July 2013 Housing Commentary

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July 2013 Housing Scorecard

	M/M	Y/Y
Housing Starts[A]	Δ5.9%	Δ20.9%
Single-Family Starts[A]	∇2.2%	Δ15.4%
Housing Permits[A]	Δ2.7%	Δ12.4%
Housing Completions[A]	Δ1.8%	Δ15.0%
New Single-Family House Sales[A]	∇13.4%	Δ6.8%
Existing House Sales[B]	Δ6.5%	Δ17.2%
Private Residential Construction Spending[A]	Δ0.6%	Δ 17.2%
Single-Family Construction Spending[A]	∇ 0.5%	Δ29.3%

M/M = month-over-month; Y/Y = year-over-year

Source: [A]U.S. Department of Commerce-Construction ; [B] National Association of Realtors® (NAR®)

New Housing Starts

	Total Starts*	Single-Family Starts	Multi-Family 2-4 unit Starts	Multi-Family 5 or more unit Starts
July	943,000	591,000	15,000	290,000
June	918,000	604,000	11,000	231,000
2012	839,000	512,000	12,000	217,000
M/M change	5.9%	-2.2%	36.4%	25.5%
Y/Y change	20.9%	15.4%	25.0%	33.6%

* All start data are presented at a seasonally adjusted annual rate (SAAR)

Source: U.S. Department of Commerce-Construction: www.census.gov/construction/nrc/pdf/newresconst.pdf

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New Housing Permits and Completions

	Total Permits*	Single-Family Permits	Multi-Family 2-4 unit Permits	Multi-Family 5 or more unit Permits
July	943,000	613,000	27,000	303,000
June	918,000	625,000	26,000	267,000
2012	839,000	520,000	29,000	290,000
M/M change	2.7%	-1.9%	3.8%	13.5%
Y/Y change	12.4%	17.9%	-6.9%	4.5%

	Total Completions*	Single-Family Completions	Multi-Family 2-4 unit Completions	Multi-Family 5 or more unit Completions
July	774,000	571,000	8,000	195,000
June	760,000	539,000	13,000	207,000
2012	673,000	466,000	9,000	198,000
M/M change	1.8%	5.9%	-38.5%	-5.8%
Y/Y change	15.0%	22.5%	-11.1%	-1.5%

Source: U.S. Department of Commerce-Construction: www.census.gov/construction/nrc/pdf/newresconst.pdf

* All data are SAAR

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New and Existing House Sales

	New Single-Family Sales*	Median Price	Month's Supply	Existing House Sales [B*]	Median Price [B]	Month's Supply [B]
July	394,000	$257,200	5.2	5,390,000	$213,500	5.1
June	455,000	$258,500	4.3	5,060,000	$214,000	5.1
2012	369,000	$237,400	4.6	4,660,000	$187,700	6.3
M/M change	-13.4%	-4.9%	20.9%	6.5%	-0.2%	0.0%
Y/Y change	6.8%	6.8%	13.0%	17.2%	13.7%	-18.8%

* All sales data are SAAR

Source: U.S. Department of Commerce-Construction: www.census.gov/construction/nrs/pdf/newressales.pdf; [B]NAR®: www.realtor.org/news-releases/2013/04/march-existing-home-sales-slip-due-to-limited-inventory-prices-maintain-uptrend

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Existing House Sales

National Association of Realtors (NAR®)[B]
July 2013 sales data:

Distressed house sales: 15% of sales –
(9% foreclosures and 6% short-sales)

Distressed house sales: 15% in June
and 24% in July 2012

All-cash sales: decreased to 31%; 31% in June

Investors are still purchasing a substantial portion
of "all cash" sale houses – 31%;
31% in June 2013 and 27% in July 2012

First-time buyers: decreased to 29% (29% in June 2013)
and were 34% in July 2012

Source: [B] NAR® www.realtor.org/topics/existing-home-sales; 6/20/13

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July 2013 Construction Spending

Private Construction: $334.58 billion (SAAR)

0.6% above the revised June estimate of $332.65 billion (SAAR)
17.2% above the July 2012 estimate of $285.55 billion (SAAR)

July SF construction: $168.19 billion (SAAR)
0.5% greater than June: $167.35 billion (SAAR)
29.3% greater than July 2012: $130.08 billion (SAAR)

July MF construction: $31.87 billion (SAAR)
0.1% greater than June: $31.83 billion (SAAR)
39.3% greater than July 2012: $22.88 billion (SAAR)

July Improvement[C] construction: $134.51 billion (SAAR)
0.8% greater than June: $133.47 billion (SAAR)
17.6% greater than July 2012: $114.40 billion (SAAR)

[C] The US DOC does not report improvements directly, this is an estimation. All data is the SAAR and is reported in nominal US$.

Source: U.S. Department of Commerce-C30 Construction: www.census.gov/construction/c30/pdf/privsa.pdf

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Conclusions

The housing market continues to marginally improve – although in the past months there have been some "hiccups" in certain subsectors. Reviewing current data, several sectors appear to be stagnating and in these same sectors, the data is less than 50 percent of their respective long-run averages. Once again, the near-term outlook on the U.S. housing market remains unchanged – there are potentially several negative macro-factors or headwinds at this point in time for a robust housing recovery based on historical long-term averages.

Why?

1) government debt
2) European recession, China slow-down
3) weak domestic demand
4) a lack of well-paying jobs,
5) a sluggish economy
6) declining real median annual household incomes,
7) strict home loan lending standards, and
8) new banking regulations.

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Housing comments –August , 2013

Still lots of headwinds to deal with:

- economy is getting better, albeit very slowly
- government debt issues – all levels of government – exacerbates the job problem
- Much of Europe in recession , but getting better – China is slowing too
- Housing's main problems - Weak domestic economy made worse by slowing world economy; weak job market; weak income growth; high debt levels; and tight credit environment

- Demand , Debt and uncertainty are some of serious problems that are impacting the economy – but, getting better
- Three major concerns going forward –
  - (1) can the economy (and housing) stand on its own (without Fed stimulus) ???
  - (2) Uncertainty is key reason holding back job creating investments . Ex., impact of health care legislation; Dodd/Frank; dysfunctional "Washington"; ……
  - (3) Will rising rates derail the housing market?
- Longer term – what will be the mix of single family versus multi family?
- Will people continue to live in the suburbs?
- What happens to house size?

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Some questions going forward:

(1) Sustainable housing recovery?

(2) Economy – Inflation; deflation; or disinflation?

Hyper Inflation from running the printing presses for past 3 – 5 years

Deflation – 1930's – weak demand

Disinflation – slower rate of inflation

(3) What kind of housing market will we get? My guess is more multi family; smaller single family homes; and more people (young people and retired) will choose to live in the city (e. g., suburb living not as popular anymore).

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Housing, Economy, and wood products

They are “joined at the hip”

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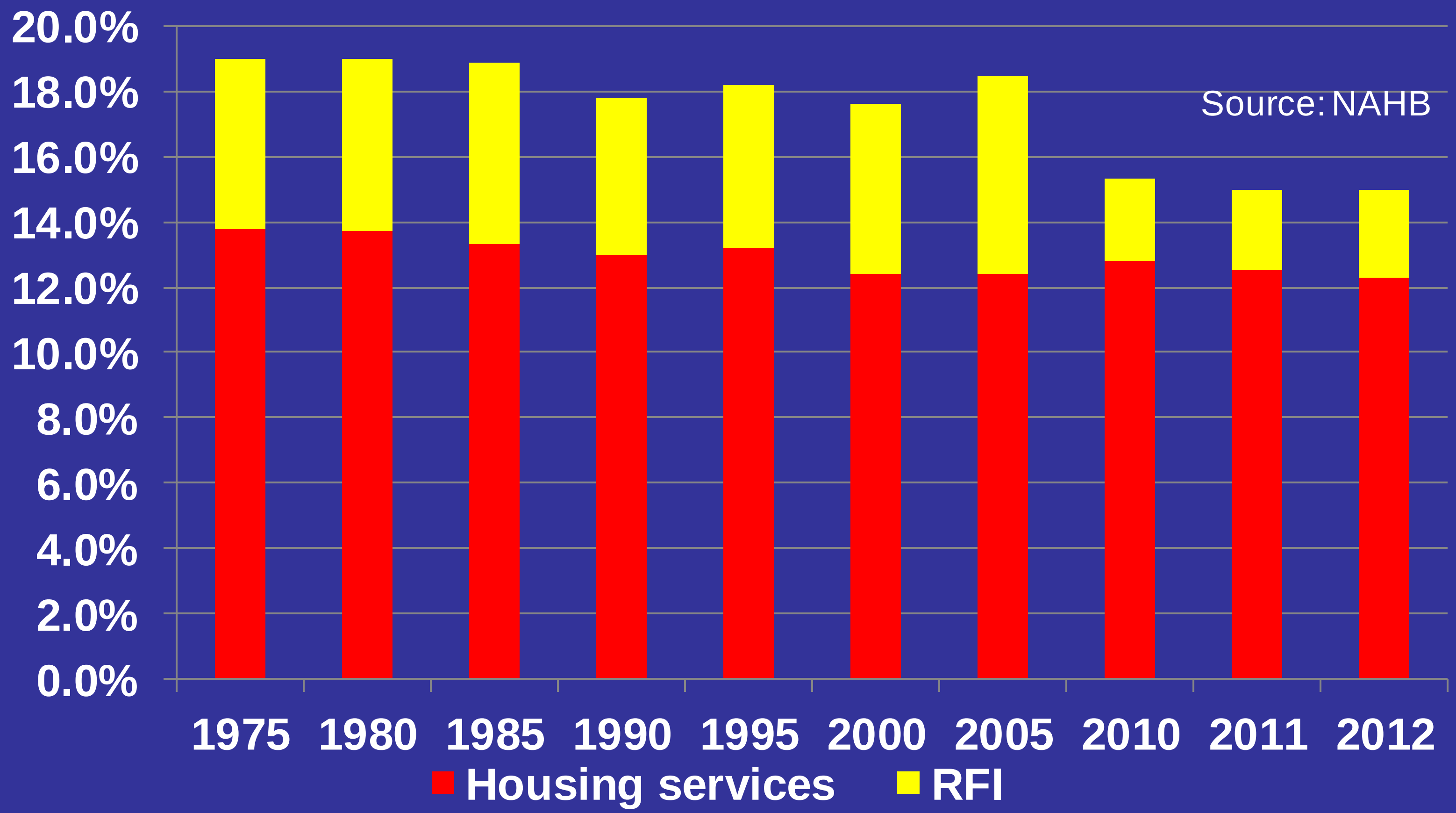
Housing's contribution to GDP (%) – historically, it is almost 20% of the economy when you include housing services and fixed investment, but today it is down to 15%. In reality, it is even more important when you include purchased furniture, landscaping, general maintenance, etc.

key reason why the economic recovery remains muted

Housing services = gross rents paid by renters (incl utilities) + owner's imputed rent (how much It would cost to rent owner occupied homes) plus utility payments

RFI (residential investment) = construction of new SF and multifamily structures, remodeling, manufactured homes , plus broker's fees



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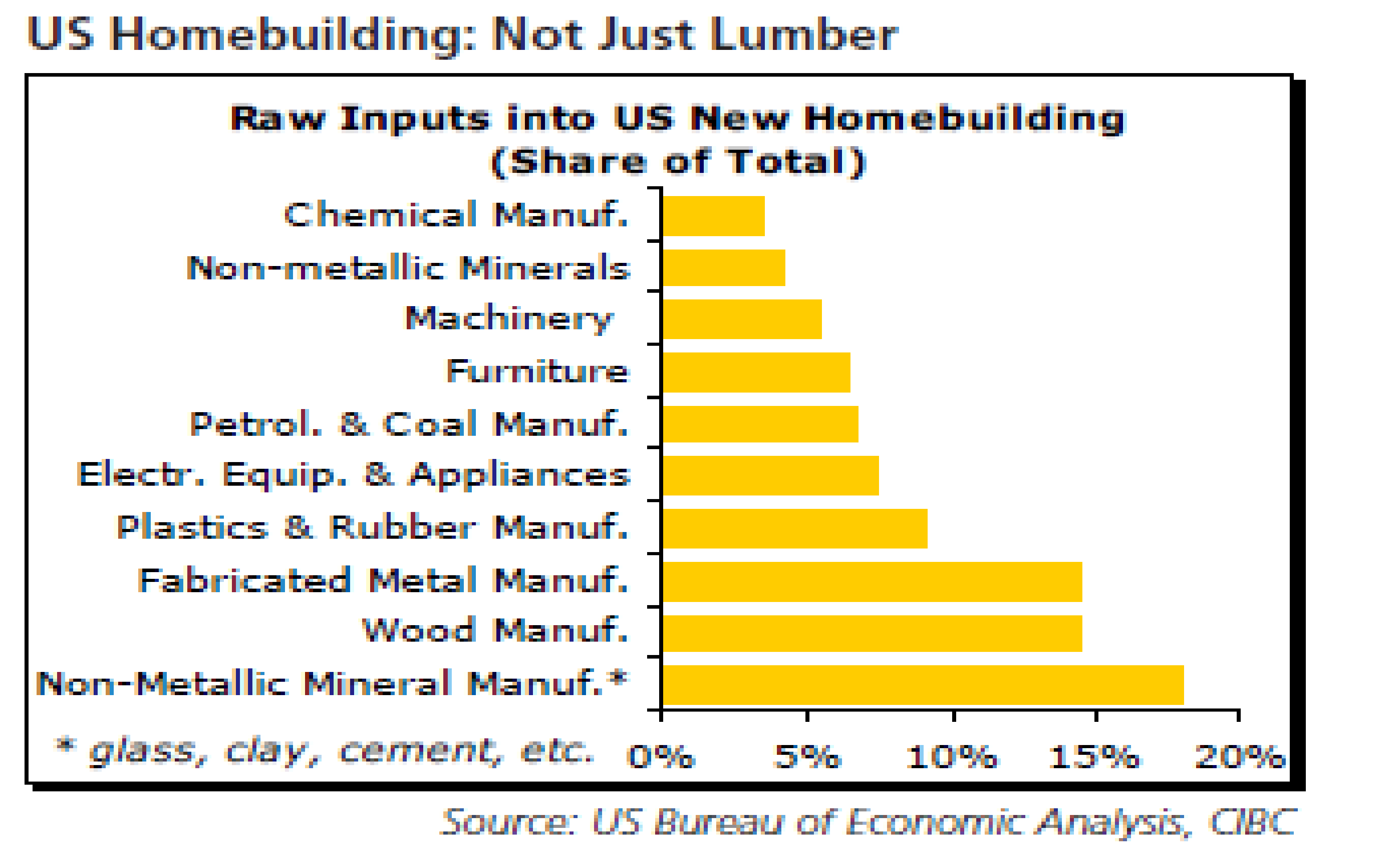
Housing is important to wood products, but other Products benefit too



Source: CIBC (http://research.cibcwm.com/economic_public/download/feature3.pdf)

