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## January New Home Sales: Low Inventories Cap Near-Term Upside

- New home sales were essentially flat at an annual rate of 481,000 units in January from December's (revised) sales pace of 482,000 units.
- Months supply of inventory stands at 5.4 months; the median new home sale price rose by 9.1 percent on a year-over-year basis.

New home sales were essentially unchanged in January, with an annual sales rate of 481,000 units compared to December's revised sales rate of 482,000 units. This is somewhat encouraging, at least in light of the pattern seen in 2014 in which a sizeable jump in new home sales in a given month was revised sharply lower in the next. Indeed, when December sales were originally reported to have jumped to an annual rate of 481,000 units from an annual rate of 431,000 units in November we began our write-up by saying "stop us if you've heard this one before." Instead of downward revisions, however, November sales were revised higher, to an annual rate of 446,000 units while December sales were revised nominally higher. On a six-month moving average basis, one way to weed out the noise in the month-to-month data, new home sales are running at a rate of 464,000 units, the highest sales rate since mid-2008. It is also worth noting that the raw, i.e., not seasonally adjusted, data show 38,000 new homes were sold in January, the best sales figure for the month since 2008, though still below the longer-run (1963 through 2007) average of 51,000 new home sales each January. Still, at 441,000 units, the 12-month moving sum of not seasonally adjusted sales (our preferred way of viewing the new home sales data) stands at the highest level since February 2009 when, as seen in the chart to the side, sales were hastily beating a retreat from an abnormally high peak.

To be sure, we are encouraged by the gradual improvement in new home sales, but at the same time remain guarded in our expectations for any acceleration in the pace of that improvement over coming months. We can sum up the root of our concern with a single word – inventory. Or, perhaps we should say we can sum up the root of our concern with three words – lack of inventory. As the middle chart shows, physical inventories of new homes for sale is up from historic lows in early 2012 (the data go back to 1960) but are nowhere near the longer-term historical average. Yes, new homes can be sold before ground has been broken – in January homes on which construction had not yet been started accounted for 30.6 percent of all new home sales – but the broader point remains a lack of inventory is hindering the pace of new home sales (as for existing home sales).

We find little basis for expecting a meaningful increase in inventory, at least over the next several months. This is perhaps best illustrated in the bottom chart, which shows a regional breakdown of starts of new homes intended for sale. One point many analysts seem to overlook is not all new homes built are intended to be put on the market for sale – during Q4 2014, for instance, just over 73 percent of all single family completions were intended for sale. We have indexed single family starts intended for sale to the average number of such units started in each region over the 2000-2002 period, which we longingly refer to as "the last normal years we've seen in the housing market" and, on this basis, construction of new single family homes intended for sale is, again, nowhere near levels that could be expected to prevail in a normal housing market, and this doesn't even account for the growth in households in the intervening years.

Another underlying trend that has largely escaped notice but which nonetheless may be having a material adverse impact on new home sales is the fact that builders have increasingly gravitated towards the high end of the market. Sure, builders build where the demand is, or at least where the demand that can actually procure mortgage financing is, but in any event homes priced at or above \$300,000 have accounted for a steadily increasing share of all new home sales – 49 percent over the past four months. This, at least in our view, starts at the lower end of the market, the lack of first time buyers who will either buy a new home or, more likely, buy an existing home and thus facilitate a move-up new home purchase by an existing homeowner, is being felt across a wide swath of the price spectrum. Until this changes, the rate of new construction intended for sale and the rate of new home sales will be somewhat capped. To us, this is a change that will come only gradually, which helps account for our below consensus forecasts for single family construction and sales in 2015.

