Is the Dallas Fed right to label this a housing bubble?

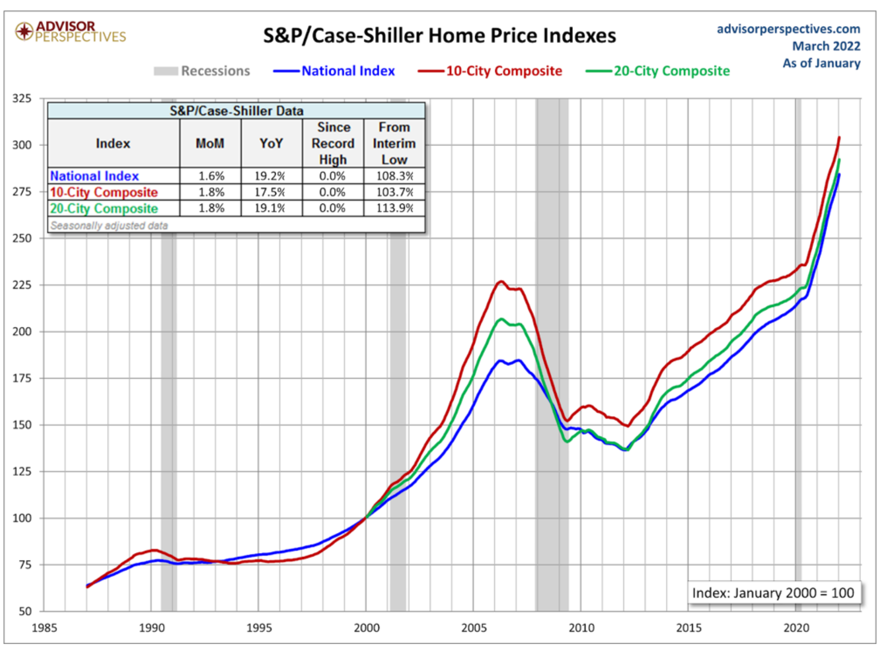
No, they're not, and their own data and statements prove this

Are we headed to a housing bubble? The **Dallas Fed** on Thursday published an article titled: Real-Time Market Monitoring Finds Signs Of a Brewing U.S. Housing Bubble. The online reaction was immediate — housing must be about to crash. I disagree with this conclusion. That's not to say that the data points the Fed used are incorrect — in fact, we *are* in a savagely unhealthy housing market, but it's not a bubble.

Let me explain.

First, because there is no speculative debt demand going on today, there can't be a housing bubble. We aren't anywhere close to the housing bubble dynamics we had from 2002 to 2008; that environment is simply impossible to replicate.

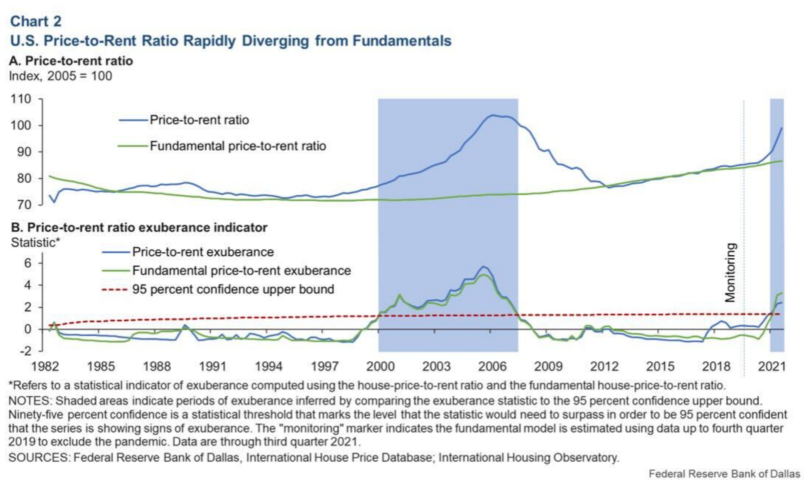
My rule of thumb has always been, if you're going to use the phrase housing bubble, you need to point to when the bubble started, because a bubble means that prices would fall back to some earlier point in time. For the housing bubble 2.0 crew, this would mean home prices would have to get back to 2012 in a short amount of time.



Home prices have grown 108.3% since the 2012 lows and that is the magnitude of decline we would need to see to justify using the term "housing bubble." The notion that educated homeowners with positive cash flow — who aren't showing any stress in making their low payments thanks to historically low mortgage rates — would sell at 50%, 60% to 70% off current values and go back to renting, doesn't seem realistic. Especially in a year when inventory has crashed to all-time lows and demand for those houses is still so high.

The people at the Dallas Fed aren't cheap professional troll artists with terrible housing YouTube crash videos, so what's going on? I'm going to take their talking points and explain in detail why this isn't the housing bubble of 2002-2005.

