Post #17. Cracks in the real estate market. Date 2025-1-28

This writing of this post was spurred by the large drop in the BLS new tenant rent index (NTR) in Q4-2024, which was released on the 21st of January 2025. We investigate the implications of the latest NTR data in the wider context of house rent inflation and its relationship with housing prices.

This post is a short summary of an extensive research on the US Economy where we provide a cautious outlook for 2025 and detail the reasons **why** investors should adjust their risk appetite accordingly. See below for further details.

This post provides early evidence that the scenario we outline in our extensive report appears to already be unfolding, which we expect will accelerate throughout 2025. Macroeconomics trends are slow to manifest, and we expect that an "acute phase" of the unfolding ordeal will occur sometime in 2025 and become evident to the wider market in 3 to 6 months' time.

1. BLS Tenant Rent indexes.

The Bureau of Labor Statistics publishes two research index series that use data sourced from data collected in the CPI Housing Survey shown in the previous section. The All Tenant Regressed Rent Index (ATRR index) and the New Tenant Rent Index (NTR index) are published on a quarterly basis and are aimed at providing a more accurate measure of the rent/shelter price inflation that is suffered by tenants and owners. While the BLS started publishing the ATRR since 1999, the NTR index started only in 2005.

The main difference between the ATRR and NTR index compared to the CPI indexes for rent inflation lies in the methodology used for its computation, as the computation of the NTR and ATRR are sourced from the same data that is used to compute the CPI indexes. The main difference in the methods of computation is that the ATRR and NTR indexes use changes in pairs of observed rents for the same property, instead of average rents. The methodology is the same as used by the Case-Shiller indexes for house prices that are now the standard for measuring house price inflation.

New Tenant Rent Index[1]

The New Tenant Rent Index (NTR index) and All Tenant Regressed Rent Index (ATRR index) are research index series published by the BLS that use data sourced from data collected in the CPI Housing Survey, shown in the previous section. The NTR Index uses only a subset of the data the official CPI uses, namely the first survey observations after new tenants move into their sampled housing units.

The New Tenant Rent Index (NTR index) can be understood as a measure of prices renters would face if they changed housing units every period.

All Tenant Regressed Rent Index

The All Tenant Regressed Rent Index (ATRR) is a measure with a scope similar to the CPI, but using methodology similar to the New Tenant Rent Index. The All Tenant Regressed Rent Index measures

[1] https://www.bls.gov/pir/new-tenant-rent.htm

the rent paid by all renters, both new and continuing, and incorporates most of the survey data used for the CPI Rent of primary residence index.

Figure 1 shows the quarterly time series of the NTR index and ATRR index published by the BLS. Further below we'll compare the changes in these indexes with the CPI-rent measures. For now, by looking at the chart we can observe that both the NTR and ATRR indexes has similar behaviour over time with the NTR being more volatile in nature. The latest data released on the 21st of January of 2025 that shows a large drop in the NTR index in Q4 of 2024, spurred the writing of this research update in the context of our US Economy outlook for 2025. If confirmed to be accurate, this data point could be an early sign of the crack in the housing market.

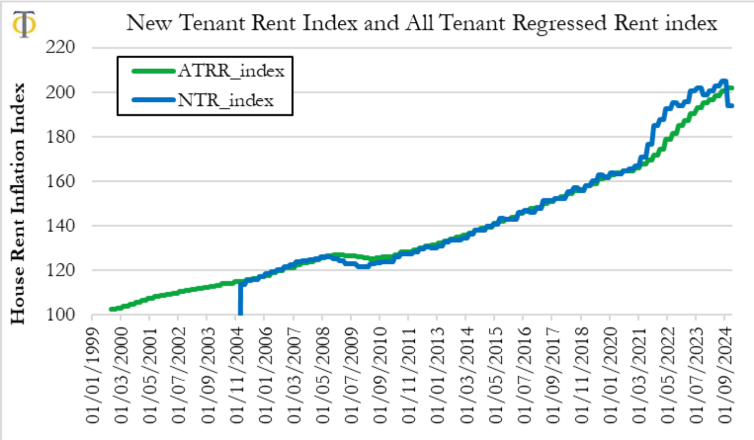


Figure 1 - Quarterly time series of BLS New Tenant Rent Index (NTR) and All Tenant Regressed Rent Index (ATRR). Source: Bureau of Labor Statistics.

2. House rent inflation based on CPI measures

One of the components within the CPI release is the index for shelter which refers to the service that a housing unit provides its occupants. Shelter service is one of the largest parts of the CPI market basket accounting for about 36.2% of total CPI in December of 2023, as reported by the BLS[2].

Most of the cost of shelter for renter-occupied housing is rent. For an owner-occupied unit, most of the cost of shelter is the implicit rent that owner occupants would have to pay if they were renting their homes, without furnishings or utilities. Owners' equivalent rent of residences (OER) and rent of primary residence (rent) measure most of the change in the shelter cost consumers experience.

In Figure 2 we compare the time series for CPI-Shelter and CPI-Rent and the broad CPI measure, from September of 1999 to December of 2024, where the prices are rebased to a reference date of 9/1999, with a value of 100.