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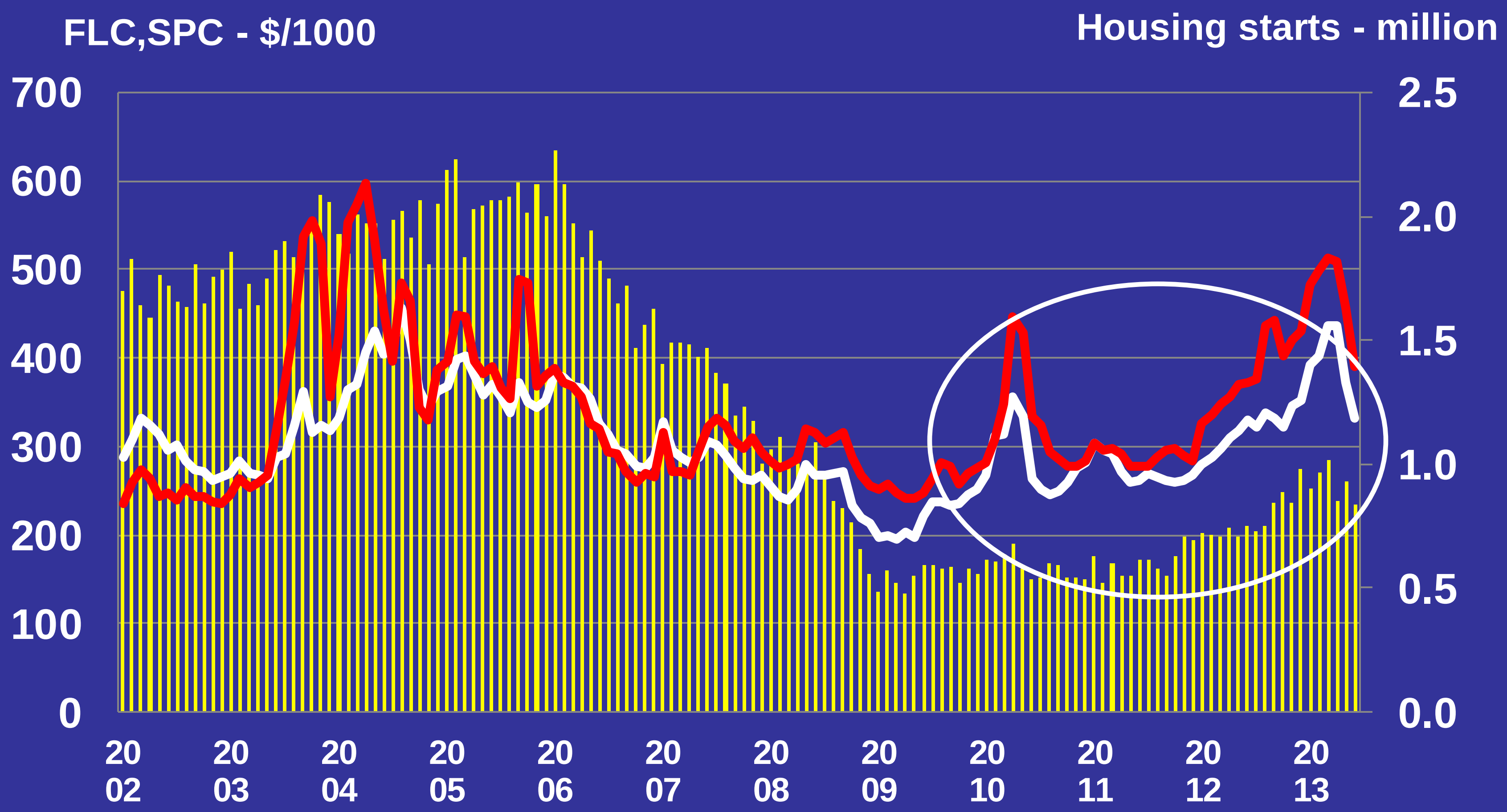
Housing starts and wood product prices – Economics 101

Following housing bust in 2008, wood prices fell and production capacity was reduced.
So, when housing starts increased , there was an imbalance between demand and supply of wood products . The price mechanism brings demand and supply into balance. Initially, prices fell almost 50% - this instigated production cutbacks of 50% or more – then, as housing begins to turn around, prices increase - this encourages Production increases for wood products – and the cycle starts over.



Sources: Prices – Random Lengths (http://www.randomlengths.com/); starts (Bureau of Census (http://www.census.gov/construction/nrc/)

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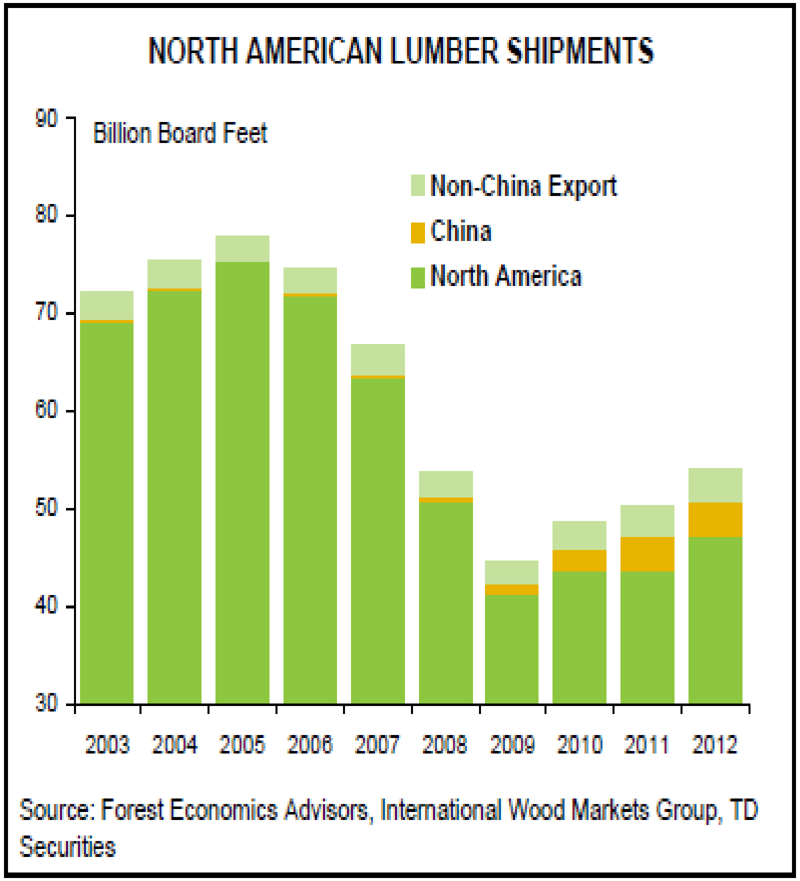
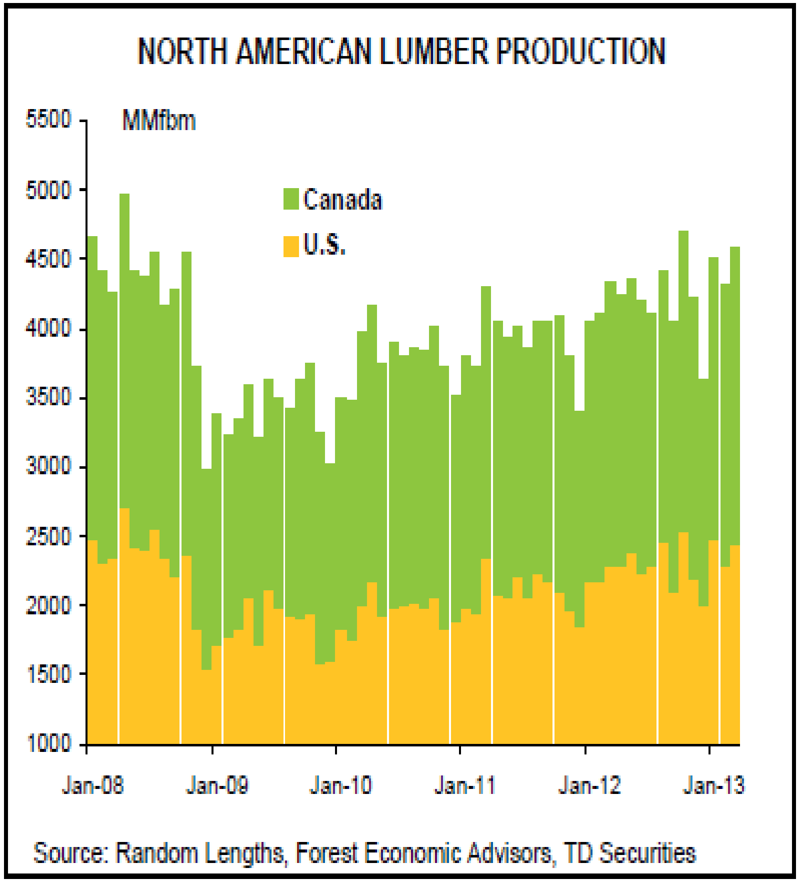
North American Lumber Shipments and Production





Source: TD Economics (http://www.td.com/document/PDF/economics/special/LumberPriceCorrectionWillNotLast.pdf)

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British Columbia’s Lumber Supply projected to fall 40%
(Impact of Mountain Pine Beetle Infestations)

	AAC	Lumber production
2005	68 MMCM	15 BBF
2013	59 MMCM	
2018	40 MMCM	9 BBF - - *40% drop*

BC’s share of NA production ~ 20- 25%
A 40% drop in BC ~ 8 – 10% drop in NA production
This has to impact lumber pricing

Source: Random Lengths (May 31, 2013)

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Wood product pricing should be solid for the next two years or so due to - -

(1) improving domestic housing market and export
(2) demand for wood products outstrips supply as previous production cutbacks catch up with demand
(3) structural products (framing lumber, OSB, plywood), and hardwood based products like furniture, kitchen cabinets, flooring, all benefit from residential construction including new construction plus remodeling.

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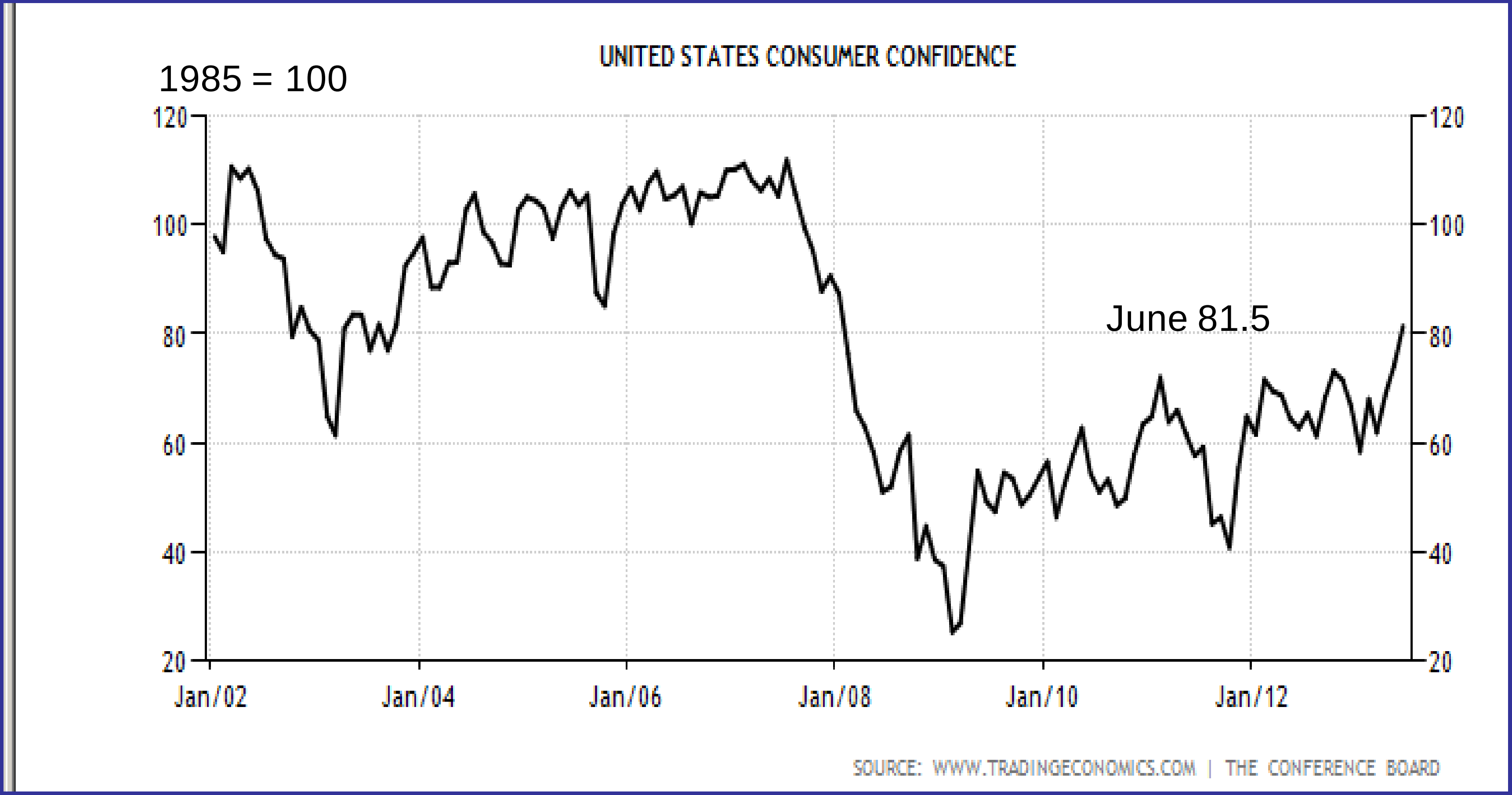
Consumer Confidence at 5 year high – good news As consumer spending is 70% of the economy



Source: (http://www.tradingeconomics.com/united-states/consumer-confidence)

