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DAVID STARK

PRESIDENT
Stark Company Realtors®

NEW TREND? TOO EARLY TO TELL

Three months ago, we speculated that perhaps we were starting to see the first glimmers of change to the low-inventory/high-demand market of the past four years. We based our thoughts on the preliminary, yet provocative, data we had at the time. We were anxious to see how the summer played out, with hope that more clarity would come by the end of the third quarter. Unfortunately, we must report that as of this writing, clarity has remained elusive. While many of the forces we identified in July are still with us, the data is far from conclusive as to whether the market is starting to move back to equilibrium.

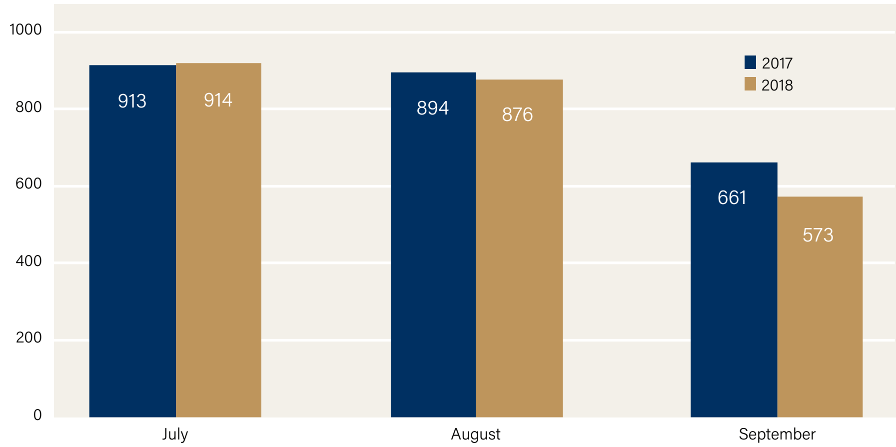
REAL ESTATE MARKET SOURCE
OF SOUTH CENTRAL WISCONSIN

THERE ARE STILL SOME STRAWS IN THE WIND, but we can't say for sure if there's a storm behind them. Like the rainy weather we've had for the last 45 days, it seems like the market has settled in, and we're not sure when it's going to move out.

On the whole, home closings for the third quarter played out much like the second. July closings were virtually identical in number to July of 2017. Then, we saw a relatively small two percent drop in August followed by a substantial 13 percent drop in September. Overall, third quarter closings were down over four percent from last year; down only a little over one percent year to date. What's interesting is the uneven pace of sales month by month.

We've seen this pattern all year. Offers in March and April were exceptionally strong, then seemed to die off in May and June. That's what led us to hypothesize last quarter that *something may be changing.* Then, just as suddenly, July and August picked up again and offers were robust. September started out gangbusters until mid-month, when activity died again. What looked like an up month on the fifteenth turned into a slightly down month by the end.

DANE COUNTY CLOSINGS IN THE THIRD QUARTER



Total Dane County homes sales for 2018 remain nearly on pace with this time last year. However, third quarter sales mimic the pattern we saw in second quarter—a strong first month, a small decline in the second month followed by a drop in the third month.

This inconsistency is largely responsible for the confusion over exactly what's happening. It's been difficult to identify clear trends when the market seems to suddenly ebb and flow without warning or apparent reason. Given we're approaching the season when activity is normally at its lowest, we'll have to wait out the next three months before we can start to see how the 2019 market will behave. For now at least, we can review the major forces in play to see how they're setting up as winter approaches.

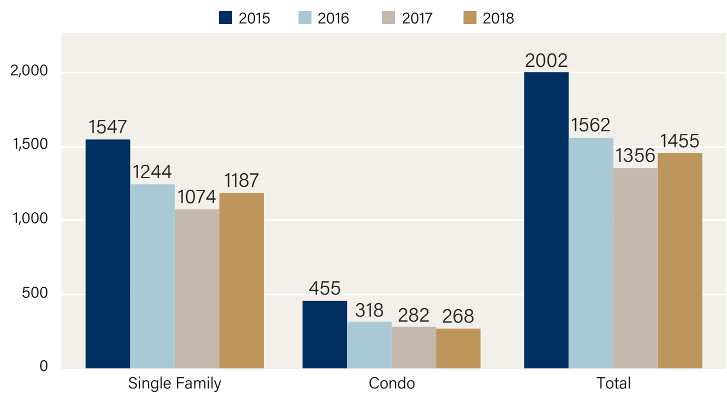
MORE HOMES ON THE MARKET?

It's virtually impossible to write about today's real estate market without at least mentioning inventories (the number of homes for sale on the market). There is perhaps an interesting development here that bears watching. For the first time since the end of the recession, inventories at the end of the third quarter were *up* from the same time last year. (See chart on page two.) The increase was all in single family homes, where inventories were up ten percent from last year. Condo inventories continued their slow decline, down about five percent.

