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### August New Home Sales: Sales On A Roll, But Downside Risks Remain

- › New home sales rose to an annual rate of 1.011 million units in August from July’s (revised) sales rate of 965,000 units
- › Months supply of inventory stands at 3.3 months; the median new home sale price fell by 4.3 percent year-on-year

Total new home sales rose to an annualized rate of 1.011 million units in August, besting our above-consensus forecast of 981,000 units and easily ahead of the consensus forecast of 900,000 units. At the same time, prior estimates of sales from May through July were revised significantly higher, which doesn’t alter what all along has been our view of the new homes market but which does at least bring the Census estimates more in line with the tone of industry analysis and builder commentary during this time span. On a not seasonally adjusted basis, there were 83,000 new home sales in August, just ahead of our forecast of 82,000 sales, which does suggest the headline (i.e., seasonally adjusted and annualized) sales number was flattered by a favorable seasonal adjustment factor, though not nearly to the extent as was the case with August existing home sales. The August data (and the revisions to the prior few months) point to continued strong demand for new home sales, fueled by low mortgage interest rates and a harder push to exurban areas in reaction to the pandemic. But, while affirming what has been our above-consensus outlook for sales in the near term, the August data leave us with the same concerns as to how long this strength in sales can be sustained. Inventories of new homes for sale remain lean, affordability remains a concern even if a material and sustained increase in mortgage interest rates seems a remote possibility, and there are signs that the recovery in the labor market is stalling. As such, while further increases in new home sales won’t surprise us, we do think that there are limits on how much higher sales can climb, even if at present we can’t clearly define those limits.

The 83,000 new homes sold in August bring the year-to-date total for not seasonally adjusted sales to 542,000 units, which is an increase of 14.8 percent over 2019’s year-to-date total through August. This contrasts with existing home sales, where the year-to-date total of unadjusted sales was down by 3.2 percent through August. The 83,000 new home sales in July (revised up from the initial estimate) and August make these the best months for new home sales since April 2007. On a year-to-date basis through August, unadjusted new home sales are up by 30.0 percent in the Northeast region, by 26.5 percent in the Midwest region, by 13.8 percent in the South region, and by 11.8 percent in the West region. The 52,000 new home sales in the South region in August mark that region’s highest monthly total since May 2006 – the South accounts for roughly 58 percent of all new home sales. It does bear noting that sales in the West and South regions could be quite volatile over the next few months, reflecting the impact of the severe fires in the West and flooding in the South.

Though not nearly to the extent as in the market for existing homes, inventories of new homes for sale remain lean and builders are increasingly pressed to keep pace with demand. Though the ongoing shift to exurban areas – which the pandemic did not start but which it has intensified – has helped alleviate shortages of buildable lots and a more stringent regulatory environment, labor shortages remain a constraint on supply. True, builders can work off backlogs of unfilled orders over time, but at some point this becomes a drag on sales, and some builders have taken to raising prices as a means of managing demand, which gets us back to our point on affordability. Even should one not buy our caveats on the demand side, it’s hard to ignore what remain pressing supply constraints. To that point, spec inventories fell further in August, continuing a downward slide that began in early-2019, as our middle chart shows.

Lean inventories and higher materials costs, even allowing for the recent easing of lumber prices, are keeping upward pressure on new home prices. The median price did fall in August thanks to a jump in sales in the \$200,000-\$300,000 price range, but this is unlikely to be sustained in the months ahead. It is also interesting to note that while the new home “premium,” i.e., the gap between median sales prices for new and existing homes, does continue to narrow, this is because the median existing home sales price is rising so rapidly as opposed to a sustained easing of the median new home sales price. Inventory constraints remain a headwind to sales of both existing and new homes, meaning that as long as demand remains robust, diminished affordability becomes an increasing threat to home sales.