"**Our evidence points to abnormal U.S. housing market behavior for the first time since the boom of the early 2000s. Reasons for concern are clear in certain economic indicators—the price-to-rent ratio, in particular, and the price-to-income ratio—which show signs that 2021 house prices appear increasingly out of step with fundamentals."**



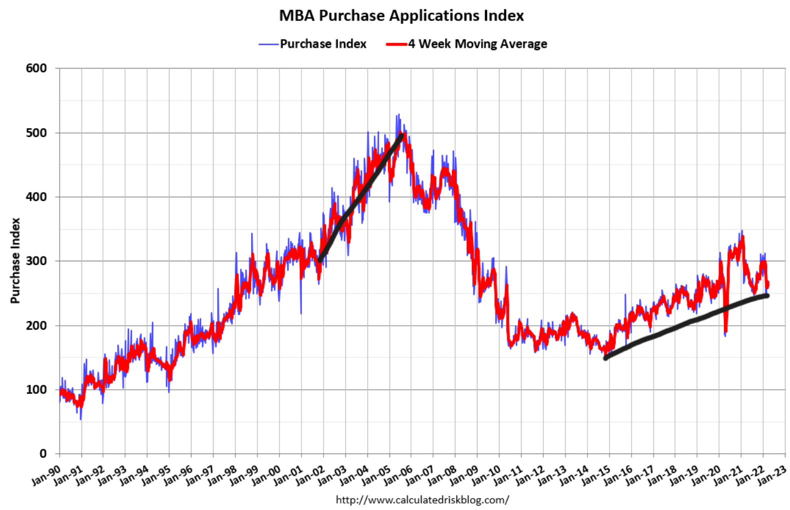
I agree with this statement and they're actually calmer about it than I am. I went from calling this an unhealthy housing market to a savagely unhealthy housing market because of price growth. I set a cumulative price growth model of 23% for five years. This got smashed in two years, and inventory levels broke to all-time lows this year. So, for me, I need pricing to be flat to negative this year, next year, and in 2024 just to keep that 23% price model in check. They're just highlighting what I have been saying for some time: home price growth is too hot.

In reality, the Dallas Fed and I may have different talking points, but we are saying the same thing: home price growth is too hot. But, importantly, home prices getting too hot doesn't create a bubble. A housing bubble does have robust demand, but it's speculative demand. Once the drivers of that speculation fall out, demand just collapses. Today, people aren't buying homes because they are speculating that home prices will increase double digits each year, they're simply buying a home to live in for a long time.

"**Based on present evidence, there is no expectation that fallout from a housing correction would be comparable to the 2007–09 Global Financial Crisis in terms of**

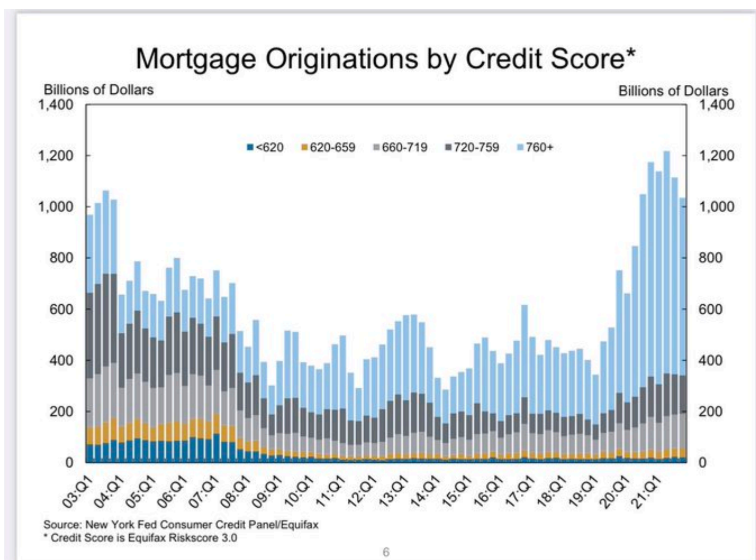
magnitude or macroeconomic gravity. Among other things, household balance sheets appear in better shape, and excessive borrowing doesn't appear to be fueling the housing market boom."

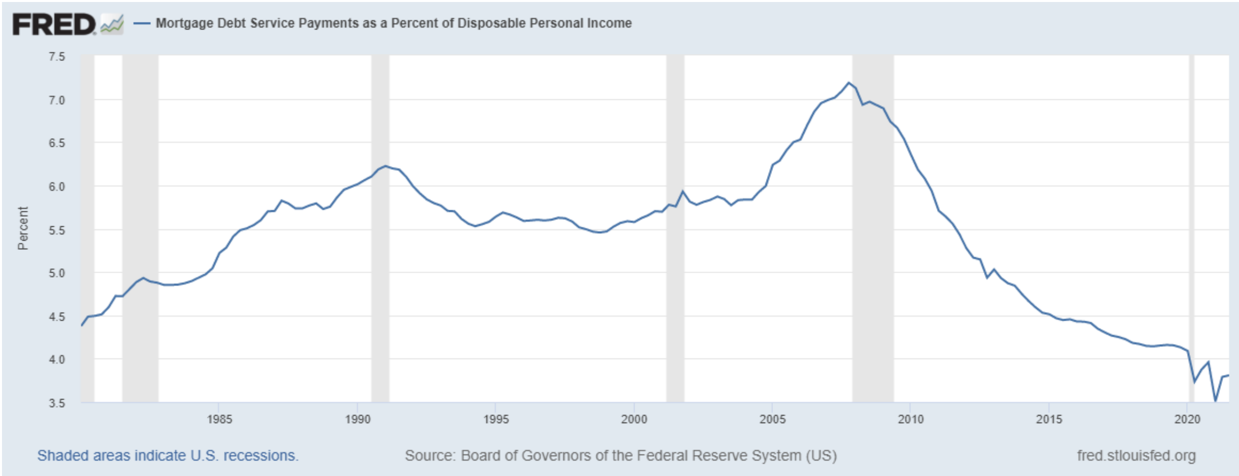
Given the above statement about homeowners' balance sheets and the fact that we don't have excessive borrowing, the headline about a housing bubble brewing is an overreach until we see those factors come into play.



