

## Conversations with Commerce Trust

### Housing: Affordability, Interest Rates, and Economic Impact

Recorded May 13, 2026

**David Hagee:** Hello, and welcome to Conversations with Commerce Trust, our show about the markets, investment themes, and economic insights that matter to you. I'm your host, David Hagee, Chief Investment Officer with Commerce Trust. Today, we're looking at the housing market with Scott Colbert, our Chief Economist and Director of Fixed Income. Welcome back to the podcast, Scott.

**Scott Colbert:** Hi, David.

**David:** Great to have you here talking about the economy and housing, and I think this is an area that, you know, as we talk about, say, inflation, or overall economic growth. It's a bit overlooked in terms of its economic impact here. So, maybe at the very start of things, let's spend a little bit of time around the supply-demand dynamics inside housing right now. Scott, what are you seeing out there?

**Scott:** Well, of course, housing right now, with, you know, new home construction being a big boost, a driver to the economy, is about 3.6% of GDP. Historically, this is low. Because, of course, new home sales are low. Mostly because affordability is nearly at the lowest levels ever. So, the contribution from housing specifically into gross domestic product (GDP) is below average.

On the other hand, since people are spending so much money housing themselves, and it's their biggest cost, it's certainly the biggest driver of the CPI (Consumer Price Index), with, of course, 34-35% of the CPI being either indirect housing, meaning owner's equivalent rent, which is really just implied rent, or actual rents themselves. So, for the average household it's 35% of their income, and with affordability down, interest rates up and price is up, it's not as big a contributor. You probably know more than I do what the home builders stocks have done so far this year.

**David:** Yeah, certainly the homebuilder stocks are off in a significant way post the Iranian conflict here. You know, I am struck by this, that home builders should be in a good position. If we look at the U.S. post-great financial crisis. Really, you saw the amount of new home building, single-family homes, decline. Every year, call it, we lose 1-2% of our housing stock just from being sort of derelict and, and gotten old. I think that puts us at a point of roughly 3 to 5 million units short of kind of an equilibrium point out there on the supply side. And as you mentioned, coupled with higher interest rates you don't see people wanting to move out of their existing homes. You know, let's spend a minute on affordability and unpack that somewhat. So, when we talk about affordability, how are we examining affordability?

**Scott:** Well, the National Association of Realtors puts out two affordability indexes. One for average affordability, and of course, they're using median numbers, so, can the median family afford the median-priced home? And this is nearly at a record low simply because, pre-COVID, the median home price was \$286,000. It's now \$422,000. So, over the last 6 years the median home prices increased 47%. But the median income has only gone from about \$89,000 to \$112,000 per median family. So, incomes have only



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grown 25%, and of course, the biggest whammy to this whole thing is what? A doubling of interest rates. Six years ago, the average 30-year mortgage was 3.25%. Right now, as we sit here today, it's about 6.4%, up about 50 basis points just in the last month and a half or two post the Iranian conflict. So those key drivers are pushing affordability down and making homes relatively unaffordable. It's even, it's much, much worse for first-time buyers. And the first-time buyers, they basically survey the people that are renting homes that are 25 to 44 years old, what they're paying for rent, and what their income is. The average income of the average renter, headed by someone 25 to 44 years old, is only \$70,000, compared to the median family income of \$112,000, so you can imagine they can afford much less home. So, you know, they're basically unable to afford the entry-level house.

**David:** Yeah, I mean, that's a real problem. Of course, home ownership inside the United States is a significant asset for almost every household out there. So as people look at their balance sheets, owning assets in this market has been a good thing. And that they've been able to see appreciation, mostly on the stock side, but on the housing side, it's been tougher for first-time homebuyers, as you mentioned, to be able to get in there. You know, I'm struck by a conversation we had around, we would need, what, incomes to go up by 30%, or home prices to fall by 40% to get back to that sort of cocktail of making enough money, having interest rates where they're at today, to be able to get into the median home price.

**Scott:** If we wanted to get back to average home affordability, we certainly need to see mortgage rates down, home prices stabilize, and incomes rise to get us there. And it's really, you know, we're still a significant way away from average historic home affordability.

There are 45 million people who rent in this country, 45 million households that rent, and about 90 million single-family homeowners. So that's kind of the proportion there in the country, and of course, as you said, we're probably underhoused and under-apartmented, because post the great financial crisis, we were building at the peak 1.4 million new single-family and apartment units per year at the top of the market. That's now down to about 680,000 or 700,000, just about half the level that we built at the peak. The average level is close to average right now, today, if you take out those highs and lows, but of course, we're a much larger country going back, you know, over the last 25 years.

**David:** Yeah, it is interesting, you know, between the housing stock that becomes no longer sort of livable out there and the lack of building going on, it's a real pinch right now. You know, I'm struck by the other piece to this is that, a major investment theme across 2026 is this AI (artificial intelligence) build-out continues to power the U.S. economy at the margins, sort of eating up construction talent, though. So it seems like, between that and, no net immigration, it seems like our construction costs might be a little higher, driving that median home price a little bit higher as well.



