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Housing Market Trends in Grand Rapids

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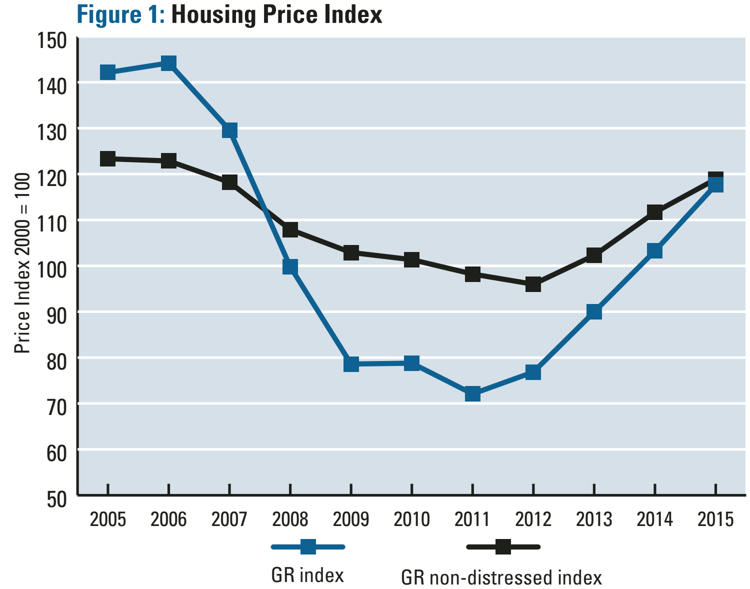
Housing market conditions continued to improve during 2015 in the U.S., with prices, sales, and construction activities rising to levels not seen since 2007–2008. Home prices rose by 5% in the U.S. during the last 12 months ending in September 2015 (S&P/Case-Shiller 20-City Price Index; S&P Dow Jones Indices LLC). Meanwhile, in the first 10 months of 2015, home sales were 7% higher than in the same period of 2014 (National Association of Realtors), and private housing starts (construction) were 10% higher, reaching an annual rate of 1.1 million units (Federal Reserve Bank of St. Louis). Housing markets have been helped by better demand conditions, with low unemployment rates, reaching 5% in November (Federal Reserve Bank of St. Louis), and low mortgage rates, at an average of 3.8% during 2015 vs. 4.2% in 2014 (Freddie Mac). Optimism about future home prices and sales are also driving up demand. On the negative side, delinquency rate on residential loans is still much higher than the historical average. After reaching a peak of 11.3% in 2010, the delinquency rate was down to 5.8% during the 3rd quarter of 2015, compared with 2% before the foreclosure crisis (Federal Reserve Bank). Another issue is that homeownership rates continue to drop to levels last seen in the 1980s or 1990s. In the Midwest region, it went down to 68% in the 3rd quarter of 2015 after reaching a peak of 74% in 2004 (Federal Reserve Bank of St. Louis). Among the culprits are strict credit standards, low wage growth, and demographic and employment trends, which make ownership less enticing, especially to younger people.

At the local level, our quality-adjusted price index shows that home prices continue to rise following a trend that started in 2012. Figure 1 presents two indexes for Grand Rapids. The non-distressed index excludes houses with sale prices below $50,000, which are the ones more likely affected by the foreclosure crisis (the estimation of these indexes is discussed in a technical note at the end of the article). Based on the non-distressed index, prices in 2015 rose by 6.5%, after rising by 9% in 2014. This price growth is justified by sales rising without a corresponding increase to the number of houses available for sale. During the first 9 months of 2015, sales of single-family homes rose by 12% compared to the same period in 2014 in the region of activity of the Grand Rapids Association of Realtors. However, inventory-to-sales ratio reached a very low 2.6 months' supply in September 2015 (the average in 2014 was 3.2). In response to the increasing demand and low supply of units for sale, construction of new homes has risen. The annualized rate of permits in Grand Rapids city is now back to the level in 2005 (see Table 1). Construction in the remaining of Kent County has also recovered significantly.

Despite growth in the last 3 years, the latest housing price index for Grand Rapids is still below the peak in 2006. For comparison purposes, home prices in higher income suburban communities in the region had already surpassed their 2006 peak values during 2014. The Grand Rapids housing market recovery has been slowed down by the high rate of foreclosures during the housing crisis, a reflection of the lower income and worse employment conditions in the city (see comparison in Table 1).

With foreclosure activity declining, prices of cheaper houses are recovering faster, so that both price indexes shown in Figure 1 are now about 20% higher than in 2000. However, during the same period, the inflation rate has been 38% (based on the

Figure 1: Housing Price Index



See Technical notes at the end of the article for details.
Source: Indexes computed using data from IS BS&A

Table 1: Building Permits, Income, and Employment

Area	Building Permits (annual rate) 2005	2009	2014	2015*	Median Household Income 2013	Worker Population Change 2005 to 2013
Grand Rapids city	318	30	203	327	$39,227	-9.2%
Kent County	2,941	645	1,711	*NA*	$51,667	+1.8%

Annual rate of building permits based on data until October 2015. Median household income comes from the American Community Survey 2009-2013 estimates. Worker population comes from the Longitudinal Employer-Household Dynamics (LEHD) estimates. Source: U.S. Census Bureau.

CPI - Consumer Price Index; Bureau of Labor Statistics), which implies that the real value of Grand Rapids housing is still far below the 2000 level. This decrease in real value reflects the economic issues that the city has faced in the last 15 years, including loss of population, low income growth of residents, and high foreclosure rates. Recent improvements in housing and employment conditions may help revert this long term decline in home value in the next few years.

Gross rental rates in Kent County have increased faster than the average rental rates in the 30 largest counties in Michigan, rising 27% compared to 21% since 2005. In addition, the increases in gross rents have accelerated in recent years doubling the average Michigan increase in 2014. Much of the increase in Kent County has been on the high end of the market with an increase in gross rents above $1,000. This has accelerated building of multi-family units in the Grand Rapids area and is also making single family housing more price competitive, as the increase in gross rental rates has substantially exceeded price increases in single family homes.

In conclusion, economic and housing market conditions continue to improve in the region. Demand for both rental and owned housing has risen this year, with inventory of homes reaching very low levels, especially in the higher end of the market. These trends indicate that the local market will see more growth in prices, sales, and construction activity next year. One concern is the risk of a severe slowdown of U.S. economic growth due to the weakening of foreign economies. On the other hand, if the economy improves, we will likely see interest rates rising next year. It is still unclear how much the sales of homes will be affected by rising mortgage rates, but it should slow down the growth in home prices.

Technical note

The repeat-sale housing price index shown in Figure 1 is set at 100 in 2000, so it can be interpreted as the amount of money needed to buy a house for every $100 that was needed to buy the same house in 2000. The index is computed by comparing sales prices of the same houses over time. The use of repeat-sales is a way to control for variation in quality across houses. Thus, the estimation does not include prices of houses that were not resold during the period analyzed. It also disregards the impact of renovation or deterioration of houses. Nonetheless, it is a widely accepted method to measure the average changes in prices in a broad housing market. Our indexes were computed using sales from 2000 to October 2015, with prices as low as $10,000 and as high as $500,000 in 2015. This value-boundary helps to better reflect changes in the prices of typical homes in the market. ■

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