MarketWatch

NORTHERN VIRGINIA
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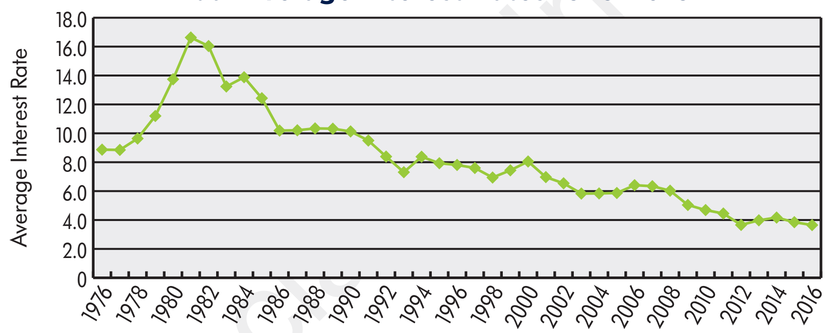
The Impact of Rising Mortgage Rates

It finally happened – after years of speculation and expectation, mortgage interest rates have climbed since the national elections in November.

During the past forty years, the interest rate for 30-year fixed rate mortgages has averaged 8.2%. From the beginning of 2000 through 2012, the average was just under 6.0%. But from early 2013 until mid-November of last year, rates averaged an astoundingly low 3.8%. It's a funny thing – when rates stay low for an extended period of time, people get used to them, and also tend to forget that they couldn't stay that way forever.

Annual Average Interest Rates 1976-2016



In the weeks after the election, rates moved from 3.5% to 4.3%, and have since floated between 4.0% and 4.2%. To be sure, mortgage interest rates are still very low, but potential homeowners have lost about 6% of their purchasing power in just a few weeks. The monthly principal and interest payment on a $400,000 mortgage in early November was roughly $1,800. A borrower getting that same mortgage today would pay $1,925.

So a big jump in a short time is a market killer, right? In fact, at least on the short term, exactly the opposite is happening. Many buyers who have been sitting on the fence have decided to purchase before rates go much higher. During the past three months, contract activity is up 12% compared to the same time period a year earlier. This uptick in activity may seem counterintuitive, but it is what we have always seen when rates rise.

From May to August 2013 rates jumped a full percentage point from 3.5% to 4.5% – but contract activity rose 13% from the same time in 2012 when rates averaged 3.6%. It is also likely that, given the recent action by the Federal Reserve Chair raising its target rate, mortgage rates will continue to trend higher through the rest of 2017.

We're not suggesting that rising rates are good for the real estate market, and there is no doubt that higher rates will price some out of the market and prompt others to lower their price point. Yet rising rates are not a huge negative either, at least in the short term. It is important to view these increases in a broader context. The fundamental reason that rates are climbing is that the national economy is improving. And that means household income is rising, the job market is improving and more people will be in a position to buy.

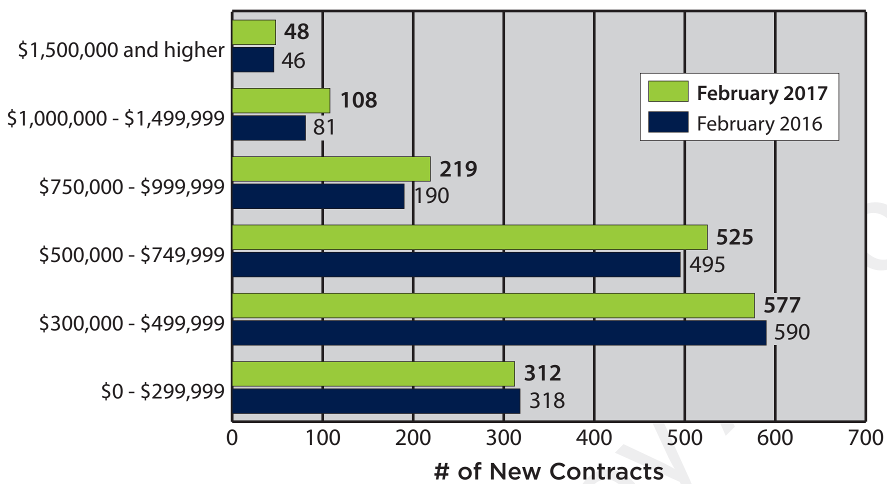
We'd like to offer one more bit of historical perspective. When John McEnearney opened the doors to our company in July 1980, mortgage rates stood at 12.0%. One year later they were 17.0%. That's right: 17.0%. And people still bought houses. To be sure, it was a lot tougher, but owning a home was just as important then as it is now.

FULLY AVAILABLE LISTINGS
Northern Virginia - February 29, 2016 vs. February 28, 2017

FULLY AVAILABLE LISTINGS

- The month-end inventory **decreased 12.2%** February 2017 compared to February 2016 – but the number of homes coming on the market **increased 5.8%**.
- Inventory is down for homes priced less than $750,000.
- **31.3%** of all homes on the market have had at least one price reduction since coming on the market.
- In February 2016, 33.0% of all homes on the market had at least one price reduction.

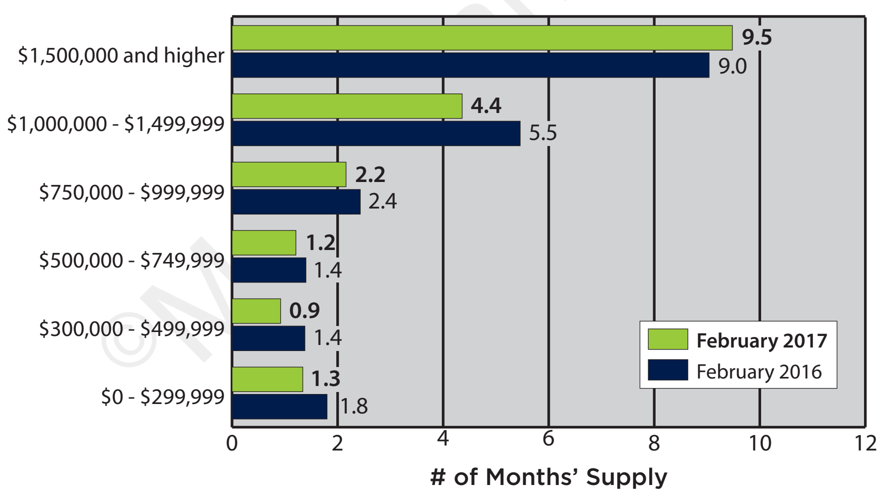
NEW CONTRACT ACTIVITY
Northern Virginia - February 2016 vs. February 2017



CONTRACT ACTIVITY

- The number of new contracts ratified in February 2017 was **up 4.0%** from the number of contracts ratified in February 2016, and was up for the top four price categories.
- Contract activity year-to-date is **up 8.6%**.
- **19.3%** of all homes going under contract in February 2017 had at least one price reduction before going under contract. Last February it was 27.1%.

MONTHS' SUPPLY
Northern Virginia - End of February 2016 vs. End of February 2017



MONTHS' SUPPLY

- The overall supply of homes on the market at the end of February was **1.7 months**, which was a **decrease of 15.6%** compared to the end of February 2016, when supply stood at 2.0 months.
- Price category supply ranges from a low of 0.9 months for homes priced between $300,000 and $499,999 and a high of 9.5 months for homes priced $1,500,000 and higher.

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