[2] https://www.bls.gov/cpi/

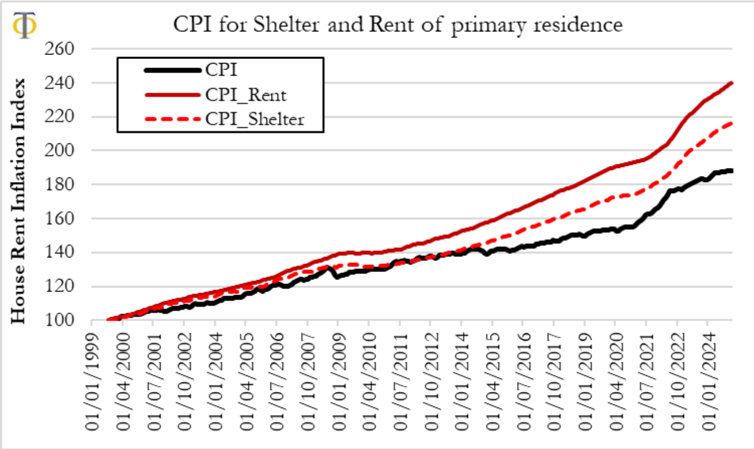


Figure 2 - Rebased time series for overall CPI, CPI Shelter and Rent of Primary Residence components (CPI-Rent). Reference: 9/1999 = 100. Source: BLS and St. Louis Fed FRED.

We observe that since 1999, rent prices for primary residence have risen faster than for overall shelter, which is predominantly related to owners' equivalent rent. This means that since 1999 house owners experienced lower inflation than renters. We also observe that both prices rises in CPI_Rent and CPI_Shelter have outpaced those in the overall CPI.

3. Deflated house prices.

Next, we investigate the equivalent trends in real house prices which now are deflated using different inflation measures, namely, the house rent indexes. Figure 3 shows the times series of real house prices from 1987 to December of 2024 where the Case-Shiller index is deflated by the CPI, CPI_Shelter and CPI_Rent.

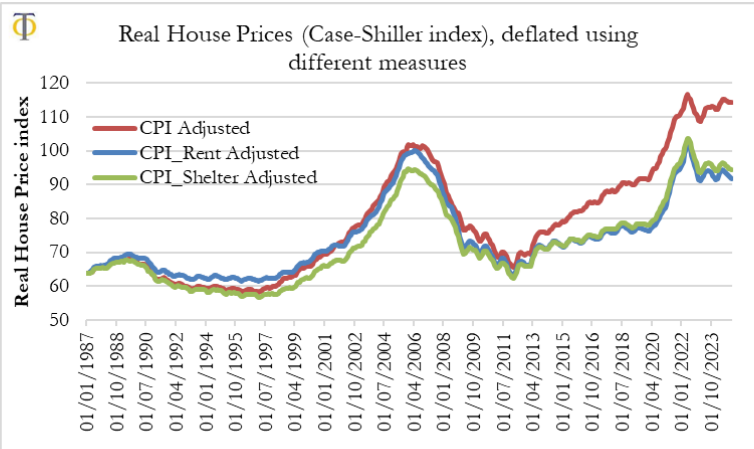


Figure 3 - Time series of the Case-Shiller House Price index deflated by different house rent inflation measures.

Even after adjusting for CPI_Rent or CPI_Shelter, real house prices are currently at levels similar to those observed in 2006, before the great recession. The chart also shows the large rise in house price inflation relative to rents occurred from 2020 to 2022. The pull back from 2022 to 2024 was small, when compared to the previous increase which indicates that further adjustments could occur in 2025.

4. Summary

We believe that the recent drop in the NTR index was not a statistical fluke but instead originates from lower demand for new tenancies which leads to lower prices. The lack of demand is likely driven by a sudden outflow of illegal immigrants from the US that anticipate the change in immigration policy when the new Trump administration is installed[3]. Consequently, we believe that, if the data point was not erroneous, that the scenario we portray in our US Economy outlook for 2025 is already starting to play out.

If we are correct, in the coming months we'll see an acceleration of this process with likely continued downward pressure on the NTR index. Additionally, we believe that this will also have a downward effect on house prices, housing construction and inflation.

An important caveat is that the most recent data points in the NTR index can suffer large revisions due to its computation methodology and sample characteristics, which means that we should be cautious on making definite statements before extra confirmatory data is released.

This post offers just a snapshot of the unfolding economic situation which we explain in detail in our US Economy outlook for 2025 report. To understand the wider context of the coming economic downturn, we published a detailed analysis in our US Economy outlook for 2025 report package.

Our US Economy outlook for 2025 report:

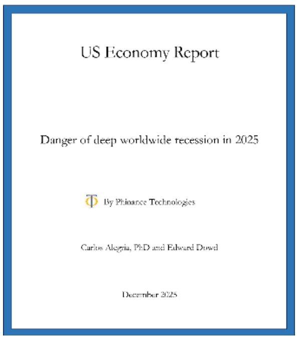
The full report is an extensive analysis that provides insights into the most consequential forces that will be acting on the US economy in 2025.

The report is aimed for decisions makers for investments and risk management, providing a roadmap to understand and successfully navigate the economic conundrum that the US and global economies will be facing in 2025.

With the insights detailed within the report, instead of being adrift and navigating blind the noise and drama typically associated with economic turmoil, our readers will be better positioned to anticipate and take action of unfolding risk and opportunities.

The report package includes:

- Full report on the US Economy outlook for 2025
- Executive presentation aimed at executive level decision makers.
- 1h Video with Ed Dowd and Carlos Alegria go through the executive presentation.


US Economy Report

Danger of deep worldwide recession in 2025

By Phinance Technologies

Carlos Alegria, PhD and Edward Dowd

December 2025

[3] https://abcnews.go.com/US/wireStory/immigrants-leaving-us-deportations-trumps-threats-loom-117734619