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May Residential Construction: A Curiously Subdued Move Toward Normal

- › Total housing starts rose to an annualized rate of 974,000 units; total housing permits rose to an annualized rate of 1.220 million units
- › Single family starts rose to 675,000 units and single family permits rose to 745,000 units (seasonally adjusted annualized rates)
- › Multi-family starts rose to 299,000 units and multi-family permits rose to 475,000 units (seasonally adjusted annualized rates)

Total housing starts rose to an annualized rate of 974,000 units in May, short of what we and the consensus expected, with total housing permits increasing to an annualized rate of 1.220 million units, also short of what we and the consensus expected. That permit issuance and starts in the multi-family segment were a bit softer than our forecast anticipated isn't concerning, given the inherent month-to-month volatility in this segment. That single family permit issuance and starts underperformed our forecast by such a wide margin is curious, particularly given that our misses are concentrated in the South region, which includes both Florida and Texas. These were amongst the states in which restrictions on economic activity were not as onerous and had begun to ease earlier relative to most other states. Moreover, various industry reports pointed to a much more pronounced pick-up in construction in May, which helped shape our forecast. Given the momentum on display prior to the COVID-19 virus, the question now becomes whether May was more of a transition month, with activity in the South picking up in June, or whether lingering disruptions in the labor market will take a heavier toll on homebuilding. Given that the South region accounts for such a large share (roughly 56 percent) of total single family housing starts, this is a question with more than regional significance attached to it.

On a not seasonally adjusted basis, there were 89,300 total housing starts in May, well below our forecast of 102,800 total starts. As noted above, the South region underperformed our forecasts, with both single family starts (34,000 units) and multi-family starts (8,800 units) falling well short of our forecasts. The 8,800 multi-family starts is the lowest monthly total in the South region since August 2017, when construction was disrupted by hurricanes. Single family starts also decreased in the Midwest region in May while rising in the Northeast and South regions.

On a not seasonally adjusted basis, there were a total of 105,100 housing units permitted in May, below our forecast of 117,000 units. As with housing starts, single family housing permits (66,100 units) fell short of our forecast (76,500 units), and while the South region

accounted for most of our forecast miss, single family permit issuance in the Midwest and South region came in slightly below our forecasts. May saw total housing completions of 93,000 units (not seasonally adjusted), little changed from the 93,900 units completed in April, though the mix of completions shifted as single family completions fell while multi-family completions edged higher. Over the past 12 months, there have been a total of 1,233,700 housing units completed, with 899,600 single family units and 334,100 multi-family units completed.

The slight increase in multi-family completions in May didn't even begin to put a dent in what remains a sizable backlog of multi-family units under construction. As of May, there were 669,000 multi-family units under construction in the midst of the largest and most persistent backlog of multi-family units under construction since the mid-1970s. That job losses in March and April were highly concentrated amongst lower wage industry groups means the drag on multi-family demand could persist, adding to our concerns about the supply side of the multi-family segment of the market.

We are also concerned about the supply side of the single family segment of the housing market, but for quite the opposite reason. The single family segment remains considerably undersupplied, which has been the case for years. The appropriate reference point in our first chart below isn't the spike associated with the housing market excesses prior to the 2007-09 recession, but to earlier years when single family starts of between 1.0 and 1.2 million were considered "normal." Single family starts had been pushing toward that 1.0 million mark prior to March, and it remains to be seen whether, or when, that push will resume – which very much goes to our point about the curious softness in the May data for the South region. Applications for purchase mortgage loans now stand at a more than 11-year high, mortgage rates remain quite favorable, and builder sentiment has improved markedly. As such, we expect the pace of single family construction to pick up in the months ahead, particularly in the South region.

