

REALTORS' ASSOCIATION OF SOUTH CENTRAL WISCONSIN

2023 Single-Family and Multifamily Real Estate Outlook

Mark J. Eppli, Ph.D. Graaskamp Center for Real Estate Wisconsin School of Business, University of Wisconsin January 19, 2023



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2023 Macroeconomic Outlook

- I. Housing Demographics
- II. Single-family Mortgage Market
- III. Single-family Housing Market
- IV. Multifamily Capital and Property Markets



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Housing Demographics

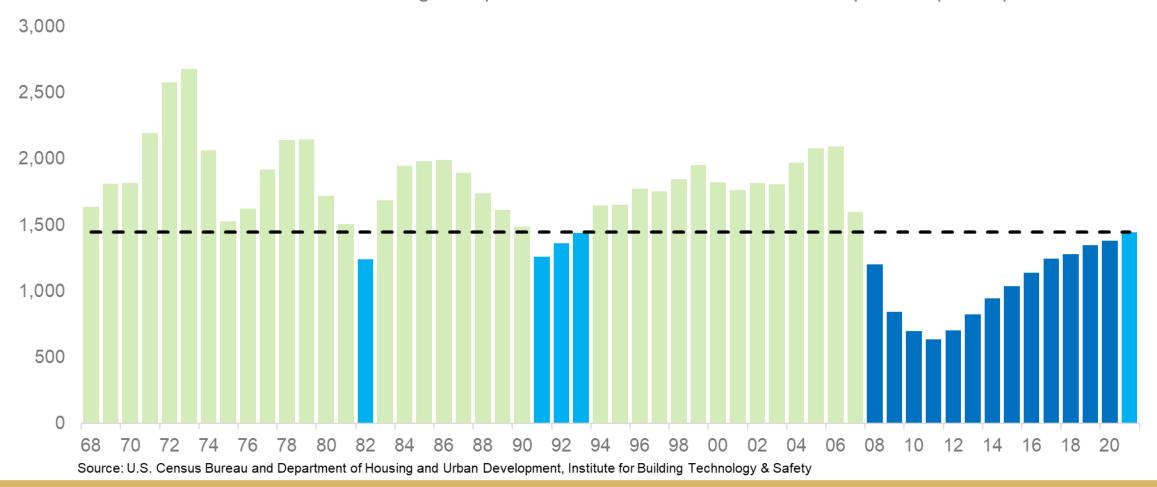


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Housing supply growth averaged a low 1,008,000 units from 2008-2022...

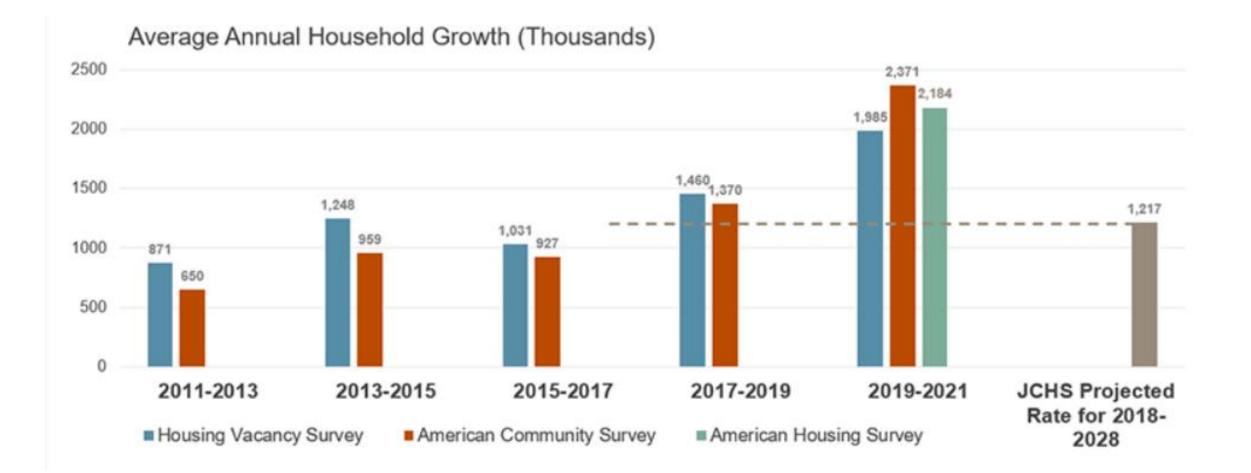


U.S. Annual Housing Completions and Manufactured Home Shipments (1000s)



JAMES A. GRAASKAMP CENTER for real estate Source: Freddie Mac, Chief Economist Sam Khater, Presented at The Graaskamp Center Outlook Conference, October 6, 2022.

.... household growth (demand) wildly exceeded expectations for the period 2019-2021





JAMES A. GRAASKAMP CENTER for real estate Source: Daniel McCue, Joint Center for Housing Studies, "The Surge in Household Growth and What it Suggests about the future of Housing Demand, January 17, 2023.

.... most of the unexpected growth is in younger age cohorts

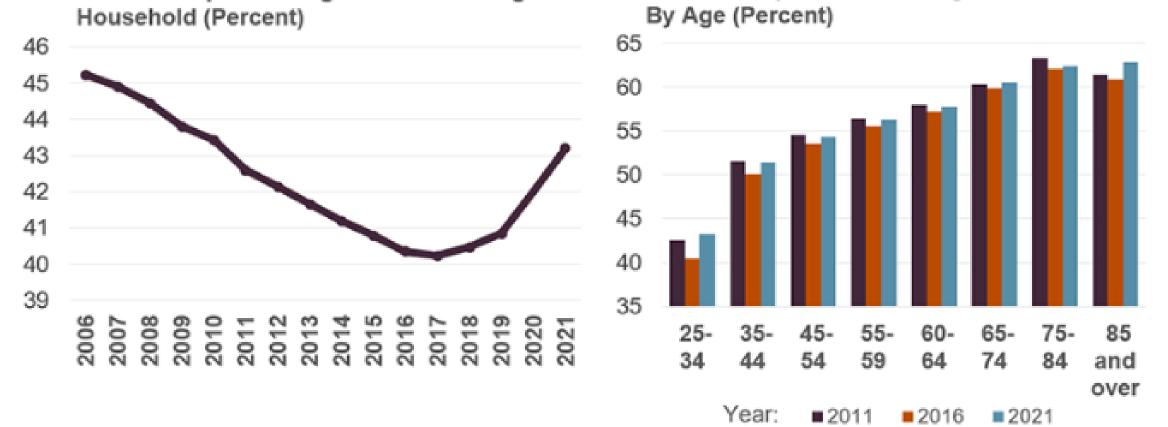


Annual Household Growth, By Age (Thousands of Households)



JAMES A. GRAASKAMP CENTER *for* REAL ESTATE Source: Daniel McCue, Joint Center for Housing Studies, "The Surge in Household Growth and What it Suggests about the future of Housing Demand, January 17, 2023.

