Philadelphia's Regional Housing Market Maintains Its Strong Trends

Prices, sales, inventories, turnover and other indicators continue to break new records.

March 5, 2021: An exceptional confluence of factors are at work to make the market so hot. Here's the latest numbers, supplied by Houwzer LLC.:

- **Both city and suburban house prices closed out 2020 with significant gains, but the city continues to outpace the suburbs.** The general level of suburban house prices rose 2.4% in Q4, while the general level of house prices in Philadelphia grew by 5.0% during the same period. With these increases, house prices in the city are now an average of 12.8% higher than they were one year ago, while suburban house prices are an average of 5.6% higher from where they were one year ago. For context: house prices across the US appreciated an average of 10.8%[1] in 2020, and the average historic annual appreciation rate of house prices across the Philadelphia region is 4-5% per year.

- **Philadelphia's above-average price appreciation puts its homeowners in a much different place than their suburban counterparts.** Since 2012, when post-bubble house prices hit bottom and the current expansionary cycle began, city house prices have risen an average of nearly 66%, while suburban house prices have only risen an average of 24%.

- **Despite Philadelphia's higher rate of appreciation, its general <u>level</u> of prices still remains well below that of its suburbs.** The median house price in the city is currently $210,000 compared to $295,000 in the suburbs. A year ago, they were $166,750 and $260,000, respectively. Note: this gap becomes even larger if you compare prices in Philadelphia to only those of its suburbs in Pennsylvania and exclude those in Delaware and New Jersey.

- **House price changes across the region in Q4 were both uniformly positive and larger than average.** From lowest to highest, the average annual change in house price levels by county in 2020 was: Chester (+2.1%), Montgomery (+3.0%), New Castle (+3.3%), Bucks (+4.0%), Mercer (+4.2%), Burlington (+5.2%), Delaware (+6.1%), Camden (+6.8%), Salem (+7.7%), Gloucester (+8.0%) and Philadelphia (+12.8%).

- **Home sales continue to rebound from their pandemic-driven lows to levels well above their historic average.** 26,016 houses changed hands across the region in Q4, up 59% from 16,363 sales during the quarantine in Q2, and up 24% from 20,961 sales in the same quarter one year ago[2]. This quarter was the second-highest volume of regional home sales since the data began being tracked in 2005.

- **Million-dollar sales across the region remain especially strong.** There were 418 home sales at a price of one million dollars or more across the region in Q4, with nearly 90% of them occurring in the suburbs. This was the second-highest volume of +$1m sales since 470 such sales in the

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[1] Source: Federal Housing Finance Agency, www.fhfa.gov

[2] Since home sales volume in this region is highly seasonal, it is standard industry practice to compare quarterly (or monthly) sales volume to the same quarter (or month) one year ago, rather than to the previous quarter (or month).

previous quarter of Q3. By contrast, the region typically averages 180 such sales in any given quarter.

- **The supply of homes available for purchase remains severely restricted…and continues to fall to new lows.** There are currently only 9,156 homes listed "for sale" across the Philadelphia metro area. Not only is this a new all-time low (down from 17,366 one year ago), but is well below the region's historic average of approximately 30,000 homes available for sale in any given month.

- **The pace of sales continues to quicken…and also set a new record.** The average number of days (DOM) it takes a listed home to sell in the Philadelphia region is currently 31 days, down from 52 days just a year ago. While average DOM varies across the US, the historic average in this region is 60-70 days.

- **Low Supply + High Demand + Rapid Turnover = A Very Strong Seller's Market.** At the current pace of sales, there is only a 2.1 months' supply of inventory ("MSI"[3]) in Philadelphia and a 1.0 months' supply in the suburbs[4]. Both are new all-time lows, and are well below the 5-month threshold that the industry considers indicative of a balanced market[5]. Such conditions strongly favor sellers at the expense of buyers in setting both the price and terms of sale.

- **Zillow has recently become very bullish on its outlook for the Philadelphia region's house prices.** Zillow's house price forecast is currently predicting that the general level of house prices in the region will increase by 10.9% over the next 12 months[6]. Its previous forecast from 3 months ago was for a 5.6% increase, and its forecast prior to that (during the height of the pandemic last spring) had actually been for a decline of 2.3%.

This quarter's trends are essentially a repeat of the trends reported last quarter. As such, it bears repeating the same analysis of these trends: there is nothing in the region's economy or demographics that can point to why prices and sales should be not only increasing at such a rapid rate, but also hitting all-new highs in the process. The region's employment level, economic output, population and household incomes are not growing at nearly the requisite pace to rationalize how hot the local housing market has become[7]. Rather, the current market is drinking from a "strong cocktail" of unprecedentedly low interest rates, unprecedentedly low inventories and an unprecedented shift in demand for housing (and away from traditional office, retail and restaurant space) as a result of the COVID pandemic.

Of these three conditions, the most concerning is the very low level of inventories. That is because they are traditionally a short-to-intermediate driver of house price fluctuations, rather than a long-term determinant; i.e. they are not considered a "fundamental driver" of either house prices or sales. The underlying reasons for such an exceptional lack of supply are numerous:

- The conversion of millions of houses to rentals in the wake of the last housing downturn
- Exceptionally low levels of new home construction over the last decade

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[3] Months' Supply of Inventory is how many months it would take for the current inventory of homes listed for sale, given the current pace of sales. 5-7 months is generally considered by the industry to be typical of a balanced market.

[4] Source: Brokermetrics via Houwzer LLC

[5] Source: https://realtytimes.com/advicefromtheexpert/item/38353-how-to-determine-if-it-s-a-buyers-sellers-or-a-balanced-real-estate-market?rtmpage=

[6] Source: https://www.zillow.com/philadelphia-camden-wilmington-metro-pa_r394974/home-values/

[7] Although there is anecdotal evidence of high-income New York households relocating to the Philadelphia area, there has been no substantial hard evidence…yet.

- Boomers aging in place rather than downsizing to a new dwelling
- Current landlords reluctant to give up their income-producing properties[8]
- Pandemic-driven mortgage forbearance plans and eviction moratoriums
- Potential sellers being reluctant to compromise their "social distancing" by allowing strangers to walk through their homes.
- Lastly: why sell your current home if your choice of your next home is so restricted, and prices are so high?

But, the one thing these factors have in common is that they all work to incentivize current homeowners to remain in place…*<u>even if these homeowners are both willing and able to move</u>*.

However, these conditions will eventually go away, and then one of two things must happen: either prices will correct downwards or else they will stagnate while jobs, population and incomes catch up to their level. In the meantime, it would seem advisable not to drink too much or too quickly from the currently available cocktail. Over-consuming a strong drink can only ever end one way.

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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.

[8] This is because the rental market has been doing so well since the last downturn: many displaced households were forced to switch to renting, and the Millennial/Gen Z demographic cohorts continue to disproportionately rent.