ECONOMIC UPDATE

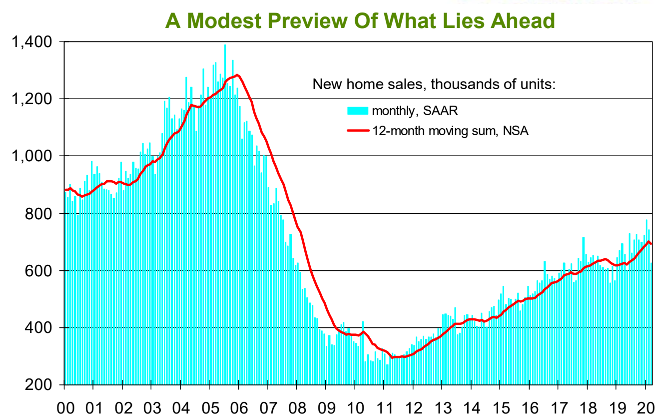
REGIONS

April 23, 2020

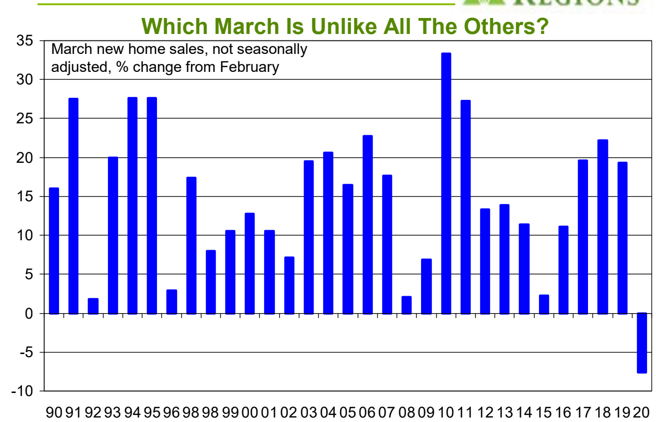
March New Home Sales: A Modest Preview Of What Lies Ahead

- New home sales fell to an annual rate of 627,000 units in March from February's (revised) sales rate of 741,000 units
- Months supply of inventory stands at 6.4 months; the median new home sale price rose by 3.5 percent year-on-year

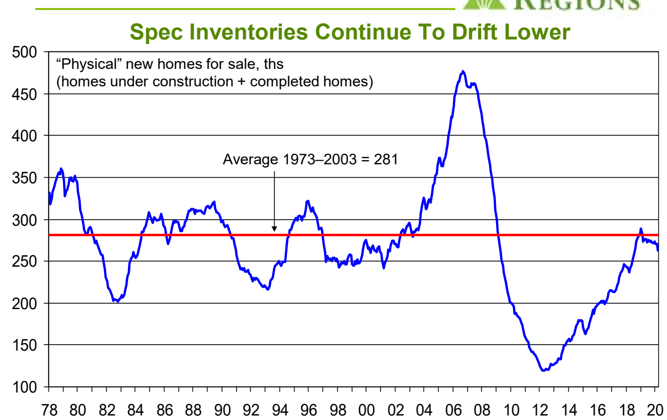
Total new home sales fell to an annualized rate of 627,000 units in March, weaker than our forecast of 662,000 units. Ahead of today's release, the two main questions we had were the extent to which the effects of the coronavirus would impact new home sales in March and to what extent would the Census data capture this impact. As to the latter question, Census reports that their data collection methods did change, reflecting factors such as social distancing and some local government offices either being closed or operating at diminished capacity. But, Census reports that response rates were within a normal range, and that the quality of the new home sales data is also within normal range, which may or may not make anyone feel any better about the data given how the initial estimate of new home sales in any given month is prone to sizable revision. Of more significance, sales activity did slow and cancelations of previously signed sales contracts increased over the back half of March. The latter point is important, because the Census data on new home sales do not account for cancellations – new home sales are booked when the sales contract is signed, regardless of whether the sale is ultimately closed. As such, reported new home sales will overstate sales during times of rising cancellations, but with builders reporting that cancellations have risen sharply in April, this will be a bigger issue in the April data than in the March data.



On a not seasonally adjusted basis, our forecast anticipated 64,000 new home sales. As we noted in this week's *Economic Preview*, this would have been a decline from unadjusted sales in February, making this the first time in the life of the new home sales data, which go back to 1963, that unadjusted new home sales declined in the month of March. As it turns out, unadjusted sales were weaker than our forecast anticipated, with sales of 61,000 units, reflecting a 7.58 percent decline from unadjusted sales in February. In a typical year, March is the month in which not seasonally adjusted sales post the largest increase of any month, so any weakness in unadjusted sales will be significantly amplified by seasonal adjustment, as is reflected in the headline sales number – March's seasonally adjusted and annualized sales rate is 15.38 percent lower than February's, which is the largest such decline since July 2013. Still, given that sales were solid over the first half of March before faltering over the second half of the month, it is the April data that will offer a more complete picture of the extent to which the coronavirus and the efforts to contain it have impacted new home sales.



That builder sentiment plummeted in April – the NAHB's index of builder sentiment posted the largest monthly decline in the 30-year history of the survey – offers an early glimpse of the impact on new home sales. Buyer traffic has fallen off sharply; while most new home communities remain open, viewings are by appointment only, which clearly has taken a toll on traffic. Still, while overall traffic is down, several builders are reporting that the "quality" of the traffic that remains is very high, i.e., those who are still shopping are motivated to buy, and favorable mortgage interest rates are helping sustain this motivation. Additionally, activity amongst first-time buyers has picked up; coming from rentals, first-time buyers do not have to worry about selling a home before purchasing a new home.



Still, the bottom line is that low mortgage interest rates are not providing as much of a lift to home sales (new or existing) as would otherwise be the case, given that many lenders have tightened lending standards, either requiring higher minimum credit scores or charging rate premiums for those with lower credit scores, and many lenders are also being more strict on back-end debt-to-income ratios. That applications for purchase mortgage loans are down better than 30 percent year-on-year as of mid-April reflects the extent to which home sales are being impacted and also affirms our point that the April sales data will be much weaker than the March data. If there is a silver lining to be found here, it is that builders are better positioned to withstand a decline in sales than has been the case in past cycles. Spec inventories have remained below longer-term averages, and had been declining over recent months, even as sales were strong. The current downturn in home sales comes amidst a persistent undersupply of homes – new and existing – for sale, in stark contrast to the massive oversupply seen in the last cycle. The decline in sales, though severe, figures to be fairly short-lived, meaning builders are better positioned to withstand it.

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