

# THE INFLATION RELATION TO HOUSING

REPORTS ON HOUSING  
ECONOMICS EXPLAINED

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## UNDERSTANDING AN INFLATED MARKET

Southern California's housing market has experienced home appreciation this year, but with mortgage rates eclipsing 7%, that may change. It is crucial to acknowledge that amidst the rising housing costs and mortgage rates, many American families are now grappling with financial stability despite recent improvements in inflation rates. A recent report from Reports on Housing released in July paints the affordability predicament in today's market. It highlights that many families in Southern California pay a much more significant portion of their monthly income on a mortgage payment. Given these circumstances, it becomes increasingly imperative to grasp the connection between inflation and home prices within the housing market.

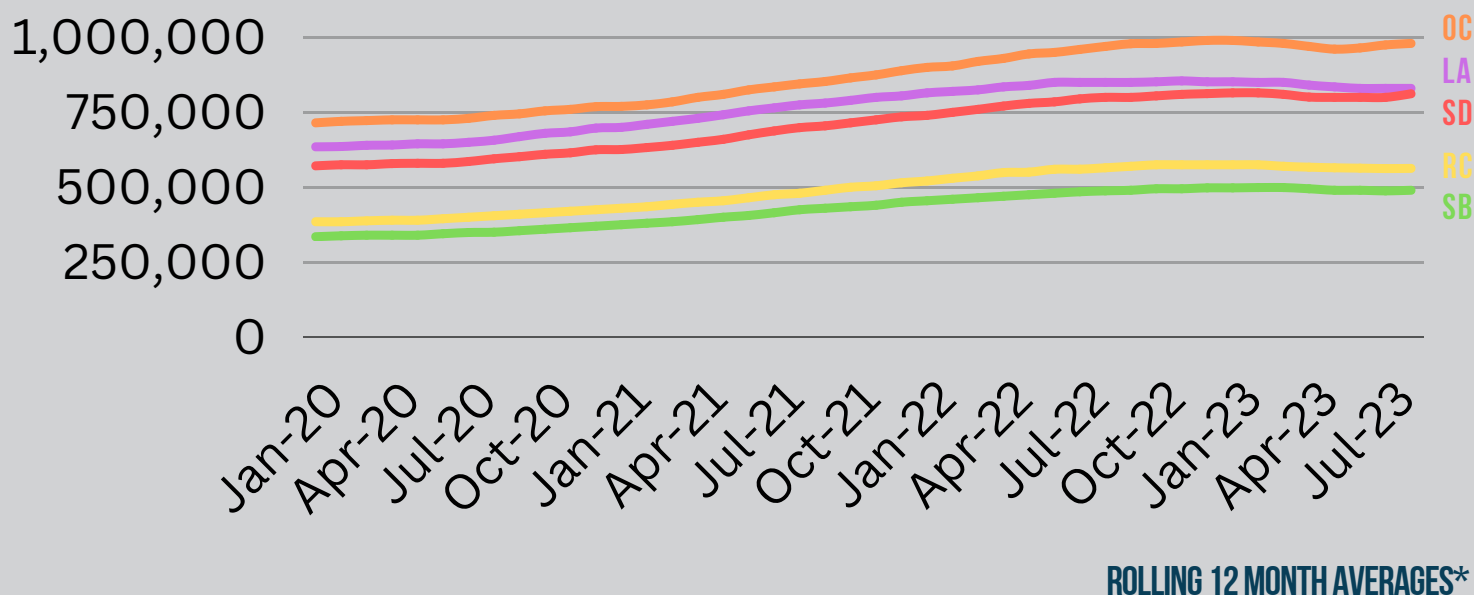
Inflation, by definition, is the rate at which prices escalate over a specific period. It serves as a broad metric, encompassing a nation's overall price surge or the heightened cost of living. Nevertheless, inflation can also be meticulously calculated for specific goods and services, such as food or haircuts.

Regardless of the context, inflation quantifies how much more expensive a set of goods and services has become over a predefined period, typically a year. It's worth noting that the Federal Reserve typically aims for an inflation rate of around 2%.

Understanding how housing influences inflation hinges on comprehending the underlying objectives of our inflation metrics. The Consumer Price Index (CPI) primarily functions as a cost-of-living index designed to gauge the prices of various goods and services households consume. It is not intended to measure the worth of family investment assets, such as stocks. This dichotomy presents a unique challenge when it comes to owner-occupied housing because a house's price encompasses both its value as an investment asset, which the CPI ideally disregards and its role as a good that offers a fundamental service – shelter – to the residing families, whose costs the CPI aims to integrate.



## SOUTHERN CALIFORNIA MEDIAN SALES PRICE 2020 - 2023



## THE RISING COST OF HOUSING

The cost of living for consumers depends on the prices of numerous goods and services and the proportion of each in their household budget. Government agencies conduct household surveys to identify a basket of frequently purchased items to calculate the average consumer's cost of living. This basket's cost, expressed relative to a base year, constitutes the consumer price index (CPI). The percentage change in the CPI over a specified period quantifies consumer price inflation, the most widely used metric for inflation assessment. For instance, if the base year's CPI is 100 and the current CPI is 110, inflation is calculated at 10 percent over the given period.

As of August 2023, the Consumer Price Index (CPI) exhibited a 0.6 percent increase from July. According to the most recent data from the U.S. Bureau of Labor Statistics, released on September 12th, the index showed a 3.8 percent increase over the past year before seasonal adjustments. This represents a slight uptick from July's rate of 3.2 percent.

Despite this modest increase from July's inflation reading, it's noteworthy that inflation has significantly declined from its peak of 9.1 percent in the summer of 2022. Before this past July, it had consistently declined for 12 consecutive months.

However, even with reduced inflation readings, the shelter category, which encompasses housing costs, remained the primary contributor to the CPI's monthly all-items increase. In July alone, shelter costs surged by 0.4 percent and have risen by 7.7 percent over the past year.

In light of these trends, it's crucial for prospective homeowners and individuals invested in the housing market to remain vigilant about the ongoing relationship between inflation and housing prices. As housing costs continue to exert an influence on inflation rates, understanding this dynamic can empower individuals to make informed financial decisions in an ever-evolving economic landscape.