CALIFORNIA ASSOCIATION OF REALTORS®
Market Snapshot

Closing on 2013 – Questioning Housing Affordability

Following the strong beginning to the year, the last quarter of 2013 is shaping to close on a mediocre note. Sales have slowed significantly and so has the price appreciation for single family existing homes in California. However, the slowdown may not be that different than what we have seen in the past. Let's put things into perspective by looking at some numbers. The average percent decrease from October to November in the past 5 years was 13.2 percent. For 2013, October to November decline of 13.6 percent is larger than the average, but not significantly higher. In other words, the double-digit decrease on a month to month basis is not out of the ordinary for this time of the year, at least not for the last 5 years. One troubling statistic however is the decline in pending sales on a year-over-year basis in November 2013. The decline was smaller than that observed from October 2012 to October 2013, which was 10.4 percent, but the decrease was slightly higher than the last 3-month year-to-year average decline of 9.1 percent. One must keep in mind though that mortgage rates hit historical lows in September through November of 2012, while the sales also reached the highest point of last year in October of 2012. Given the very strong housing market in the fall of 2012, it is difficult to make any determination about the weakness of the current market by simply comparing it to the last fall.

The question is whether the recent declines in sales are due to weaknesses in the housing fundamentals or the economic fundamentals. The economic fundamentals are certainly improving and are better than anything we saw in the last 5 years. The housing fundamentals for primary home buyers are at question. If the increase in interest rates is the culprit, then the question we should ask is whether the housing recovery is sustainable in the prevailing affordability environment.

The statewide housing affordability index (HAI) for the 3rd quarter of 2013 is 32 percent, which is much stronger than that observed in 2005-2006 boom years. The index of 32 indicates that 32 percent of households can buy a median priced home. The HAI actually decreased significantly from 2012 when it peaked at 56 percent in the first quarter of 2012. Assuming that home prices stay at or around the current level for the next two to three quarters, the housing affordability index should be floating around at the high 20's and the low 30's for the state as a whole. Just as a point of reference, the historical average going back to 1988 for HAI is 31.9 percent. That is hard to believe! So while the affordability has decreased, it is still at the historical average.

With that said, what should we expect in 2014? In the short run, the pending sales index suggests that sales of existing homes will remain at the current levels through the end of the first quarter. Assuming that the economy will have a decent growth in 2014, the housing market should be stronger for the last 3 quarters of 2014. However, housing affordability will remain an issue in 2014, especially in the Bay Area where prices rose precipitously over the last couple of years and, unlike the rest of the state, have not yet slowed down.

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