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## Housing Market

# Is this time different?

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## Key Takeaways

- Housing affordability has worsened with rising mortgage rates and higher building costs. However higher rents and historically low vacancy rates have kept mortgage payments relatively cheaper than rent.
- Millennials, representing the largest cohort buying homes, are chasing their homeownership dreams on their own terms. According to the 2022 BofA Homebuyer Insights Report, homebuyers are getting creative in how they are saving by either turning a passion into moonlighting or taking on freelance work.
- Supply has reached new record lows and historically tight inventories will underpin demand for new housing and construction.

Rising rates, higher building costs, elevated commodity prices and rumblings about a recession might historically be considered a recipe for turmoil in the housing market. However, strong household balance sheets, rising rents and demographic tailwinds lead us to think this time could be different.

This year is likely to be more challenging for the housing market given significant headwinds to affordability and ongoing supply-side challenges. The Russia-Ukraine conflict adds a new factor to the mix as higher oil and commodity prices will weigh on the consumer's ability to spend elsewhere, as well as increasing uncertainty and recession concerns and supporting higher input costs for builders. In this report, we highlight three main housing themes:

**Better to buy vs rent, but high barriers:** Both are more expensive, but mortgage payments are still relatively cheaper. That said, affordability from a home price/down payment perspective is the worst it's ever been, meaning extreme barriers to entry. Consumers remain steadfast in their interest to buy, but are uncertain if now is the time to buy.

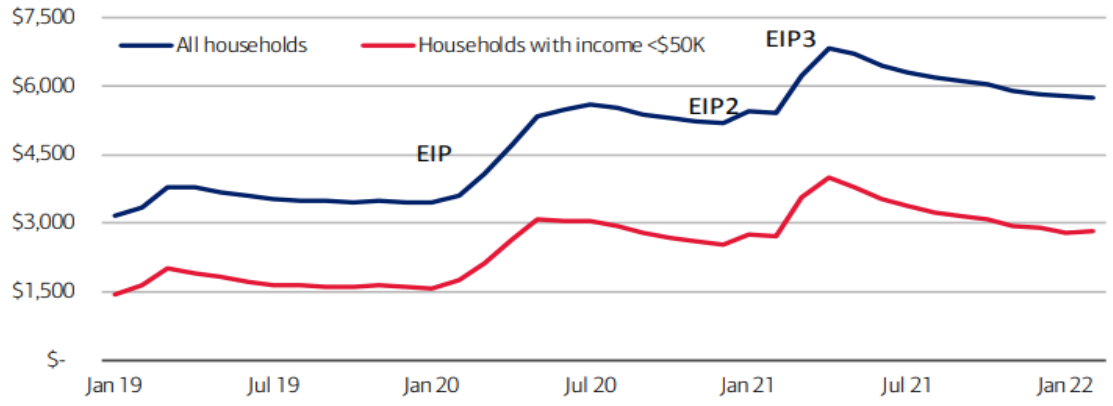
**Supply remains biggest constraint:** Monthly supply and inventory levels remain historically low. Builders have been bogged down by chaotic supply chains resulting in homes under construction exceeding annualized completions for the first time in history, and housing units authorized, but not started, have also reached a record high (back to 1999).

**Migration:** 2021 was a year of elevated domestic migration between US states. Last year, states like Idaho, Montana and Arizona experienced significant net inflows as people flocked to more affordable regions of the country.

## Skyrocketing rents keep relative cost to own attractive

Affordability has worsened with rising mortgage rates and higher building costs. However, higher rents and historically low vacancy rates have kept mortgage payments relatively cheaper than rent. We think the biggest risk to new home demand is entry-level buyers' ability to make down payments. Strong household balance sheets, wealth transfer (boomers lending to millennials) and robust labor markets could be offsets.

**Exhibit 1: Median household savings and checking balances ($) for a fixed cohort of savers as of 2019**[1]
Households still have higher savings levels than before the pandemic, likely thanks to stimulus




**Source:** BAC Internal Data. EIP – Economic Incentive Program

The massive rates move this year suggests that the affordability index will see another significant shift down. Further strong home price gains will add to the affordability pullback—the BofA Global Research Economics team expects 10% appreciation in Case-Shiller home prices this year, largely due to the historical supply-demand imbalance, though risks may be for high single digits. Despite a likely record decline in housing affordability this year, on a level basis housing will remain historically affordable. That said, the barriers to entry are the highest they've ever been from the perspective of affording the down payment. This is typically the biggest financial hurdle for first-time homebuyers.