.... growth is coming from a turnaround in headship rates across all ages



Share of Population Heading a Household, By Age (Percent)



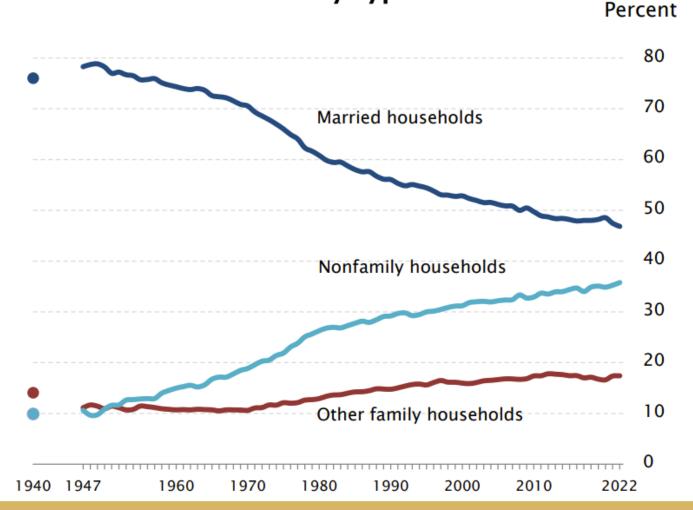
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Share of Population Aged 25-34 Heading a

Source: Daniel McCue, Joint Center for Housing Studies, "The Surge in Household Growth and What it Suggests about the future of Housing Demand, January 17, 2023.

.... married households (as a % of all HHs) went from 78% in 1947 to less than 50% in 2022



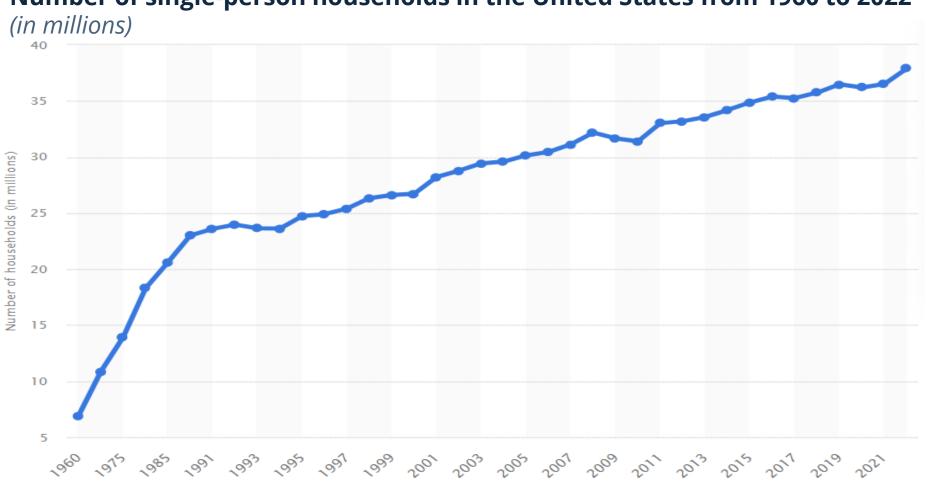




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JAMES A. GRAASKAMP CENTER for REAL ESTATE Source: U.S. Census retrieved on January 18, 2023 at: https://www.census.gov/data/tables/time-series/demo/families/households.html.

.... single-person household growth is expanding the number households



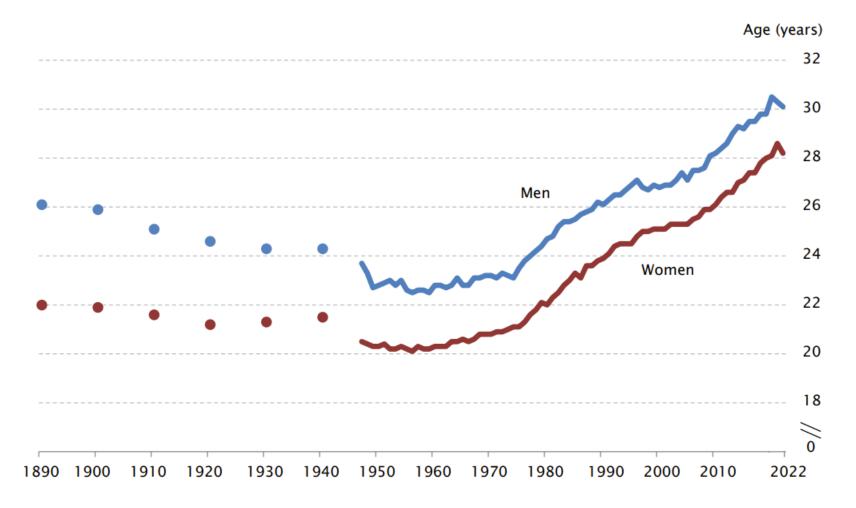
Number of single-person households in the United States from 1960 to 2022



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Source: Statista retrieved on January 18, 2023 at: https://www.statista.com/statistics/242022/number-of-single-person-households-in-the-us/

.... first-time marriage is being significantly delayed Median age at first marriage: 1890 to present

