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2017 Residential Real Estate Market Forecast

North Bay Residential Real Estate Market is Decelerating and Showing Signs of Fatigue

The residential real estate market in the North Bay counties of Marin, Napa and Sonoma is decelerating and showing signs of fatigue after five consecutive years of growth, according to a recent survey from Terra Firma Global Partners, a residential real estate services firm with nine North Bay offices.

Using the most common metrics to measure the markets, single-family home and condominium sales in the three North Bay counties seem to have plateaued, and the forecast for 2017 is for home and condo sales to remain flat with a chance to actually decline in some micro-markets.

During the first nine months of this year, compared with the first nine months of 2015, 15% fewer homes and condos traded ownership in Marin County, 5.3% fewer in Sonoma and 9.6% fewer sales occurred in Napa counties.

Sales velocity is clearly down in all three counties and for a variety of reasons, some of which are true for each county. The common theme relates to supply and demand, with limited supply in high demand markets driving up pricing in all three counties but particularly in Marin and Sonoma County, where the median price of sold homes increased 9% during the first nine months of 2016 compared with the first nine months of 2015. In Napa County, the median home and condo sale price increased 1.75% during the first nine months this year.

The median sale price means that half of all homes sold above the median figure and half of the homes sold below the median figure. See table below for specific pricing in each county.

Lack of inventory is an issue in each county, with only 2.5 months of supply available in Marin (homes and condos listed for sale) as of Sept. 30 this year, 1.8 months of supply in Sonoma and 2.85 months of supply in Napa counties, according to data compiled from BAREIS® (Bay Area Real Estate Information Services) and NorCal MLS®. The data was mined by Terra Firma Global Partners' Senior Associate Jaime Pera for Marin County, Senior Associate Trish McLean, CRS and Certified Green Real Estate Professional for Sonoma County and Senior Associate Ellen Politz for Napa County.

The average price per square foot increased nominally in Marin and Sonoma counties for the reporting periods, largely because home prices have been rising since 2011 with the biggest spikes coming in 2014 and 2015. That left little room for big price increases in 2016 – at least in Marin and Sonoma, which is another sign of a decelerating market. In Marin, the price per foot increase was 3% in 2016 and stood at $662 a foot at the end of September this year compared with $642 per foot at the end of September in 2015. The price per foot was 4.9% more in in Sonoma County ($381 vs. $364) yet in Napa County, the price per foot shot up 19% ($483 vs $391) during the first three quarters of this year.

Days on the market (DOM), while an imperfect measurement because DOM is reported differently by all of the sales agents in the industry, is still a good indicator as to which direction the markets are heading. DOM in Marin declined by 9% in the first three quarters of this year and by 1.5% in Sonoma, yet increased by 4% in Napa County. The 9% median price increase in Marin combined with the shortened DOM has taken the Marin County housing market to unprecedented heights and begs the question – how much higher can it go, if at all? The relatively flat DOM in Sonoma County and modest increase in days on the market in Napa County indicates the markets have stabilized there.

As markets go, Marin County typically lags and follows home sales trends in San Francisco, while Sonoma lags and follows Marin County and Napa lags and follows Sonoma County.

Total Homes and Condos Sold 1Q2016 through 3Q2016
Marin: 1,928
Same Period 2015: 2,264
Percentage Change: -15%

Total Homes and Condos Sold 1Q2016 through 3Q2016
Sonoma: 3,953
Same Period 2015: 4,156
Percentage Change: -5.3%

Total Homes and Condos Sold 1Q2016 through 3Q2016
Napa: 1,242
Same Period 2015: 1,123
Percentage Change: -9.6%

Average Price Per Square Foot 1Q2016 through 3Q2016
Marin: $662
Same Period 2015: $642
Percentage Change: 3%

Average Price Per Square Foot 1Q2016 through 3Q2016
Sonoma: $381
Same Period 2015: $364
Percentage Change: 4.9%

Average Price Per Square Foot 1Q2016 through 3Q2016
Napa: $483
Same Period 2015: $391
Percentage Change: 19%

Median Price September 30, 2016 of 2016 compared with September 30, 2015

Marin: $1,014,817 vs. $930,786
Percentage Change: 9%

Sonoma: $545,000 vs. $500,000
Percentage Change: 9.0%

Napa: $629,000 vs. $618,000
Percentage Change: 1.75%

Average Days on Market First 9 Months of 2016 compared with First 9 Months of 2015:

Marin: 49 vs. 54
Percentage Change: -9%

Sonoma: 62 vs. 63
Percentage Change: -1.5%

Napa: 89 vs. 85.5
Percentage Change: 4%

Shifting Markets

"In Sonoma County, we are seeing more price adjustments and more negotiations for repairs occurring. Repairs and repair credits are hard to quantify, but it is an indicator of a softening market, or at least movement toward a more level market. While this is one indicator of a stabilizing market, we are still seeing strong competition among buyers for available homes. There's an interesting subset of data in the percentage of agents reporting "Multiple Offers" in MLS. This isn't a required field, so there may be more sales getting multiple offers than are being reported, but we know at least these number of homes have received offers from more than one buyer. In Sonoma County, through Sept 30 this year, 1,438 homes sold with multiple offers, compared to 1,335 homes during the same period of 2015, or a 7% increase," reported Trish McLean.