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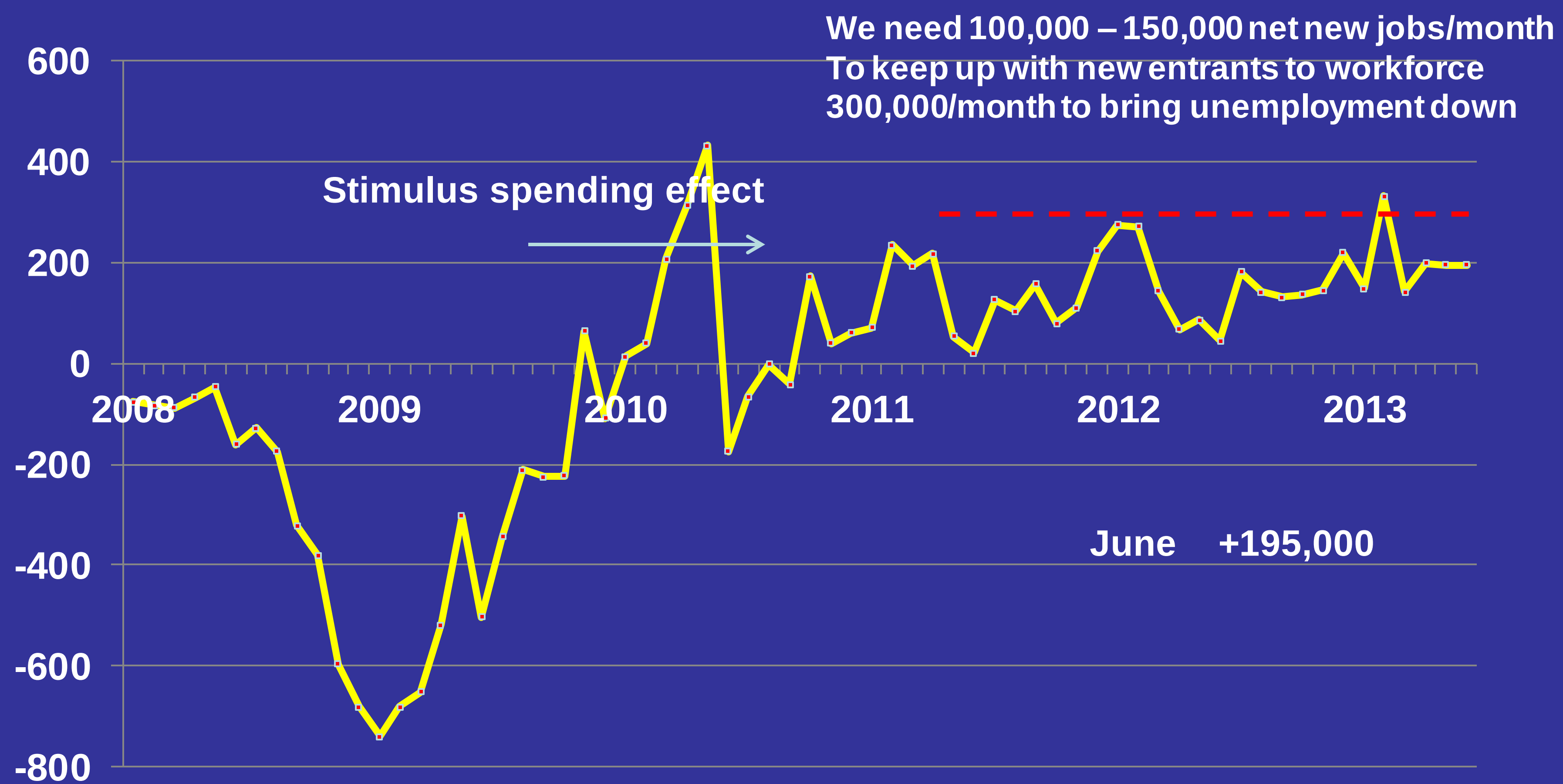
Although confidence is up, Wages continue a disturbing Downward trend

Source: S. Goldstein, Market Watch May 27 (http://blogs.marketwatch.com/thetell/2013/05/28/confidence-may-be-on-the-move-but-wages-are-not/)

Employment situation - our biggest problem - it's getting better, but the jobs recovery remains weak by past standards, and many jobs
Don't include health care or retirement benefits (because they are
Often part time jobs) – those kinds of jobs don't encourage people to buy houses

Net change in non farm payrolls – monthly, thousands



Source: U.S. BLS (www.bls.gov)

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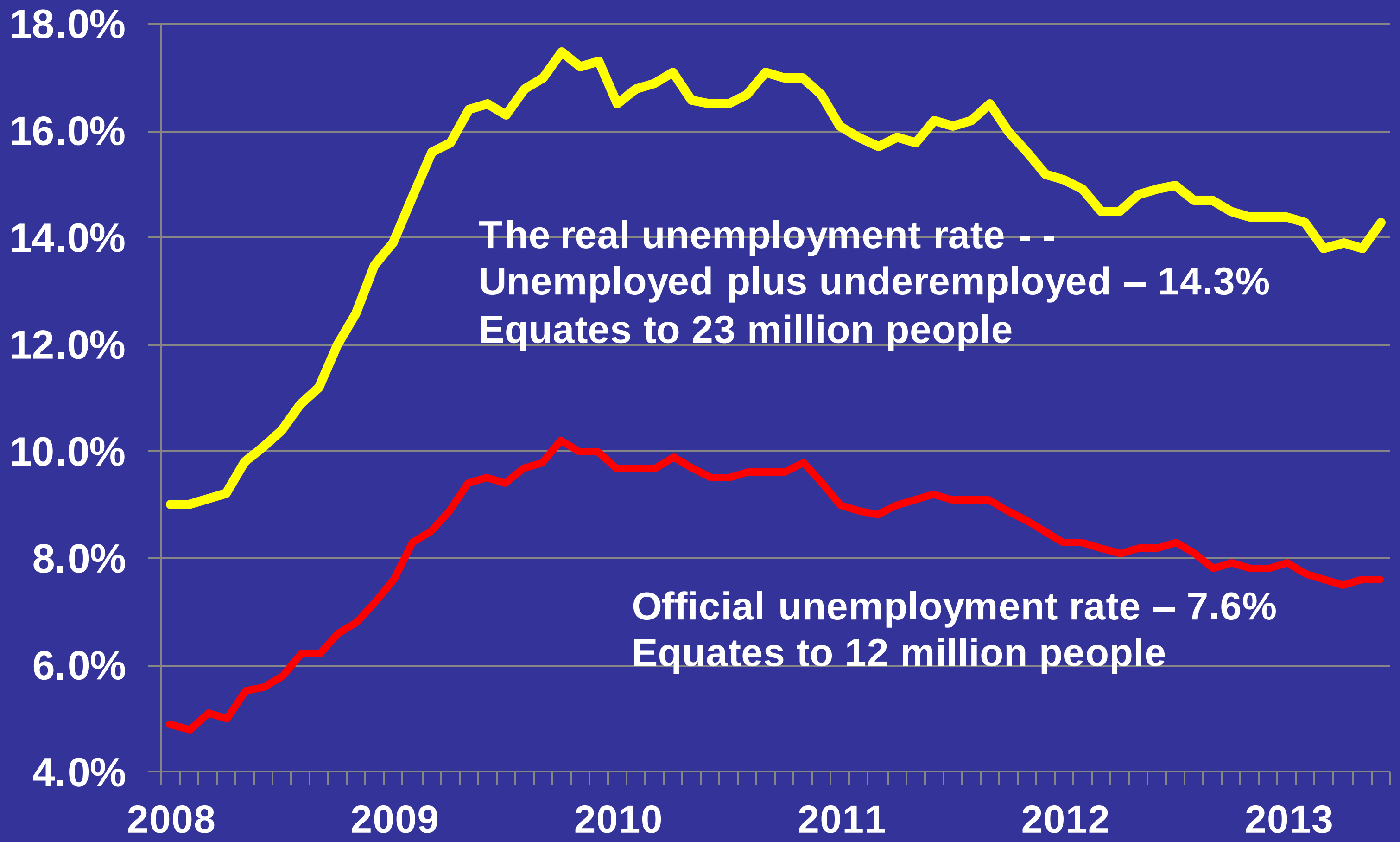
Unemployment remains high and will remain relatively high for several years – but, it's getting better "slowly"

There are about 23 million people either unemployed , underemployed, or stopped Looking – **they are not buying houses



Source - - BLS: http://www.bls.gov/news.release/pdf/empsit.pdf; http://data.bls.gov/cgi-bin/surveymost?ln

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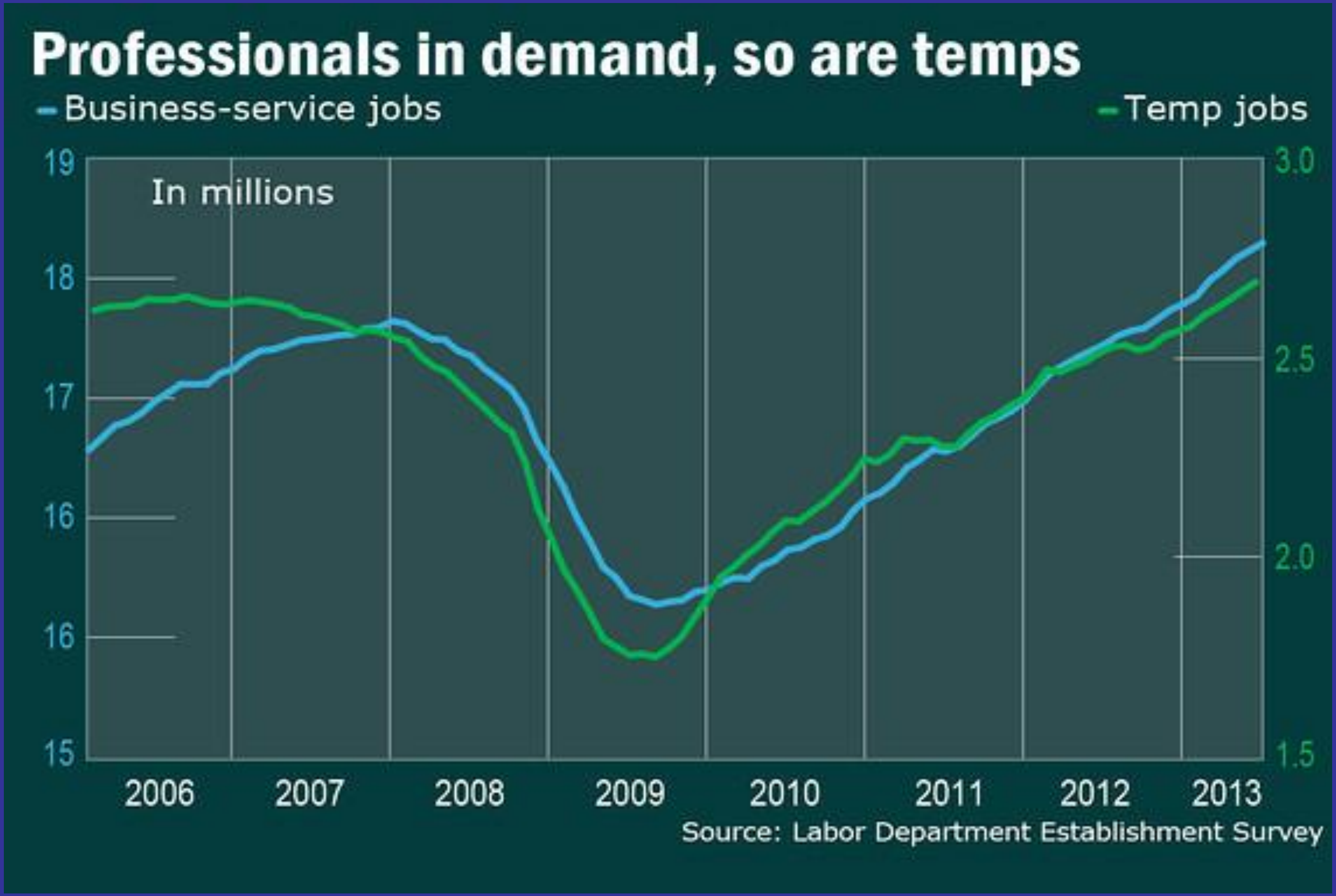
Source: marketwatch : (http://www.marketwatch.com/Story/story/print?guid=5C9788D6-FB68-11E2-A97E-002128040CF6)

Employment - - We're still 2.5 million below pre recession levels

Source: marketwatch : (http://www.marketwatch.com/Story/story/print?guid=5C9788D6-FB68-11E2-A97E-002128040CF6)

Where the growth is - -
30% of jobs created in past 5 years are “temporary jobs”



Source: marketwatch : (http://www.marketwatch.com/Story/story/print?guid=5C9788D6-FB68-11E2-A97E-002128040CF6)

Other economic issues –

- The workforce is shrinking and
  Labor force participation rate is lowest since WWII
  Some implications – more problems funding social programs

- Capacity utilization remains below 80% - that means firms won't invest and that means weak job growth (and weak income growth)

- Inflation not a problem yet

- Going forward, unemployment will be a huge drag on the federal (and other government levels) budgets – implications for taxes, spending, domestic programs, and job creation

- Major questions going forward are inflation, disinflation, deflation, or continued weak growth (disinflation is weakening inflation (i.e., today) whereas deflation is general fall in prices (i.e., 1930's). My guess is continuing weak growth (less than 3% GDP) with moderate pick up in inflation . There are too many headwinds for stronger growth, and deflation is just too ugly to contemplate.

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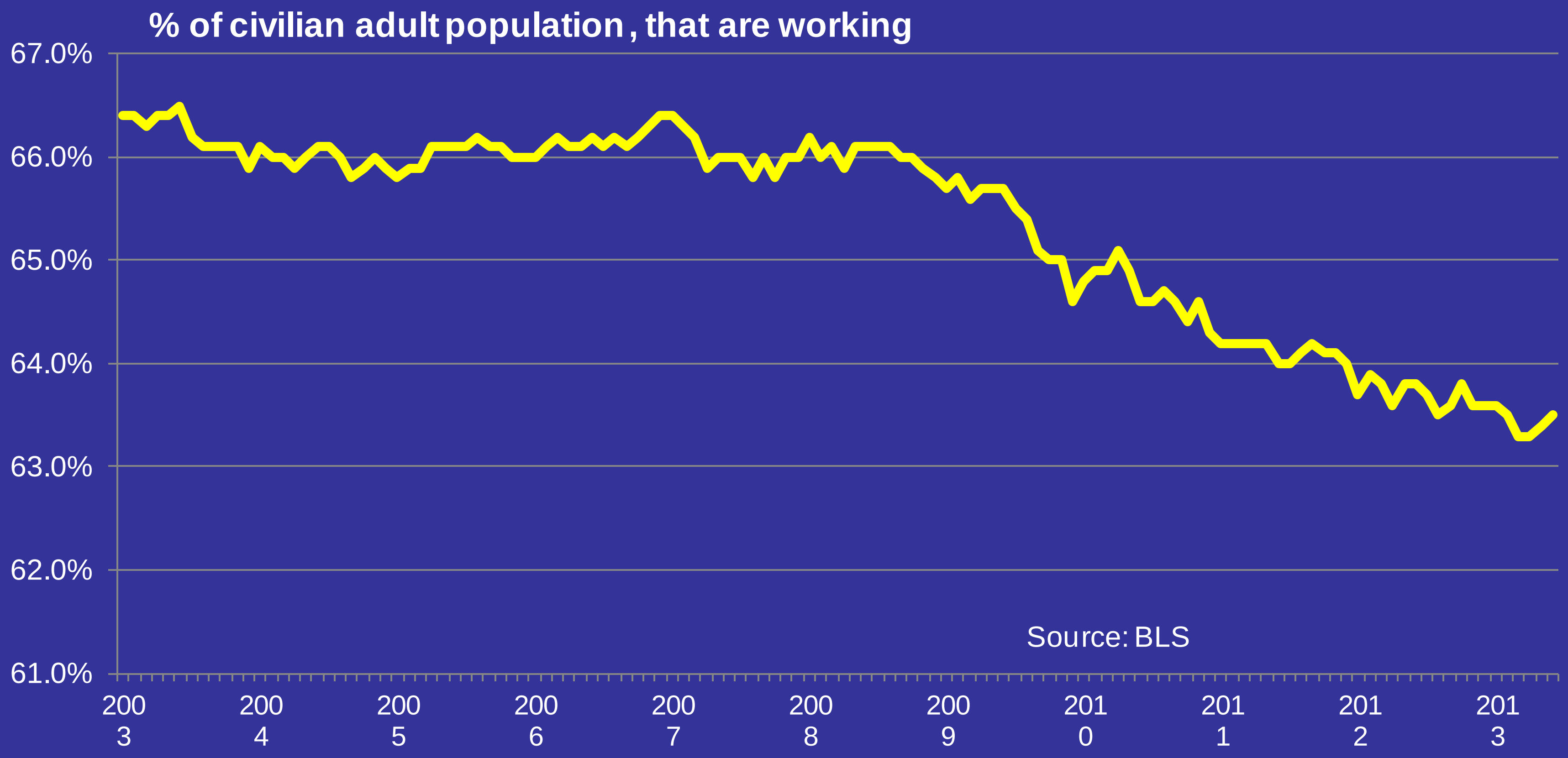
Labor force participation rate is shrinking -

Major problems for social programs with our aging population – fewer people paying taxes, but more people collecting SSI, Medicare, etc.