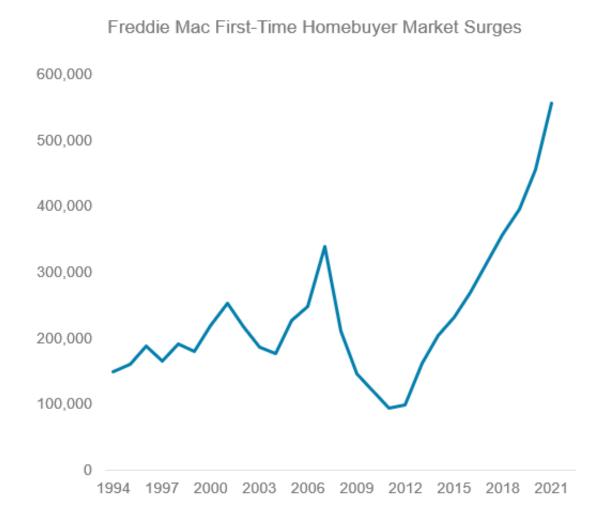




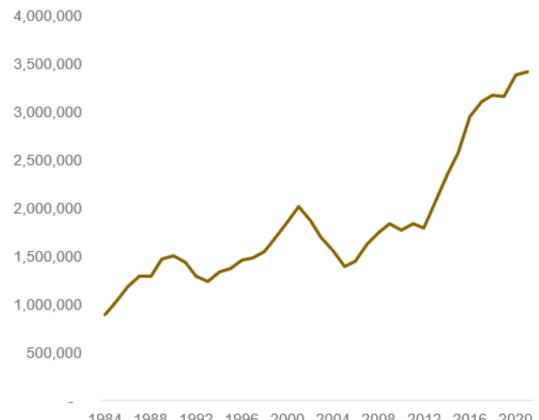
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JAMES A. GRAASKAMP CENTER for real estate Source: U.S. Census retrieved on January 18, 2023 at: https://www.census.gov/data/tables/time-series/demo/families/marital.html.

.... first-time homebuyers are in the market, many with high incomes





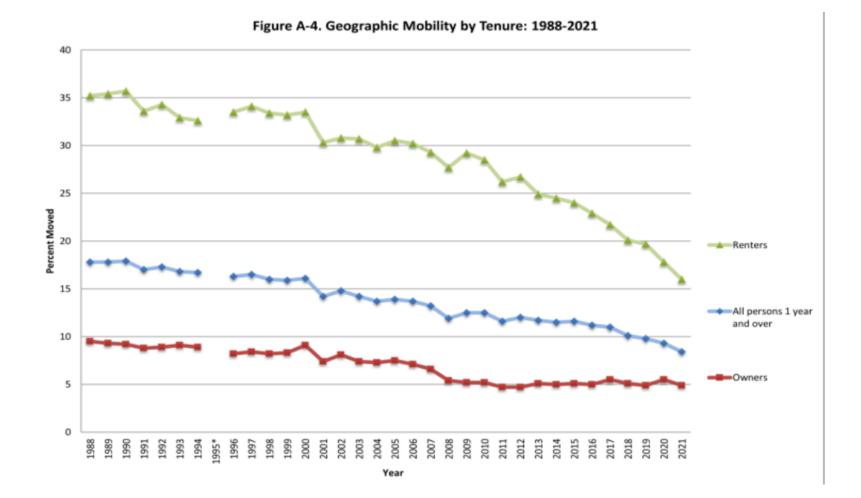


1984 1988 1992 1996 2000 2004 2008 2012 2016 2020



JAMES A. GRAASKAMP CENTER for real estate Source: Freddie Mac, Chief Economist Sam Khater, Presented at The Graaskamp Center Outlook Conference, October 6, 2022.

.... U.S. mobility rates are the lowest since the data was first collected in 1947.





JAMES A. GRAASKAMP CENTER for real estate Source: Freddie Mac, Chief Economist Sam Khater Presented at the NAHB Mortgage Roundtable May 12, 2022.

Housing Demographics

- Housing supply is inadequate which will keep prices from falling much in the economic challenges in 2023
- Housing demand was underestimated as headship rates increased
- First-time homebuyers are growing

SUMMARY: Demographics are destiny and housing demographics are very strong from the demand side in a supply constrained market.



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Residential Mortgage Market



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Mortgage market Context: slide #1 of 3

Mortgage Statistics

	Percent of Homes with a Mortgage	Average FICO Credit Score	Average Mortgage Payment
United States	62%	739	\$1,358
Wisconsin	63%	750	\$1,058



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Source: Federal Housing Finance Agency, National Mortgage Database, Mortgages Outstanding on June 30, 2022 and the Graaskamp Center.

Mortgage market context slide #2 of 3 . . .

Mark-to-Market Loan to Value (all mortgages in the U.S.)

					Percent
	Average	Percent less	Percent	Percent	greater than
	LTVR	than 60%	60-70%	70-80%	80%
United States	48%	78%	19%	10%	1%
Wisconsin	45%	70%	9%	7%	0%



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JAMES A. GRAASKAMP CENTER for real estate Source: Federal Housing Finance Agency, National Mortgage Database, Mortgages Outstanding on June 30, 2022 and the Graaskamp Center.

Mortgage market context slide #3 of 3

Interest Rate at Origination (all mortgages in the U.S.)

	Average				Percent
	Interest	Percent less	Percent	Percent	greater than
	Rate	than 3.0%	3.0-4.0%	4.0-5.0%	5.0%
United States	3.6%	28%	44%	19%	10%
Wisconsin	3.7%	28%	43%	19%	11%

