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REDFIN

Redfin Reports Just 3 in 100 Pandemic Homebuyers Would Fall Underwater With Next Year's Projected 4% Home-Price Decline

Recent homebuyers in certain places, like Sacramento and Phoenix, are at higher risk of falling underwater on their mortgage, while Florida homeowners are at even lower risk

SEATTLE--(BUSINESS WIRE)-- (NASDAQ: RDFN) — Only 3.4% of U.S. homeowners who bought in the last two years would be underwater on their mortgage if home values were to fall 4% by the end of 2023, according to a new report from Redfin (redfin.com), the technology-powered real estate brokerage.

The typical home bought over the last two years will have gained $27,000 in value, even with prices falling 4% next year as Redfin economists predict. Prices would need to fall by double digits in 2023—a highly unlikely scenario—for the typical pandemic home purchase to lose value.

Change in home prices, Nov. 2022-Dec. 2023	Share of homeowners who would be underwater on their mortgage	Change in home value* for the typical homeowner
flat	1.6%	$44,279
-4%	3.4%	$27,318
-8%	6.3%	$10,950
-12%	10.3%	-$5,026
Homeowners who purchased their home between Jan. 2021 and Sept. 2022 only *Relative to purchase price		

If home prices fall 8% in 2023—more than the expected drop—still just 6.3% of new homeowners would be underwater. Prices would need to fall about 12% for the share of underwater homeowners to reach double digits.

Homeowners who bought from January 2021 through September 2022 are likely to have low fixed mortgage payments and good enough credit to meet tight lending standards. And even though they haven't owned their home for long, those new homeowners are likely to have already earned plentiful equity because prices skyrocketed so much during the pandemic and because they were likely to have made big down payments. That's especially true for those who bought in 2021, when mortgage rates sat near record-low 3% levels all year and home prices had yet to peak. Someone who bought a $400,000 home with a 3% rate would have a monthly payment just under $2,000; for the sake of comparison, the monthly payment would be $2,500 with a 6% rate.

Homeowners who bought before 2021 are even less likely to sink underwater with next year's anticipated price declines, partly because they have built up more equity and partly because many of them refinanced when rates were at an all-time low.

A foreclosure crisis is unlikely—but middle-class homeowners may lose a substantial chunk of wealth with declining home values

“Even with anticipated price declines, next year’s housing downturn won’t come anywhere close to the foreclosure crisis we saw during the Great Recession in most parts of the country,” said Redfin Senior Economist Sheharyar Bokhari. “Recent homebuyers have enough equity—both because they’re likely to have made relatively large down payments with a low rate and because values rose so much so fast—that most aren’t at risk of owing more than their house is worth. Even if a homeowner is at risk of falling behind on their mortgage payments next year—say they lose their job and inflation has claimed a big chunk of their savings—having equity means they could sell instead of face foreclosure. It’s also worth noting that not many Americans are expected to lose jobs next year, as even if the U.S. does enter a recession it’s expected to be mild.”

Even though a foreclosure crisis is highly unlikely, middle-class homeowners do stand to lose a substantial chunk of their wealth if home values fall, as a big share of their assets tend to be in real estate. The typical American earning the median income holds about 38% of their wealth in real estate, versus about 27% to 30% for higher earners. The share of wealth held in real estate has also increased more during the pandemic for middle-class homeowners than higher earners, rising about 4 percentage points for middle-class households and 2 to 3 percentage points for higher earners. But the loss would be temporary and only on paper for homeowners who don’t sell soon, as home values are likely to increase once rates come down and the economy recovers.

Homeowners in popular pandemic destinations and expensive West Coast cities are at higher risk of falling underwater

Some parts of the U.S., including pandemic boomtowns and tech hot spots, are at higher risk of homeowners falling underwater. Just over 9% of recent Sacramento homebuyers would be underwater with a 4% price drop, the highest share of the metros in Redfin’s analysis.

“Home prices have dropped quickly and substantially after skyrocketing during the pandemic. It has been a shock to the system for homeowners and sellers, though they’re getting used to the new reality,” said Sacramento Redfin agent Alison Williams. “In a way, a correction like this was inevitable; prices can’t keep going up by double digits forever. And the silver lining is that people who have been hoping to buy their first home but were priced out may be able to enter the market when prices—and hopefully rates—come down next year.”

The typical Sacramento home bought in the last two years would lose roughly $17,000 in value with a 4% price decline next year, one of just five metros in Redfin’s analysis where homes would lose value at that size drop. The others are all tech towns, mostly in the Bay Area: San Francisco, San Jose, Oakland and Seattle.

It’s also worth noting that prices in pandemic boomtowns and tech towns are likely to fall more than the national average, which means a higher share of homeowners would fall underwater. With an 8% decline, 14.4% of new Sacramento homeowners would be underwater.

In terms of risk of falling underwater, after Sacramento comes Phoenix, where 7.3% of recent buyers would fall underwater with a 4% price decline. Next come Virginia Beach (7.3%), Oakland (6.6%) and Seattle (6.4%).

Phoenix homeowners are at relatively high risk of falling underwater for similar reasons as those in Sacramento: They're both among the top 10 destinations for relocating homebuyers, a major factor in prices shooting up about 30% in both metros from January 2021 to their May 2022 peak. They're two of just a few metros where prices have started falling year over year.

Homeowners in many parts of Florida are even less likely to fall underwater

Florida homeowners are least likely to fall underwater on their mortgage payments. With a 4% home-price drop in 2023, less than 0.5% of homeowners who bought in the last two years in Miami, Fort Lauderdale or West Palm Beach would be underwater. Those are the only U.S. metros of the places included in Redfin's analysis where nearly zero homeowners would be underwater.

Even if home prices were to drop 12% in 2023, the typical new homeowner in those three metros would gain value.

"Recent homebuyers in parts of Florida are sitting pretty because home prices there have risen even more dramatically than they have in the rest of the country and they haven't come close to falling," Bokhari said. "In fact, prices in Miami, Fort Lauderdale and West Palm Beach are still up by double digits from a year ago. Values in Florida are resilient because there's still a fair amount of demand from remote workers and retirees who are relocating from more expensive areas."

To view the full report, including a full metro-level table and methodology, please visit: https://www.redfin.com/news/pandemic-homebuyers-underwater-unlikely

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Redfin Journalist Services:
Kenneth Applewhaite, 206-588-6863
press@redfin.com

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