Given housing costs are rising broadly, the question many households face is which is less painful: to buy or to rent? Using Zillow Home Value and Observed Rent Indexes, we find that the home price/rent ratio has worsened dramatically since the pandemic. The hurdle from home prices and affording the down payment is the worst on record, tilting the equation towards renting. Consumers appear to understand they are stuck between a rock and a hard place when it comes to buying or renting. If you can afford the historically high down payment, then you will save money on the mortgage compared to paying rent.

## Buyers get creative in their efforts to raise funds

To put themselves in a better financial position to purchase a home, many buyers are getting creative in how they're saving. Whether turning a passion into moonlighting or taking on freelance work, Bank of America found that the majority of homebuyers (56%) are willing to consider a second job to earn supplemental income for a home purchase according to the 2022 BofA Homebuyer Insights Report. For instance, approximately one-third of prospective homebuyers would consider starting an online store to sell handcrafted pieces (34%) or selling some of their belongings (31%) to save for a home.[2]

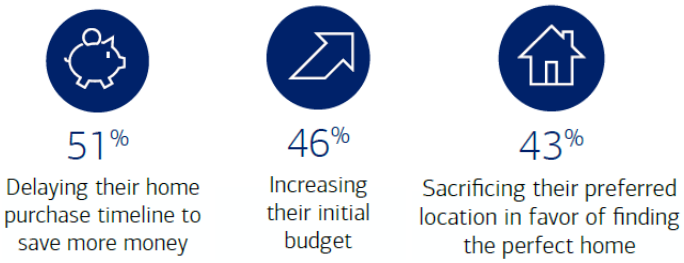
## Millennials are chasing homeownership dreams on their own terms

As millennials surpass baby boomers as the nation's largest adult generation, they are a driving force behind today's competitive homebuying market. This group now represents the largest cohort buying homes and face unique motivations and pressures. One-third (34%) say they feel the pressures of adulthood, meaning they feel like they should be buying a home at their age. Over half (53%) are motivated by the desire to set down roots for their growing family, and 43% want to start building equity in a home.[3] Home purchases show little sign of slowing during this spring homebuying season, characterized by surging demand and low inventory. Homes are being snapped up quickly, with two-thirds (65%) of prospective homebuyers saying they would make an offer within three days of viewing a home, and 20% saying they would make an offer immediately.

This generation is navigating home buying on their own terms. As mentioned in the 2022 BofA Homebuyer Insights Report, less than one-third (29%) would seek financial help from their family to buy their home. However, millennials would consider delaying their home purchase to save more money (51%), increasing their initial budget (46%) and sacrificing their preferred location in favor of finding the perfect home (43%).

[1] Includes those households that had a consumer deposit account all 38 months from January 2019 through February 2022.
[2] 2022 BofA Homebuyer Insights Report (HBIR)
[3] National Association of Realtors: Home Buyers and Sellers Generational Trends

**Exhibit 2: Millennials are chasing their homeownership dreams on their own terms**
Millennials are a driving force behind today's competitive homebuying market

