ECONOMIC UPDATE
REGIONS
March 23, 2016



## February New Home Sales: Have We Reached The "New Normal"?

- New home sales rose to an annual rate of 512,000 units in February from January's revised sales rate of 502,000 units.
- Months supply of inventory stands at 5.6 months; the median new home sale price rose by 2.6 percent on a year-over-year basis.

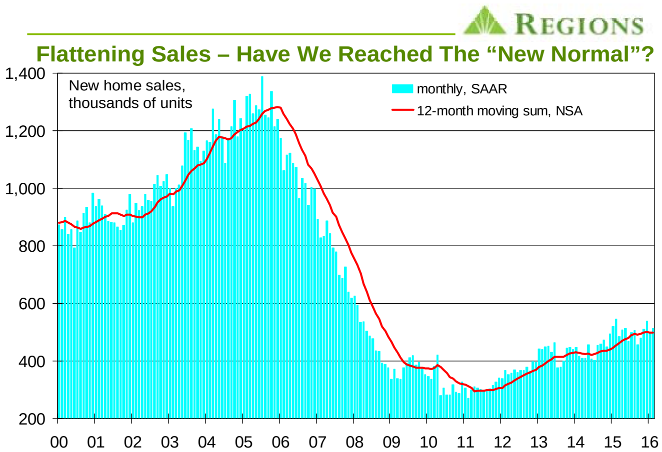
New home sales rose to an annualized rate of 512,000 units in February, right in line with the consensus estimate, from an upwardly revised January sales rate of 502,000 units. The increase in February, however, was driven solely by the West region, making up for January's sharp drop in sales stemming from abnormally high rainfall (thanks, El Nino) across the region. Sales in the Midwest, Northeast, and South regions fell in February. Inventories of new homes for sale posted another in a string of modest advances and the months supply metric remained at 5.6 months, consistent with the theme of an undersupplied market. The median sales price settled in at just under $299,000, reflecting a 2.6 percent increase from a year ago.

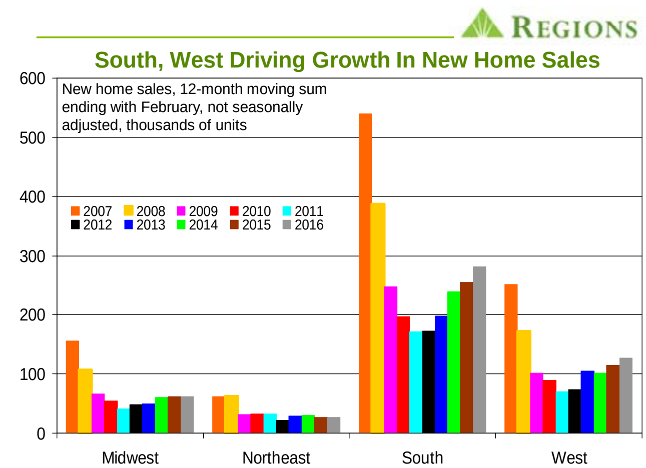
Now that we've fulfilled our duty of relaying the seasonally adjusted annualized rate headline numbers, we can get to the task of discussing the data in our preferred manner. Not seasonally adjusted (or annualized) sales hit 44,000 units in February, the best month since last June. This was also our forecast for raw sales, but our forecast for the headline sales number – 540,000 units – proved to be well off the mark as the February seasonal adjustment factor was much lower than we expected. This was also the case in the existing home sales data – one likely cause is that this February was a leap year so there would have been an added adjustment to eliminate the impact of the extra sales day. Still, as we have routinely pointed out, accounting for these issues helps dress up the headline numbers but tells us nothing about the underlying trend. Our preferred metric – the 12-month moving sum of raw sales, stands at 499,000 units, which reflects a 9.7 percent increase from a year ago – compared to a 6.1 percent decline in the seasonally adjusted annualized headline number.

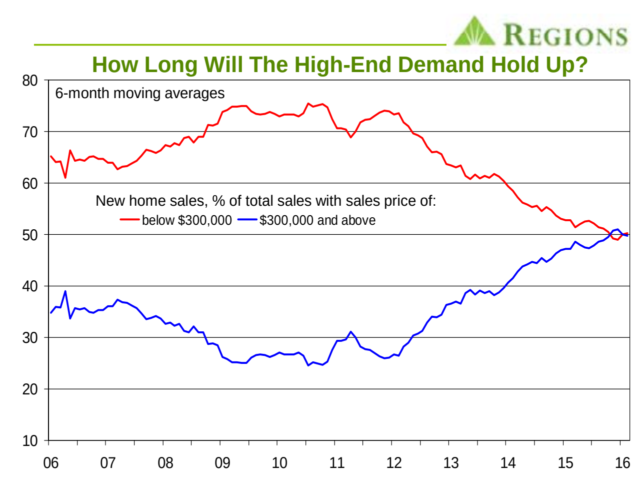
What we find of more interest is that the 12-month moving sum of sales has flattened out at an average of 500,000 units over the past few months, raising the question of whether this is as good as it gets. We strongly doubt that to be the case and expect coming months to fall back into the pattern of slow but steady improvement seen over the past few years. As seen in the middle chart, though, the growth in new home sales over the course of this cycle has been driven almost exclusively by the South and West regions, while sales in the Midwest and Northeast have barely budged. As for growth in overall new home sales, while rising, inventories of new homes for sale remain well below historical norms as builders continue to point to constraints on lots, labor, and materials, constraints which have shown some signs of easing but continue to throttle development.

Another factor, at least in our view, acting as a brake on the pace of growth in sales is the ongoing focus on the higher price points. As seen in the bottom chart, sales of homes priced at or above $300,000 began to account for an increasing share of total new home sales back in 2012 and that share has since risen steadily. As we put it, builders are making up for in margin what they are lacking in volume. It should also be noted that many of the homes sold in the early phases of this recovery had been built, or at least started, in 2006-08, when there was far more activity on the lower end of the price spectrum. Recall that when sales fell off the table builders got caught out having started on a considerable number of spec homes, and that for almost four years completions ran well ahead of starts and sales. Once that backlog was cleared, builders of course built fewer spec homes and what they were building were higher priced homes, which has largely continued. While DR Horton has made considerable headway focusing on entry level new homes other large builders have yet to follow suit. We continue to wonder, though, how much more support there is on the high end of the market.

Despite the flattening out of the trend sales rate, we continue to expect new home sales to turn up, albeit at the same slow and steady pace, in the months ahead. We'd argue one upside risk to our below-consensus forecast would be more builders moving into the lower price points, which we believe would drive a faster pace of sales.

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