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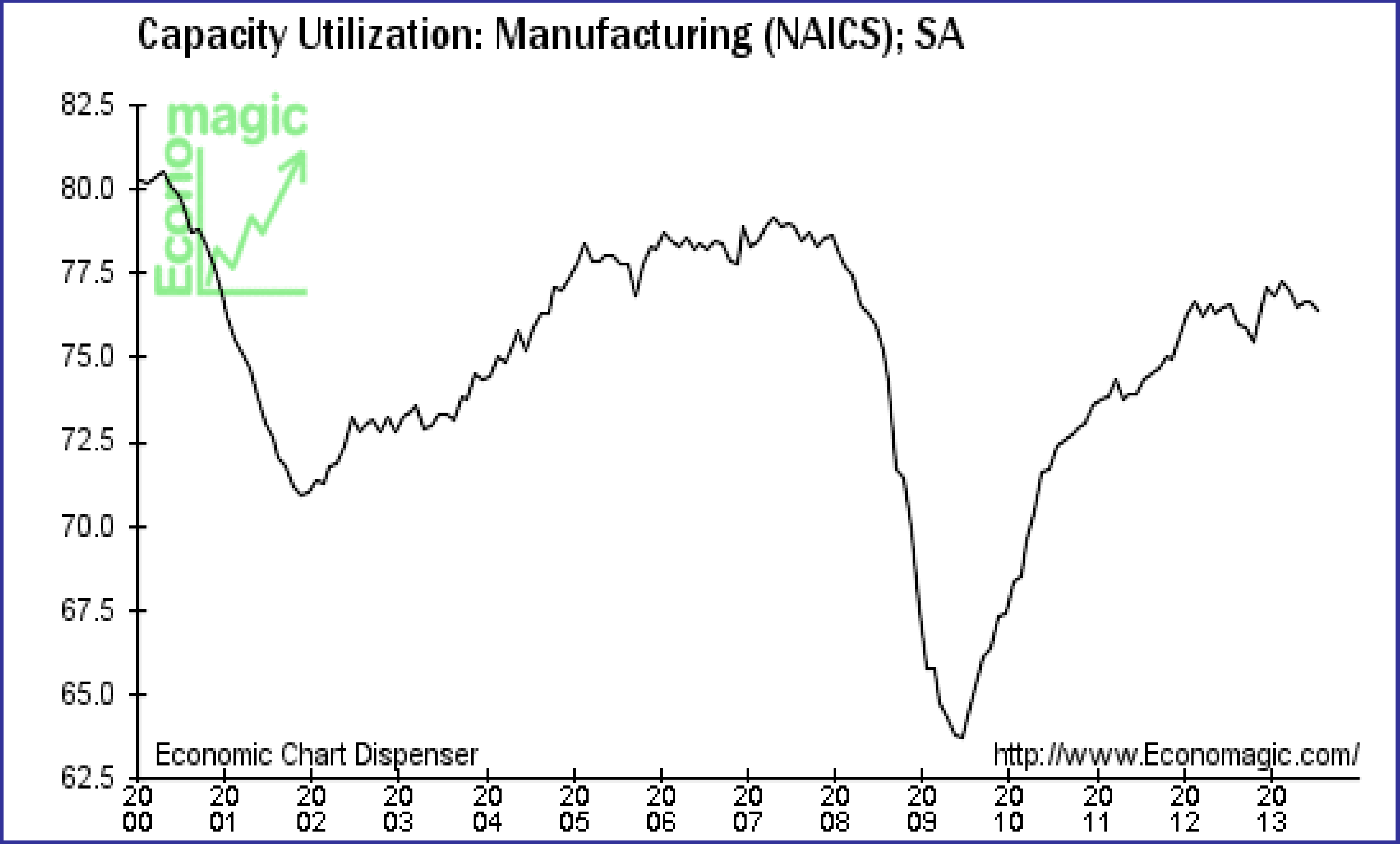
Inflation not a problem yet

Manufacturing Excess Capacity: Until we get back to 80%, Firms won't invest in new capacity – that means weak income growth and continuing employment problems – but, it's getting Better!!



Source: Economagic (http://www.economagic.com/em-cgi/data.exe/frbg17/B00004_utlsa)

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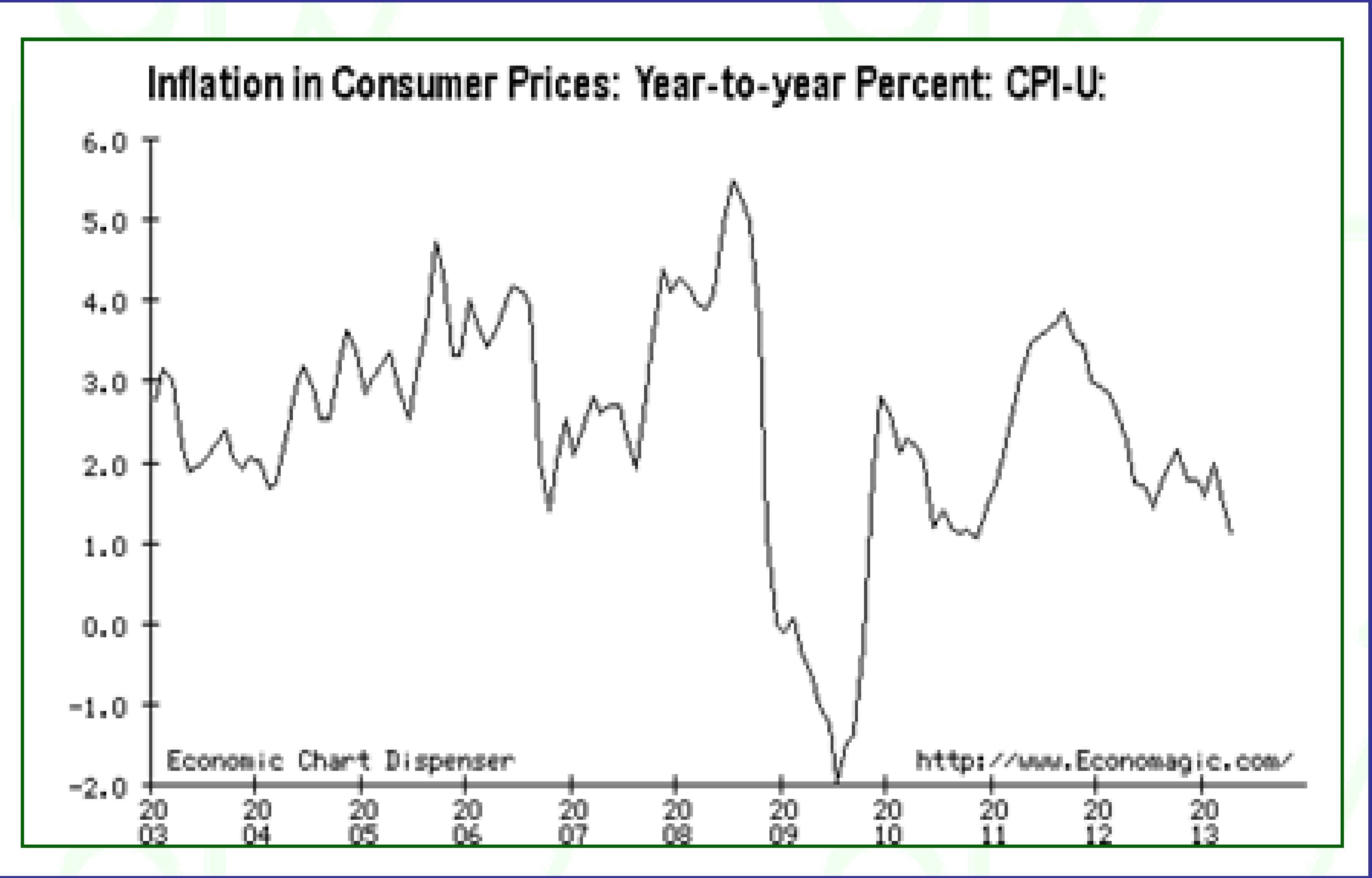
Inflation not a problem yet



Source: Economagic (http://www.economagic.com/em-cgi/daychart.exe/form)

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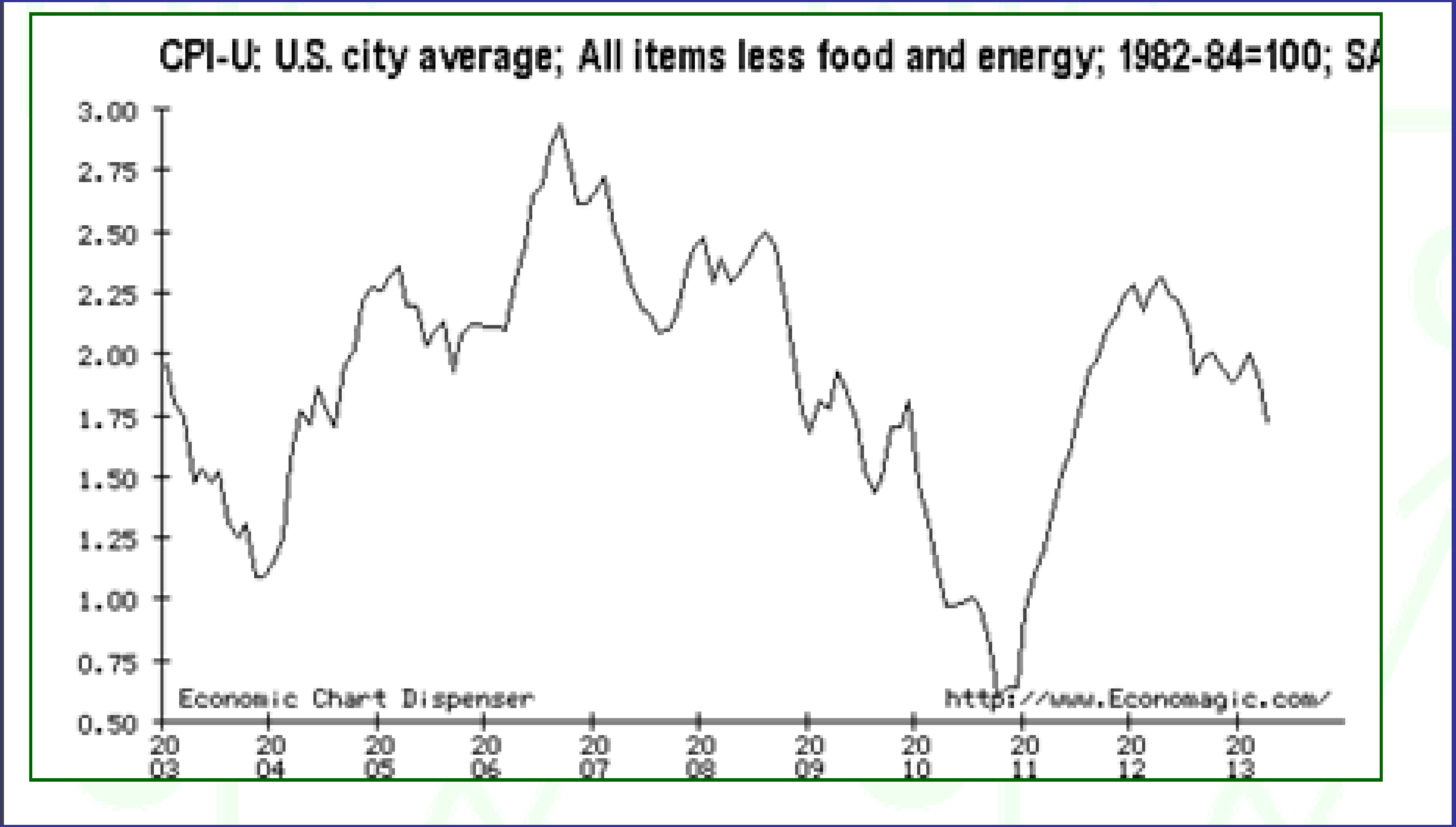
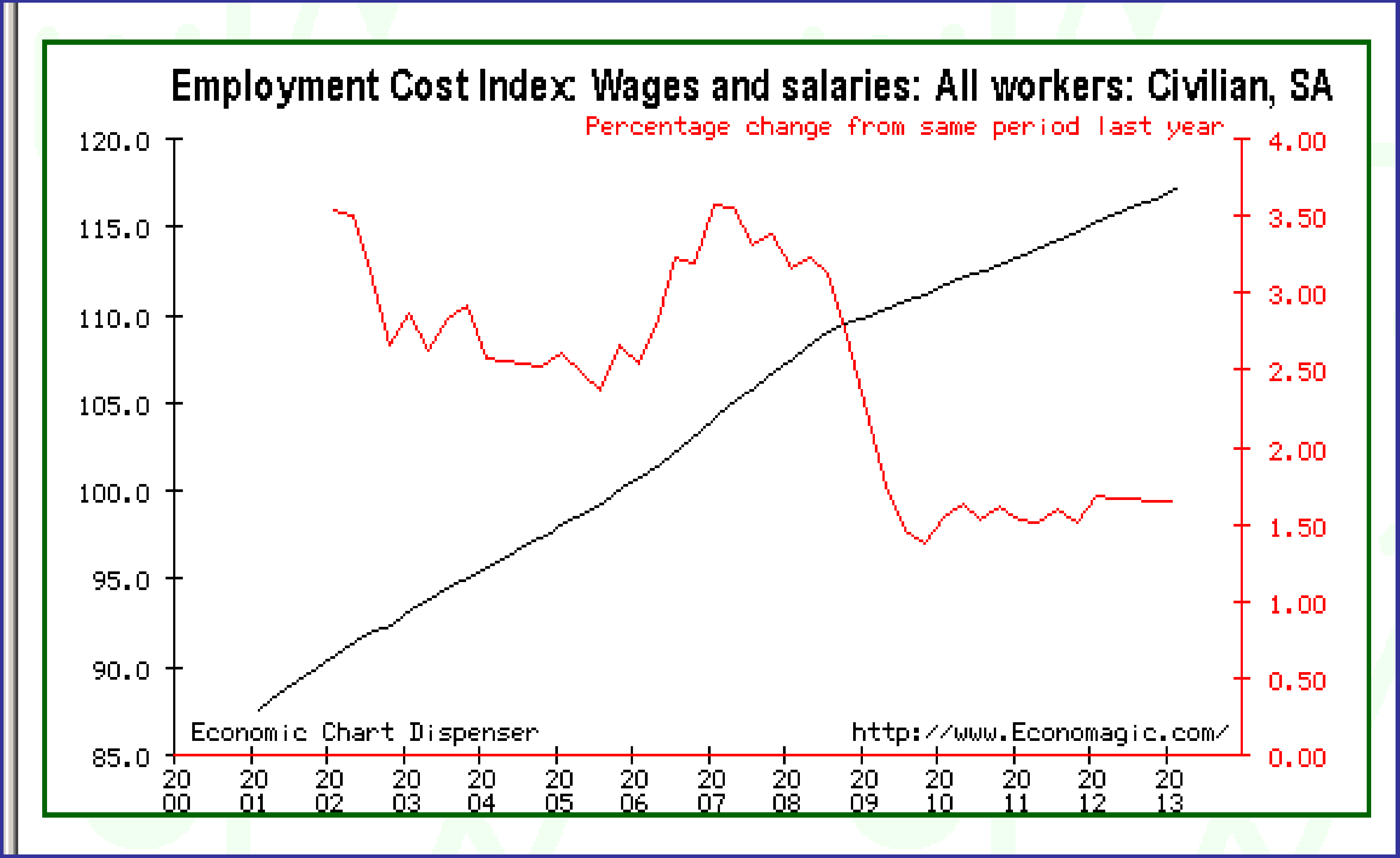
Core Inflation (year over year) not a problem either



