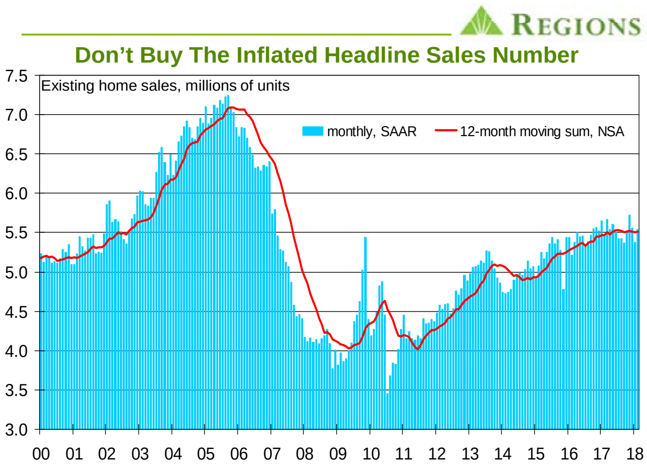
ECONOMIC UPDATE
REGIONS
March 21, 2018

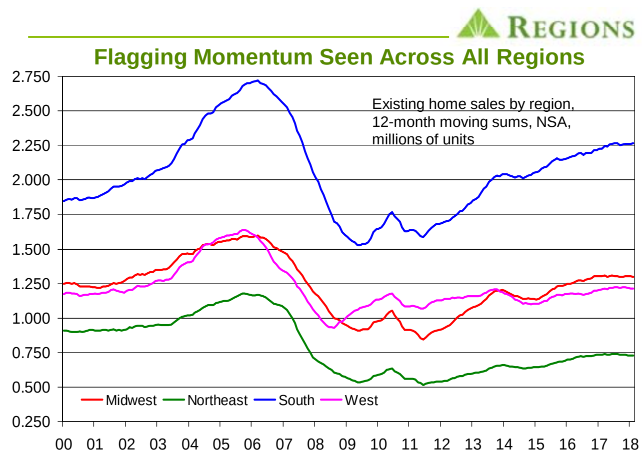
February Existing Home Sales: Don't Buy The Inflated Headline Sales Number

- Existing home sales rose to an annualized rate of 5.540 million units in February from January's sales rate of 5.380 million units.
- Months supply of inventory stands at 3.4 months; the median existing home sale price rose by 5.9 percent on a year-over-year basis.

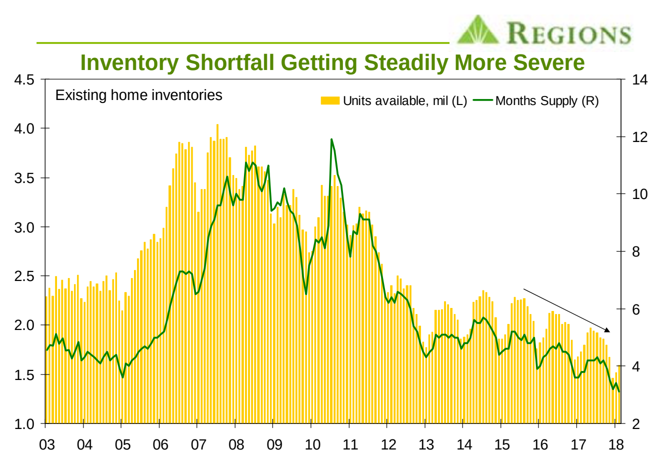
Well, problem solved. Total existing home sales jumped to an annualized sales rate of 5.540 million units in February from January's lackluster sales rate of 5.380 million units. Those of us who have been bleating on about shortages of homes for sale surely must feel silly in the wake of today's release, as the jump in sales in February must prove the housing shortage is no more. Except of course it still is, and the only cause we have for feeling silly is for badly underestimating the seasonal adjustment factor used to derive the seasonally adjusted annualized headline sales number, which is to say none at all. On a not seasonally adjusted basis, there were 319,000 total sales in February, slightly ahead of our forecast of 314,000 sales. That our forecast of the headline sales number – 5.360 million units – was so far below the reported headline number simply reflects the extent to which that headline number is inflated by the seasonal adjustment factor. And, underneath that headline number, the details of today's release do not at all change what for some time now has been our housing market story, i.e., notably lean inventories remain a material drag on sales and continue to drive robust house price appreciation. While we're not at this point quite yet, continued robust price appreciation combined with higher mortgage rates will at some point take a toll on affordability and further restrict sales.



On a not seasonally adjusted basis, the 319,000 sales in February reflect a 1.9 percent increase from January, well below the average increase of 5.1 percent for the month of February in the life of the data. And, as we routinely note, we view the running 12-month sum of not seasonally adjusted sales as the most reliable gauge sales of underlying sales trends. As of February, the running 12-month sum (seen in the red line in our top chart) stands at 5.509 million units and has basically not budged over the past six months. Our middle chart takes this one step further, as it presents the running 12-month total of unadjusted sales for each of the broad geographic regions. As seen in the chart, sales have flattened out in each of the four broad regions, and there is little in the inventory data to suggest any meaningful change in these trends any time soon.



We are in that time of the year in which listings begin to rise ahead of the peak selling season. February saw listings rise by 4.6 percent from January, which is the largest monthly increase since last April (the NAR's inventory data are not seasonally adjusted) but still smaller than the average increase for the month of February. More significantly, even with the increase in February listings are down 8.1 percent year-on-year, the 33rd consecutive month in which listings are down year-on-year. As our bottom chart shows, 2018 is on pace to be the fourth consecutive year in which the seasonal peak in inventories is lower than that of the prior year. As of February, the months supply metric stands at 3.4 months, compared to the 6.0 months figure that imply a balanced market.



The median number of days on market for sales that closed in February was 37 days, well below normal and down from 45 days a year ago. We've touched on what we see as the main factors behind the growing inventory shortfall on a number of occasions in a number of forums; the short list includes a significantly smaller inventory of distress properties, owners in negative equity positions, the rise of single family REITs, and rising mortgage interest rates. While the drag from negative equity has diminished considerably over the past several quarters, we believe the drag from rising mortgage interest rates is only beginning to gather pace. In other words, the higher mortgage rates go, the larger will be the pool of current owners unlikely to move if doing so entails trading up into a more expensive home at a higher mortgage interest rate. Keep in mind that for almost two years mortgage rates were below 4.0 percent, so anyone who took out or refinanced into a new mortgage at those low rates will be increasingly unlikely to give that rate up.

Our premise has for some time been that the issues in the housing market lie on the supply side of the market, not the demand side. We've yet to see anything to cause us to change our view, the gyrations in the headline sales numbers notwithstanding.

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