Over the years, I have tried to express that we won't have a repeat of 2002-2005 when it comes to a speculative mortgage debt expansion on unsound credit. Instead, homeowners have the best financial profile in America's history. This is why I like to show the MBA mortgage purchase application chart. Yes, it had a 1% growth week to week, but as you can see, even with this week's data, we aren't seeing a credit boom in America. The speculative debt boom we saw from 2002-to 2005 can't be repeated with the current lending standards in place. This is a good thing, it protects us well in downturns.

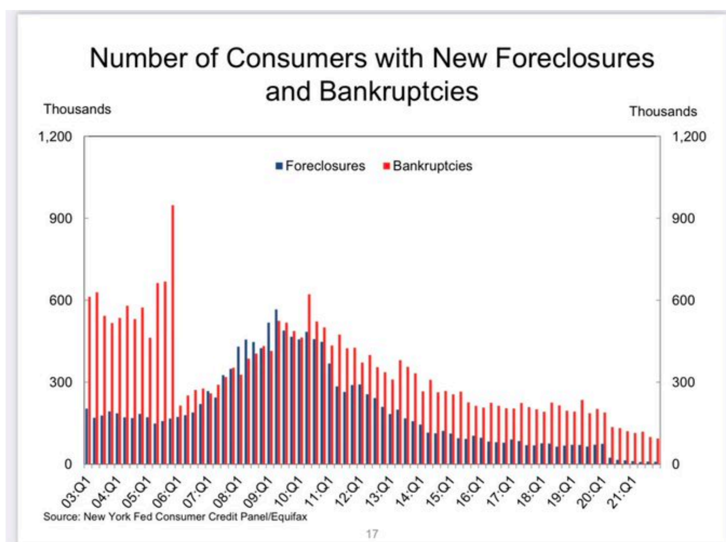
Remember that the forbearance crash bros got it so wrong because they never took into account the balance sheets of American households, which are fantastic. Fixed low debt cost with rising wages creates better cash flow





Post-2010, the lending standards have been great — we made American mortgage debt great again! In the past, the speculative credit boom led to people filing for bankruptcies and foreclosures in 2005, 2006, 2007 and 2008. Then after all that, we had the great recession.

Things are much different this time around. When you have a great credit profile, you don't see a surge in credit stress right before the recession.



Another important long-run anchor—tied directly to housing affordability—is the ratio of house prices to disposable income. Chart 3 shows dates of episodes of exuberance for this measure of housing affordability. These data—unlike our previous metrics—do not yet display evidence of explosiveness in the third quarter of 2021. But the rapid increase in the statistic close to the threshold during 2021 indicates that U.S. real house prices may soon become untethered from personal disposable income per capita.

I believe the Dallas Fed is really stating the obvious here that home prices have gotten too hot lately and we need to be mindful of this. Of course, I've been saying we need higher rates to cool down the marketplace. I don't see anything wrong here with what they're saying or the models they're using. Heck, I am talking about using credit controls if higher rates don't calm down-home price growth, so in that way, the Dallas Fed is much more diplomatic than I am. But again, rising prices by themselves don't lead to a bubble, you need excessive speculation, as they have noted.

All in all, I liked the piece from the Dallas Fed and I believe people should read it. Many people might come away with different takes, but I came away with one take, which is the same thing I have been saying: The housing market has gone into a savagely unhealthy stage because inventory is too low and the forced bidding action is creating too much price growth.

Sometimes people see a headline with the word bubble in it and everyone goes straight back to 2008. Well, 2008 wasn't really about 2008, it was the marketplace from 2002 to 2008, which clearly is something we don't have right now in housing. I believe the Dallas Fed explained that to a small degree.

Each economic cycle is unique with its own set of new variables. Of course housing in the years 2020-2024 means something to me because it's been a period of time that I have been focusing on. Of course, nothing goes as planned: COVID-19, the Russian Invasion of Ukraine and the lack of goods to build homes in a timely manner are all new variables. We just had to take the data one day, one week, and a month at a time and try to find out where the market is going. Right now, that's not a bubble.