Source: Economagic (http://www.economagic.com/em-cgi/daychart.exe/form)

Wages are main source of inflation – this chart suggests that
Inflation is not a problem yet! (focus on the red line) – believe
It or not, some inflation is good – it suggests that demand is strong



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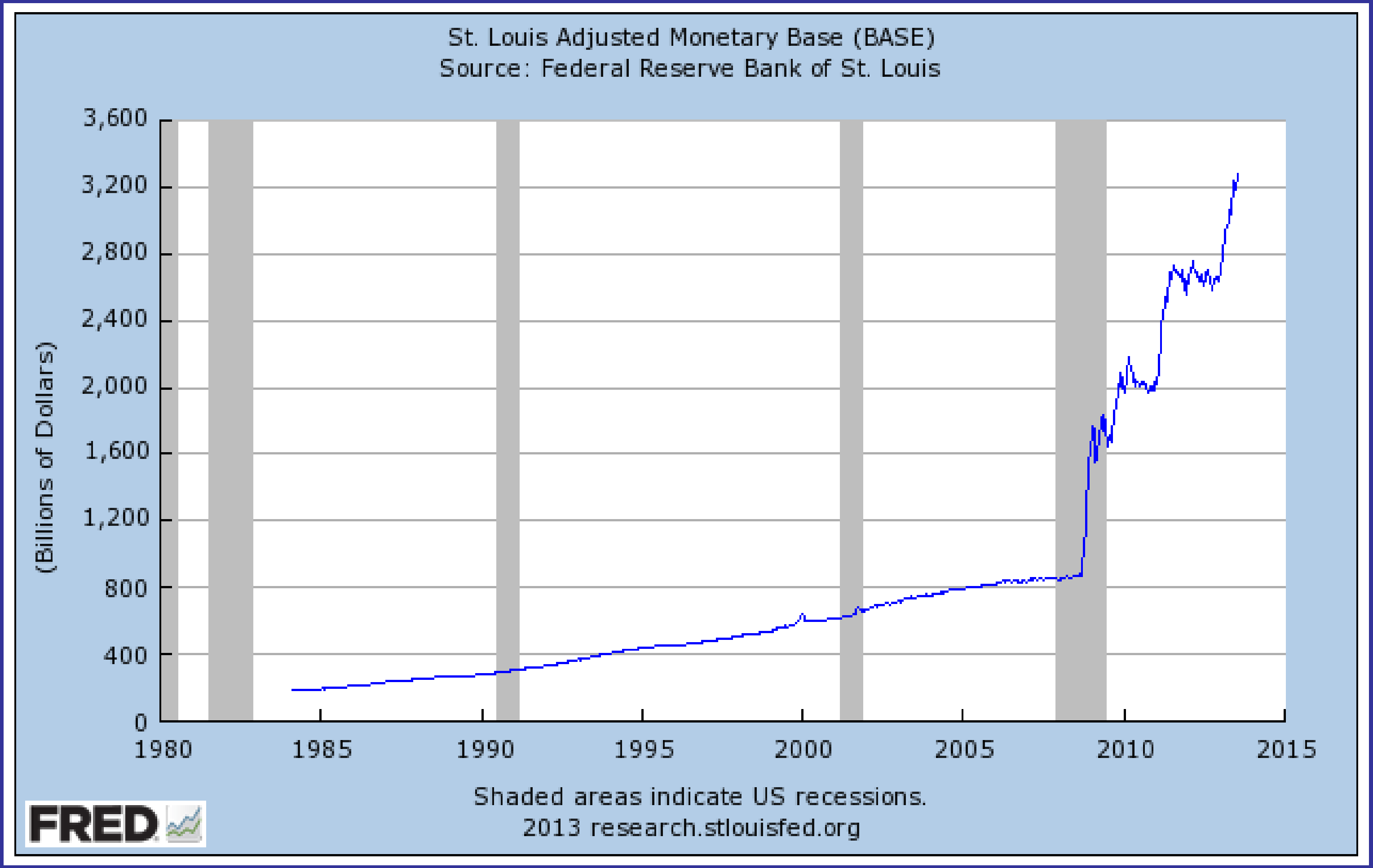
QE1,2,3 – FED "money printing"



(http://seekingalpha.com/article/1577542-the-case-for-inflation-rising-rates-commodity-strength-and-equity-weakness?source=email_macro_view&ifp=0)

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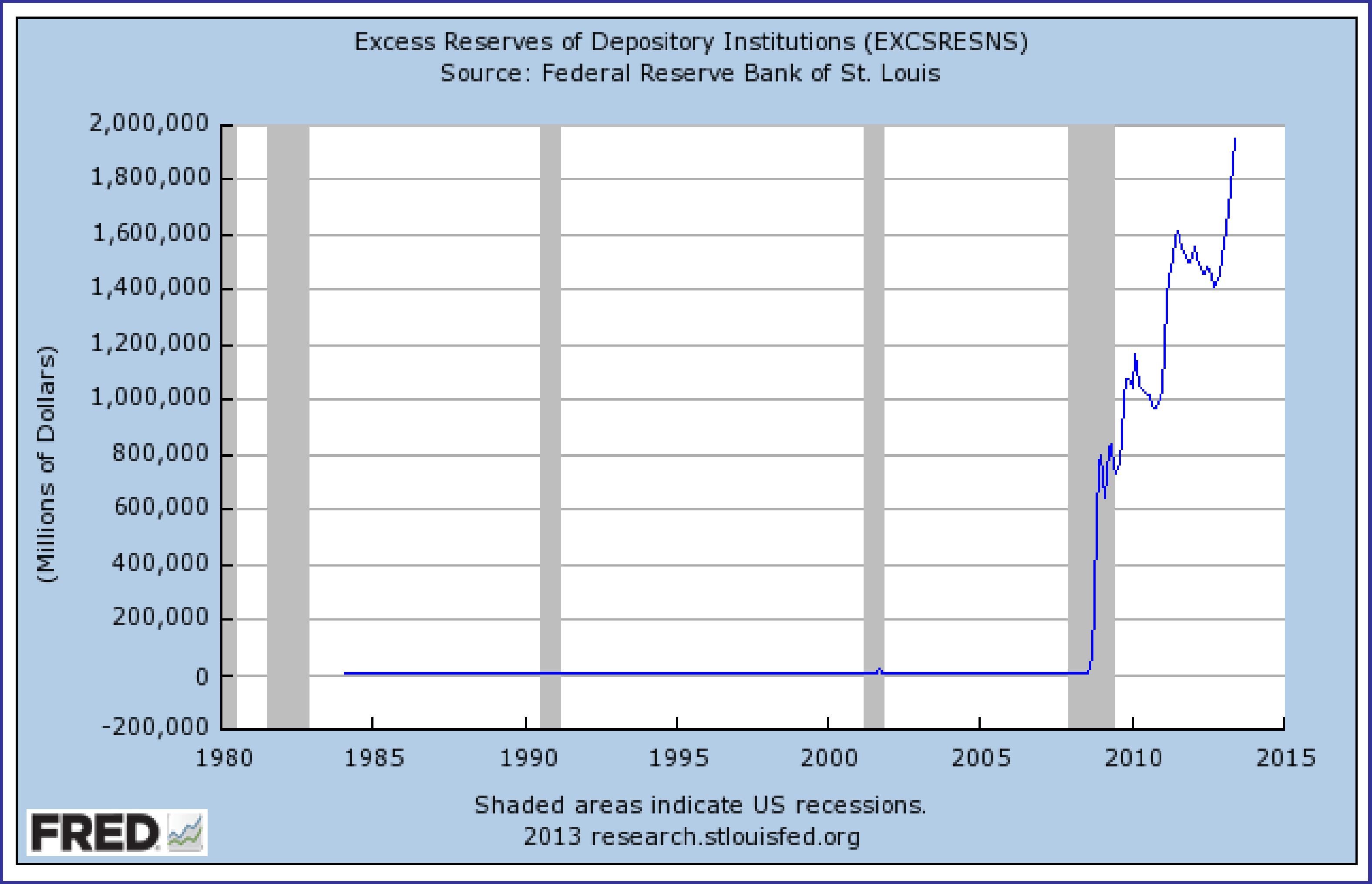
QE is not causing inflation because most of the $ remain as Excess reserves with the banks – i.e., they are not lending The money!!!



(http://seekingalpha.com/article/1577542-the-case-for-inflation-rising-rates-commodity-strength-and-equity-weakness?source=email_macro_view&ifp=0)

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Some additional housing headwinds

A. This economic recovery is much slower than
Previous ones

Why

(1) This recession was a financial recession
(2) Previous ones were typical economic recession
(i.e., economy overheats, the Fed increases
interest rates to cool things down, ….
(3) Financial recession are more serious and
require more time to heal damaged credit, etc.

B. And, mortgage rates are trending upward as the Fed
pulls back on QE/money printing

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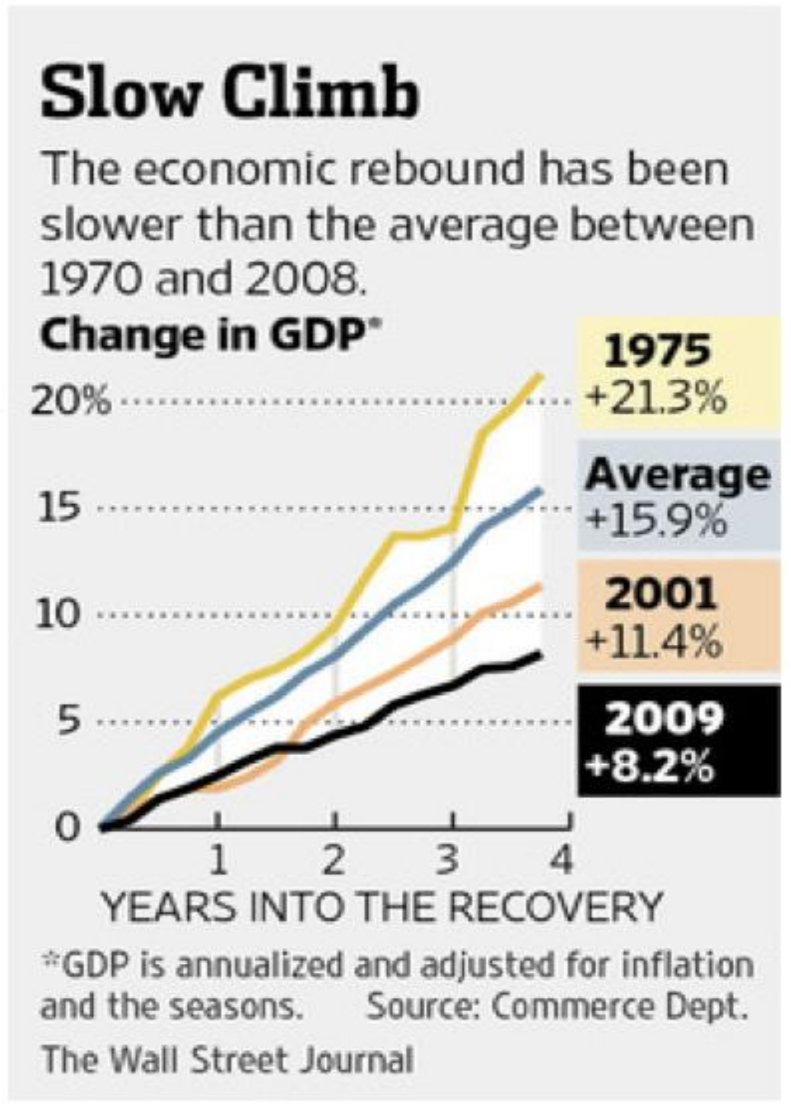
A comparison of GDP growth following recessions

Recovery from this recession much slower



Source: Wall Street Journal (http://online.wsj.com)

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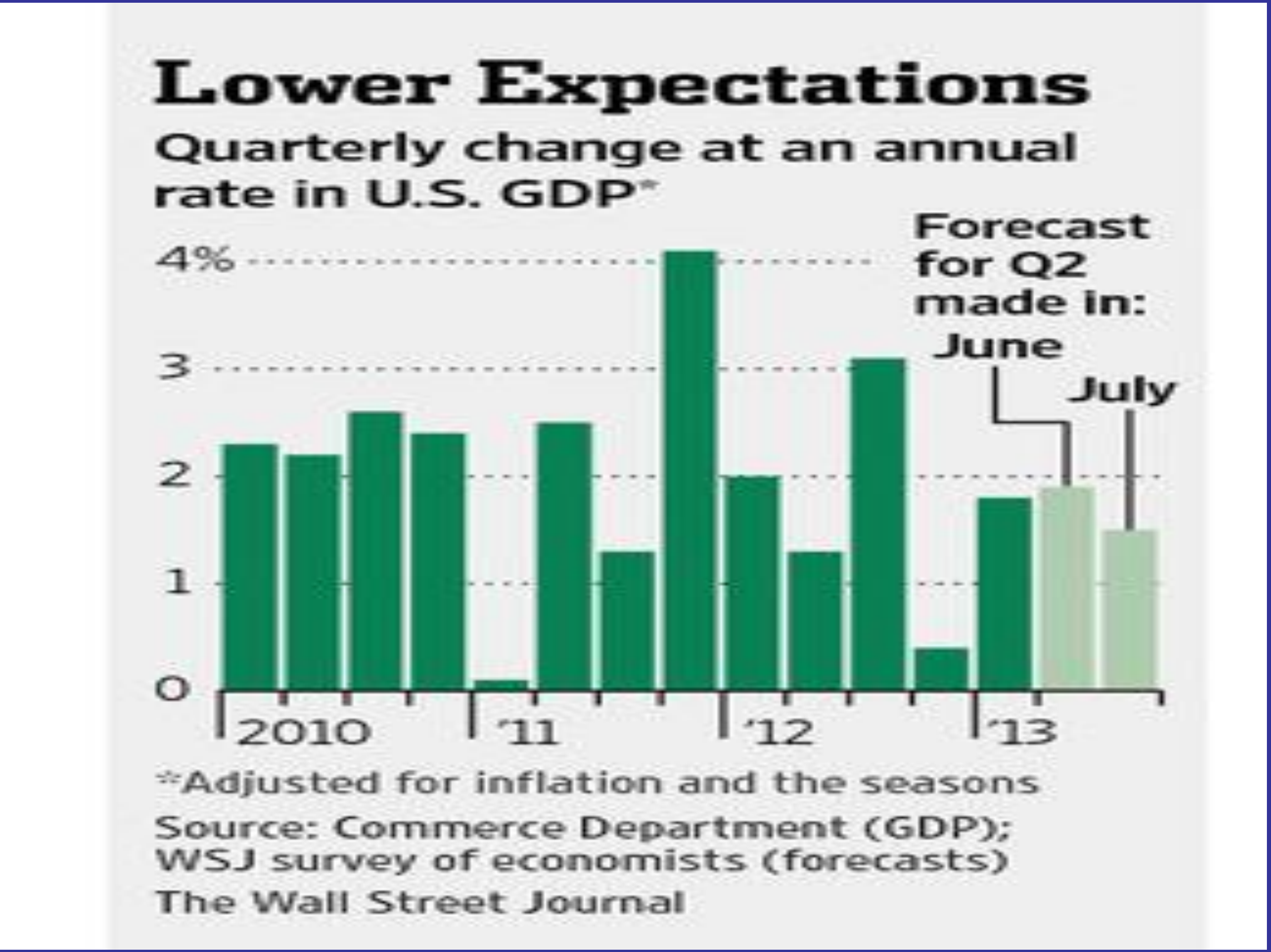
And, Analysts continue to reduce outlooks for 2013



