Housing market shows 2 of 3 bubble components, but economists still won’t say bubble

Economists are still debating whether the U.S. is facing a housing bubble, according to a new Fortune article. Journalist Lance Lambert breaks down the three components of a “textbook definition” of a housing bubble: exuberant demand, spiking home prices well above what incomes can support that hit overvaluation levels, and finally a housing bubble that pops, driving home prices down.

Lambert says that every quarter, Moody’s Analytics calculates an “overvalued” or “undervalued” figure for around 400 markets to find out whether fundamentals, including local income levels, could support local home prices.

Trouble comes when we reach the overvalued level, he says.

In the first quarter of 2020, Moody’s estimated the median U.S. regional housing market was “overvalued” by just 2.1%. Over the past year, U.S. home prices are up 20.4% while private sector wages climbed 4.8%, “the perfect recipe for housing overvaluation to return,” according to the article.

In the first quarter of 2022, Moody’s estimated the median regional housing market was “overvalued” by 23%, a 20.9 percentage point jump in two years, which is why housing economists are on high alert, Lambert says.

Speculation has also jumped, which is another sign. Investors’ purchases of single-family homes hit an all-time high of 28% earlier this year, the article said, and Redfin found investor purchases were up this year in 31 of the 33 major housing markets it measured.

And, Lambert says, you can’t get a housing bubble without speculation and FOMO.

However, the article says, we’re still missing the bust component. This time there was no subprime lending boom, and the combination of tighter lending standards and healthier balance sheets should, according to many industry insiders, prevent a housing correction from turning into a housing crash, Lambert said.