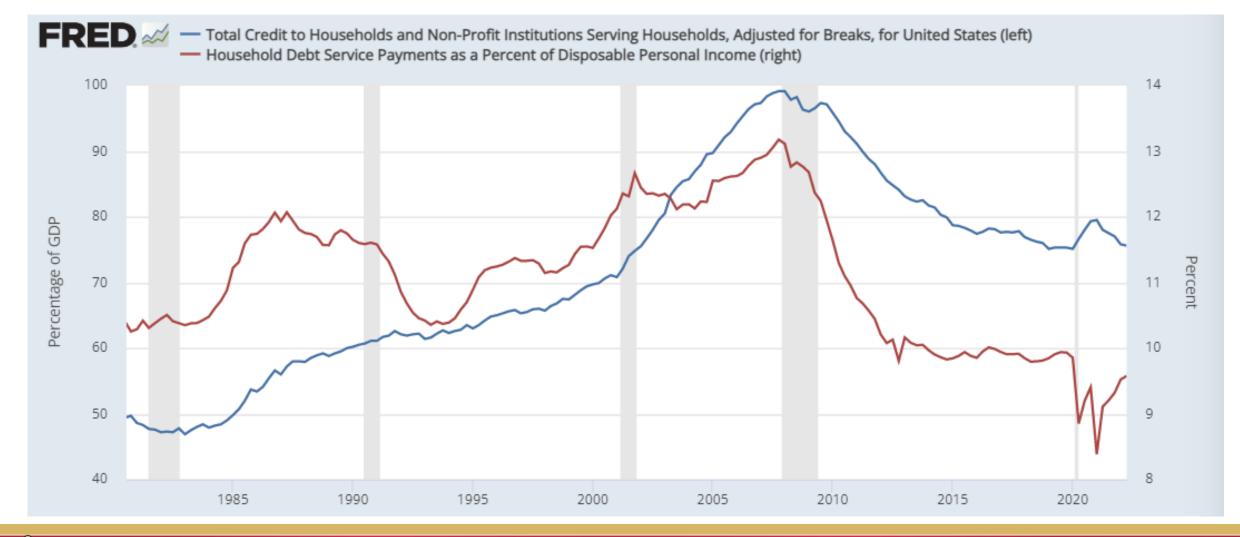


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Source: Federal Housing Finance Agency, National Mortgage Database, Mortgages Outstanding on June 30, 2022 and the Graaskamp Center.

Homebuyers have debt service and debt capacity . . .

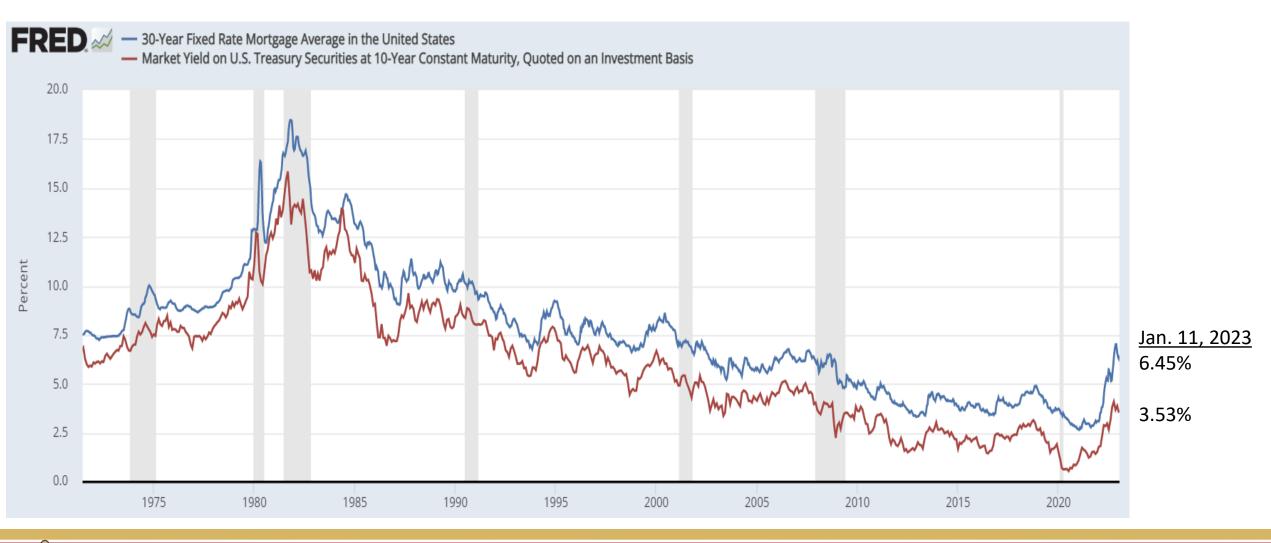




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JAMES A. GRAASKAMP CENTER *for* REAL ESTATE Source: Federal Reserve Economic Data.

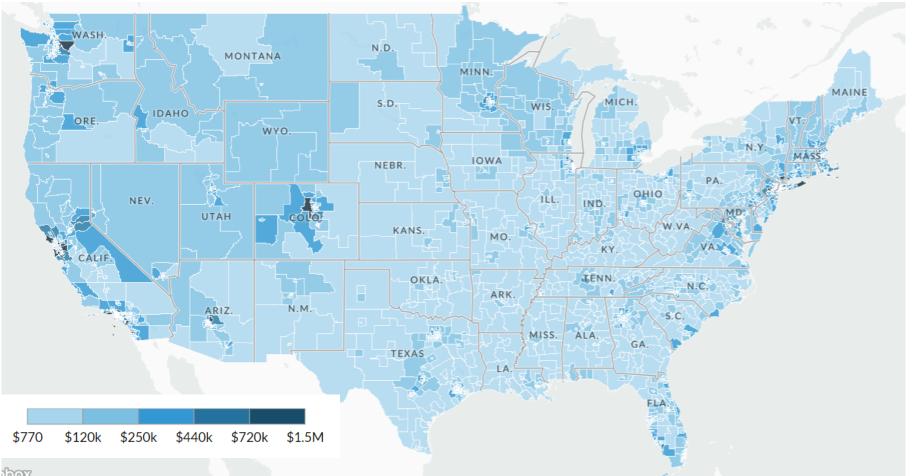
....average 30-year mortgage spread over 10-year U.S.T. are 1.79% (currently 2.92%)....





JAMES A. GRAASKAMP CENTER for real estate Source: Federal Reserve Economic Data.

.... net worth in Wisconsin counties bests many other areas in the nation....



