



# The Impact of Higher Rates and Inflation on Home Price Appreciation

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With the recent increase in the 30-year mortgage rate, housing investors are seeking to understand the impact of rising rates and inflation on home price appreciation (HPA). Unison Investment Management has examined historical rising rate environments and the effect on HPA, which we highlight in the Summary of Findings section below.

## Factors Influencing HPA

- Housing inventory remains constrained, and building material inflation and supply chain issues have slowed the pace at which builders can increase inventory.
- Demand may temporarily slow a bit, but the largest cohort of home buyers (Millennials) are reaching peak home-buying age and are buying into supply-constrained markets.
- Supply is further constrained by baby boomers retiring in place in contrast to previous generations.
- Historically, wages have outpaced inflation even in the highly inflationary decade of the '70s.
- Recent very low unemployment is driving wage growth.
- These effects are particularly acute in densely populated urban areas with diversified economic drivers of local GDP.
- Mortgage rates remain historically low.

## Historical Lookback

- From 1970 to 1980, inflation and rates rose quite dramatically — it was also a period of substantial home price growth.
- Rates have been decreasing reasonably consistently from 1980 to the present, but there have been periods of increases.
- HPA has been persistently positive during those periods, except for the GFC as this period of decrease was driven by poor underwriting standards and increased leverage by borrowers.
- Although the cost of money increased during those periods, the dynamic of housing supply and demand, with a consistent increase in wages, supported housing prices.







## Summary of Findings

- The Fed's increase in rates is intended to cool inflation — as the impact of that is felt, the housing market is likely to find a more natural supply/demand balance and long-term appreciation.
- Higher inflation will likely increase wage growth, which could offset the increase in debt service.
- In particular, home prices increased substantially during the very high rate and inflation period of the late '70s and early '80s.
- Residential Real Estate is the largest US asset class and historically there has been a positive correlation between a rise in mortgage rates and higher inflation with home price appreciation which is manifested in the fact that housing and housing-related expenses are close to 40% of CPI.
- Analyzing the last 51 years, when mortgage rates increased by more than 0.25% or CPI by more than 4%, home prices appreciated by 4.49% annually on average.<sup>1</sup> If we further limit the scope to the years with rising mortgage rates and severe inflation, such incidences were often accompanied by the higher-than-average home price appreciation.

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1. Home Price Appreciation: S&P/Case-Shiller U.S. National Home Price Index. Sample period: Jan 1987 to Feb 2022. Source: FRED, Mortgage Rates: 30-Year Fixed, CPI: Consumer Price Index for All Urban Consumers

Additional supporting data can be found on Unison Investment Management's website in the "Whitepaper" section under the report name "The Impact of Higher Rates and Inflation on HPA" <https://www.unisonim.com/white-papers>.

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