ECONOMIC UPDATE

REGIONS

November 17, 2017

October Residential Construction: An October Surprise Of A Different Sort

- Total housing starts rose to an annualized rate of 1.290 million units; total housing permits rose to an annualized rate of 1.297 million units.
- Single family starts rose to 877,000 units while single family permits rose to 839,000 units (annualized rates).
- Multi-family starts rose to 413,000 units and multi-family permits rose to 458,000 units (annualized rates).

In the political realm, the term "October surprise" conjures up dread, at least amongst those worrying they might be the subject of such a surprise. In the seemingly more staid realm of residential construction, surprises actually come fairly frequently, but determining whether they are good surprises or bad surprises is often open to interpretation. Which is how we'll characterize the report on October residential construction. Total housing starts blasted past expectations in October, with the annualized rate of 1.290 million units coming in well above the highest forecast. This is also the case with total housing permits, with the annualized rate of 1.297 units also coming in ahead of the most optimistic forecast. At the risk of eliciting yet another "there they go again" reaction from our readers, we'll put the October data down as a bad surprise, as jumps in multi-family permits and starts are the primary factors behind this October surprise.

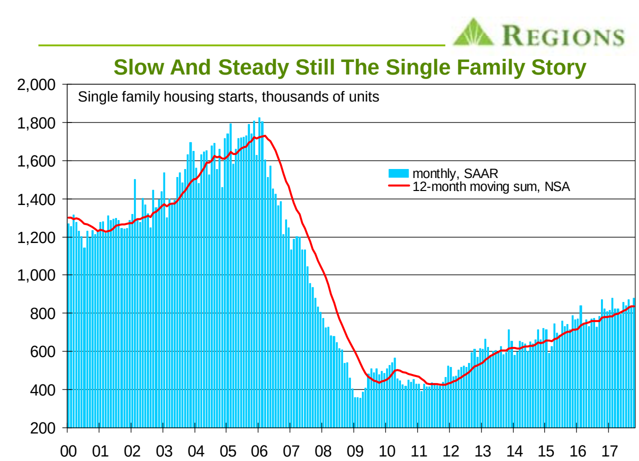
On a not seasonally adjusted basis, there were 112,300 total housing starts in October, easily topping our forecast of 101,200 starts. The unadjusted data show total housing permits of 112,100 units, topping our forecast of 106,800 units. For both permits and starts, we had the single family segment pegged, but multi-family permits and starts came in well above our forecasts. That and some favorable seasonal adjustment led to the jumps in the seasonally adjusted annualized data. On this basis, multi-family permits came in at an annualized rate of 458,000 units, up from a rate of 402,000 units in September, while multi-family permits came in at an annual rate of 413,000 units, up from September's rate of 302,000 units.

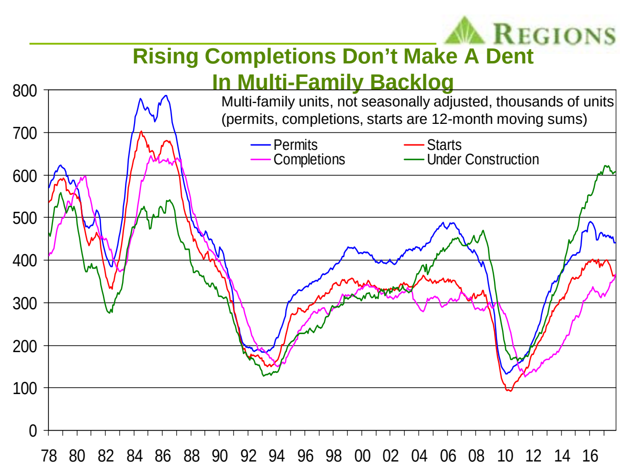
While the tendency may be to assume the jumps in October reflect post-hurricane rebuilding efforts in Texas and Florida, the (not seasonally adjusted) data offer mixed evidence. There were 13,000 multi-family starts in the South region in October, up from 11,600 in September and 8,700 in August, but the October figure simply puts multi-family starts back at what had been the run rate prior to the storms. But, combined starts in the Midwest and Northeast regions in October were roughly double the combined total for September. The 7,800 multi-family starts in the Northeast region in October were the highest monthly total since mid-2015, when the pending expiration of tax credits in New York was inflating multi-family starts.

As we have noted on many occasions, the backlog of multi-family units under construction remains larger than at any point since the mid-1970s. This reflects high levels of multi-family permits and starts and what has been a notably slow pace of multi-family completions. While October saw a jump in completions, this didn't really make a dent in the backlog of multi-family units under construction, as seen in the chart below. It is worth noting that banks have been tightening lending standards on multi-family loans over the past few quarters while also reporting waning demand for multi-family loans. The way to reconcile these seemingly conflicting trends is to note that private equity has rushed into any void left by commercial banks pulling in the reins on multi-family lending. We've been quite clear in our view that, yes, there is solid demand for multi-family rental units, just not nearly enough to absorb the supply in the pipeline.

The single family segment of the market is a different story, one in which supply is not keeping pace with healthy growth in demand. The 74,900 single family starts in October (not seasonally adjusted) bring the running 12-month total (the best gauge of underlying trends) to 837,700 units, the highest such total since May 2008. Shortages of lots and labor combined with rising materials costs have dampened the pace of growth in single family construction for some time now, and we do not expect this to change any time soon.

Our 2017 outlook called for slow but steady growth in single family activity and steadily easing multi-family activity leaving total housing starts up modestly. Our view has not changed, but the October data are a reminder that even we are correct in our assessment of the path of the housing market, there can still be plenty of surprises along the way.





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