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## May New Home Sales: We Expected Little, And Got Even Less . . .

- > New home sales fell to an annual rate of 0.769 million units in May from April's (revised) sales rate of 0.817 million units
- > Months supply of inventory stands at 5.1 months; the median new home sale price rose by 18.1 percent year-on-year

We expected little and got even less. That's about the most charitable spin we can put on the report on May new home sales. Total new home sales fell to an annualized rate of 769,000 units in May, below our low-end forecast of 806,000 units but an extreme makeover from the consensus forecast of 865,000 units. Moreover, earlier estimates of sales over the prior three months were revised down substantially; prior estimates put the average monthly sales rate over the February-April period at 878,000 units, but the revised data show an average monthly sales rate of 842,000 units, though we'll note that the revised data are more in keeping with the industry data and builder commentary that we track. While there was some modest improvement on the inventory front, the market remains meaningfully undersupplied which, along with higher materials costs, has contributed to rapidly rising home prices. The median new home sales price was up 18.1 percent year-on-year in May. There are factors on both the demand side and the supply side of the market that have weighed on sales over the past few months, and we expect this to remain the case in the months ahead.

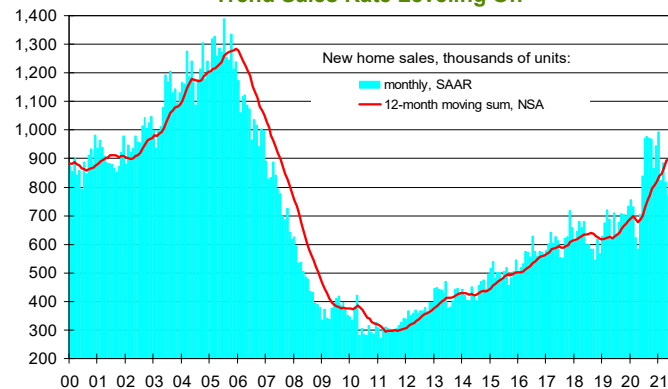
On a not seasonally adjusted basis, there were 69,000 new home sales in May, below our forecast of 73,000 sales and down 8.0 percent from April, meaning sales were much weaker this May than is typically the case for the month. Sales fell sharply in the South region, from 45,000 units in April to 38,000 units in May, with sales down slightly in the Midwest region, unchanged in the West region, and up modestly in the Northeast region. The decline in sales in the South region, which accounts for over one-half of all new home sales, has been hard and fast; recall that sales in the South region jumped to 53,000 units in March, the region's highest monthly sales total since April 2006. Nationally, the unadjusted data show that over the past twelve months there have been a total of 898,000 new home sales. While this is the highest such total since July 2007, further increases in this metric, which we see as the most reliable gauge of the underlying trend rate of sales, will be difficult to sustain.

Supply side factors are weighing on sales. Many builders have either curtailed the number of build-to-order sales then are engaging in or cut them out altogether. In part, this reflects the extent to which order backlogs have grown, and limiting new orders will buy time for builders to work down these backlogs. Keep in mind that new home sales are booked at the time the sales contract is signed, and this could come at any stage of construction, i.e., before construction has started, while construction is underway, and after construction has been completed. We have for some time been pointing to the elevated share of new home sales accounted for by units on which construction had not yet started, thus adding to backlogs of units builders are committed to delivering. In an atmosphere in which materials prices are rising and materials delivery times are being stretched, sitting on growing backlogs of unfilled orders becomes increasingly less comfortable. Recent months have seen more builders turn to spec construction, i.e., starting units and not pricing them until construction is well underway, which passes pricing risk on to buyers. This is behind the modest increase in spec inventories as the number of completed homes for sale, the other component of spec inventories, has declined dramatically over the past several months.

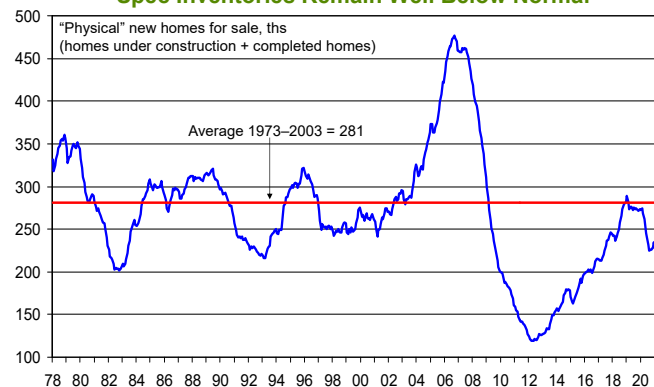
The decline in sales isn't all about supply, or lack thereof, as there are signs that demand for home purchases is softening. For instance, applications for purchase mortgage loans remain elevated relative to the levels seen over the past decade but are nonetheless slipping. Part of this could simply reflect record-low mortgage interest rates having pulled some demand forward into the back half of 2020, and we have for some time been pointing to this as one factor that could lead an easing in the pace of new home sales. That said, it is likely that affordability constraints are becoming more binding, even with mortgage interest rates having been fairly stable over the past several weeks. This simply reflects the extent to which home prices, new and existing, have risen. For builders, there is little latitude on the pricing front given the extent to which physical shortages of materials have contributed to higher input costs, though the recent drop in lumber prices offers some hope of relief. Though having softened, demand nonetheless remains fairly strong, meaning that supply side factors are likely to remain the more binding constraint on sales in the months ahead.



### Trend Sales Rate Leveling Off




### Spec Inventories Remain Well Below Normal




### It Isn't All About Supply . . .

