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September New Home Sales: Don't Get Too Attached To The Headline Sales Number

- > New home sales rose to an annual rate of 800,000 units in September from August's (revised) sales rate of 702,000 units
- > Months supply of inventory stands at 5.7 months; the median new home sale price rose by 18.7 percent year-on-year

Total new home sales rose to an annualized rate of 800,000 units in September, topping the consensus forecast of 759,000 units and our forecast of 787,000 units, the highest forecast in any of the surveys we participate in. At the same time, prior estimates of sales over the June through August period were revised lower, with an average monthly sales rate of 699,000 for the three-month period compared to prior estimates of 718,000 units. The downward revision to August sales was particularly harsh, with sales now reported at 702,000 units compared to the initial estimate of 740,000 units (annual rates). More often than not over the past several months, the revisions have been to the downside, suggesting that one not get too attached to the initial estimate of September sales. Even aside from potential revisions, there is less to the September headline sales number than meets the eye. Sales in the South region were much stronger than we anticipated and what was suggested by the September data on single family housing permits and starts, which bore the effects of Hurricane Ida. At the same time, sales in the Midwest and West regions were well below what was implied by the September construction data. Clearly, the market for new homes is not functioning normally after months of builders operating under self-imposed sales caps while constraints on materials supplies have weighed on both starts and completions. Still, while there are signs that demand has softened a bit relative to earlier in 2021, that by no means implies that demand has dried up, and builders are still contending with sizable backlogs of unfilled orders. Though the prospect of higher mortgage interest rates looms over the market, we do expect sales to increase over coming months, but we expect the pace at which sales increase to remain somewhat uneven largely due to lingering supply-side constraints.

On a not seasonally adjusted basis, there were 65,000 new home sales in September, a touch better than our forecast of 63,000 sales, but August sales were revised significantly lower, from 62,000 units in the initial estimate to 57,000 units in the revised data. Based on the revised August data, unadjusted sales rose by 14.0 percent in September, which is notable in that September is typically a weak month for new home sales, with an average September decline of 5.4 percent over the 2000-2020 period. As such, the increase in unadjusted sales this September was magnified in the seasonally adjusted data, flattering the headline sales number. There were 41,000 sales in the South region, up from 34,000 sales in August and the most since April, but sales in the Midwest and West regions were flat in September. As of September, the running 12-month total of not seasonally adjusted new home sales fell further and now stands at 817,000 units. This metric, which we see as the most reliable gauge of the trend sales rate, peaked at 893,000 units in May but has now fallen for four straight months. As the over-the-year comparisons will get easier over the next few months, the trend sales rate should flatten out, but the pace of subsequent increases will be somewhat uneven.

It is important to put the declining trend sales rate in proper perspective. Recall that over the summer months many builders began to limit, or in some cases halt, sales as constraints on supplies and labor shortages made it impossible to keep pace with robust growth in demand. Moreover, given rapidly increasing materials prices, it was harder and harder for builders to price units so far in advance of work being started, which led many builders to cap pre-sales (sales of units on which construction had not yet started). At the same time, builders were starting units but not pricing them until construction was well underway, which effectively shifted pricing risk from the builders to the buyers. These shifts can be seen in the details of the sales data, with pre-sales accounting for a smaller share of total new home sales while units in the construction phase began to account for a rising share. This shift has also fueled the increase in spec inventories, defined as units either under construction or finished, but we prefer to think of it as "spec-lite" in that, with demand remaining strong, rising spec inventories posed little risk to builders. Still, if we are correct on this point, the increase in spec inventories is doing little in the way of providing relief from what remains a sizable imbalance between supply and demand. As noted above, while demand has eased a bit, the market remains undersupplied, and with supply-side constraints and sizable order backlogs, it will be some time before the market for new homes is truly balanced.