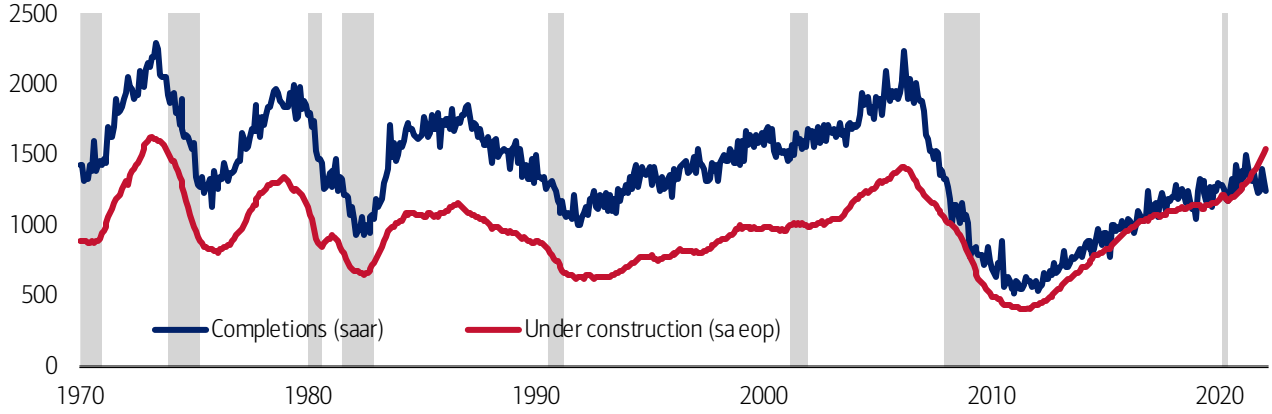



**Source:** 2022 BofA Homebuyer Insights Report

## Supply remains biggest constraint

One of the biggest challenges in the housing market has been dwindling supply, which has reached new record lows. Strong demand has been part of the equation for lower months' supply, with new and existing single family home sales soaring. Homes spent an average of 25 days on the market in February 2022, less than half as long as two years ago (56 days). This is despite more than half (56%) of prospective homebuyers surveyed reporting being hesitant to purchase due to high home prices,[4] which are expected to increase 10% by the end of 2022.

**Exhibit 3: Housing completions & under construction (000s units)**
Builders are getting bogged down as work in progress exceeds completions




**Source:** BofA Global Research, Census Bureau

At this point, the lack of supply is well-known. However, builders are also facing challenges. Lots, labor, lumber has been the catchphrase in recent years, highlighting the three main issues in ramping up new construction, even before the pandemic. Homebuilders have been impacted by the pandemic-related supply chain chaos, extending build timelines. The number of homes under construction exceeded the number of annualized housing completions for the first time in history in June 2021, and the gap has increased further since then.

The slower building timeline means an increasing backlog, given robust demand for housing supply. Consistent with this, the number of units authorized but not started reached a record high of 280k. This compares to the peak of 231k during the housing bubble. This backlog underpins the starts and new sales trajectory even if the rates shock causes housing demand to pull back via existing home sales. The Russia-Ukraine conflict threatens to add further hiccups, with materials prices being pushed higher. Lumber prices have soared over 47% over the past year and are now only 14% below the all-time peak. Russia is one of the largest lumber exporters in the world, which could pressure prices even higher, as well as a major producer of metals such as aluminum and copper.

## Buyers migrate to lower cost of living states

One way to get around the higher cost of living in your current neighborhood is to move to a completely new city or state. 2021 was a year of elevated domestic migration between US states.

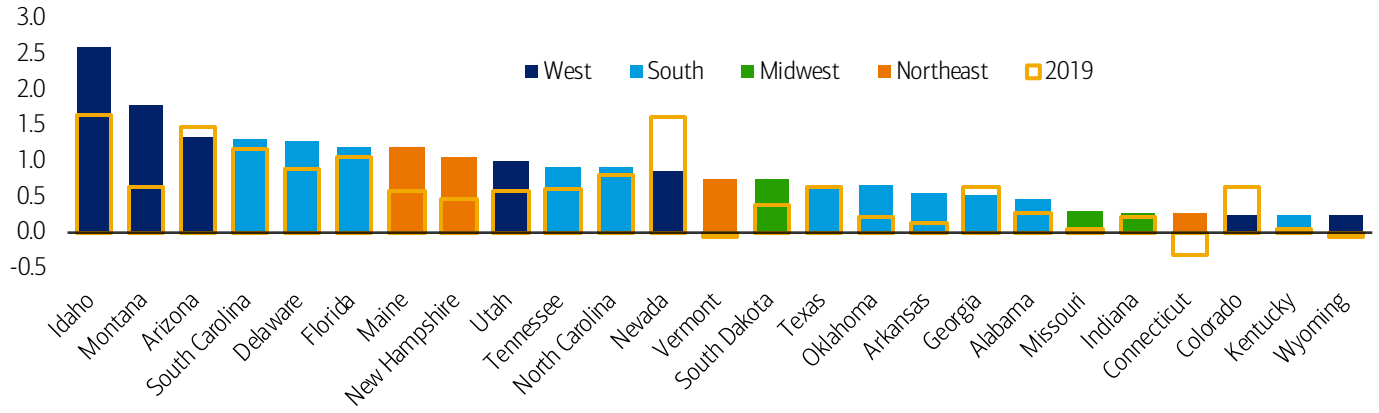
[4] Redfin Data Center: Median Days on Market

Last year, the states that saw the biggest inflow of people, as a share of their population were Idaho, Montana, Arizona, South Carolina, Delaware, and Florida, which are all located in the West and South of the US. These states all saw positive net migration in 2019, and, with the exception of Arizona, the pandemic accelerated these pre-existing flows.