Yet asking rates for homes have not lowered on any wide scale in Marin County, Jaime Pera reported. However, Pera wrote that the lower end of the market is shrinking and so is the middle part of the market, while the high end market is growing. Based on homes and condos listed for sale, as of 9.30 this year there were 163 homes on the market priced below $1 million, or down 16% compared with Sept. 30 of 2015. There were 252 homes for sale priced below $1.5 million – 11% fewer than a year earlier. Yet 32% of Marin homes for sale were priced at $2 million or more at the close of the third quarter this year, or 7% more than the same period a year ago.

Regarding inventory, McLean wrote that "we'd have to go back to 2011 to find more than two months of inventory…indicating that (at least for now) under two months of inventory is the new normal."

Ellen Politz attributes the lack of inventory to broader ownership trends with lower turnover, citing a California Association of REALTORS® report that homeowners are staying in their homes for an average of 10 years instead of a range from five-to-seven years.

"Marriage is down, and the millennials aren't pursuing the American Dream of getting married, buying homes and having kids the way previous generations have. Instead, they are looking to experience life and travel. So housing is not turning over at the same rate as the households are not changing as they once did," Politz wrote.

Mortgage rates are likely to rise, making it harder for first-time buyers and move-up buyers to afford to buy their first homes or to trade up. With real wage increases occurring in the U.S. following regular monthly gains in employment, the Federal Reserve appears poised to increase interest rates by a quarter point when it meets in December, and Fed bankers have publicly stated that another rate increase is likely in the first half of 2017.

The Fear Factor

Both McLean and Pera cited fear as a market driver in written comments that they included with their data findings.

"Another factor affecting inventory is fear… sellers who are concerned that they won't be able to find a replacement property so they don't want to sell their home," wrote McLean.

Similarly, "there are a lot of sellers on the fence about downsizing, not knowing where they are going to go plus as a general rule they have fear about downsizing and making a mistake," Pera wrote.

Looking Ahead

Higher borrowing costs are nearly a certainty and "could feel like a double whammy," Politz stated, because borrowing rates actually declined by nearly 50 basis points from the end of the third quarter 2015 to the end of September this year. The 30-year fixed rate mortgage average in the United States was 3.9% at the end of the third quarter in 2015 and had fallen to 3.45% by Sept. 30, 2016, according to data compiled by Freddie Mac and reported by the St. Louis Federal Reserve. Even so, Politz noted, "assuming that rates go up, we will only be moving from super low to low, historically speaking."

"The silver lining in the shifting market is that the move-up / move-down market is gaining strength as more and more agents are willing to broker deals between parties involving contingencies for selling or buying property. I just closed two transactions for a client who was doing a move-up purchase. They were concerned about selling their house and ending up homeless. We got their home "ready" to sell…pest inspection, cleaning, professional photography, etc. so that we could take action the moment they found a house they wanted. We also found a house that had been on the market for two weeks (which can seem like an eternity to the seller). That seller was willing to accept our full price offer and give us time to find a buyer for our house, largely because they also needed time to find a house to move to! So both buyer and seller had the same challenge…wanting to move and needing someone who would be understanding. In the end, this "daisy chain" of escrows closed successfully with a minimum of drama. It's cooperation like that and trust that keeps the market moving," McLean wrote.

"Over the last five years we have seen the housing market increase at a rate that significantly outpaces income growth. In 2017, with the (forecasted) increasing interest rate environment, simple economics tell us housing prices have to respond by softening to absorb the rate increases. Well priced, updated homes will continue to be highly sought after as buyers generally are willing to pay more for them, rather than fix up a property themselves. Today's buyers are weary that we have reached new heights in the real estate market and they are watching and waiting to see if things hold or fold," Politz wrote.

"I'd say that 2017 is a good year to start taking some chips off the table particularly if the goal is to downsize in the next couple of years. There is no point in waiting. I expect next year to be like this year with relatively low levels of inventory. Properties that are priced correctly, are updated, and are in the right neighborhoods will sell quickly with multiple offers. Homes that are overpriced with inflexible sellers will sit and likely end up selling for less than if they had been priced correctly in the first place. I expect prices to continue to rise, but at a slower pace than 2016 as buyers are starting to resist price increases. Downsizers will continue to ponder the question: Where do I move to? When they finally figure this out we will have more inventory. If they wait too long and sell during a period of rising interest rates, slowing sales, and growing inventory they will pay the price for having waited too long to make a decision," concluded Pera.