ECONOMIC UPDATE

REGIONS

February 24, 2023

January New Home Sales: Strong January Can't Reverse Downward Trend

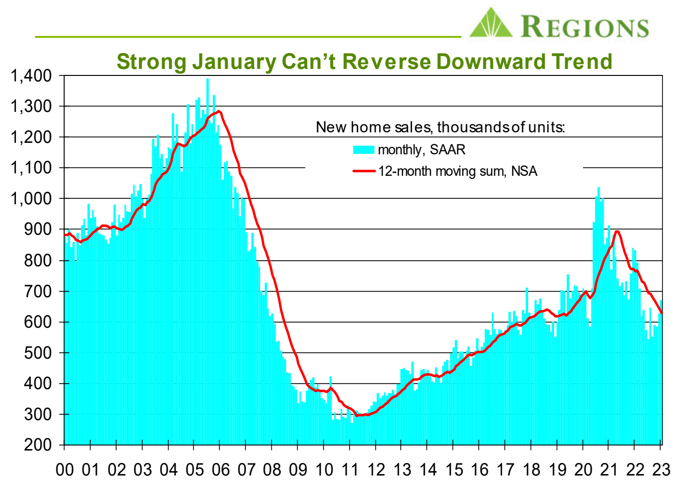
- New home sales rose to an annual rate of 670,000 units in January from December's (revised) sales rate of 625,000 units
- Months supply of inventory stands at 7.9 months; the median new home sale price fell by 0.7 percent year-on-year

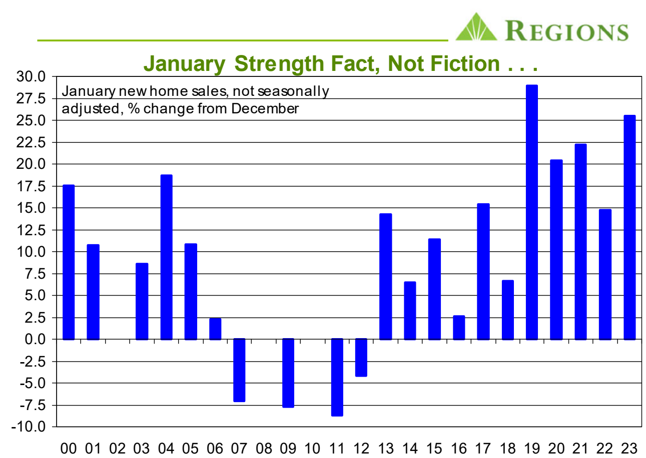
Total new home sales rose to an annualized rate of 670,000 units in January, trouncing our below-consensus forecast of 588,000 units. We'll gladly take our lumps on this one as, unlike much of the economic data for the month of January, the strength in new home sales is genuine as opposed to being little more than overly generous seasonal adjustment making numbers look better than is actually the case. For instance, our forecast anticipated not seasonally adjusted sales of 50,000 units, which would have been a 6.4 percent increase from December. As this would have been smaller than the typical January increase, we anticipated seasonal adjustment pushing the headline sales number lower. Instead, not seasonally adjusted sales came in at 59,000 units, a 25.6 percent increase from December and, as our middle chart shows, the largest January increase since 2019. January sales clearly benefitted from mortgage interest rates having been in retreat since topping out at over seven percent in October, and at the same time builders were more willing to offer concessions to help clear what had become significantly elevated spec inventories. It is worth emphasizing that the median new home sales price fell substantially in January, to the point that it was down 0.7 percent year-on-year. Recall that new home sales are booked at the signing of the sales contract, meaning that they are a much timelier gauge of how buyers are responding to changes, for better or worse, in affordability, whether via changes in mortgage rates or prices, than is the case with existing home sales, which are booked at closing. It is also worth recalling that Census reports new home sales on a gross basis, i.e., the data are not adjusted for cancellations, which had been on the rise over the prior several months. Builders report cancellation rates had mostly normalized in January, which further goes to our point that the January sales number is genuine. That said, don't get too used to it. Aside from the typical revisions to the initial estimate of sales in any given month – prior estimates of sales over the October-December period were revised lower, on net – mortgage interest rates have reversed course in February, and purchase mortgage loan applications have plummeted. That does not bode well for February new home sales, but we'll get to that a month from now . . .

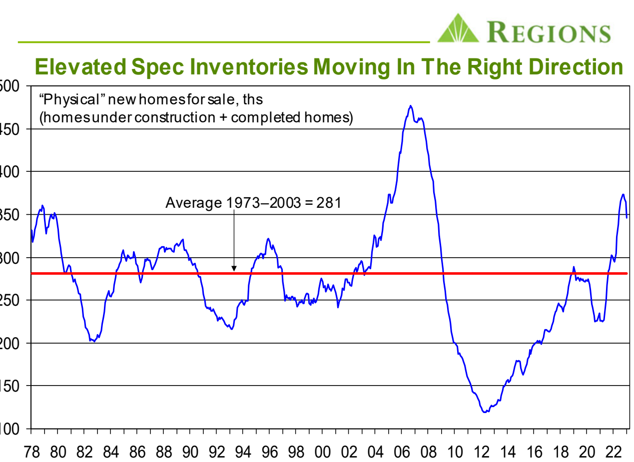
As noted above, on a not seasonally adjusted basis there were 59,000 new home sales in January, the highest monthly total since last March. The South region, which as defined by Census includes both Florida and Texas and which accounts for well over half of all new home sales, drove most of January's increase, with sales rising from 30,000 units in December to 41,000 sales in January. Sales were up modestly in the West region and flat in both the Midwest and Northeast regions. Still, despite the jump in sales in January, the running twelve-month sum of not seasonally adjusted sales, our preferred gauge of underlying sales trends, fell to 630,000 units in January, the lowest print since June 2019 when it also was at 630,000 units. The difference, of course, is that back then the trend sales rate was rising while at present it is falling and, if we are correct in expecting higher mortgage rates to dampen sales, will fall further in the months ahead.

The composition of sales across stages of construction in January is of note. Units under construction accounted for 39 percent of all new home sales in January, a smaller share than seen over much of 2021 and 2022, while completed units accounted for 35.6 percent of January sales, down sharply from the share over the prior three months. In contrast, sales of units not yet started accounted for 25.4 percent of January sales, the highest such share since last February. So, while builders were able to clear out some of their spec inventories in January, they also took considerably more new orders, thus adding to still-elevated inventories of units awaiting construction. To our earlier point about cancellations, it should not be lost that cancelation rates were normalizing during a time when mortgage rates were falling, and now that mortgage rates have reversed course, do not rule out cancellation rates doing the same, to the extent that buyers sign sales contracts prior to having locked their mortgage rate in place.

The January new home sales data are in line with our view that there is still meaningful pent-up demand for home purchases that will be drawn out by improvements in affordability. At the same time, however, rising mortgage rates will demonstrate how sensitive buyers are to affordability moving in the opposite direction, as we expect to see in the February data.







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