We think the increase in single family inventory may be significant. The fact that it breaks the relentless trend downward that we've seen since 2012 is itself worth noting. While not a huge jump, it's enough to get your attention. The cause seems to be twofold. First, of course, is the decline in September closings—not as many people bought houses. But more interesting to us is the fact that the number of *new* single family listings that came on the market in September was *up 11 percent* from last year. This also breaks a trend where the number of new listings was down pretty much every month all year. Until now. Will it continue? We'll be monitoring this closely to find out.

As we've discussed in previous editions, the shortage of housing inventory is a national phenomenon, not just a local one. The shortage of new construction both during and after the recession, coupled with baby boomers staying longer in their homes while the huge Millennial generation is hitting peak home-buying age are all contributors to a problem that won't quickly or easily be solved. It will be solved eventually, but it will take time. Our guess is that it will be a gradual movement over a couple years, rather than a sudden one. But it has to start somewhere, and perhaps this is the beginning.

DANE COUNTY THIRD QUARTER INVENTORIES



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PRICES STILL GOING UP

It comes as no surprise that prices continued to move upward in the third quarter. The Dane County median‡ rose another 1.5 percent over the past three months; up 5.6 percent year-over-year. Although significant, this is still less than the 7.2 percent increase between 2016 and 2017, and not much above the longterm market average of four percent. We predicted a slowdown in appreciation in our last edition, based on the slight decline in sales and upward pressure on mortgage rates (see below). With inventories perhaps starting to creep upward too, it would not shock us to see price increases moderate even further next year and beyond.

One of the primary drivers of price increases for the last four years has been multiple buyers bidding for scarce inventory. We were hearing stories that multiple offers were declining this summer, but we were unable to confirm it in the data until September, when the incidence of multiple offers finally declined for the first time.

Up to that point, multiple offers had been running well ahead of previous years. It's also possible that *the sheer number of buyers* bidding against each other, on each house, is lower than it was this spring. That instead of one house getting five competing offers, it's now only getting two. The MLS does not track the number of offers on each property; only whether there is more than one, so there's no real way to know.

That said, it feels like there is less pressure now. It should be noted that we're talking about closings here, which means that the offers themselves were negotiated 30 to 60 days earlier. That may explain why it took a while for this to show up in the data. If it continues through the winter, we may have another sign of change on our hands.

INTEREST RATES

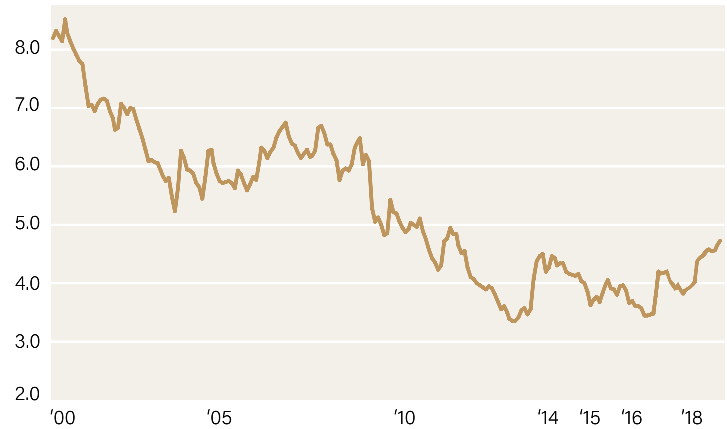
This is another topic we can't seem to avoid discussing. As before, the pressure on mortgage rates is decidedly up. While the latest Freddie Mac data shows the current average 30-year rate at just over 4.7 percent, we've seen individual lenders occasionally quoting five percent as of late. On October 5, *Mortgage News Daily* was quoting the average 30-year rate at 5.02 percent. It appears that the forces keeping rates lower than expected—for longer than expected—have finally turned.

These forces are well known. It starts with the Federal Reserve, which has been raising its benchmark rates as well as curtailing its mortgage buying for a couple of years now. But it's not just the Fed. Extremely strong economic growth, record low unemployment and the appearance of rising wages, is leading to potentially higher inflation, which pushes rates up. Add in increased government borrowing needs, and the upward pressures on interest rates are clear. The 10-year treasury bond, which exerts the greatest influence on mortgage rates, recently moved above three percent for the first time since the recession. Finally, the normalization of interest rates is at hand.