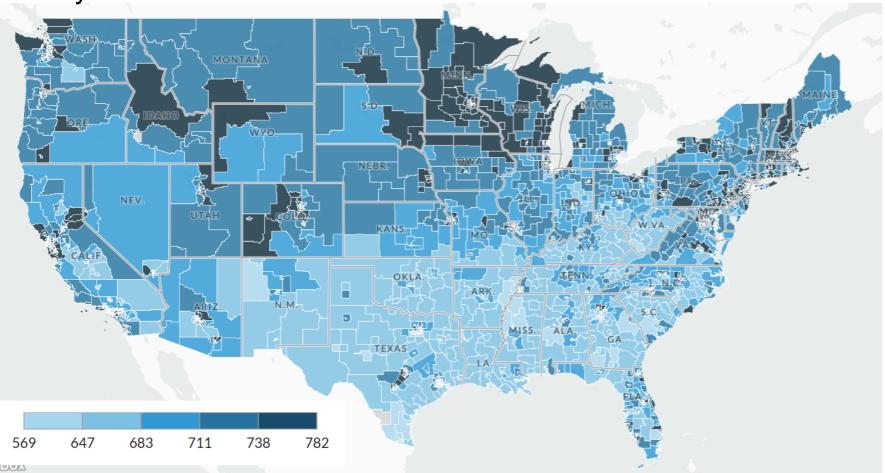
County-level Median Net Worth in U.S.



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JAMES A. GRAASKAMP CENTER for real estate Source: Urban Institute, "Financial Health and Wealth, Dashboard," at: https://apps.urban.org/features/financial-health-wealth-dashboard/

....Wisconsin credit scores are among the best in the nation....



County-level Median Credit Scores in U.S.

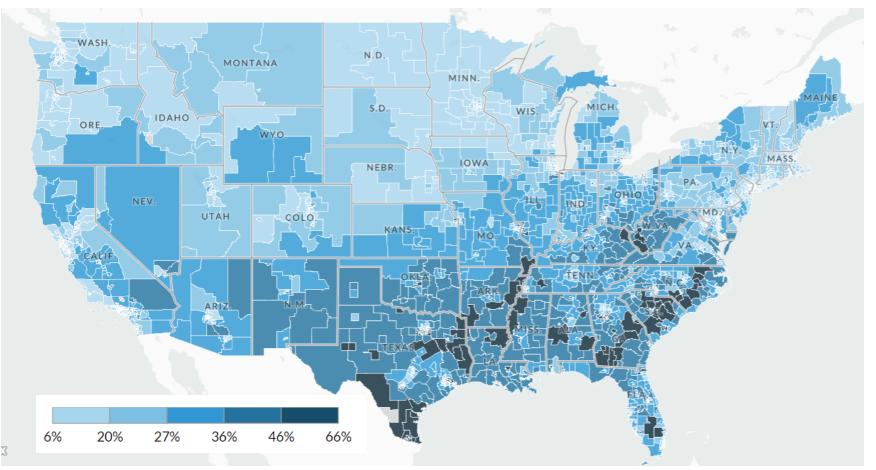


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JAMES A. GRAASKAMP CENTER for REAL ESTATE Source: Urban Institute, "Financial Health and Wealth, Dashboard," at: https://apps.urban.org/features/financial-health-wealth-dashboard/

.... Wisconsin delinquency rates are low

County-level Mortgage Delinquency Rates in U.S.





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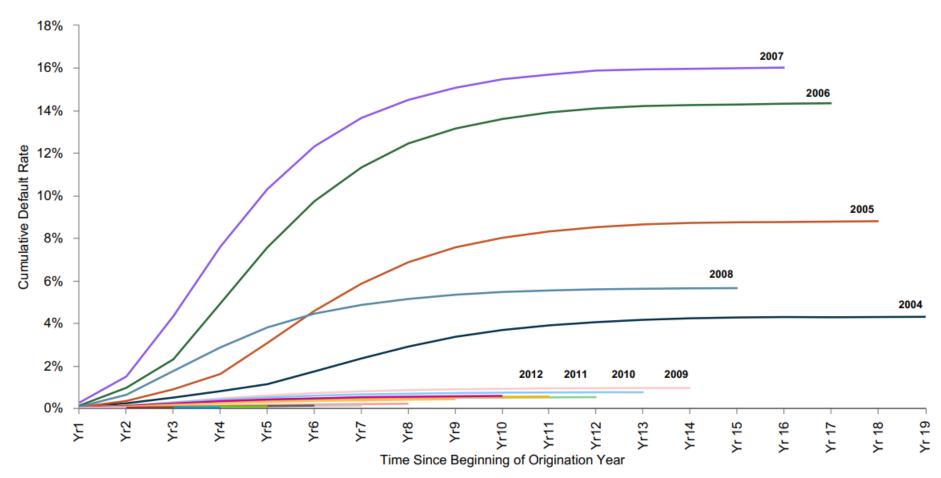
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Source: Urban Institute, "Financial Health and Wealth, Dashboard," at: https://apps.urban.org/features/financial-health-wealth-dashboard/

.... the national mortgage market is performing well.

Single-Family Cumulative Default Rates

Cumulative Default Rates of Single-Family Conventional Guaranty Book of Business by Origination Year⁽⁵⁴⁾





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Source: Fannie Mae, Financial Supplement Q3 2022, November 8, 2022.

Interest Rates/Mortgage Market

- The mortgage credit markets are in sound shape solid credit scores, low loanto-value ratios, and low loss rates (very different from 2007)
- Mortgage interest rates include outsized credit risk premiums
- The Fed's resolve to push the short-term Fed Funds rates up to reduce inflation, keeping long-term mortgage interest rates at or below current rates
- Borrowers in Wisconsin are better positioned than the rest of the U.S. in terms of net worth, mortgage payments, and loan-to-value

SUMMARY: Mortgage interest rates have peaked and will slowly settle into the **mid-5% range (maybe lower)** by year-end 2023.



