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July New Home Sales: Sales Finding Firmer Footing

- › New home sales rose to an annual rate of 708,000 units in July from June's (revised) sales rate of 701,000 units
- › Months supply of inventory stands at 6.2 months; the median new home sale price rose by 18.4 percent year-on-year

Total new home sales rose to an annualized rate of 708,000 units in July, landing between the consensus forecast of 697,000 units and our forecast of 722,000 units. Revisions to estimates of sales over recent months were kind, with upward revisions to April, May, and June, breaking the pattern of sharp downward revisions that had taken hold. While the data indicate some relief on the supply side of the market, we think that is to some extent misleading given what have been notable changes in selling strategies amongst many builders over recent months. Be that as it may, the median new home sales price rose 18.4 percent year-on-year, which reflects meaningfully higher materials costs combined with strong demand, even if less strong than had been the case. While we look for sales to advance further over coming months, the pace of any such advance is likely to remain fairly moderate, with builders exercising more control over the pace of construction and sales than had been the case up until a few months ago.

On a not seasonally adjusted basis, there were 63,000 new home sales in July, matching June sales (which were revised higher) and topping our forecast of 61,000 sales. As a side note, that not seasonally adjusted sales topped our forecast while the seasonally adjusted annualized sales rate fell short of our forecast simply reflects the July seasonal adjustment factor being smaller than we had anticipated, which matters not a whit. Unadjusted sales fell in the Midwest and Northeast regions and rose in the South and West regions; the decline in sales in the Midwest stands out, as the 6,000 sales were that region's lowest monthly total since February 2020. As noted in our top chart, the running 12-month total of not seasonally adjusted new home sales fell further in July, now standing at 854,000 units. This metric, which we see as the most reliable gauge of the trend rate of sales, hit a peak of 892,000 units in both April and May and has now fallen for two straight months.

While we expect further declines in the trend sales rate in the months ahead, it helps to put this in proper perspective. Recall that it was last June that new home sales began to shoot higher as falling mortgage rates fueled robust demand. Over the past few months, however, sales have slowed sharply, and year-on-year declines in sales are pulling the running 12-month total lower. Also recall that new home sales can occur at any phase of the construction process – before construction has started, while construction is in progress, and after construction has been completed. When sales began to shoot higher last year, units on which construction had not yet started began to account for a higher share of sales. Thus, while booking sales, builders were falling further behind on actual construction and delivery which, in the light of subsequent increases in materials prices and growing constraints on materials supplies, simply became untenable. One way builders reacted was the self-imposed caps on sales that became fairly widespread over recent months, with builders instead focusing on clearing backlogs of unfilled orders. Going back to the Midwest region, while sales were notably low in July, single family starts in the region were quite strong, which would go to our point about builders focusing on clearing order backlogs. Indeed, across each of the four broad Census regions, the ratio of single family sales to single family starts has fallen significantly over recent months. Many builders have begun to lift sales caps, but they are doing so gradually, as order backlogs remain substantial.

Another manner in which builders responded to higher prices for and uncertain supplies of materials was to begin construction but not price, and sell, homes until construction was well underway, thus transferring pricing risk to buyers. In other words, homes under construction are accounting for a significantly higher share of sales than is typically the case. We think this is a main factor behind the reported increases in spec inventories over recent months, but if we are correct on this point the increase in spec inventories is doing little in the way of providing relief from what remains a sizable imbalance between supply and demand. That imbalance is contributing to strong price appreciation, which is causing some prospective buyers to turn away from the market. To the extent that builders make some headway in paring down order backlogs and recent relief on materials prices holds, there is further upside room for new home sales in the months ahead, but the pace will be gradual.

