

ECONOMIC UPDATE



REGIONS

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March New Home Sales: Underlying Trend Shows Continued Improvement

- > New home sales fell to an annual rate of 481,000 units in March from February's (revised) sales pace of 543,000 units.
- > Months supply of inventory stands at 5.3 months; the median new home sale price fell by * percent on a year-over-year basis.

If perception is indeed reality, today's report on March new home sales is a huge miss (relative to expectations), yet another sign the U.S. economy is losing steam, further proof the "American Dream" has turned into a nightmare for homebuilders, and, just for good measure, a disgrace to the human race. After all, new home sales fell to an annualized sales rate of 481,000 units in March, well below consensus estimates of a sales rate of 522,000 units. As we view the world (or, at least the economic data), however, today's report on new home sales is none of the above, and instead falls right in line with what we see as further steady improvement in the housing market, even if that improvement is coming at what is to some a frustratingly slow pace.

As we routinely point out the data on new residential construction and home sales are best viewed in the context of the underlying trends in the not seasonally adjusted data. Especially new home sales, which is one of the most inherently volatile data series out there and one subject to a sampling error so large so as to render the headline number irrelevant – in March we can be reasonably sure new home sales fell somewhere between 400,000 and 600,000 units on a seasonally adjusted annualized basis, but we can't really be too much more precise than that. Sure, it may be more fun to fully embrace the swings between euphoria and angst incited by the fluctuating headline numbers, and even the headlines themselves, such as today's "new home sales crater in March" but that doesn't really shed any light on the underlying trends, which, after all, are what matters. For instance, the red line in the top chart shows the 12-month moving sum of new home sales, which in March rose to 461,000 units, which is the best such reading since January 2009.

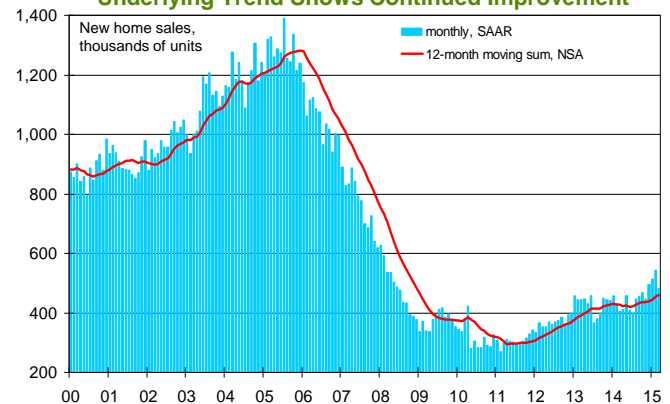
In order for one to see the March new home sales report as a disappointment or a disaster ("crater" – really?) one would have to believe the February headline number which, by the way, was revised even higher in today's report. The point we made last month is that February number, and to a lesser extent the January number, were badly out of alignment with data on new home construction and inventories. The middle chart shows how undersupplied the new home sales market continues to be, with inventories of "physical" homes for sale not only well below historical norms but sinking a bit further in March. This in part reflects ongoing constraints such as smaller and mid-level builders continuing to face less friendly financing environments, and supply constraints on buildable lots and construction workers. To be sure, new homes can be booked as sales before construction has begun, but there is nothing in the data to suggest a spike in the share of such sales so as to be consistent with the headline sales numbers in January and February. The data we use to construct the middle chart are not seasonally adjusted and as such are consistent with the sales figure represented by the red line in the top chart. As with the case of existing homes, lean inventories are acting as a constraint on sales of new homes.

Another constraint on new home sales is tied to the shortfall in first time homebuyers, which can be seen in the above-normal share of home sales accounted for by homes priced at or above \$300,000. Sure, builders build where the demand is, or at least where the demand that can actually procure mortgage financing is, but in any event we believe this 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 range of the price spectrum. Until this changes, the rate of new construction intended for sale and the rate of new home sales will remain sluggish and what activity there is will remain more concentrated in the higher ends of the price scale than is normally the case. To us, this is a pattern that will change only gradually.

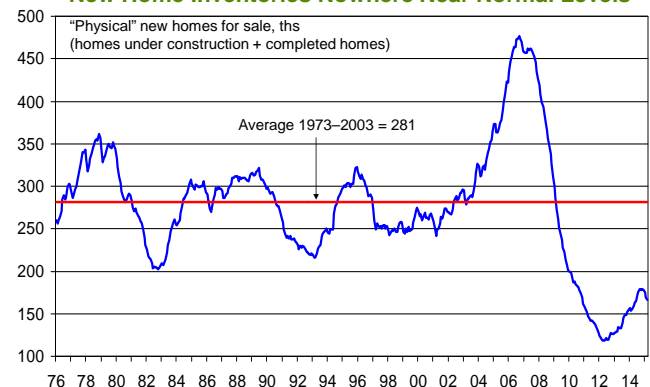
The headlines, and the headline numbers, are what they are, but what the March report on new home sales is, at least to us, is further progress on what we have from day one said will be a slow journey back to normal housing market conditions.



Underlying Trend Shows Continued Improvement



New Home Inventories Nowhere Near Normal Levels



Builders Increasingly Gravitate To The High End

