

HIGHLIGHTS

2001 Average Implied Annual Growth 7.8 Percent

Annual Growth for 2000 Represents Highest Rate in Two Decades

The second quarter 2001 HPI data indicate that house price growth in the first 2 quarters of this year remains quite rapid (7.8% at an annual rate) but has slowed from last year's faster rate of 9.5%¹. The increase last year is the largest since the 1970s, a period of much greater general price inflation. Signs of incipient economic weakness, such as stock market declines throughout the latter half of 2000 and into 2001, have apparently had little impact on the healthy housing market. In fact, until this Spring, housing markets continued to gain momentum as more signs of economic weakness appeared. Lower mortgage rates are partly responsible; eventually however, changes in other fundamental determinants of housing prices, such as income and consumer expectations also affect house price growth.

While many variables impact housing price growth, the relationship between housing prices and income is straightforward and reasonably good data is available for tracking purposes. On the other hand, for example, data that measures consumer expectations regarding future housing inflation is not readily available from a reliable source. For simplicity we illustrate the movements in housing prices consecutively with personal income over the past 6 years². A reasonably clear pattern emerges. Both housing prices and income rose in recent years. A strong economy is reflected in peak growth rates of both housing prices and income in 2000. Income growth in 2001 has declined substantially since end-year 2000, and housing prices are also growing less rapidly than in 2000.

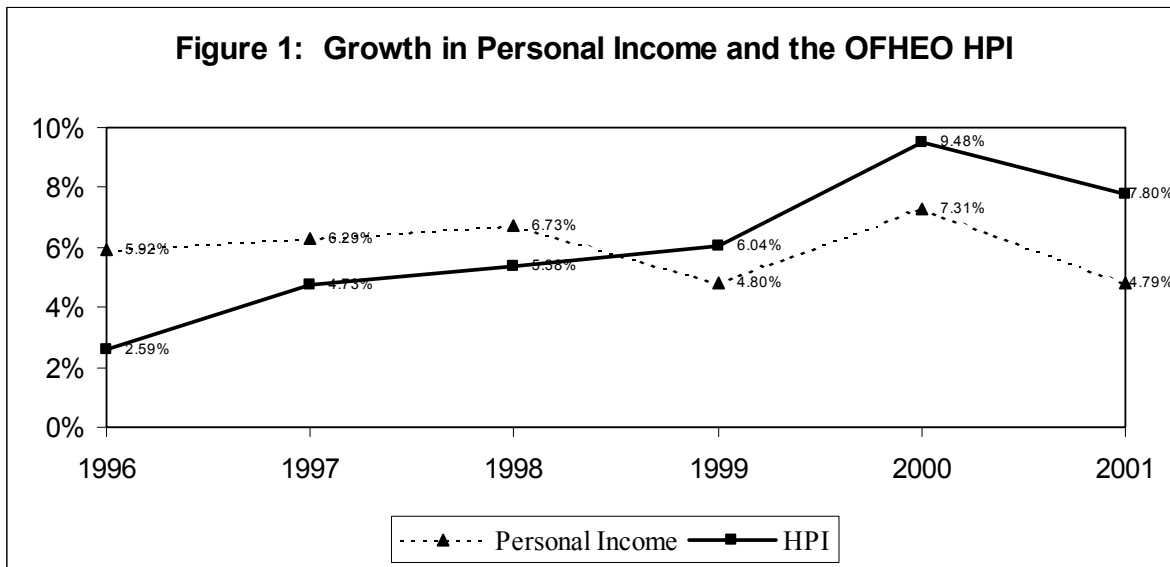
Interestingly, in the earlier years, income grew more rapidly than housing prices, as housing prices struggled to revive from their early- and mid-1990s slump. Eventually, housing price growth caught up to and surpassed income growth in 1999, and the gap has been growing since that time. Generally, this gap should not persist, as new supply eventually drives down housing price responses to income changes. However, while we see lower housing price growth in 2001 than in 2000, we also see a rising gap between house price and income movement. When compared to changes in income, price growth is still remarkably strong. A growth rate of 7.8 percent in the presence of a 4.8 percent increase in

¹ The addition of new historical data with each release of the OFHEO HPI results in revisions that are most pronounced in the most recent quarters. The annual rate of 9.5 percent is the revised figure for the end of 2000, and is higher than that reported in the 4th Quarter 2000 HPI Report.

² Quarterly personal income is available from the National Income and Product Accounts and is distributed through the Bureau of Economic Analysis. The data is obtained from www.bea.gov. The growth rates reported are calculated consistently with HPI growth. That is, the rates for each year up until 2000 are percentage changes measured from 4th quarter to 4th quarter. The rate reported for 2001 is the implied annual rate obtained from the average of the first 2 quarters.

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income illustrates a continued strong propensity for individuals to choose to consume housing over and above many other goods or investment vehicles. This is also clearly exemplified in the fact that the index of the costs of other goods for the same time period (averaged over the first 2 quarters of 2001) was only 3.7 percent³.



³ The price index of other goods is obtained from the CPI Less Shelter, and is available from the Bureau of Labor Statistics at www.bls.gov.