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September New Home Sales: Weaker Than Headline Number Implies, But Why?

- New home sales fell to an annual rate of 0.959 million units in September from August's (revised) sales rate of 0.994 million units
- Months supply of inventory stands at 3.6 months; the median new home sale price rose by 3.5 percent year-on-year

Let's start with a round of "which one is not like the others": a) single family housing permits and single family starts atypically strong for the month of September; b) homebuilder confidence at record highs; c) industry reports and commentary from builders indicating builders not being able to keep pace with demand; d) new home sales not only coming in well below expectations but being atypically weak for the month of September. If you selected "d" then, well, congratulations, you've demonstrated a firm grasp of the obvious. What would be really impressive would be being able to make sense out of new home sales being so at odds with other data series produced by the same agency. Other than the explanation we offered in our weekly *Economic Preview* – that one never knows with new home sales, which seem to derive an undue amount of pleasure from mocking forecasters – we're not sure how else to account for the data on September new home sales. Total new home sales fell to an annualized rate of 959,000 units in September, easily below the consensus forecast of 1.023 million units and our forecast of 1.092 million units. Not seasonally adjusted sales fell to 75,000 units, cruelly mocking our forecast of 89,000 units and down from 82,000 units in August. As we also noted in our *Preview*, September has historically been a seasonally weak month for housing market activity – with single family permits, single family starts, existing home sales, and new home sales tending to decline in September. The first three of these metrics not only increased in September but did so to a degree that made a mockery out of the normal seasonal patterns. That single family permits and starts help inform the Census Bureau's estimate of new home sales suggested new home sales would also outperform typical seasonal patterns. Okay, sure, they kind of did, just not in the manner we expected. The 8.5 percent in not seasonally adjusted new home sales this September was larger than the average September decline of 7.5 percent over the 1990-2019 period. Which is the kind of "outperformance" we can live without.

To be clear, it isn't the headline sales number but rather the number of not seasonally adjusted sales in September – 75,000 units – that seems so out of line. A seemingly plausible explanation would be that, as with existing home sales, inventory constraints are acting as a meaningful drag on new home sales. To be sure, we have for some time been pointing to this as an issue in the market for new homes, and in our *Economic Preview* we cited spec inventories as one of the beneath the headline numbers to watch. Spec inventories did fall further in September and are at the lowest level since May 2017. But, one offset for builders is that new home sales can be booked at any stage of the construction process or before construction has started. Units on which construction had not yet started accounted for one-third of all new home sales in September, which along with the further decline in spec inventories signals that builders are having trouble keeping pace with demand. It could be that sparse inventories of completed or under construction homes were suddenly more of an impediment to sales in September, or it could be that builders simply stopped taking orders in the face of growing backlogs of unfilled orders. Neither, however, seems all that satisfying as an explanation for how weak not seasonally adjusted new home sales were in September.

The reality is that it seldom pays to spend too much time trying to make sense out of whatever we're told new home sales are in any given month. Instead, the focus should remain on the underlying sales trend. Even with sales being weak in September, the running 12-month total of not seasonally adjusted sales, which we see as the best gauge of the underlying sales trend, rose to 771,000 units, the highest such total since December 2007. As we are in a seasonally weak time of the year, the trend sales rate can be expected to level off, which is not to say demand is set to take a tumble. We do, however, remain concerned over affordability, which is true of both new and existing homes. 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.