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Single-Family Housing Market



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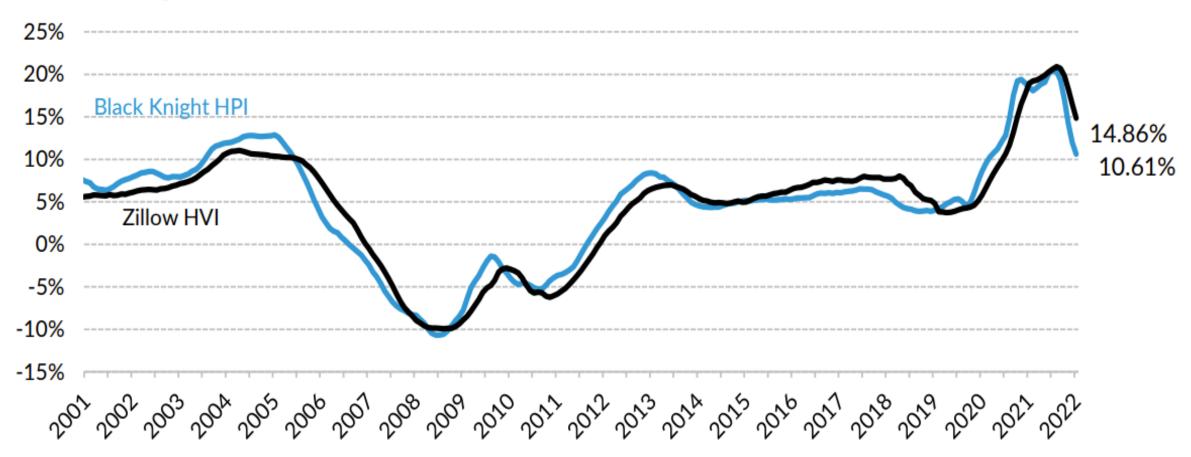
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National house price appreciation is cooling. . . .

Change in Single-Family House Prices

Year-over-year growth





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Source: Urban Institute, "Housing Finance at a Glance," November 2022, p. 22.

.... the national supply of for-sale housing remains tight

Months of Supply

Months of supply





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Source: Urban Institute, "Housing Finance at a Glance," November 2022, p. 20.

.... Wisconsin's supply of housing is tighter than the national average....

	Months		Months		Months
Urban-Rural Classification	Supply	Price	Supply	Region	Supply
Metropolitan Counties	2.4	\$0 - \$124,999	2.1	Central	2.5
Micropolitan Counties	2.5	\$125,000 - \$199,999	2.0	North	3.3
Rural	3.6	\$200,000 - \$349,000	2.2	Northeast	2.7
State	2.6	\$350,000 - \$499,999	3.1	Southwest	2.5
		\$500,000+	4.8	Southeast	2.3
		State	2.6	West	2.9
				State	2.6

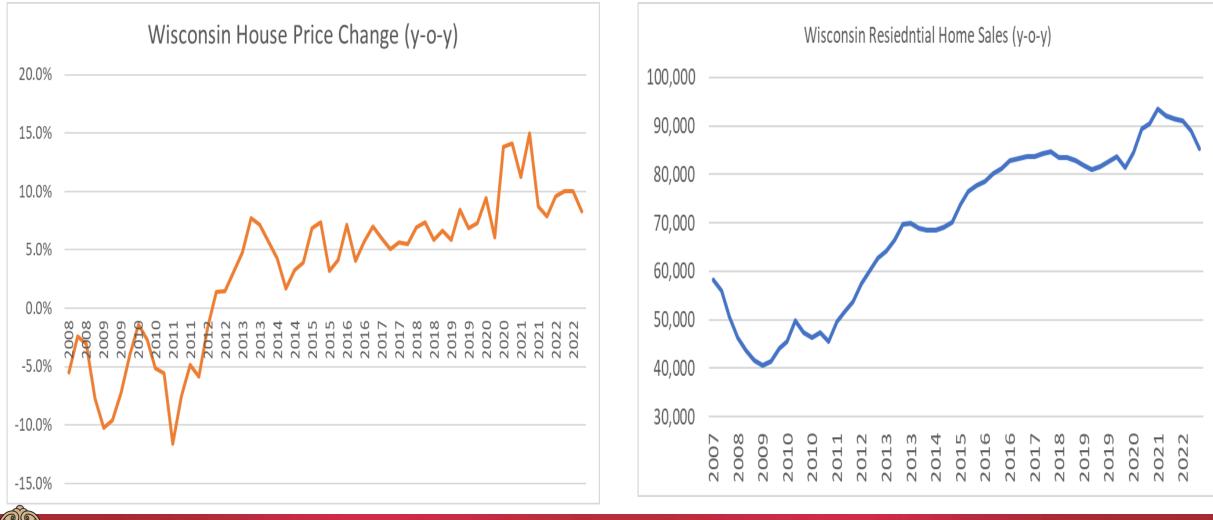


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Source: Wisconsin REALTORS Association October 2022 Wisconsin Real Estate Report and the Graaskamp Center.

.... Wisconsin price appreciation continues as home sales begin to flag





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Source: Wisconsin REALTORS Association October 2022 Wisconsin Real Estate Report and the Graaskamp Center.

.... year-over-year sales and new listings are a concern....

Summary of Wisconsin Housing Statistics				
	Monthly			
	Dec Dec %			
	2022	2021	Change	
Unit Sales	4,840	7,433	-34.9%	
Median Price	\$250,000	\$237,000	+5.5%	
New Listings	2,760	3,848	-28.3%	
Total Listings	12,606	15,335	-17.8%	
Months of Inventory	1.9	2.0	-5.0%	
Average Days on Market	73	75	-2.7%	
WI Housing Affordability Index	148	213	-30.5%	



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Source: Wisconsin REALTORS Association December 2022 Wisconsin Real Estate Report.

