growth rate peaked in the second quarter of 2021 with a year-over percentage increase of 28.3%. Only Idaho, with a 37% increase in the second quarter of 2021, exceeded Utah’s year-over percentage gain. Price increases continue decelerating, slowing to a 10.7% year-over increase in the third quarter of 2022. Monthly year-over price data from UtahRealEstate.com show that since March 2022, the rate of price increases in Utah decelerated for eight consecutive months, although still slightly growing overall statewide (see Table 26.1).

High Mortgage Payment Hinders Homeownership

The rapid increase in interest rates makes homeownership more difficult for many would-be homeowners. Potential homeowners face steep financial challenges without trade-up equity from an existing home. Comparing the mortgage payment required to purchase the median-priced home in October 2021 to October 2022 best illustrates this challenge.

Over 12 months, the median sales price of a single-family home in the four Wasatch Front counties rose from $522,000 to $550,000. During the same period, the 30-year mortgage interest rate increased from 3.07% to 6.90%. Driven primarily by higher interest rates, the monthly mortgage payment increased from $2,921 to $4,276, a 46% increase in a single year. Given these assumptions, the 46% increase would apply to homes at all price levels, above or below the median price.

Using the standard rule that a mortgage payment should not exceed 28% of gross income, the income required to finance the median price home jumps from $125,185 in 2021 to $183,257 in 2022.

Affordability Worsens for Renters

Compounding the affordability challenge, over the past five years, the median income of renters grew by 19% (U.S. Census Bureau) while rents in the Wasatch Front counties increased at roughly double that rate (see Table 26.3). That is, Wasatch Front rental rates grew twice as fast as renters’ income. In the past year
alone, rental rates in Salt Lake County increased by 9.4% and 11.6% in Weber County, with somewhat more moderate, but still high, increases in Davis County (7.3%) and Utah County (7.1%).

In the past two years, many renters received some temporary financial assistance from the Emergency Rental Assistance Program (ERAP). ERAP provided $385 million in federal assistance for Utah renter households. Authorized by the Consolidated Appropriations Act of 2021 and expanded by the American Rescue Plan Act of 2021, the assistance helps tenants unable to pay their rent or utilities due to circumstances related to the COVID-19 pandemic.

Program requirements insulate the 35,000 renter households living in Low-Income Housing Tax Credit units from rising rents. About one in eight renters in Utah live in affordable tax credit units. Rents in these units fall at least 10% below market rents, and tax credit requirements preserve unit affordability for 50 years. In the next two years, the inventory of tax credit units will increase by nearly 10% when the 3,000 units currently under construction are completed.

In addition to the tax credit program, federal Section 8 Housing Choice Vouchers provide rental assistance to about 12,000 renter households. Unfortunately, the number of renters who qualify for tax credit units and Section 8 Vouchers far exceeds the number of available units and vouchers. Consequently, in 2022 at least 50,000 Utah renter households are very low-income renters (≤50% Area Median Income[AMI]) and pay at least 50% of their income for housing and utilities. These households receive no rental assistance and live in market-rate rental units. Nearly 40,000 of these households are extremely low-income households (≤30% AMI) and pay at least 50% of their income for rent and utilities.

2023 Outlook

Housing prices in Utah nearly doubled in the past five years, growing much faster than incomes and overall inflation. A correction is due in 2023. In a best-case scenario, declines occur in the first and second quarters, but over four quarters, prices finish at about the 2022 level. But a year-over price decline is possible given the extraordinary 42% increase in prices from the fourth quarter of 2020 through the second quarter of 2022. Absent a serious recession and substantial job losses, the estimated worst-case scenario is a one-year price decline of 10% followed by stable prices in 2024.

In addition to a price correction, 2023 will likely feature a decline in existing home sales, builder discounts on new homes, continued upward pressure on rents, and additional state legislation addressing housing, including housing assistance for renters and potential homeowners. Finally, 2023 brings a respite from price increases, but with interest rates likely to remain above 6%, the housing market will see only marginal improvement in affordability.

About Housing Affordability

Two concepts of affordability: affordable housing versus housing affordability. Affordable housing refers to a specific type of housing, generally government-assisted rental housing targeted for very low to extremely low-income households. Housing affordability is a much broader term and refers to the general level of housing prices relative to the general level of household incomes. The term does not refer to any particular type of housing. The two concepts are not mutually exclusive or in conflict but are complementary with affordable housing being a subset of housing affordability.

Figure 1: 30-Year Conventional Fixed Rate Mortgage and Effective Federal Funds Interest Rates, 1972–2022e

Note: e=estimate
Source: Freddie Mac (FHLMC)
Table 1: Year-over Monthly Percent Increase in the Median Home Sales Price in Utah (single-family, condominium, twin home, and townhouse), 2022

<table>
<thead>
<tr>
<th>Month</th>
<th>Year Over % Change</th>
</tr>
</thead>
<tbody>
<tr>
<td>January</td>
<td>27.6%</td>
</tr>
<tr>
<td>February</td>
<td>28.2%</td>
</tr>
<tr>
<td>March</td>
<td>29.0%</td>
</tr>
<tr>
<td>April</td>
<td>24.4%</td>
</tr>
<tr>
<td>May</td>
<td>23.8%</td>
</tr>
<tr>
<td>June</td>
<td>17.8%</td>
</tr>
</tbody>
</table>

Source: UtahRealEstate.com

Table 2: Mortgage Payment for Median Price Single-Family Home in Wasatch Front Counties, October 2021 – October 2022

<table>
<thead>
<tr>
<th>Category</th>
<th>October 2021</th>
<th>October 2022</th>
</tr>
</thead>
<tbody>
<tr>
<td>Median sales price of single-family home</td>
<td>$522,000</td>
<td>$550,000</td>
</tr>
<tr>
<td>5% down payment</td>
<td>$26,100</td>
<td>$27,500</td>
</tr>
<tr>
<td>Amount to finance</td>
<td>$495,900</td>
<td>$522,500</td>
</tr>
<tr>
<td>Interest rate</td>
<td>3.07%</td>
<td>6.90%</td>
</tr>
</tbody>
</table>

Monthly Payments

| Principal and interest payment | $2,104       | $3,421       |
| Private mortgage insurance 1% of the loan | $413    | $435       |
| Home Insurance                | $100        | $100        |
| Property tax @0.007% of home value | $304     | $320       |
| Total mortgage payment        | $2,921      | $4,276      |

Source: Kem C. Gardner Policy Institute, Freddie Mac (FHLMC), UtahRealEstate.com

Table 3: Average Rent in Wasatch Front Counties, 2018-2022

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<thead>
<tr>
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</thead>
<tbody>
<tr>
<td>Davis</td>
<td>$1,060</td>
<td>$1,369</td>
<td>$1,469</td>
<td>38.6%</td>
<td>7.3%</td>
</tr>
<tr>
<td>Salt Lake</td>
<td>$1,153</td>
<td>$1,484</td>
<td>$1,623</td>
<td>40.8%</td>
<td>9.4%</td>
</tr>
<tr>
<td>Utah</td>
<td>$1,138</td>
<td>$1,432</td>
<td>$1,534</td>
<td>34.8%</td>
<td>7.1%</td>
</tr>
<tr>
<td>Weber</td>
<td>$864</td>
<td>$1,265</td>
<td>$1,412</td>
<td>63.4%</td>
<td>11.6%</td>
</tr>
</tbody>
</table>

Note: Composite average for all types of units.
Source: CBRE, The Greater Salt Lake Area Multifamily Market.
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