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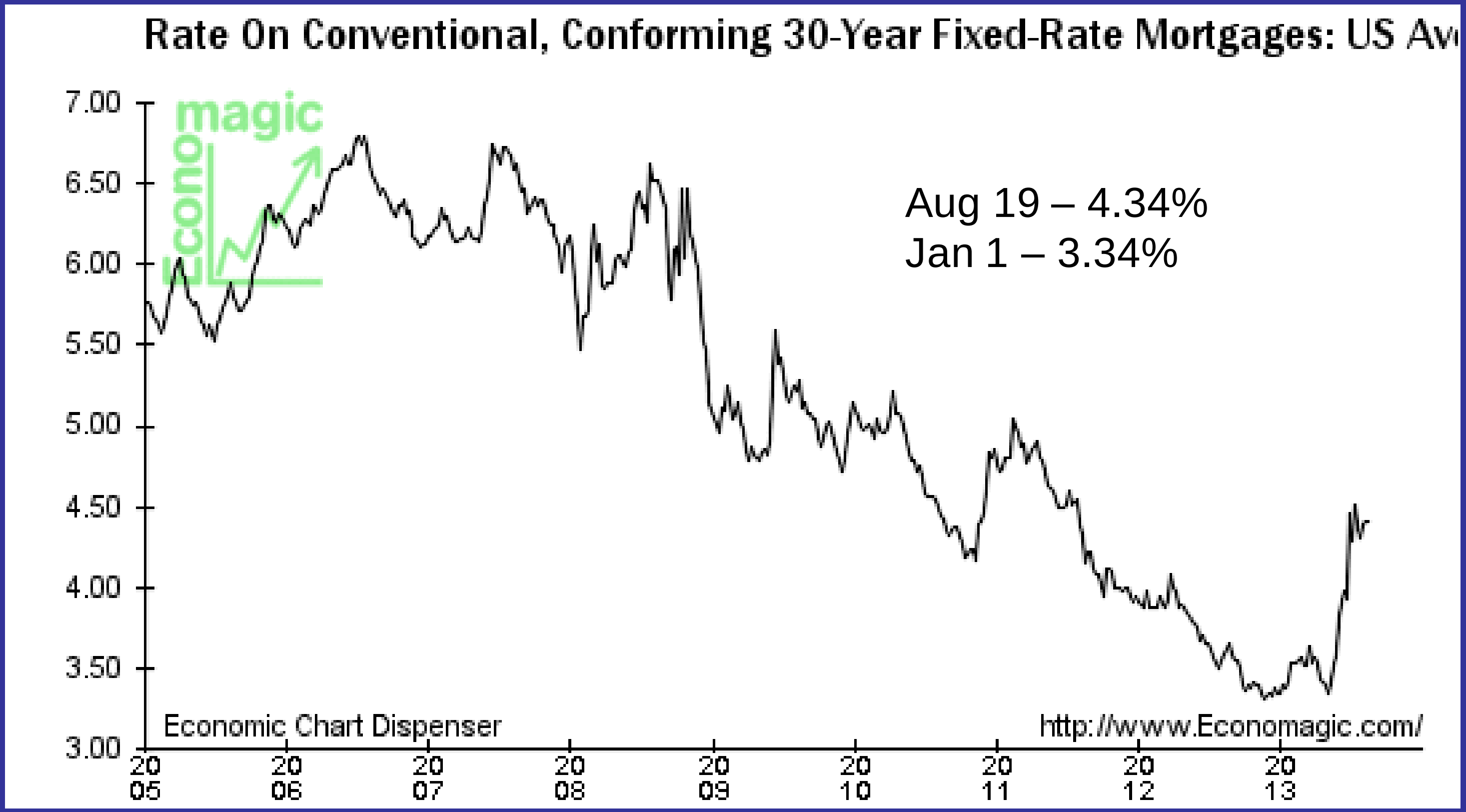
Higher Mortgage rates on the way -
Actually good for housing – it forces many people
To "get off the fence" and , anyway, rates are still historically low.



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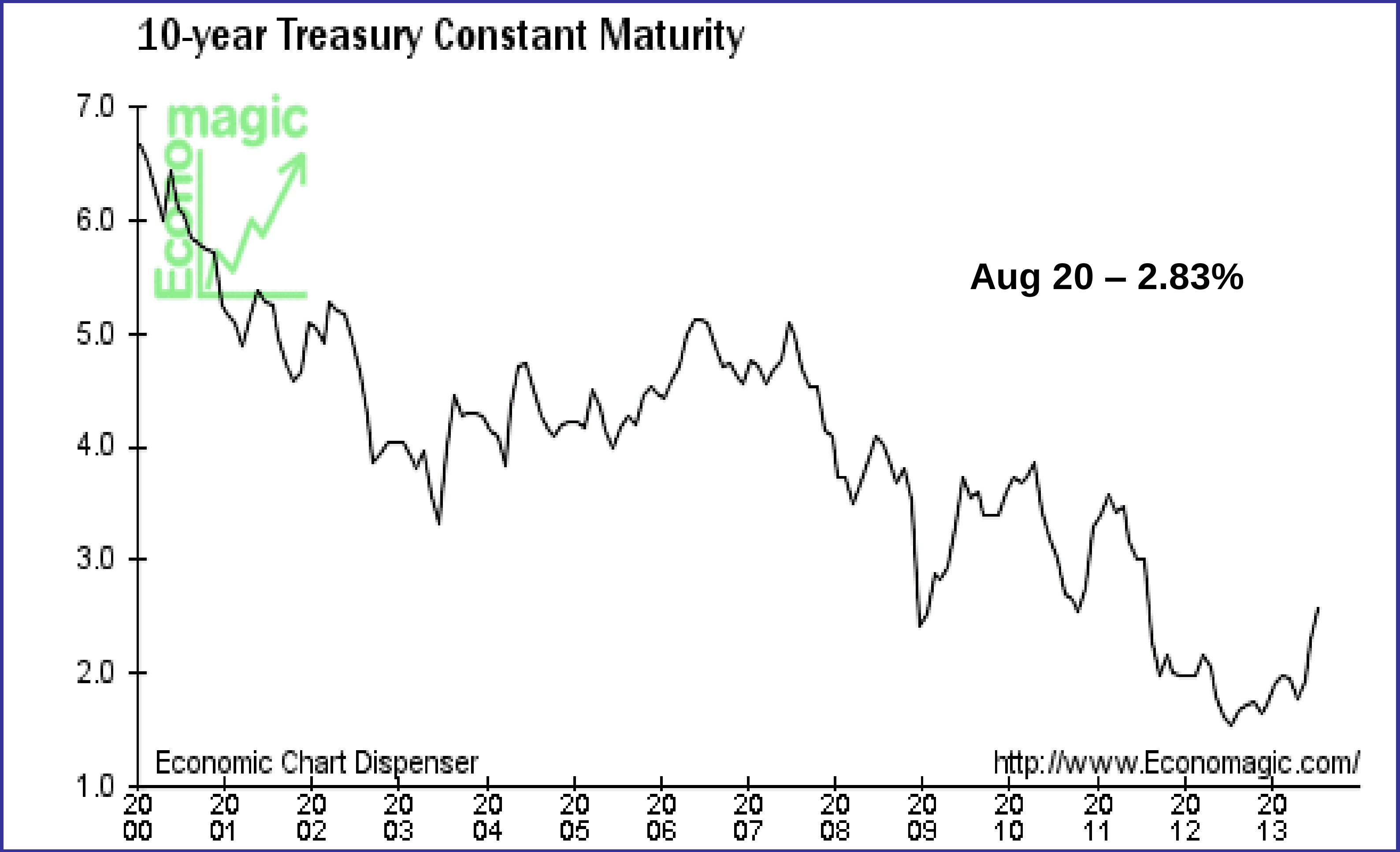
How long can we realistically expect 10 year rates
To stay below 3%? c'mon!!



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Recent Housing statistics

Background:
Markets are getting better –
Have we turned the corner? – Probably, but
The climb back will remain muted
Until we see economic growth of 3% or
More for an extended period of time!!!

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Starts are finally turning the corner??

Problems going forward: distressed resales (i.e., foreclosures) and jobs. Rising prices will moderate the foreclosure problem while good paying jobs will create demand – this will take more time!!

Single family starts, Thousand units, SAAR

Source: Census (http://www.census.gov/const/www/newresconstindex.html)

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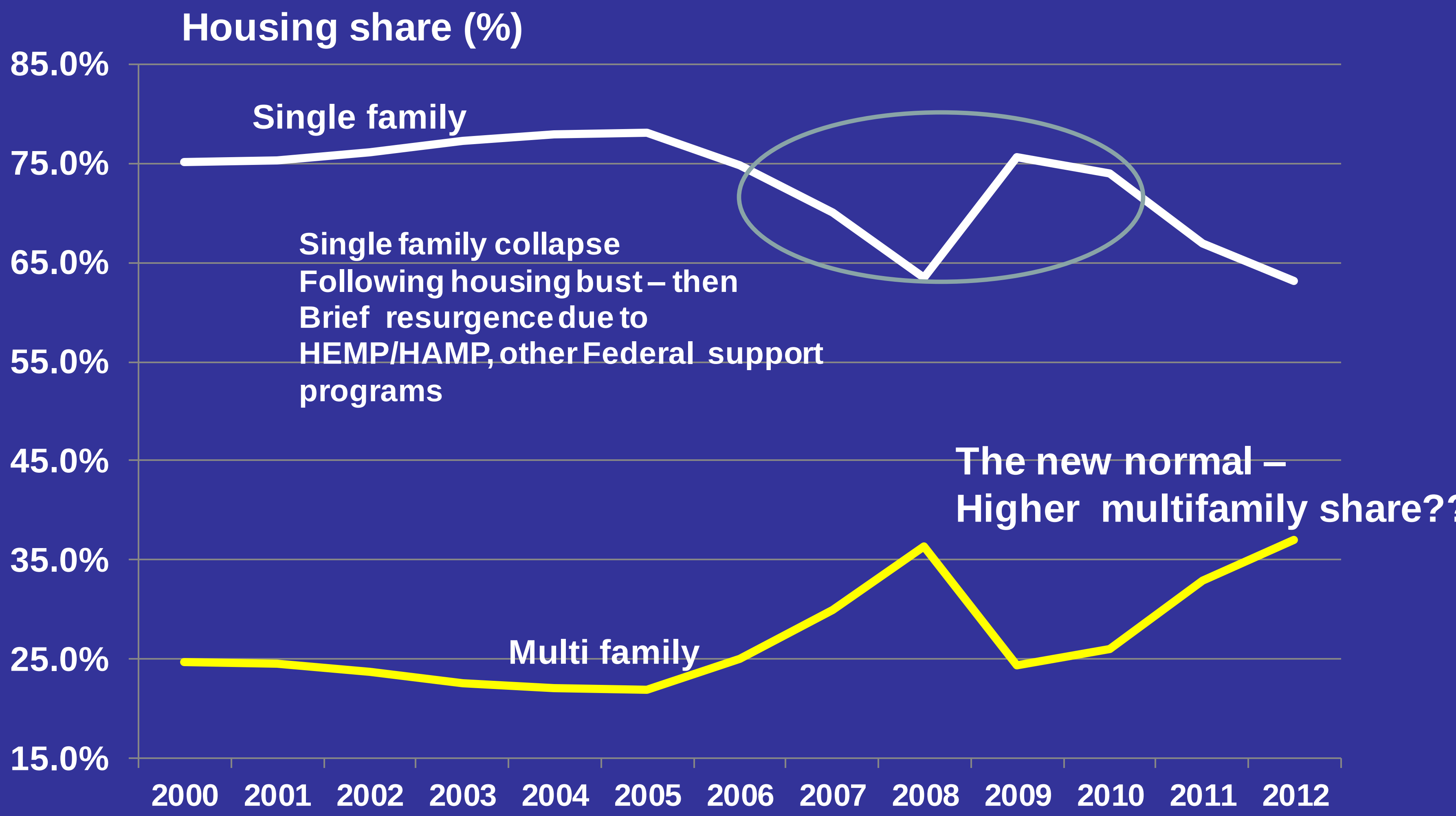
Multi family share is increasing – will it continue?
I believe it will!!



