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February New Home Sales: Underlying Trend Remains Flat

- > New home sales fell to an annual rate of 618,000 units in February from January's revised sales rate of 622,000 units.
- > Months supply of inventory stands at 5.9 months; the median new home sale price rose by 9.7 percent on a year-over-year basis.

New home sales fell to an annualized rate of 618,000 units in February from an upwardly revised sales rate of 622,000 units in January. February's preliminary tally was just shy of the consensus forecast of 620,000 units and a bit further below our forecast of 631,000 units. Prior estimates of sales in the November-January period were revised higher. As of February the months supply metric stands at 5.9 months, and while that is right at the 6.0 months figure considered to indicate a balanced market, we'd say the new homes market is anything but. Supply constraints continue to act as a brake on growth in new home sales and sales remain notably concentrated in the upper end of the price range. There is little evidence that higher mortgage rates impeded sales in February, but further increases in rates coupled with further increases in already high prices could spell trouble for new home sales.

On a not seasonally adjusted basis, there were 51,000 new home sales in February, just under our forecast of 52,000 sales. The 51,000 sales matches sales in February 2016 and reflects an 8.5 percent increase from the 47,000 sales in January, which is well below the average increase of 14.8 percent in not seasonally adjusted sales in the month of February since 1990. As our regular readers know, we think the running 12-month sum of not seasonally adjusted sales to be the most reliable indicator of underlying sales trends, and as seen with the red line in our top chart, the trend rate of sales has flattened out. Over the past 12 months there have been a total of 616,000 new home sales, unchanged from January and December. As seen in our middle chart, this flattening out in the underlying trend rate of sales is apparent in each of the four broad Census regions; while the West had been seeing a modest increase the 12-month total was unchanged in February. It is worth noting that the exact same thing is seen in the data on existing home sales, i.e., the running 12-month total has flattened out across each of the four broad regions over the past several months. And, as in the market for existing homes, we see little reason to expect much improvement over coming months.

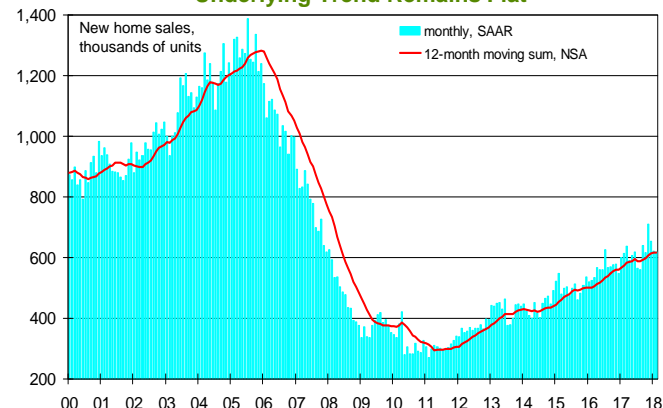
The specifics of course differ between the new home and existing home markets, but the bottom line is neither market is amply supplied. Builders of new homes remain pressed by labor shortages and more cumbersome and costly entitlement processes in many markets than has been the case in the past. One relief valve for builders is that new home sales can take place at any stage of the construction process, i.e., before construction has started, while construction is underway, or when construction has been completed. One trend we've been pointing to for some time is that units on which construction has not yet started are accounting for a notably high share of all new home sales – over one-third of all sales in February. In other words, builders are facing growing backlogs which will help sustain growth in single family starts over coming months.

Another trend we've been tracking is the elevated share of new home sales accounted for by homes priced at or above \$300,000. In February roughly 57 percent of all new home sales fell into this category and this is where that share has basically settled over the past several months, well above longer-term norms. While there is perhaps considerable potential for builders to move down the price scale and lure first-time buyers who are being shut out of the market for existing homes, it's not clear to what extent the math will work on any such move. In addition to more costly entitlement processes, builders have been contending with significantly higher materials prices. For now, there is sufficient demand at the higher price points, but we question how long this can persist, particularly if we do see significantly higher mortgage interest rates over coming months. In all honesty, however, we've been asking this question for some time now and have been a bit surprised that high end demand has held up. Of course, a fundamental rule in economics, and perhaps life in general, is that something can continue until it no longer can. But, our bottom chart is nonetheless striking, especially given the robust price appreciation we've seen in the existing homes market.

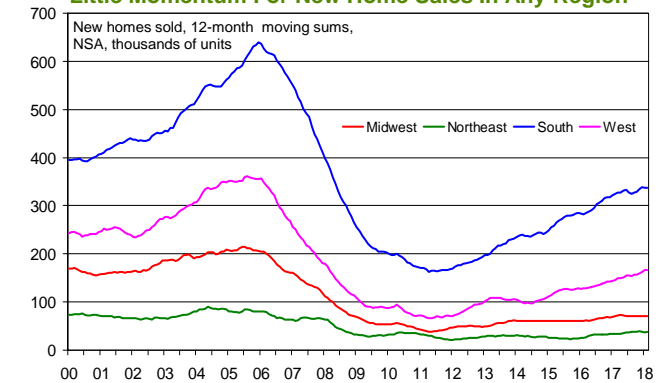
We've often noted that the issues in the housing market lie on the supply side of the market, not the demand side. Nothing we've seen thus far has changed our view on this.



Underlying Trend Remains Flat




Little Momentum For New Home Sales In Any Region




New Home "Premium" Remains Significantly Elevated

