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Mortgage rates expected to fall but sidelined buyers should adjust their expectations

Industry experts believe rates will never go back to the historic lows seen during the Covid-19 pandemic, when some buyers snagged rates below 3%.

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Homebuyers frustrated by high mortgage rates may soon get some relief if the Federal Reserve begins to lower interest rates but they should temper their expectations, experts say.

Although the Fed has signaled it could start lowering rates as soon as its July 31 meeting, industry experts believe rates will never go back to the historic lows seen during the Covid-19 pandemic, when some buyers snagged rates below 3%.

“Rates are never going to get back to where they were during the pandemic,” said Marty Green, a principal at law firm Polunsky Beitel Green. “I think getting into the 4 to 5 [percent rates] is definitely in the cards over the next 18 months or so."

That would translate into hundreds of dollars a month in savings over current rates, which are hovering around 7%. Mortgage interest rates are several points higher than the Federal Reserve rate, although that larger spread sometimes allows those rates to fall faster as overall rates go down, Green said.

But some experts are expecting rates to only drop a bit as the Fed tries to balance cuts now and a federal deficit that leads to more borrowing in the future.

"Fed rate cuts later this year and next year will help drive mortgage rates lower," said Lawrence Yun, chief economist at the National Association of Realtors. "However, due to the very large deficit now and into the future, government borrowing will lead to less funds going to mortgages than could have otherwise. That is why mortgage rates will settle near 6% and not go towards 5% or lower."

While lower mortgage rates will reduce homebuyers' monthly payments, it will also cause a surge of buyers to reenter a housing market that is still short on inventory —

which will, in turn, cause prices to climb once more.

“You have an inventory imbalance," Green said. "You have too few homes for the number of people who need them."

He said, in some markets, prices have surged so much that there's been some amount of correction. That softening has pushed down overall median home prices nationally from a peak of $442,000 in the second quarter of 2022 to $412,300 in the second quarter of 2024. That's still far higher than the $329,000 median home price in the first quarter of 2020, right before the pandemic catapulted housing demand and home prices.

Inventory is still low by historic standards, too. While the number of active listings has climbed to nearly 840,000, according to the Federal Reserve, that is still below the 1 million active listings right before the pandemic. Pre-pandemic, that number had been steadily dropping from 1.5 million listings in early 2017.

Still, the recent shift in prices and inventory — along with fewer buyers willing to swallow higher mortgage rates — has softened the edges of what was once a red-hot housing market

“We’re seeing a slow shift from a seller’s market to a buyer’s market,” Yun said in a statement. “Homes are sitting on the market a bit longer, and sellers are receiving fewer offers. More buyers are insisting on home inspections and appraisals, and inventory is definitively rising on a national basis.”

Expected mortgage-rate drops could serve as a lifeline for buyers who had to purchase homes at rates higher than 7% or who have been waiting for rates to drop to pull equity out of their house.

It could also mean a surge in homeowners seeking to refinance. Already, recent small drops in mortgage rates have driven refinancing applications up 38% during the week ending July 19 compared to the same week in 2023, according to data from the Mortgage Bankers Association.

Generations are in a housing market tug-of-war

A report from Redfin Corp. (Nasdaq: RDFN) earlier this year found the length of time people stay in their homes has more or less doubled since 2006.

In that year, the median homeowner spent about 6.5 years in a home. That number peaked at 13.4 years in 2020 before dipping to 11.9 years in 2023, essentially putting older and younger generations at odds with each other.

About 56% of baby boomers have lived in their home for at least 10 years, according to the study, while 35% of Gen Xers have lived in their home for at least a decade. Just 7% of millennials have stayed in their home for 10 years or longer.

The homes older Americans own also tend to be larger. A separate Redfin analysis found empty-nester baby boomers own twice as many three-bedroom-plus homes as do millennials with kids.

The houses that do come up for sale are increasingly in need of renovations. A report from home-improvement company Leaf Home and Morning Consult found 73% of baby boomers have been in their current homes for 11 years or more, and over half own homes built in 1980 or earlier that have never been renovated. A majority say they have no plans to do so, either.