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**Scott:** Well, Turner has an index, Turner Construction has an index, and it's, you know, the construction costs of a new home have been outpacing inflation by about 1.5% post-COVID, so whatever inflation has been, let's call it 3.5% or 4% post-COVID, the home prices for the construction cost of building a new home have increased at a faster pace. And of course, as you mentioned, you know, inventory's low existing home inventory is about, oh, you know, right now, on an annualized basis, we sell about 4 million existing homes a year. The average is five (million), so we're only selling about 80% of the homes, and as you alluded to, the reason for that, largely, is because so many people are locked in with a lower mortgage, they really can't even afford to move, because it would cost them more money just to get in to another house. So, turnover's down, and inventory's down. We only have about 3 to 4 months of supply of existing home inventory. Weirdly, this is really kind of a little strange, new home pricing. Because new home builders are building further and further away, and they're building for what the market can afford. A new home's price, on average, is actually lower than an existing home, but of course, it's much less home in a much less desirable area, so to speak.

So, we've seen the builders, you know, react to this, the lack of affordability. They've brought their prices down a little bit, subsidized things, and of course, there's quite a bit more inventory on the new home side. There's almost half of your supply on the new home side, compared to 3 to 4 months in the existing home side.

**David:** Yeah, and couple that with this idea that post-great financial crisis, 2008, 2009, banks are less willing to take on these massive projects out there in terms of just throwing in a ton of homes inside of, you know, exurbs or, you know, really far out suburbs here, so...

**Scott:** No, there's no doubt the banks got burned pretty badly during the Great Financial Crisis, you know, basically lending money at 50 to 60 to 70 cents on the dollar for subdivisions. And they've pulled back their horns. The land is much more expensive, the construction costs are more expensive, the zoning is tougher, so it's just tough to get, you know, existing inventory built.

**David:** So, understanding those dynamics a little bit better, taking a look, a little deeper dive here at the housing market, why is the housing market so important for the U.S. economy?

**Scott:** Well, it is the biggest expense of a household. Within the CPI, 34-35% of your budget is spent on housing, and when you include all the expenses on housing, not just the new homes being constructed. But, you know, what you pay for your rent, or what you're paying for your mortgage, and your insurance, and the furniture, and everything that goes into your house. It's about 16-17% of GDP. Basically, it's about the equivalent of healthcare. We don't normally think of it that way, but housing as a percent overall expense and contributor to GDP is about the same as the entire healthcare industry.



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**David:** So, as we sit here today, you know, thinking about inflation and rates. It's mid-May, we're looking at oil prices, both Brent and West Texas Intermediate above \$100 a barrel. How has the housing dynamic played into CPI? As you mentioned, it's the biggest piece of the bucket.

**Scott:** Well, right now, the CPI, post the Iranian conflict, is clocking in at 3.8% now, year over year. That's the top-line CPI. Housing, everything involved, the insurance and everything, is only clocking in at 3.1% now. Home prices have cooled. As affordability, of course, has gotten worse and worse, home price appreciation has slowed, so has rental price appreciation. They've both slowed. So, as a percent of the CPI, we do expect to see housing prices continue to cool, which will bring this so-called over-owner's equivalent rent down, which should bring the inflation component of the CPI down. So, while we're getting smacked in the face with higher oil prices. Energy, oil, basically. Gasoline as a percent of the CPI is only 3%. Housing, as I said, is more than 30%, and so we have the largest component declining, while we have one of the smaller components, one of the most visible components, of course, rising dramatically.

**David:** Yeah, and so, as we talked about a little bit earlier, again, mid-May here, the S&P is up about a little over 9%, right now, but we're looking at home builders that are down about 10%. So, it's just been a more challenging market, even though you'd look at the supply-demand characteristics and say, hey, there's a ton of demand for homes. But it circles back to this affordability, piece, where you just can't get people in. So, you know, as we think about that, you know, you have this period of energy, which is relatively small. As a nation, we're consuming 43% less energy today than we were 20 years ago.

So, you know, last time we faced an energy shock that was born out of the shut-in supply was the Arab oil embargo in the 1970s. Number one selling car in 1976, of course, was the Oldsmobile Cutlass. It got roughly 10 to 16 miles per gallon. You know, city highway. And then, you know, you factor in today that the continued number one selling truck inside the U.S. is the Ford F-150, and the Ford F-150, as of today, gets, 25 miles per gallon in the city and 26 miles per gallon on the highway. So, we've become a lot more fuel efficient, with the average household using significantly less energy. But as that bleeds into the inflation numbers, with the doubling, effectively, of oil prices. That has become a marginal, or it's been driving inflation higher at the margins there.

