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Grieving the Loss of Pandemic Mortgage Rates: Will We Reach the 'Acceptance' Stage?

Even though rates appear to have peaked, no one is predicting they'll get a lot lower

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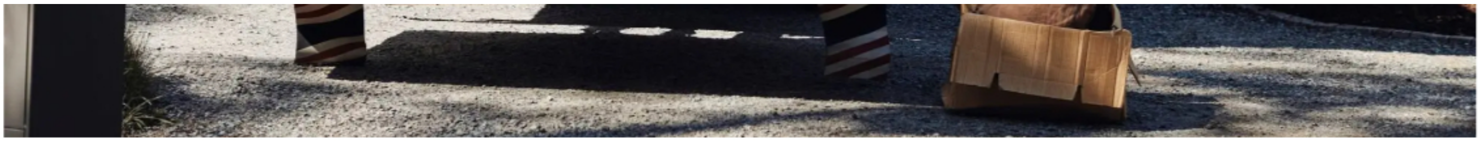

Economists say Americans have to come to terms with the fact that we're not going back to 3% mortgage rates. Maskot/Getty Images

When mortgage rates fell to record lows during the pandemic, most people who could take advantage did, stomaching rapidly rising property values in order to get in on the financing of the century.

But then rates more than doubled — nearly tripled at one point last month — stunning would-be homebuyers and in many cases pricing them right out of the market.

Now, even though rates are edging down from their recent peaks (the average 30-year rate dipped from 7.29% last week to 7.22% this week, according to Freddie Mac) it doesn't look like rates will drop significantly for quite some time. So the question is, what will it take to bring buyers back now that real estate sales have stalled?

Yelena Maleyev, a senior economist at KPMG in Chicago, said in some sense, potential buyers must grieve before they come to accept that the pandemic created a very unique circumstance that has now passed.

"We are not going back to the era of 3% mortgages," Maleyev said. "People will come to terms with the new normal, but it's going to take some time for them to go through the grief cycle."

Then what is the magic number and when, if at all, will we get there?

Will buyers require a measurably lower monthly payment or do rates just need to feel lower after such a big spike? And are expectations changing as more people come to terms with what economists have started calling a "higher for longer" projection?

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Maleyev says we may see rates dip below 7% next year, and that should be enough to get the market moving again. Others say the magic number is lower — no higher than 5.5%, according to John Burns Research & Consulting, which surveyed renters and homeowners in August and September.

Pandemic rates may have especially spoiled Americans, but it's been over two decades since 30-year rates last averaged over 7%. In fact, before this recent spike, they'd barely even topped 5% since 2010.

That's why financing a home today may require a level of acceptance, which comes after denial, anger, bargaining, and depression in Swiss psychiatrist Elisabeth Kübler-Ross's famous theory on the five stages of grief.

Rates have risen as the same Federal Reserve that big-footed the mortgage market to support an economy shaken by COVID-19 in 2020 reversed course in 2022, aggressively raising its benchmark interest rate in a deliberate attempt to slow the economy and cool out-of-control inflation.

And even though many expect the Fed to start lowering that benchmark sometime next year, most economists aren't predicting significantly lower mortgage rates for the foreseeable future.

Fannie Mae, which buys mortgages from lenders, projects that the best we can expect is 30-year rates averaging 7.1% by the end of 2024 and 6.8% by the end of 2025. Realtor.com says we'll see 6.5% a year from now. The Mortgage Bankers Association has one of the least conservative forecasts, estimating 6.1% a year from now and 5.5% in two years.

"Longer-term interest rates will gradually fall," said Charlie Dougherty, a senior economist at Wells Fargo, which expects rates to fall to 5.75% by the end of 2025.

Mark Zandi, chief economist at Moody's Analytics, said he thinks 6% would be "a key threshold for many potential buyers" assuming property prices don't go up much more and the economy avoids a recession. And that is fortunately "close" to what they can expect "through the economic cycle going forward," he wrote in a text message.

"Potential homebuyers should be patient and let rates come down," he wrote.

For people who already own a home, much of it comes down to the interest rate on their current mortgage. People who bought or refinanced during the pandemic can't sell their home without giving up their super-low rates, so they're staying put to avoid doubling their cost of borrowing.

“If you have a 3% mortgage rate, you don’t care what rates are doing right now,” said Skylar Olsen, the chief economist at the real estate website Zillow.

“But we find folks that have rates above 5% have updated their threshold” and would be willing to move if they could get a new rate in the 6% range, she said.

Here’s why. Let’s say Family A has been paying 3% on a $320,000 mortgage, having put 20% down on a $400,000 house. They’re paying $1,349 a month in principal and interest. If they were to move today and borrow the same $320,000 at 7.22% (assuming they use the home equity in their old house to offset a pricier house) their payment would go up $827 a month, to $2,176. That’s a big jump.

But compare that to Family B, who has been paying 5.5% on a $320,000 mortgage, or $1,816 a month. A move at today’s rates would add $360 a month to their costs, and if they held off for a 6.5% rate, just over $200 a month. Then the additional burden starts to feel more doable.

To be sure, no matter what the prevailing rate is, some real estate will always change hands because people can’t hold off on moves triggered by events like death, divorce, the birth of children and job changes.

And even if more buyers resign themselves to higher rates, we won’t see another buying craze like the one during the pandemic period — when the median sale price for a single-family home jumped more than $90,000 in just two years and more than 6 million homes sold in one year, the most since 2006.

“It’s likely that 2024 will present many of the same challenges the housing market faced in 2023,” Mark Fleming, chief economist of title insurer First American, said in a commentary. “If the 2020-2021 housing market was ‘too hot,’ then the 2023 market was probably ‘too cold,’ but 2024 won’t yet be ‘just right.’”

MORTGAGE RATES