Conversely, the top areas that people left were DC, New York, Illinois, California, and Hawaii. In the same way that the pandemic accelerated pre-existing net inward migration, it also generally accelerated pre-existing outward migration trends for these areas. These states are home to some of the least affordable cities in the US including New York, Chicago, San Francisco, San Jose, San Diego, and Urban Honolulu.

**Exhibit 4: Top 25 states seeing net inward migration (% state population)**

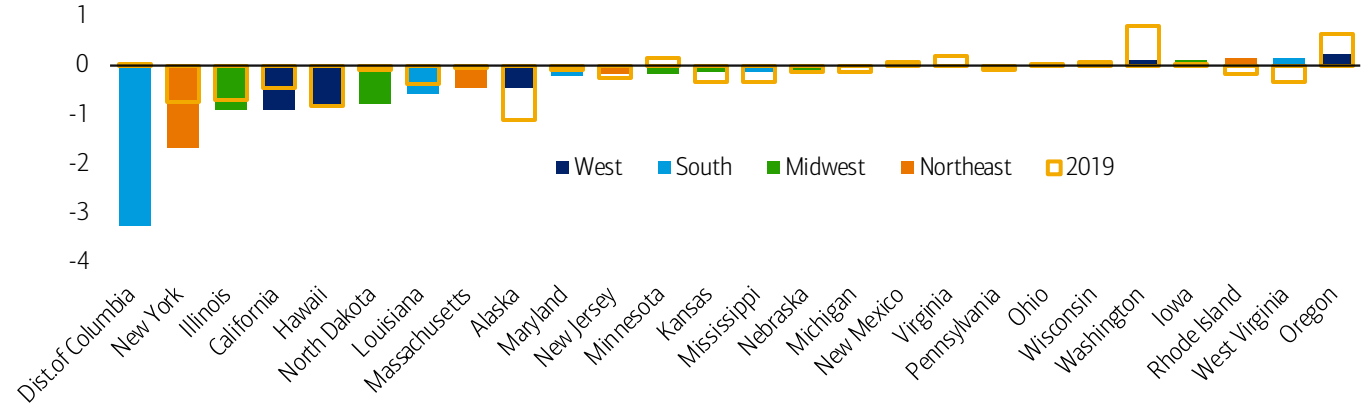
States experiencing positive net migration in 2019, and with the exception of Arizona, the pandemic accelerated these pre-existing flows




**Source:** BofA Global Research, Census Bureau

**Exhibit 5: Bottom 25 states (and DC) with net outward migration (% of regional population)**

These states are home to some of the least affordable cities in the US




**Source:** BofA Global Research, Census Bureau

## What's next for housing?

We expect demand to outpace supply and pricing to remain robust through 2022 due to favorable demographics and migration trends supporting growth in markets where there is a shortage of housing. Existing home inventory is historically low and will stay tight with current homeowners locked-in at favorable borrowing rates, while new home inventory will remain low given elongated build cycles and limited lot supply. The tight housing market is not going to ease any time soon and many prospective buyers may need to revisit their path to ownership.

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## Methodology

Selected Bank of America transaction data are used to inform the macroeconomic views expressed in this report and should be considered in the context of other economic indicators and publicly available information. In certain instances, the data may provide directional and/or predictive value. The data used are not comprehensive; they are based on aggregated and anonymized selections of Bank of America data and may reflect a degree of selection bias and limitations on the data available.

The payments data represents aggregate spend and deposit balances from Retail, Preferred, Small Business and Wealth Management clients with a deposit account or credit card. Data is not adjusted for seasonality, processing days or portfolio changes, and may be subject to periodic revisions. Aggregate card spend is based on processing date while the 'per household' measure is based on transaction date.

Bank of America credit/debit card spending per household include spending from active US households only. Only card holders making a minimum of five transactions a month are included in the dataset. Spending from corporate cards are excluded. Household credit/debit card spending data merchants who receive payments are identified and classified by the Merchant Categorization Code (MCC) defined by financial services companies. The data are mapped using proprietary methods from the MCCs to the North American Industry Classification System (NAICS), which is also used by the Census Bureau, in order to classify spending data by subsector. Spending data may also be classified by other proprietary methods not using MCCs.

Additional information about the methodology used to aggregate the data is available upon request.

# Disclosures

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