ECONOMIC UPDATE

REGIONS

January 26, 2023

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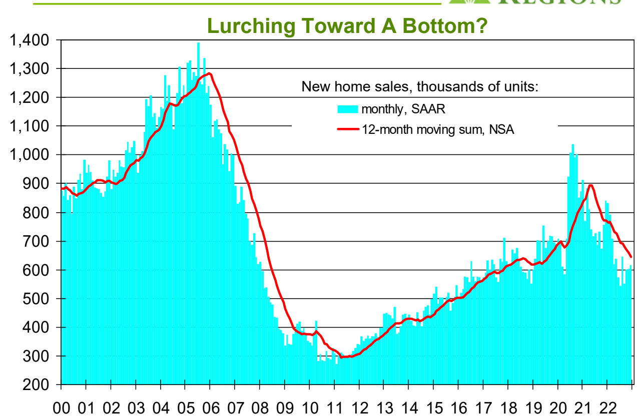
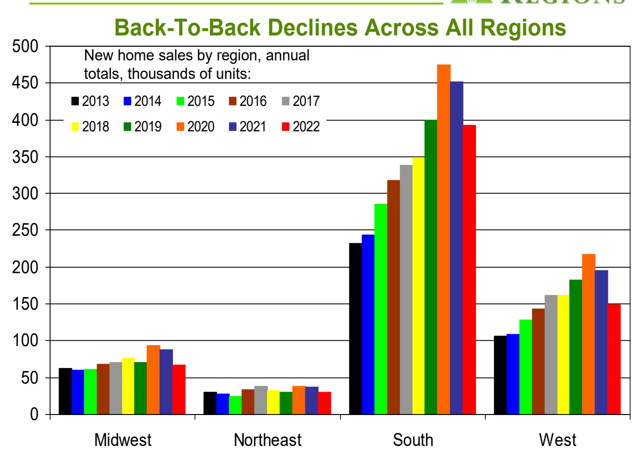
December New Home Sales: Lurching Toward A Bottom?

- New home sales <u>rose</u> to an annual rate of 616,000 units in December from November's (revised) sales rate of 602,000 units
- Months supply of inventory stands at 9.0 months; the median new home sale price <u>rose</u> by 7.8 percent year-on-year

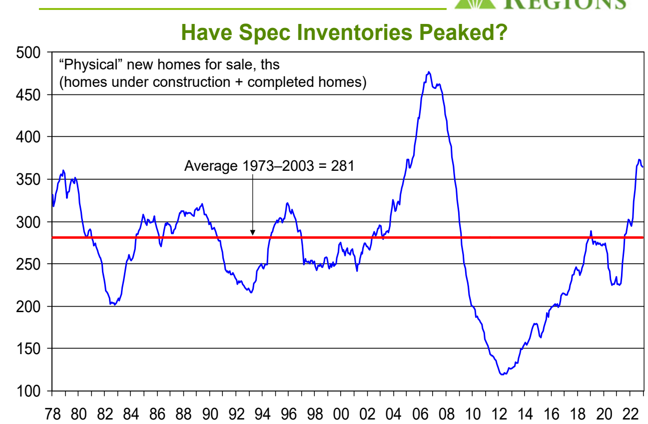
Total new home sales rose to an annualized rate of 616,000 units in December, matching our slightly above consensus forecast. On a not seasonally adjusted basis, there were 47,000 new home sales in December, a touch better than our forecast of 45,000 sales and up from 43,000 sales in November. Either way, experience tells us to not get too attached to these initial estimates of December sales, as the new home sales data are amongst the most volatile and most prone to sizable revision of the top-tier data series. To that point, the initial estimate of November sales showed an annualized sales rate of 640,000 units, which in today's release is now shown to be a rate of 602,000 units, with smaller downward revisions to both the September and October data. Still, even if the initial estimate of December sales meets the same fate as those of the prior several months, the narrative will remain the same, i.e., sales having fallen off sharply as mortgage interest rates rose left builders with growing inventories of spec homes for sale, and the market ended 2022 with inventories of new homes for sale equivalent to nine months of sales. Neither the median nor the average sales price suggests builders becoming meaningfully more aggressive in resorting to discounts in order to clear inventories; the median new home sales price was up 7.8 percent year-on-year while the average sales price, at $528,400, was virtually unchanged from November and was up 7.6 percent year-on-year. While builders have offered incentives, many have been non-price incentives, and it could be that with mortgage rates having fallen considerably from October's peak, builders don't feel all that compelled to offer more generous price concessions, particularly as there is still a high degree of pent-up demand for home purchases and inventories of existing homes for sale remain notably low. Builders seem, at least for now, content to play the long game and that may work out for them, in no small part due to how chronically undersupplied the market had been over the past several years.



For 2022 as a whole, the not seasonally adjusted data show 645,000 new home sales, a decline of 16.3 percent from 2021. Sales were down in each of the four broad Census regions, "led" by a 23.9 percent decline in the Midwest and a 23.6 percent decline in the West, with sales down 18.9 percent in the Northeast and down 13.1 percent in the South. Recall that new home sales also declined in each of the four broad Census regions in 2021, though the declines were much more severe in 2022. This helps illustrate a point we have made many times, which is that the declines in new home sales started as a supply-side story but have since become a demand side story.



Recall that many builders began to intentionally cap sales in mid-2021 as they were simply unable to keep pace with demand, and at the same time were holding off on releasing units for sale until construction was well underway. That strategy worked fine until it didn't, with rapidly rising mortgage interest rates turning the tables on builders, resulting in a significant, not to mention unwanted, increase in spec inventories of new homes for sale. At year-end 2022 spec inventories were 20.9 percent higher compared to year-end 2021. While the data show modest declines in spec inventories over the past few months of 2022, it's too soon, far too soon given the degree to which these data are revised, to conclude spec inventories have peaked. For instance, a meaningful deterioration in labor market conditions or mortgage rates reversing course and heading back up would trigger another drop in demand that would, even with single family starts having fallen off sharply, push spec inventories higher. For now, though, prospective buyers have responded to the dip in mortgage interest rates and, should this dip be extended, spec inventories will be further whittled down and those builders who have the financial capacity to hold out may not have to become much more aggressive in offering price concessions than they have been to date.



One shift we have seen over recent months is that, with single family completions having increased, completed units are accounting for a rising share of new homes for sale. Still, that rise comes off of what was in 2022 an all-time low share and, at 16.5 percent in December, the share is still far below historical norms. It could be that builders will feel greater urgency in offering concessions on completed units as they have some latitude in the pace at which under construction units are finished. We see the question not so much as whether there are buyers out there – there are – but instead how, and when, builders can draw them in.

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