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## August New Home Sales: New Home Sales Perk Up In August

- > New home sales rose to an annual rate of 552,000 units in August from July's (revised) sales pace of 522,000 units.
- > Months supply of inventory stands at 4.7 months; the median new home sale price rose by 0.3 percent on a year-over-year basis.

New home sales rose to an annualized rate of 552,000 units in August, easily ahead of both the consensus estimate and our above-consensus call of a 522,000 unit sales pace. Prior estimates for the May-July period were revised slightly lower for the three-month period. Inventories of homes for sale edged slightly higher but the months supply metric fell to 4.7 months, indicating a still undersupplied market. On a year-to-date basis through August sales are up 20.8 percent from the same period in 2014.

Rather than the seasonally adjusted annual rate basis on which the new home sales data are reported, we prefer to look at the raw, i.e., not seasonally adjusted, data as a more meaningful indicator of the underlying trend in sales. The raw data show that over the 12-month period ending with August there were 498,000 new homes sold, the highest 12-month total since November 2008. As shown in the top chart the underlying trend (the blue line) shows a steady increase in new home sales, albeit at a pace that satisfies no one. As the middle chart shows, the South and West regions are driving growth in total new home sales with sales in the Midwest basically flat for the past two-plus years and sales in the Northeast having drifted slightly lower over the past year or so.

It is by now old news that new home inventories remain lean, as is also the case in the market for existing homes. The difference, however, is that lack of physical inventory is not as binding a constraint on new home sales as on existing home sales. New home sales are booked at contract signing, which can occur after a new home has been completed, while it is under construction, or before construction has started. The data show sales of new homes on which construction has not yet started have accounted for a greater share of total new home sales over the past several months. In August 35.6 percent of total new home sales were sales of units on which construction has not yet started while over the past seven months units on which construction has not yet started have accounted for over one-third of all new home sales. The bottom chart shows that, while inventories of what we refer to as "physical" new homes (i.e., either units under construction or completed units) for sale are off of the historical lows seen in 2012, they remain far below the long-term historical norm, so builders are literally selling them faster than they can build them.

Builders continue to point to shortages of labor as a constraint on construction and sales of new homes, and to the extent this is the case this constraint will not ease quickly. Of course, the textbook answer to labor constraints is for builders to offer higher wages, but at least initially the primary effect would be a reshuffling of current workers amongst builders within a given market as opposed to new workers entering the industry, while those workers who are attracted from other industries face a learning curve that would take some time to navigate. These labor constraints are more binding on single family construction, which is far more labor intensive than multi-family construction. And, even though new home sales can be booked prior to the start of construction and such sales have accounted for a higher share of overall new home sales over recent months, this simply means it will take builders longer to clear order backlogs. Another constraint, perhaps less obvious, is a "shortage" of builders themselves, as many mid-sized regional builders did not have the financial wherewithal to make it through the downturn and subsequent lean years, contrary to the larger and better capitalized national builders. Either way, however, the bottom line is new home inventories will likely remain lean for some time to come, thus weighing on growth in sales. To some extent, though, builders are making up for in margin what they are missing out on in volume, as sales of higher priced homes continue to account for an above-normal share of all new home sales.

We do expect to see steady, though unspectacular, growth in demand for new home sales over coming quarters. Even with this slow but steady growth in demand and starts of single family homes rising steadily, builders will remain challenged to keep up, a dynamic that won't soon change.