We've been asking our agents to what extent their buyers have been sensitive to the rise in rates. So far, it appears that buyers remain unconcerned. This is good news, and is what we'd expect. As we discussed before, upward movement in rates is both inevitable and ultimately desirable. When interest rates are too low for too long, inflation gets too hot. Then, housing prices rise too far and too fast. Our housing market, and the economy in general, will be far more stable with rational market rates. And, as the accompanying chart shows, mortgage rates remain a bargain by historical standards. The only concern we've had was with regard to the pace of the increase. If rates were to move upward too quickly, it might put off potential buyers and slow the market unnecessarily. Fortunately, the movement in rates has been gradual, and buyers appear to be taking it in stride.

It's our opinion that increasing rates will cool price increases rather than put a damper on activity. To date, it seems to be playing out exactly that way. We're looking forward to seeing where rates are when the spring market opens up next year. If we could dictate how this should play out, we'd like to see any further increases take place over the next couple months, and then remain steady for the first half of 2019. If that is indeed how it happens, we should be in good shape going into next year.

30-YEAR MORTGAGE RATES, 2000-2018



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SUMMING UP

We thought the third quarter would bring us more clarity on where the market is headed, but unfortunately it didn't. Change may be in the air, but the signals are mixed, and the way forward is uncertain.

Be that as it may, we remain confident that our local housing market continues to rest on very strong footing. With record low unemployment, vigorous economic growth nationally, and a burgeoning local economy that is starting to gain national attention, there is nothing to suggest that we won't have another near record year in 2019.

Buyers and sellers should both bear this in mind as they finish out 2018 or begin to plan for next year. Regardless of the subtle changes in market dynamics, the underlying fundamentals remain very strong. It looks like another busy year ahead.

ADVICE FOR BUYERS

This is a great time of year to be a buyer, if it works for you logistically. You have far less competition, and the buying process is much more enjoyable if you're the only party negotiating. Unfortunately, we can't yet say for sure that you will be free of competition. We're still seeing multiple offers for great listings in desirable areas, so don't assume you have the field to yourself. Again, we reiterate our advice—don't just focus on new listings. That's where the competition is most likely to be intense. More homes are staying on the market beyond a few weeks. Look at those as well; there's nothing wrong with them. Also, it should be easier to know what price to offer. There are plenty of recent comparable sales your buyer's agent can show you to help judge value. Don't expect prices to move as much over the next couple months. If you can buy before the holidays, you'll also get the best mortgage rates.

ADVICE FOR SELLERS

People tend to overreact to the idea of the 'slower' season, as though there's nothing happening. There's still good activity in the fall, just less of it. The trickiest part for you now is figuring out where to price. Sellers priced very aggressively this year, and some were rewarded while others were not. Now, with inventories creeping up along with mortgage rates, it's harder to say you'll be successful if you reach too high.

The average home still sells for a bit less than list price, and now that we're into fall, buyers will be a little pickier. Our advice would be to have your agent do an absorption rate analysis for your neighborhood, and price in the front of the line if you can. In other words, be the listing everyone wants, not the one they pass over. If you get some buyers competing, you might do better than you expected.

DANE COUNTY

	Single Family			Condominiums			Total Residential		
	2018	2017	2016	2018	2017	2016	2018	2017	2016
3rd Quarter Closings*	1836	1851	1850	527	569	556	2363	2420	2406
Year-to-Date Closings	4826	4912	5027	1402	1422	1437	6228	6334	6464
Active Inventory	1187	1074	1256	268	282	353	1455	1356	1609
Months of Inventory†	2.3	2.1	2.4	1.8	1.9	2.4	2.2	2.1	2.4
12-Month Median‡	295,000	279,900	260,000	195,000	182,650	165,400	275,000	260,500	243,000

SAUK & COLUMBIA COUNTIES

	Single Family			Condominiums			Total Residential		
	2018	2017	2016	2018	2017	2016	2018	2017	2016
3rd Quarter Closings*	472	481	466	69	65	57	541	546	523
Year-to-Date Closings	1209	1174	1223	175	176	137	1384	1350	1360
Active Inventory	439	535	704	86	77	134	525	612	838
Months of Inventory†	3.4	4.1	5.3	4.6	4.2	9.0	3.5	4.2	5.7
12-Month Median‡	192,000	175,000	168,250	169,000	150,000	152,500	189,000	172,000	165,900

*Sales reported to the South Central Wisconsin Multiple Listing Service (SCWMLS) with closing dates between 7/1/18 and 9/30/18. †Months of Inventory represents the number of months it would take to sell the entire active inventory at the pace of sales for the most recent 12 months. A six-month inventory is considered balanced. ‡When all properties sold during the period are ranked in order of price, the median is the price of the home in the exact middle. The above sales figures herein are based on data supplied to the SCWMLS Corporation by its Participants. The MLS does not guarantee and is not responsible for its accuracy. Data maintained by the MLS does not reflect all real estate activity in the market. Data presented here was generated from the SCWMLS on or before 10/10/18. This is not intended to solicit existing listings.