**Scott:** Yeah, it's hard not to see that the, you know, near-term inflationary impact of oil isn't going to keep pushing the CPI slightly higher. You know, we expect the CPI probably to get to 4% year-over-year. Now, that's still a lot less than when, you know, Russia invaded Ukraine and drove oil prices up. And that's simply because that was occurring at the same time, what, we had a lot of government stimulus, ultra-low interest rates, as well as a very, you know, accommodated Fed at the time and a surging economy.



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Now the economy's cooled considerably, and we have a less accommodated Fed, and of course, interest rates have jumped, which ought to cool the economy, too. So, we do expect some modest increase in the CPI. By the end of the year, though, it should be declining.

I seriously doubt now that they're going to have the ability to lower rates before the end of the year. The market actually thinks that it might be until the end of 2027 that the Fed has its first opportunity to lower rates. But I think we have to remember, number one higher interest rates did what? Well, it's home building. Nothing is more cyclical than home building. Of course, it's depressing home sales. Number two, we probably won't have as many auto sales. This gas increase is kind of acting as a tax that ought to have its own demand destruction. And as time moves on, the inflationary impact of those tariffs will start to disappear.

So, we think that basically, you know, this will be relatively contained. You'll see a modest drop in the CPI, but probably not quick enough to give us that interest rate cut this year. And by the way, just moments ago, Kevin Warsh was not only approved as a federal governor, but as the chairman of the Federal Reserve. So, we do have Warsh coming in, we know his attitude is one to want to lower rates, but he's got to get those other 18 folks up there the 12 Fed governors and the regional, the 12 Fed presidents, as well as the other 6 Fed governors, you know, to move his direction.

**David:** Yeah, and interestingly enough, as I'm looking at Fed futures here, it's telling me that we should see rates moving up by the end of the year, as opposed to moving down. But we'll have to see where Kevin Warsh is able to summon the votes at.

**Scott:** Yeah, right now, there's just over a 50% probability that there could actually be a rate hike this year. I think it's almost 70% right now. These markets, though, are very, thinly traded, they're very susceptible to changes. Any change in direction in the economy, any change in direction of the war in the Persian Gulf. They're very sensitive to, near-term economic news. Let's just call it a flat expectation for interest rates going forward for quite a period of time.

**David:** So again, as that ties back to housing, maybe more headwinds facing the housing market, possibly good news in sort of controlling, you know, household expenses out there, but at the end of the day, continues to face a market that has considerable headwinds there.

**Scott:** Now, the good news is, if you're a buyer, you're starting to see inventory slowly accumulate. You're also starting to see the slowdown in home price appreciation. But now, as a buyer, you also need to see your income begin to grow, and hopefully those interest rates come down. Interest rates are 50 basis points higher today than they were at the beginning of the year. I think that's been the key driver that's pushed these home-building stocks down.



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**David:** So, we've talked mostly today about residential housing. Of course, that's most impactful in CPI. As I'm looking across the U.S, it's been a little bit uneven in terms of construction spend. It feels like in the Midwest, we've continued to see good, strong construction spend. I think a lot of that's going towards data centers, across the region. What are you seeing? What are the regional differences that you're seeing right now?

**Scott:** Well, in aggregate spending, the Midwest is, you know, doing the best of all of them, largely because of affordability issues. Home prices haven't surged like they have down south, out west, or up in the Northeast, and of course, all this data center build is moving towards areas where they you know, perceive the electrical rates to be the cheapest, and that tends to be, you know, the Midwest, where we still have the old, efficient coal plants, some nuclear, and on average, just lower cents per kilowatt, charge. So, you know, the Midwest is benefiting relative to the rest of the country.

It is kind of interesting, though, that the leading construction indexes, as measured by architectural billing hours, are actually down everywhere in the country except the Midwest, where they're relatively flat. So these higher interest rates are biting. They're biting residential construction.

And let's not forget, while there's a data center build-out, nobody is effectively building downtown office space, you know, in the country. The apartment build-out is still, you know, ongoing, but it's slowing.

The colleges have cut back on their construction, and healthcare, while they've been a big driver of construction, new hospitals, things like that, they've slowed materially because their reimbursement rates have slowed so much that they're not spending what they used to in terms of new construction.

**David:** Thanks, Scott. You know, as we look at portfolios today, these factors, and certainly the interest rate environment, this balancing that we're seeing right now between considerable headwinds, but also a very resilient U.S. economy, is painting an environment where companies are able to focus on operational efficiencies and driving earnings growth, and we continue to see tremendous earnings growth inside the U.S. markets.

Thanks for the interesting discussion today, Scott, I appreciate it. For more on this topic, please visit [www.commercetrustcompany.com](http://www.commercetrustcompany.com). And take a look at our mid-year outlook, coming out in June. If you've enjoyed what you've heard today, you can subscribe to our show on Apple Podcasts, Spotify, Amazon Music, or wherever you get your podcasts from. Thank you for joining us on Conversations with Commerce Trust. I'm David Hagee. We'll talk again soon.



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