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July Residential Construction: (Another) Record-High Number Of Under Construction Units

- › Total housing starts fell to an annualized rate of 1.446 million units; total housing permits fell to an annualized rate of 1.674 million units
- › Single family starts fell to 916,000 units and single family permits fell to 928,000 units (seasonally adjusted annualized rates)
- › Multi-family starts fell to 530,000 units and multi-family permits rose to 746,000 units (seasonally adjusted annualized rates)

Total housing starts fell to an annual rate of 1.446 million units in July, even weaker than our well below consensus forecast of 1.472 million units, with steep declines in both single family and multi-family starts. Total housing permits fell to an annualized rate of 1.674 million units, well above our forecast of 1.579 million units. Kind of. The not seasonally adjusted data show total permits falling short of our forecast, so that the seasonally adjusted annualized number is so much higher than our forecast reflects nothing more than a more generous seasonal adjustment factor than we anticipated, which didn't of course result in more units having actually been permitted. This is yet another example of why we pay no attention to the seasonally adjusted annualized data on residential construction and sales. In any event, the real stories here are: 1) single family permits and starts have tailed off sharply; and 2) the backlog of housing units under construction, already at a record high, grew even larger in July. While to some extent ongoing supply chain issues are delaying completions, it is also likely that single family builders are not in any great hurry to complete unsold spec units and won't be until market conditions start to firm up. In the interim, we see further room to the downside for single family permits and starts.

On a not seasonally adjusted basis, there were 130,600 housing units started in July, below our forecast of 133,600 units and down 11.4 percent from June. At 84,900 units, single family starts came in above our forecast of 83,300 units but were nonetheless down 12.8 percent from June and down 22.6 percent from April, which saw the second highest monthly total of this cycle. At the time, we attributed the spike in single family starts in April to a rush to start and sell units before mortgage interest rates rose even higher, but to the extent there was such a rush, it is now more of a hasty retreat. Single family starts in the South region, which accounts for over one-half of all single family starts in the U.S., fell to 46,000 units in July, the lowest monthly total since February 2021. Single family starts in the Northeast region curiously jumped to 7,900 units, the most in over a year and much stronger than implied by recent permit issuance in the region, which

could simply reflect reporting issues (permits for attached single family units are often booked as multi-family permits).

On a not seasonally adjusted basis, there were 133,400 housing units permitted in July, below our forecast of 134,700 units. At 75,200 units, single family permits were weaker than our forecast of 79,900 units, and July's count is the lowest monthly total since May 2020. There were 43,500 single family permits issued in the South region, the fewest in over two years and down sharply from the 64,000 single family units permitted in March, which is a testament to how rapidly single family construction is slowing.

To the extent that rising backlogs of under construction spec units are weighing on starts, both single family permits and starts will fall further in the months ahead. To that point, as of July there were 839,100 single family units under construction, the most in any month since late-2006. Toss in the 863,500 multi-family units under construction in July and you get a total of 1,702,600 housing units under construction in July, the highest total on record. While the backlog of multi-family units under construction has been bloated for several years now, the growth in the single family backlog is more recent. In part, this reflects a shift in sales tactics amongst builders in mid-2021, moving to what we called "spec-lite" construction. Builders were starting more units but not releasing them for sale until construction was well underway, allowing them more control over the timing of deliveries and enabling them to shift price risk off to the buyers at a time of rapidly rising materials costs. We noted that increases spec building posed little risk as long as demand held up, but builders clearly were wrong-footed by the rapid increase in mortgage interest rates this spring and, as such, are seeing a most unwelcome accumulation of unsold units at various phases of construction. At the same time, backlogs of units which have been permitted but not yet started remain elevated and the pace of completions remains very much rangebound. Even with relief from supply chain constraints, a faster rate of completions won't really change much for builders until more buyers come back to the market.