Multifamily Capital and Property Markets



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Dry Power – Real Estate Equity Raised

With Leverage Dry Powder For Equity Investments \$700 \$612 \$600 \$552 \$521 \$500 \$474 \$439 \$385 \$400 Billions \$343 \$337 \$300 \$200 \$100 \$0 2015 2016 2017 2018 2019 2020 2021 2022

Equity Investment interest in commercial real estate remains strong

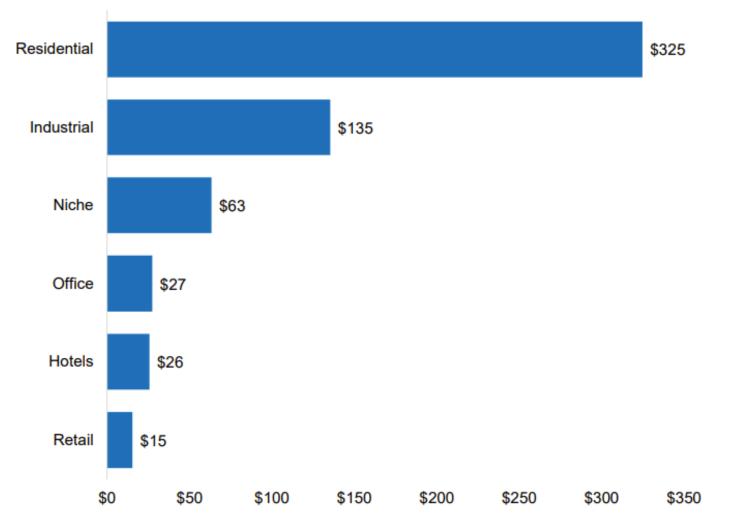


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JAMES A. GRAASKAMP CENTER for real estate Source: Newmark Research, "The National Industrial Market: Trends and Conditions," p. 58.

Dry Power – Real Estate Equity Raised

.... private equity
investment
interest remains
focused on
residential and
industrial property
types. ...

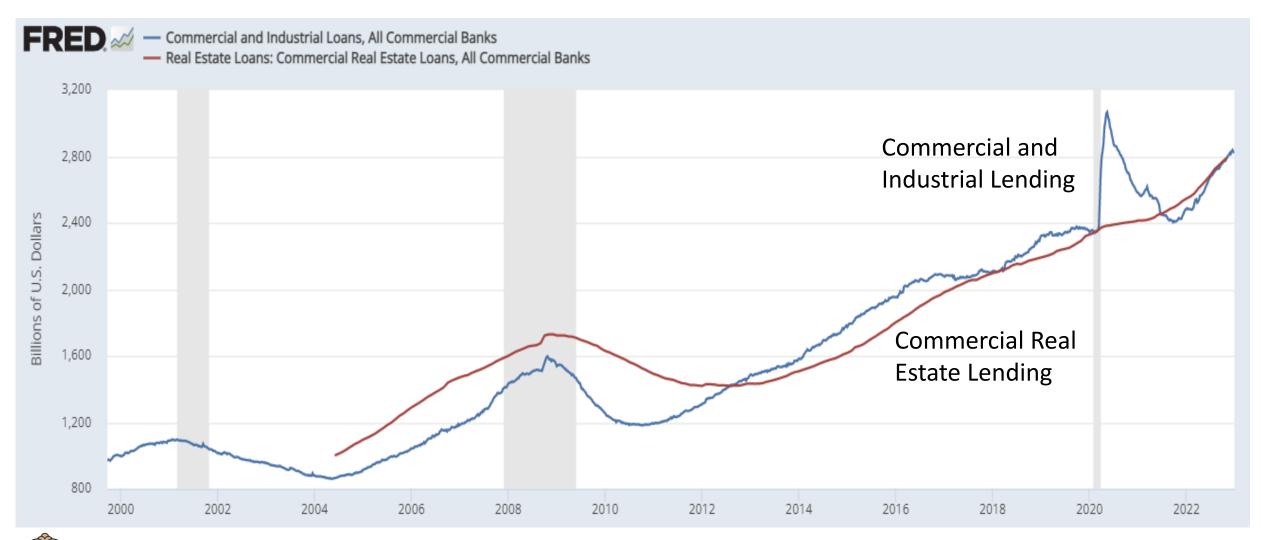




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JAMES A. GRAASKAMP CENTER for real estate Source: Newmark Research, "The National Industrial Market: Trends and Conditions," p. 58.

.... Commercial and Industrial and Commercial Real Estate lending marches on ...



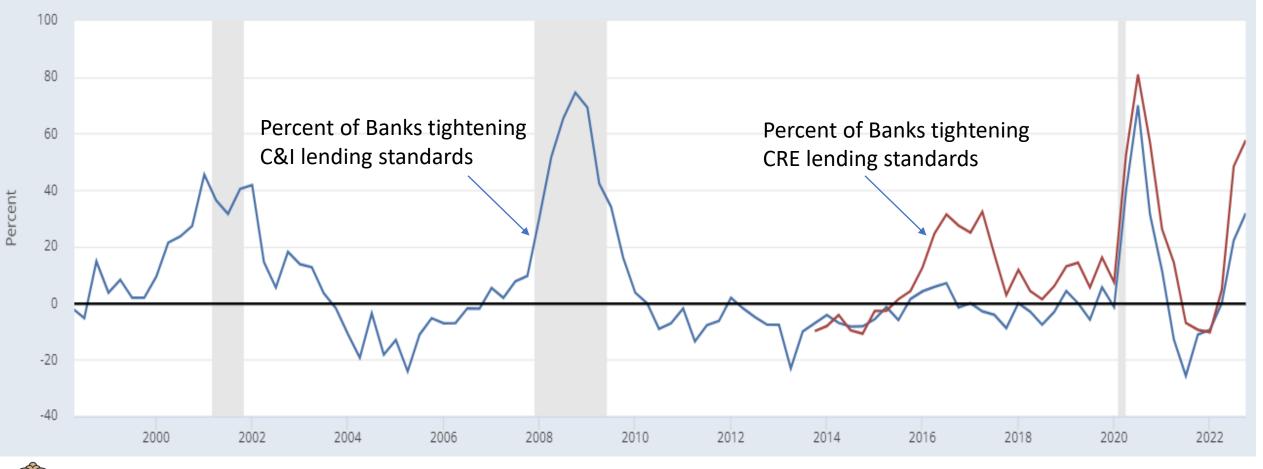


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Source: Federal Reserve Economic Data.

... however, bank CRE lending is tightening dramatically ...