Source: Census (http://www.census.gov/construction/nrc/)

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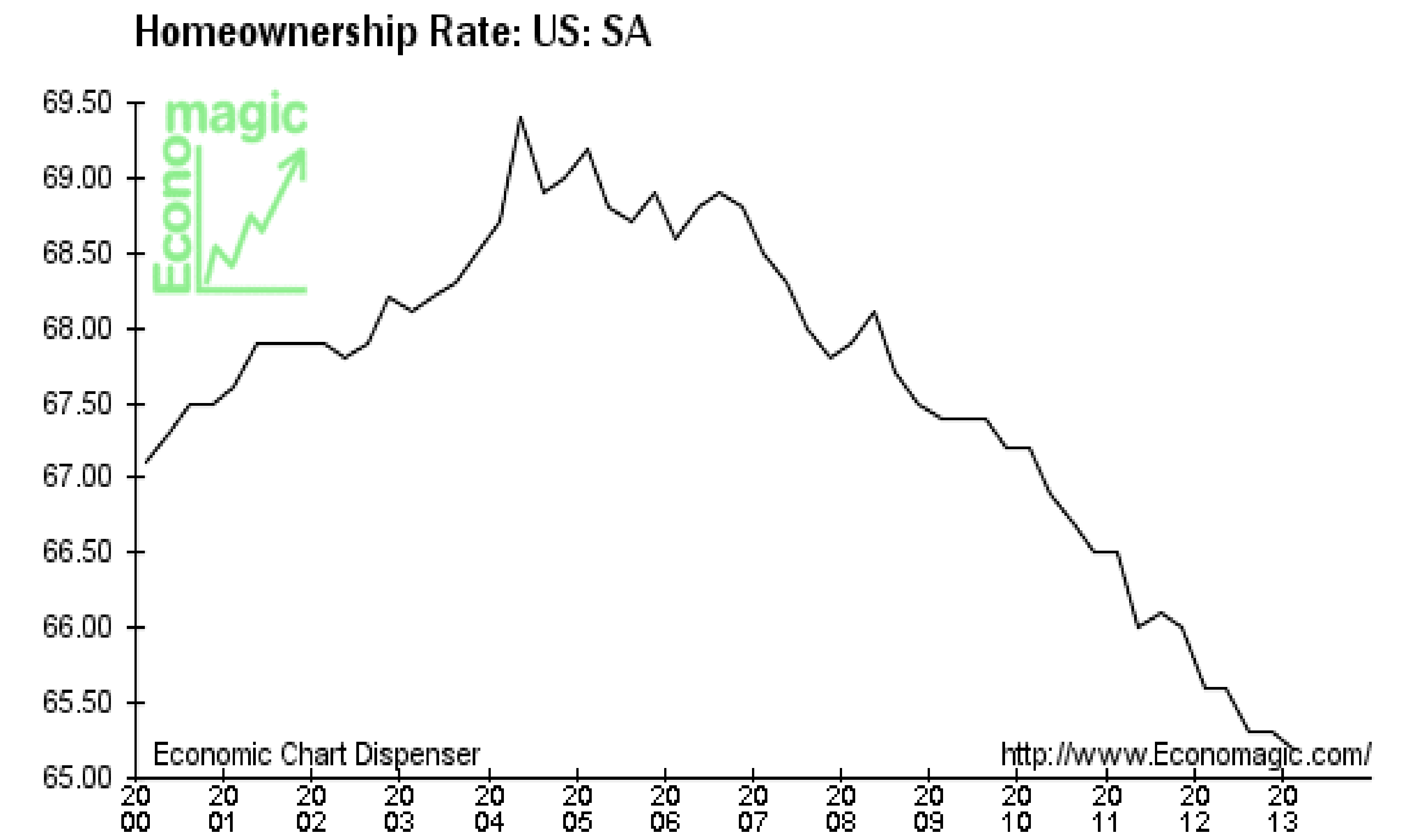
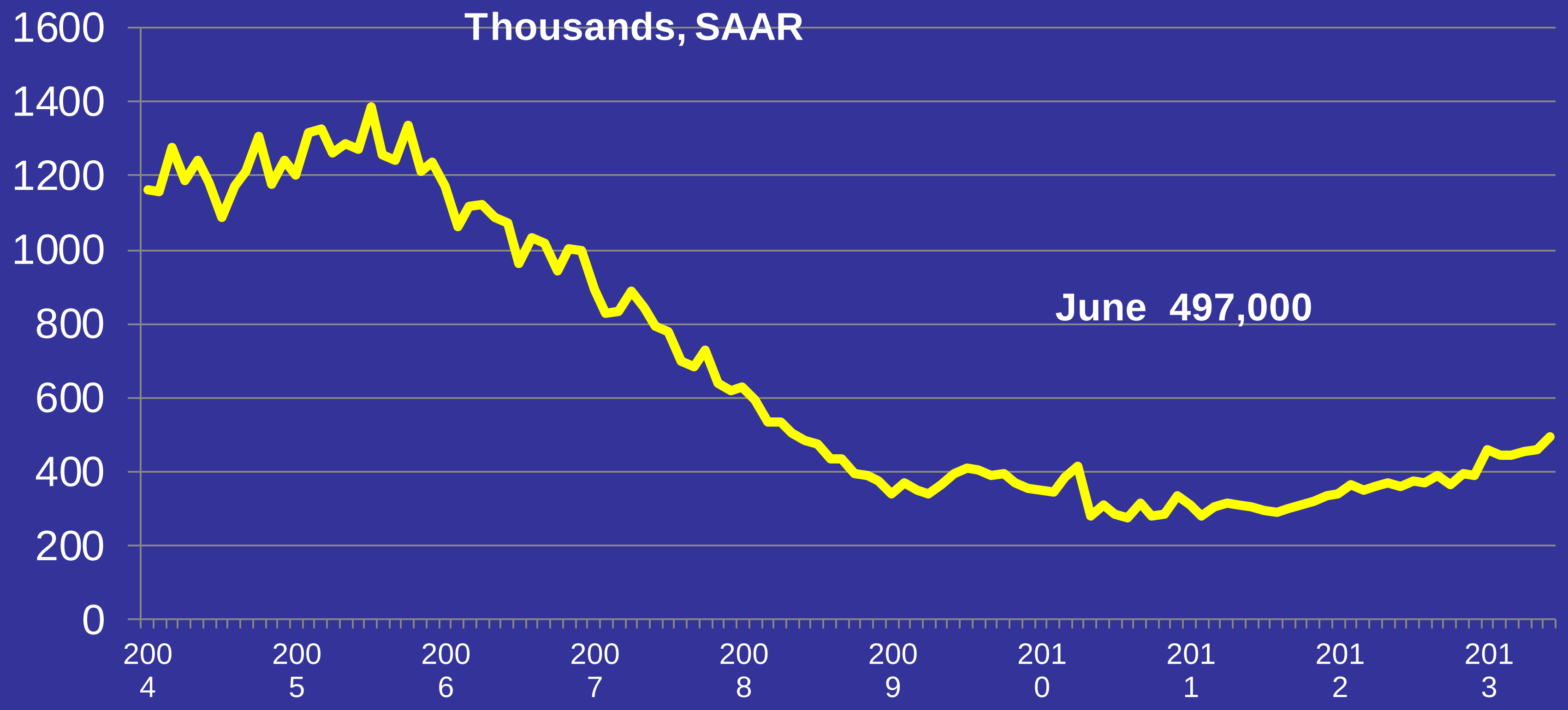
Homeownership rates have been falling for the past seven Years – big question – when the economy gets back to normal, Will people go back to single family or will we see more multi Family?? To date, the "recovery" has been mainly multifamily



Source: Census (http://www.census.gov/housing/hvs/files/qtr412/q412press.pdf)

New Single Family Home sales is the key statistic to watch – Sales drive housing starts – this drives demand for wood products!!!

Problem is price competition with resale homes, particularly distressed sales



Source: Census (http://www.census.gov/const/www/newressalesindex.html)

Resale market getting better – however, in 2012, about 25% of sales were cash only, mostly by investors – these homes were then rented - i.e., this is not your typical housing recovery

Source: NAR (http://www.realtor.org/research)

Some comments on recent house price increases - -

Let’s hope they keep increasing because higher prices
Will encourage builders to build more homes –

- - in addition - -

(1) higher prices are needed to slow foreclosures;
(2) enable people with negative equity to sell homes
 and move to better jobs;
(3) apply for refinancing - -
(4) this will turn housing market around along with
 improving economy

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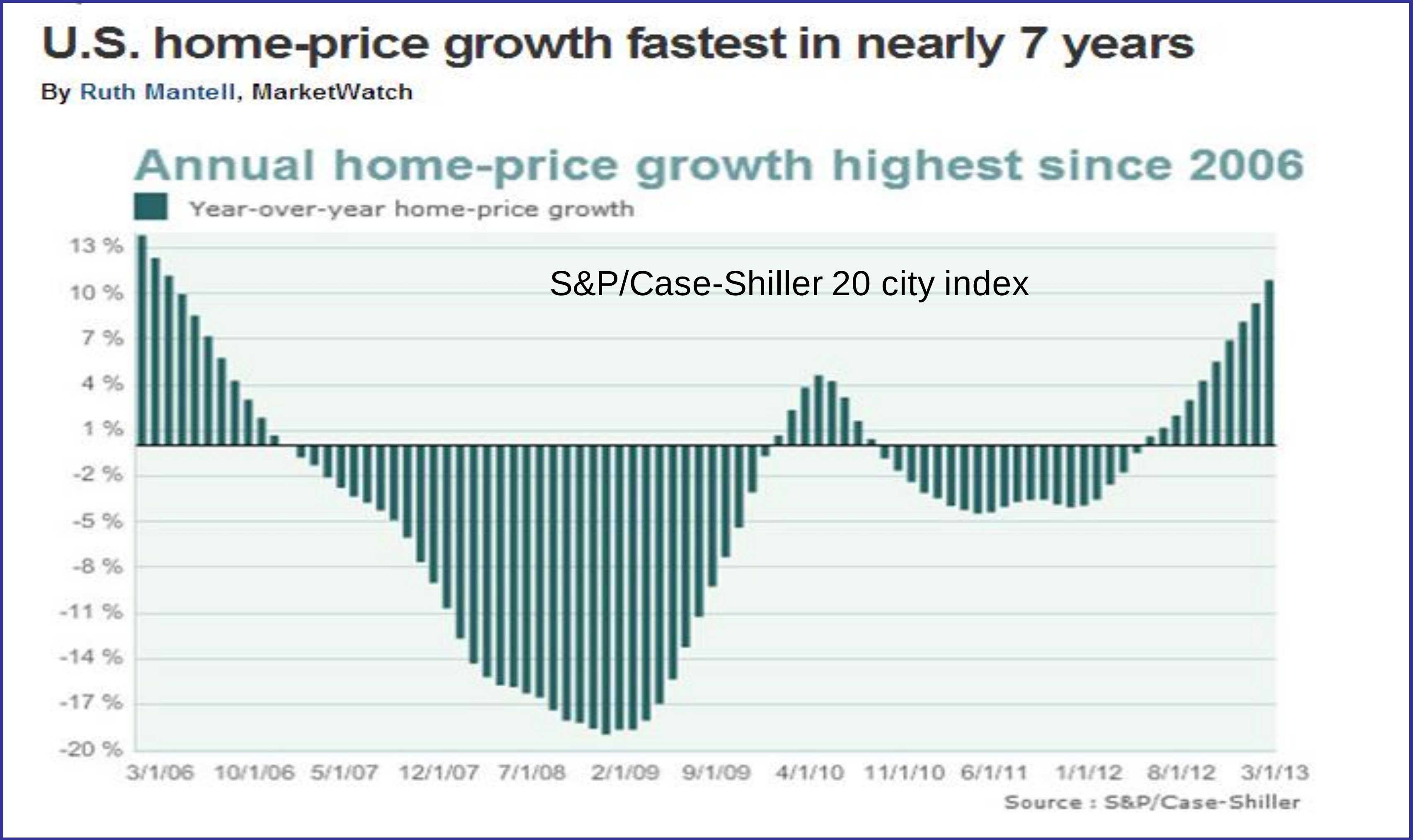
Price increase due in large part to weak supply, but, still good news –



Source: Case Shilller: (https://www.spice-indices.com/idpfiles/spice-assets/resources/public/documents/11644_cshomeprice-release-0430.pdf?force_download=true)

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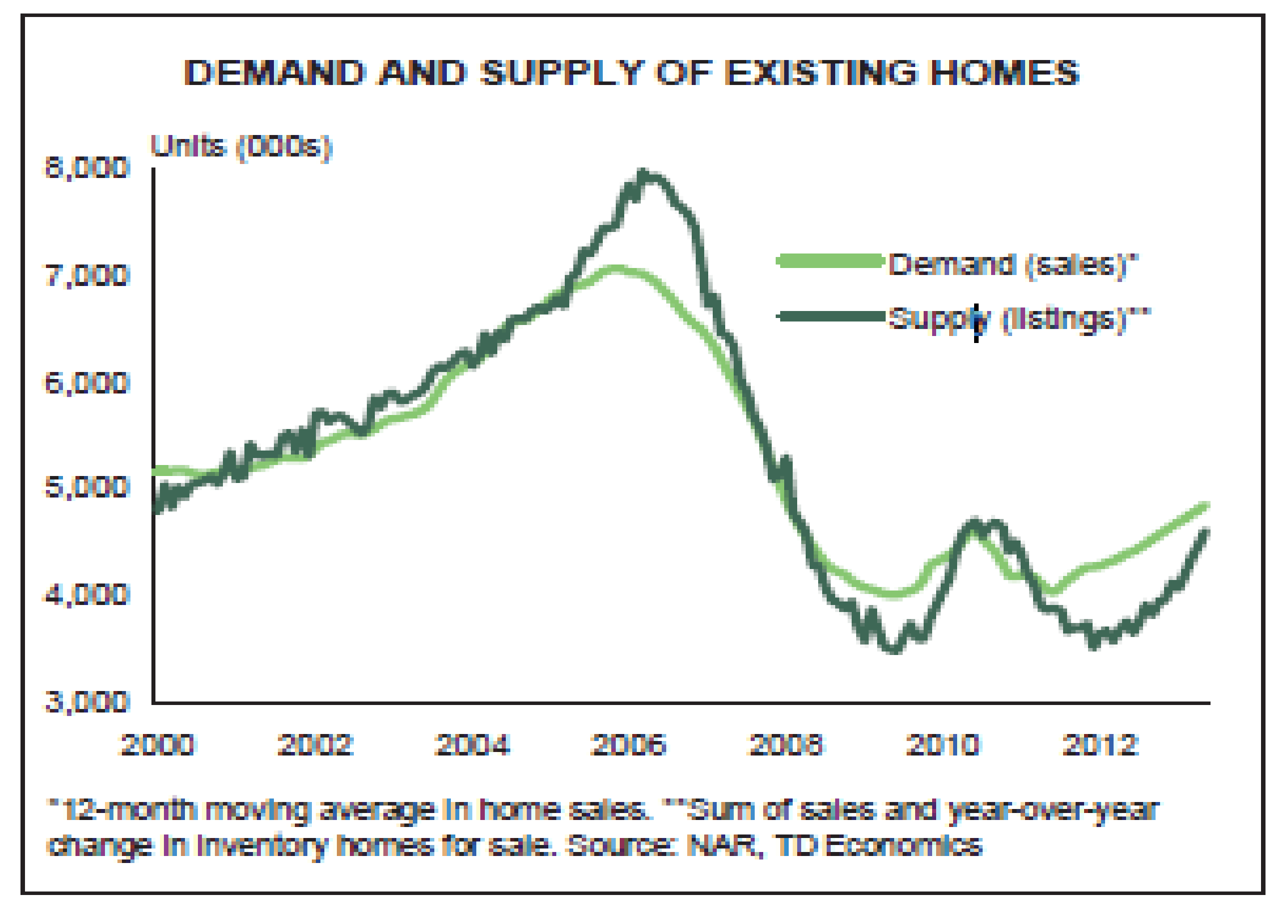
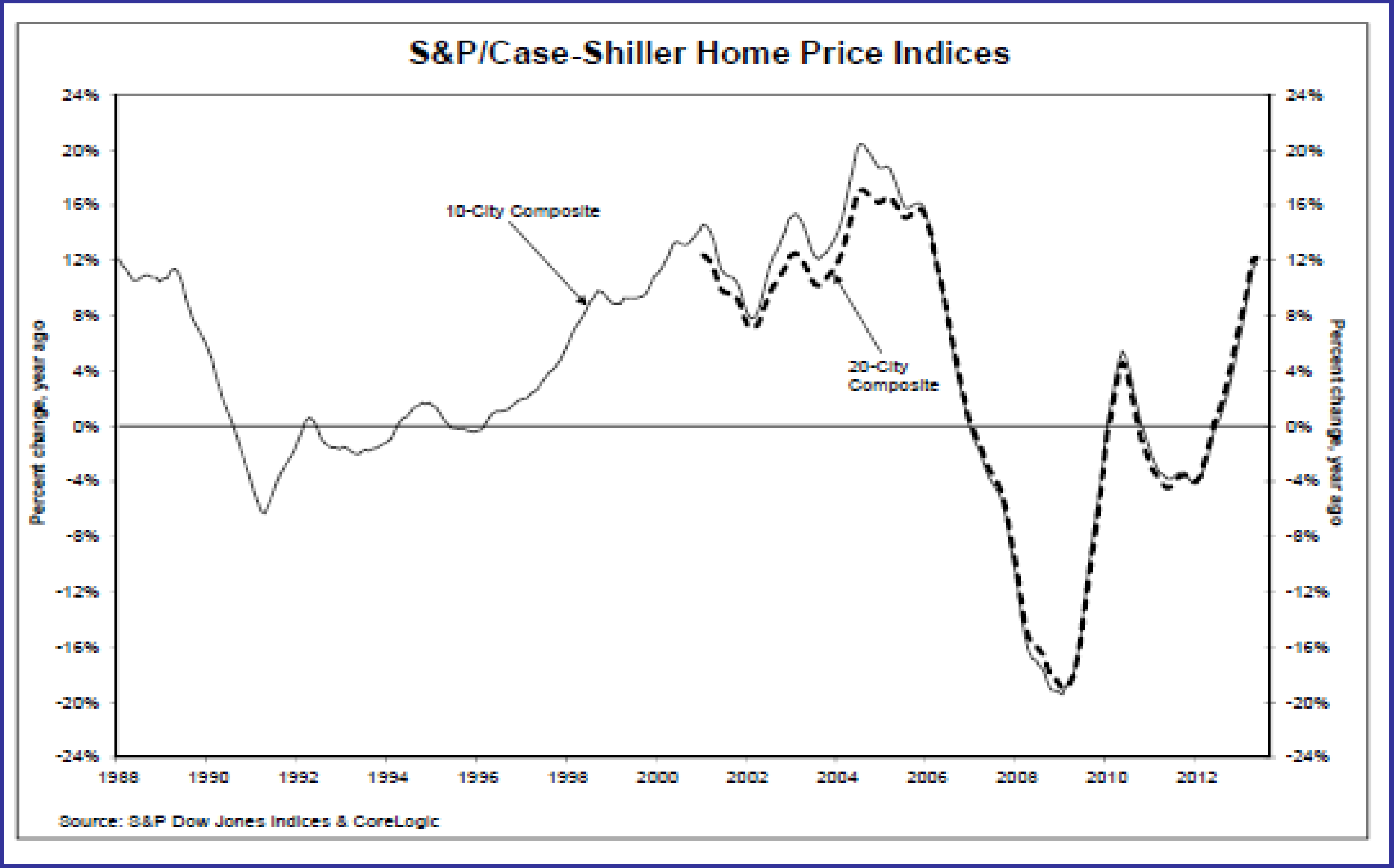
When demand exceeds supply, price rises
“Economics 101”



