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March Residential Construction: Drop In Headline Number Dramatic, But Misleading

- Total housing starts fell to an annualized rate of 1.321 million units; total housing permits fell to an annualized rate of 1.458 million units
- Single family starts fell to 1.022 million units and single family permits fell to 973,000 units (seasonally adjusted annualized rates)
- Multi-family starts fell to 299,000 units and multi-family permits fell to 485,000 units (seasonally adjusted annualized rates)

Total housing starts fell to an annual rate of 1.321 million units in March, badly lagging expectations, ours and the consensus, while total housing permits fell to an annual rate of 1.458 million units, just a bit closer to our forecast of 1.455 million units than to the 1.510 million units anticipated in the consensus forecast. The all too predictable reaction to the big miss on housing starts is that it reflects the impacts of high mortgage interest rates, as builders and buyers take to the sidelines to await the drop in mortgage rates that will trigger a burst of building and buying. Well, we at least hope they're comfortable, as that may be a long wait. Before going any further, we'll repeat a point we made in this week's *Economic Preview*, which is that in any given year March is the month which typically sees the largest increases (percentage changes) in housing permits and housing starts, for both single family and multi-family units. As such, the seasonal factors used to derive the seasonally adjusted estimates tend to be rather punitive, meaning that any shortfall from the typical March increases will be treated somewhat rudely, biasing the seasonally adjusted estimates lower. While we can't speak for others, our miss on our forecast of housing starts is more than accounted for by multi-family starts coming in lower than we had anticipated, while the unadjusted data show single family housing starts coming in a bit ahead of our forecast. In that sense, given what is clearly a significant degree of pent-up demand for home purchases, despite elevated mortgage rates, and what remains a notably large backlog of multi-family units under construction, we're not at all troubled by the headline starts number being as low as it is. Neither are we troubled by the headline permits number, which goes straight to our point about a smaller increase in unadjusted permits than is typical for the month of March being treated rudely by seasonal adjustment. Failing to account for these points helps account for the all too predictable but not all that useful reaction to the headline numbers from some quarters.

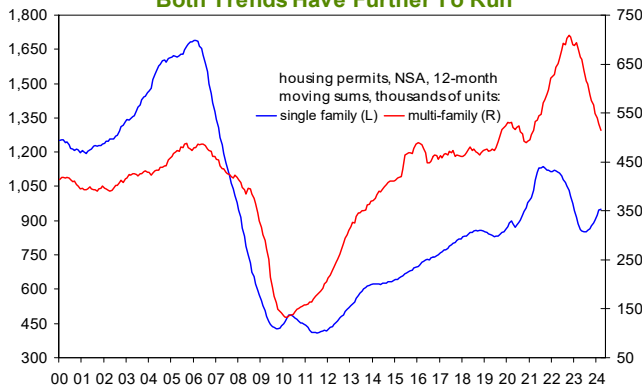
The not seasonally adjusted data show total starts of 110,900 units in March, below our forecast of 121,400 units. As noted above, however, at 87,100 units single family starts topped our forecast of 85,300 units, marking the highest monthly total for single family starts since last July.

Also, the prior estimate of single family starts in February was revised higher, in what was already a stronger performance than typically seen in February. So, while single family starts rose in March, the increase was smaller than typical for the month, hence the decline in the seasonally adjusted data. There were 23,800 multi-family units started in March, shy of our forecast. We did note in our *Economic Preview* that our forecast of multi-family starts would be lower than it was we're it not for us expecting a spike in multi-family starts in the Northeast region to follow the 10,100 multi-family permits issued in that region in February. That spike, however, did not materialize, at least not in March, while at the same time multi-family starts in the Midwest and South regions were oddly low.

We'd make more out of the drop in multi-family starts had it been accompanied by as significant of a drop in multi-family permits, which was not the case. At 39,200 units, multi-family permit issuance was only slightly below the 39,700 units permitted in February, but this small change was turned into a large change in the seasonally adjusted data. It helps to recall that, as with multi-family starts, multi-family permits are trending lower, part of the response to the bloated pipeline of units under construction. March saw 84,300 single family permits issued, up from February but, again, as this was smaller than the normal March increase, it turned into a decline in the seasonally adjusted data.

We've pointed to the backlog of units permitted but not yet started as acting as a drag on single family permit issuance, and that backlog got larger in March. In that sense, that single family starts topped single family permits in March isn't a worrying sign, as some suggest is the case. We do, however, think that the sharp increase in spec inventories over recent months may act as a weight on both permits and starts in the single family segment of the market. After spiking in February, single family completions slipped slightly in March, and continue to run below their year-ago levels, as do multi-family completions. With the sharp drop in starts, the backlog of multi-family units under construction fell slightly in March, while the single family backlog got slightly larger.

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Both Trends Have Further To Run



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Considerable Upside Room For Single Family Starts

