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Current housing bubble could take 2 paths, and both are nasty

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So when's the Fed going to start buying up millions of homes?

Assuming the answer is “it’s not,” Charles Hugh Smith of the Of Two Minds blog says prices are going to get hit hard across the country.

The latest data would hardly derail his gloomy outlook.

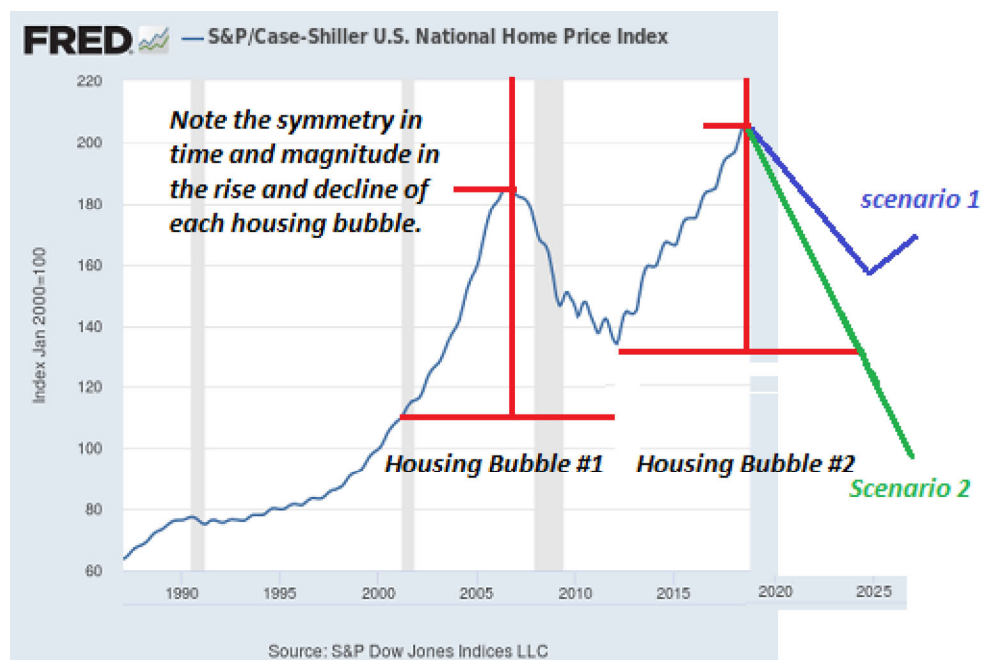
The S&P CoreLogic Case-Shiller 20-city index shows home price growth is screeching to a halt. The gauge rose 0.2% in December vs.

November and 4.2% from year ago – the slowest pace of annual growth since 2014.

Smith said that bursting bubbles tend to follow a symmetrical reversal in terms of time durations and magnitudes of their initial rise.

“If the bubble took four years to inflate and rose by X, the retrace tends to take about the same length of time and tends to retrace much or all of X,” he wrote.

He used this chart of the Case-Shiller Housing Index as an example:



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Smith explained that the Fed, by dropping interest rates to near-zero and buying mortgage-backed securities, didn't allow the first bubble on the chart to run its course. This time around, however, there are “no more saves in the Fed's locker,” he warned, adding that this decline will start this year and end around 2025.

But which path will it take?

Smith said the more realistic analysts out there would at least agree that *some* declines in prices is a possibility and that it would look like the milder scenario.

That's now how he sees it, though.

“There is a good case for scenario 2, in which price plummets below the 2012 lows and keeps on going, ultimately retracing the entire housing bubble gains from 2003,” he said, laying out several factors, such as massive student debt, insufficient income to support nose-bleed prices, the exit of Chinese buyers, etc.

“The economy has changed, and the sacrifices required to buy a house in hot markets at today's prices make no sense,” Smith concluded.

“The only question of any real interest is how low prices will drop by 2025. We're so accustomed to being surprised on the upside that we've forgotten we can be surprised on the downside as well.”

Related video: U.S. Housing Market 'Bruised But Not Broken' (provided by Bloomberg)

