



## Economics Group

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## What's Behind the Upward Trend in Housing Activity?

***The housing data have looked a little more positive over the past 3 months. While signs of a bottom have emerged, the latest housing activity data are likely being driven by a couple of unsustainable factors.***

The latest housing market data show that activity picked up in recent months. According to the National Association of Homebuilders/Wells Fargo Housing Market Index (HMI), builder confidence continued to show gains in December, increasing to 21, the third consecutive monthly increase and the highest level since May 2010. Starts and permits have also perked up, with single-family starts up 4.6 percent on a year-ago basis in November and permits up 3.6 percent over the same period. The increases mirror improvement in construction outlays and sales, which have also seen gains in the past few months.

While the increases are promising, we do not believe a “genuine” recovery in housing activity has begun. Indeed, the major obstacles that have troubled the housing market over the past few years still remain intact, including the oversupply of single-family homes and mounting distressed transactions. It is likely, however, that the recent upward trend in housing activity is due to two factors: 1) actual strength in a select few markets and 2) unseasonably warm weather during a normally slow time of year.

### Gains in Select Markets Boost Overall Activity

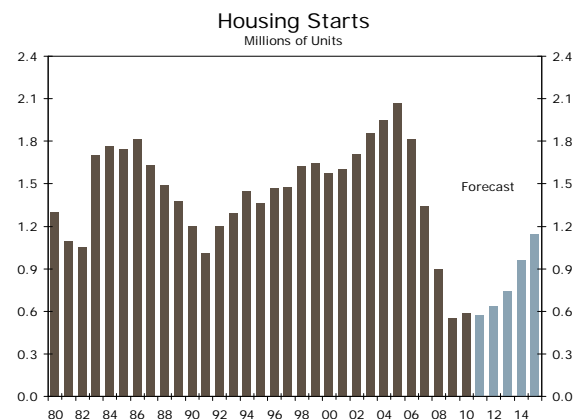
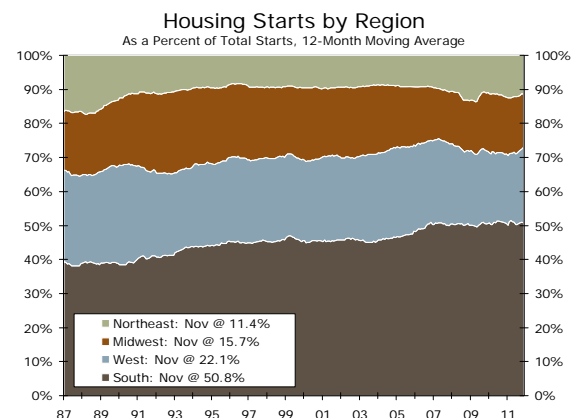
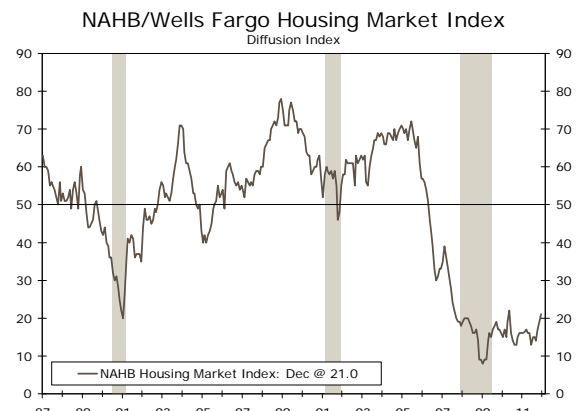
One of the more promising signs of progress is the string of gains in homebuilder sentiment. While builders continue to face competition from deeply discounted existing homes, activity has ramped up in the South. Builder confidence is up 10 points in the South since September, accounting for a large portion of the overall index's gain in recent months.

### Seasonal Adjustment Process at Play

Another likely explanation for the successive gains could be the seasonal adjustment process. Indeed, single-family housing starts rose 2.3 percent in November following a 3.6 percent increase in October, but fell 11.3 percent on a not seasonally adjusted basis on the month. Single-family housing starts usually decline this time of the year and since starts were already near record lows, activity did not fall as much as usual, resulting in a seasonally adjusted rise. A similar trend is evident in permits, construction spending and sales.

### Housing Market Outlook

We expect home prices to come under additional pressure this winter, as more foreclosures come on the market during the seasonally slow sales period. Appraisals are likely to remain conservative for at least the next year, or until the mountain of foreclosures hanging over the market finally clears. We are looking for only a modest rise in new home sales and single-family construction in 2012, but we look for prices to find a bottom by the middle of next year. The return to a “normal” housing market, where supply and demand are in balance and prices are rising 2 percent to 3 percent a year, is still, unfortunately, years away.



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