FRED - Net Percentage of Domestic Banks Tightening Standards for Commercial and Industrial Loans to Small Firms
 Net Percentage of Domestic Banks Tightening Standards for Commercial Real Estate Loans with Construction and Land Development Purposes





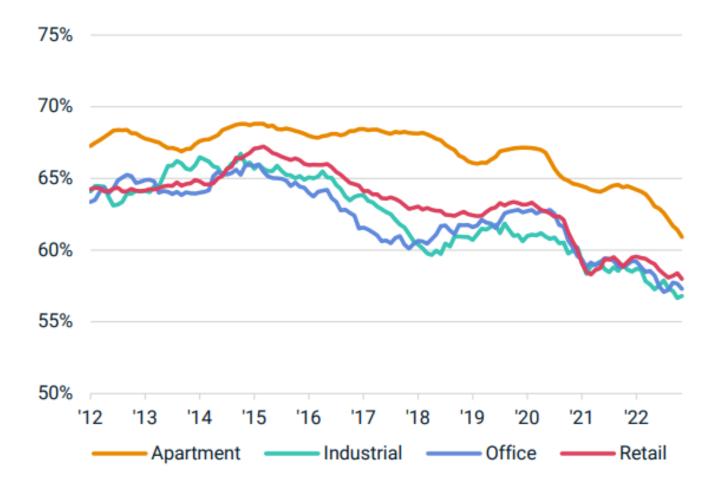
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Source: Federal Reserve Economic Data.

.... as interest rates increase, LTVRs are in decline

LTVs by Property Type

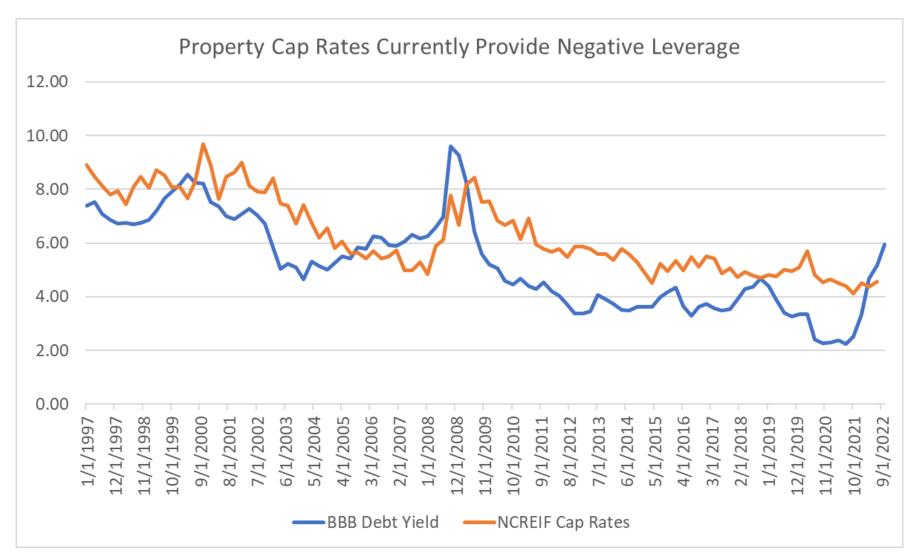




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Source: MSCI, "Capital Trends, Big Picture," November 2022, p. 3.

.... cap rates are now lower than BBB interest rates, a bad transaction omen

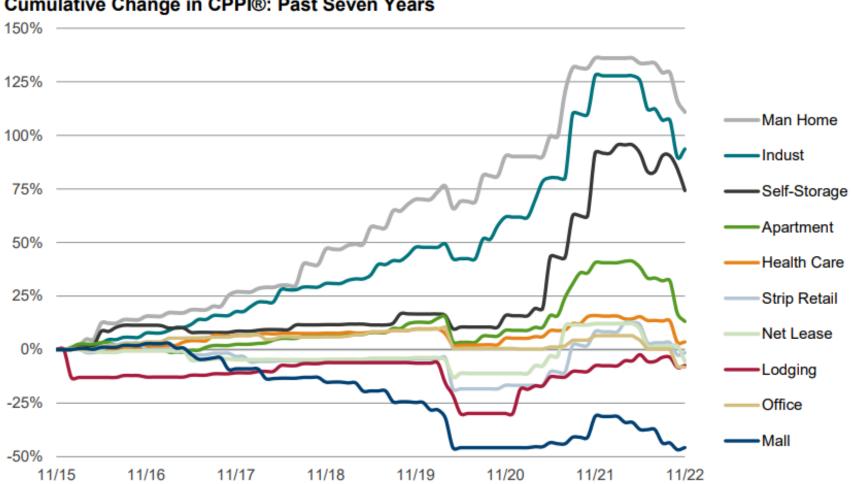


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Source: Federal Reserve Economic Data, NCREIF, and The Graaskamp Center.

Prices are falling fastest for property types with the best fundamentals . . .



Cumulative Change in CPPI®: Past Seven Years



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Source: Green Street, "Commercial Property Price Declines Slowing," December 6, 2022.

... price declines are broad-based ...

Green Street CPPI®: Sector-Level Indexes

	Index	Change in Commercial Property Values			
	Value	Past Month	Past 12 Mos	Recent Peak	
All Property	134.3	-1%	-13%	-13%	
Core Sector	134.4	0%	-16%	-16%	
Apartment	152.7	-3%	-19%	-20%	
Industrial	215.8	2%	-15%	-15%	
Mall	77.1	2%	-21%	-21%	
Office	97.9	0%	-14%	-14%	
Strip Retail	115.2	1%	-9%	-13%	
Health Care	134.9	0%	-11%	-10%	
Lodging	107.6	1%	0%	-5%	
Manufactured Home Park	289.2	-2%	-11%	-11%	
Net Lease	97.6	-7%	-16%	-16%	
Self-Storage	278.8	-6%	-9%	-11%	



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Source: Green Street, "Commercial Property Price Declines Slowing," December 6, 2022.

... interest rate hikes and construction costs accelerated the cost to own a home.

Cost of Homeownership versus Renting





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Source: CBRE, Multifamily U.S. Real Estate Market Outlook 2023

Multifamily Capital, Interest Rate, and Property Market

- Equity is sitting on the sidelines waiting for the bid-ask spread to narrow and for price discovery to begin
- Most debt providers are on the sidelines repricing loans, extending loans, and working with regulators
- Negative leverage is not sustainable, but expect greater interest rate movement down than cap rate movement up

SUMMARY: Expect a period of very slow transaction volume as the market goes through wide bid-ask spreads and then price discovery in the 2023Q2-2023q3



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