

Philadelphia's Housing Market Reacts to Pandemic, Social Unrest in Q2 **Sales activity plunges, but prices (appear to) hold steady.**

July 29, 2020: The latest quarter's housing numbers are the first to reflect the impact of both the COVID-19 pandemic and the subsequent social disorder. Here they are:

- **The average price of Philadelphia homes rose by 2.4% in Q2 on a quality- and seasonally-adjusted basis.** This increase continues the local market's continuing trend of positive, but generally decelerating house price appreciation compared to the last few years.
- **Philadelphia's house prices are currently up an average of 8.9% from one year ago (YoY).** This increase is well above the city's historic annual average appreciation rate of 4.5%, and is also above the YoY increases in recent quarters. However: this appears to be primarily due to a shift in home sales activity to relatively higher-priced dwellings in the city, rather than a citywide increase in house values (more on this below).
- **The median house price in Philadelphia in Q2 broke the \$200,000 barrier for the first time.** The city's median house price in Q2 was \$200,750. This is not only the first time that the median price has exceeded \$200,000, but it is also a nearly 15% increase over the median price of \$174,900 in the same quarter last year¹. However, this increase appears to be primarily due to a substantial change in the composition of homes that sold in Q2—which disproportionately favored relatively higher-priced homes—rather than an overall rise in the value of existing homes.
- **House price changes in individual submarkets were also uniformly positive.** From smallest to largest, the average annual change in seasonally- and quality-adjusted house prices by submarket was: Center City/Fairmount (+0.4%), South Philadelphia (+4.0%), Upper Northeast Philadelphia (+5.0%), Kensington/Frankford (+5.9%), Northwest Philadelphia (+7.5%), Lower Northeast Philadelphia (+9.1%), University City (+11.3%), West/SW Philadelphia (+13.4%), and North Philadelphia (+16.9%). However, like the YoY change in the city's median house price, these relatively large changes are principally driven by a bias in transactions towards relatively higher-priced dwellings in the most recent quarter.
- **Home sales activity experienced an unprecedented plunge this past spring.** There were just 3,125 arms-length sales in Q2, which is down a whopping 43% from 5,462 home sales in the same quarter one year ago² and also down 42% from 5,339 home sales in Q1 of this year. This last fact is especially notable because sales activity almost always increases from Q1 to Q2, regardless of the overall state of the market, due to the more favorable spring weather. The last time there was such a significant drop in sales activity was in 2008, when home sales in Philadelphia fell by 25%...as the last decade's housing began to rapidly deflate.

¹ Since raw house prices exhibit substantial seasonal fluctuations that are independent of the market's or economy's cycle, it is a standard industry practice to compare these numbers to the same time period one year ago, rather than to recent months or quarters.

² Like raw house prices, the seasonality of home sales volume make it a standard industry practice to compare these numbers to the same time period one year ago rather, than to recent months or quarters.

- **Housing inventories (the number of homes listed for sale) continue to remain at an historic low.** There are currently 2,978 houses listed for sale in Philadelphia, which is well below the historical average of approximately 5,000 houses typically listed for sale in any given month in the city. At the current pace of sales, the total supply of currently listed houses would be exhausted in 3.3 months. Since the real estate industry traditionally considers a supply of 5-7 months to be typical of a “balanced” market, the current 3.3 months’ supply strongly indicates that current market conditions heavily favor sellers over buyers.
- **Local homebuilding activity dropped significantly in Q2.** According to the volume of building permits filed with the city, Philadelphia is on track to construct approximately 2,200 new housing units by the end of this year. This is well below the annual average of approximately 3,500 new units that the city has seen during the current expansionary cycle of the previous ~8 years. The last time that current homebuilding activity was so low was in 2012, when both house prices and home sales in Philadelphia were at their previous lows.
- **Zillow’s house price forecast for Philadelphia remains negative but stable.** Housing analytics firm Zillow is currently projecting the general level of house prices in Philadelphia to decline by 1.1% over the course of the next year. This is the same forecast that it was projecting in the previous quarter.
- **But, two major industry indicators suggest some reason for optimism...or at least reduced pessimism.** After plummeting precipitously in March, both the Philadelphia Stock Exchange Housing Sector Index and the NAHB’s Homebuilder Sentiment index have largely recovered to their pre-pandemic levels. From a high of \$377 per share in February of this year, the Housing Sector Index (which reflects the value of publicly traded firms whose primary source of revenue is from the housing industry) fell to a low of \$180 by the end of March, but it has since risen back to \$364 per share. Similarly, the Homebuilder Sentiment Index (which reflects the relative optimism or pessimism of U.S. homebuilders and ranges from 0 to 100), fell from a near-high of 72 in February to a low of 30 in March, but has since recovered to its previous high of 72.

The fact that both house sales and homebuilding activity experienced such sharp drops in Q2 may not be good news, but it should not be surprising news. The combination of the quarantine, the classification of homebuilding as a “nonessential” industry, and people’s general risk aversion to social contact has kept many homebuyers, real estate agents and contractors at home for the past several months. The lifting of these conditions that began in May has since seen both renewed activity in these sectors as well as some renewed optimism (or at least reduced pessimism).

More questionable, however, is the general level of house prices. As previously mentioned, the composition of sales activity in Q2 saw a significant reduction in transactions of relatively lower-priced homes. It should be noted that such a pattern is common in the beginning of a recession and/or a downturn in the housing sector, as the tightening of credit and lending standards combined with a contracting job market disproportionately hits lower-income households the hardest. The analytical statistics in this report bear this out, since the regression which computes the typical citywide price increase (and controls for the differing characteristics of houses that sold) shows an 8.9% YoY increase in house prices, while the increase in the citywide raw median price is a much larger 14.8%. As such, the true impact of current events on Philadelphia house prices may have yet to reveal itself.

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If you would like Dr. Gillen to address your organization, business or community group with a presentation on recent trends in the local economy and real estate market, he would be happy to do so...and it's absolutely free! Just contact him at the email address above.