Source: TD Economics(http://www.td.com/document/PDF/economics/special/USHomePrices.pdf)

House prices up 12% year over year – Good news Because it will drive supply (housing starts) – Economics 101!!



(https://www.spice-indices.com/idpfiles/spice-assets/resources/public/documents/12473_cshomeprice-release-0625.pdf?force_download=true)

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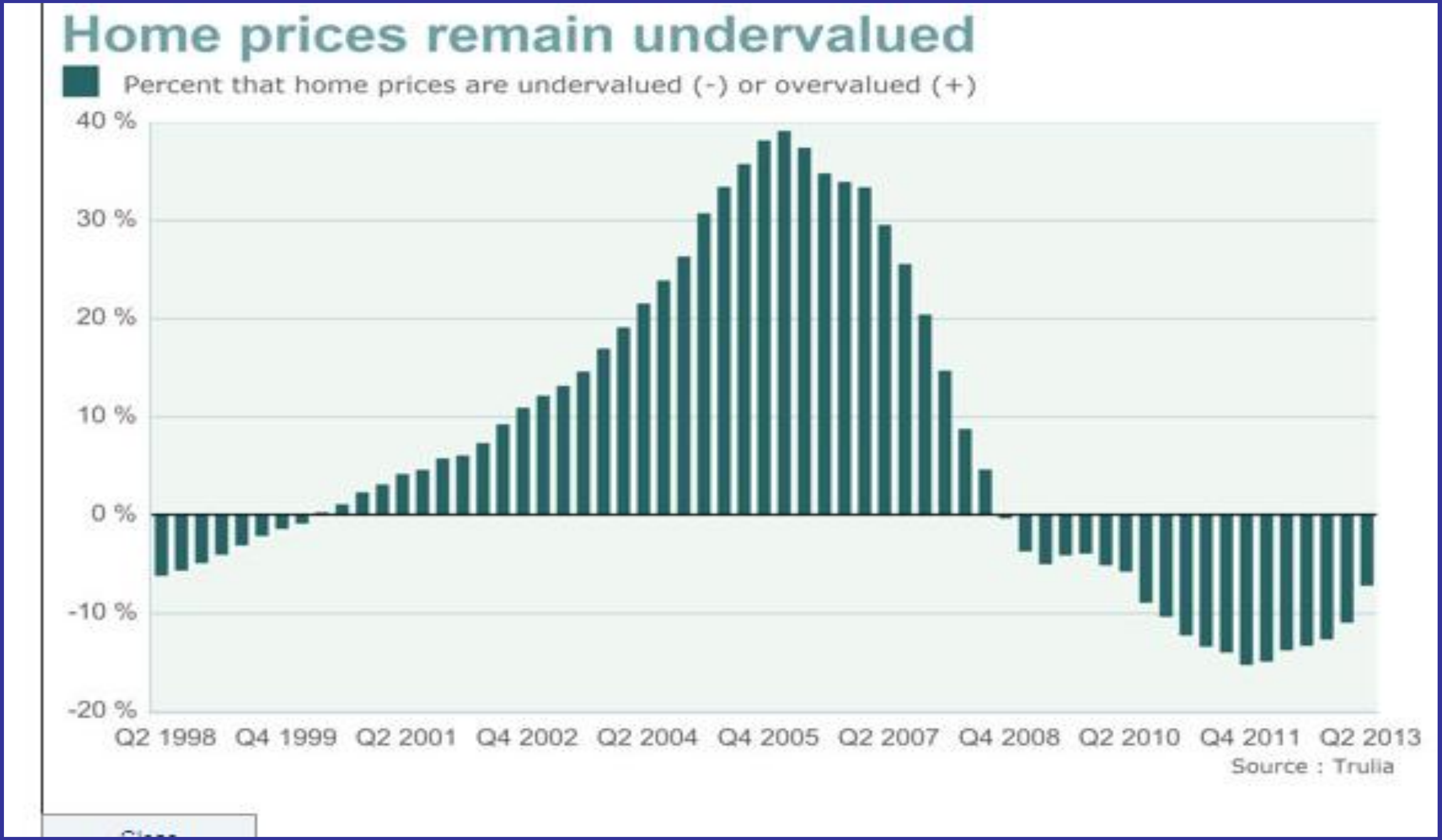
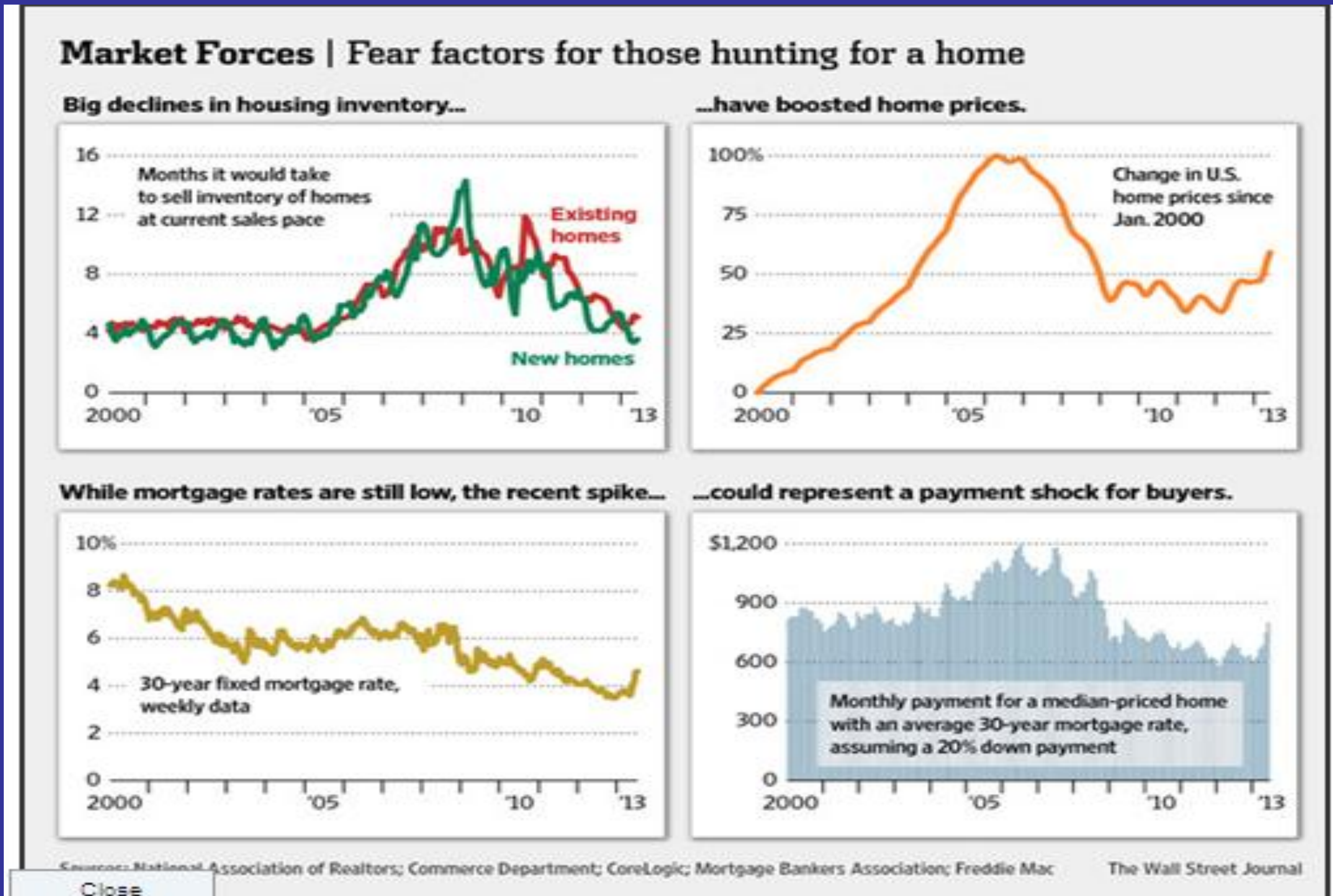
And, prices still undervalued compared with fundamentals Like price/rent ratios; affordability; etc. - this is not a bubble



(http://www.marketwatch.com/Story/story/print?guid=9E9C304A-EF17-11E2-922F-002128040CF6)

Higher prices and rates won't stop the housing recovery - -
Rates are still historically low and prices would have to increase
Another 20% before housing would become unaffordable relative to
historical levels



(http://online.wsj.com/article_email/SB10001424127887324263404578615771412506206-lMyQjAxMTAzMDMwMDEzNDAyWj.html?mod=wsj_valettop_email)

More comments re: recent house price increases

(1) Is it real and sustainable?

Due in large part to demand/supply mismatch

(Mike Santoli/Daily Ticker, May 28)

(a) Low inventories plus weak new home starts

(b) 25% of homeowners are still “underwater”

(c) 18% have little equity

i.e., 40% are “virtually trapped in their houses”

(2) Are we setting ourselves up for another “bubble” – no, we can’t be that dumb?

(3) Yes, it’s sustainable as long as the economy continues to move forward!!!

(4) *Rising prices are a good thing (because it means demand is improving)*

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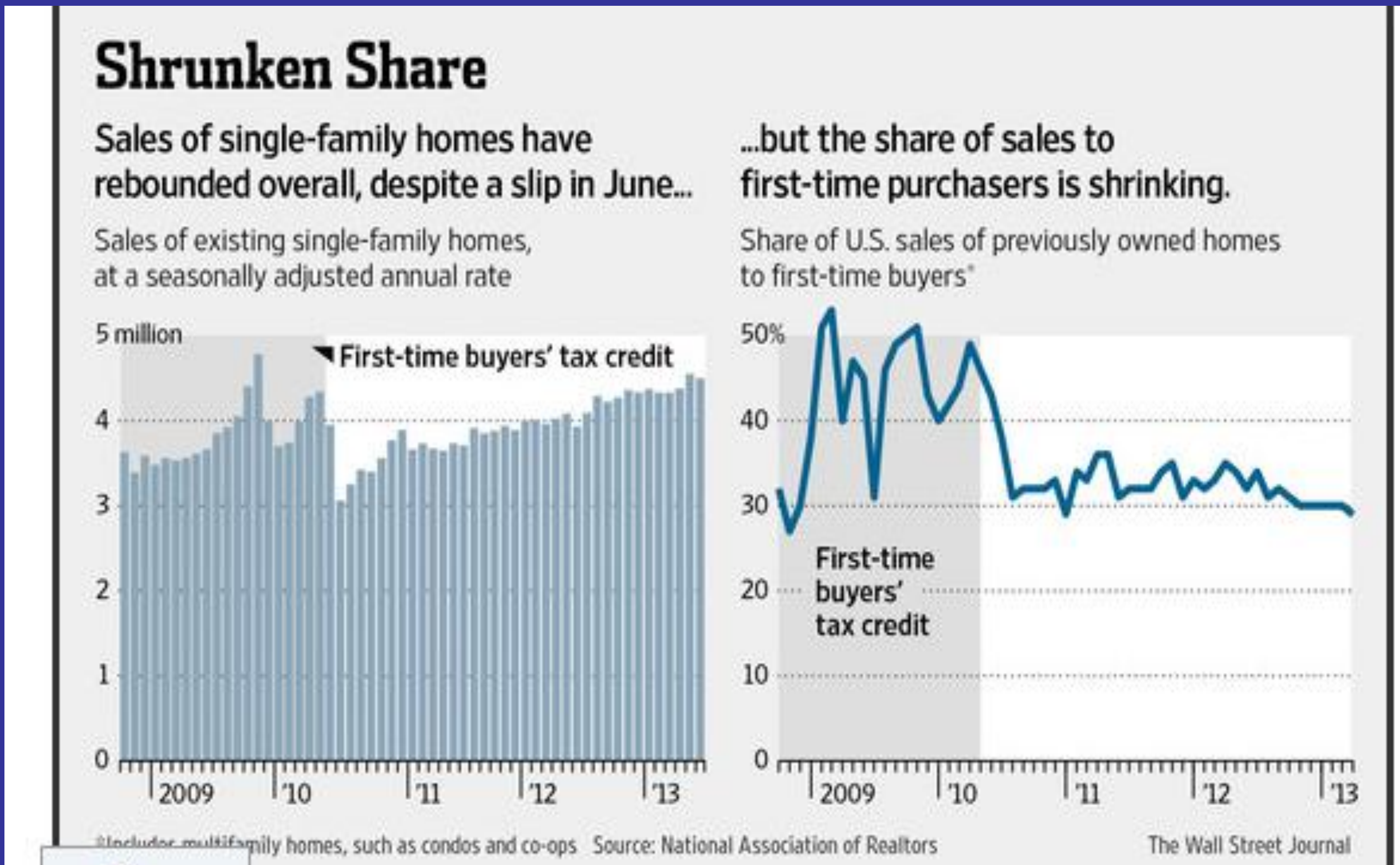
Problem with today's market – 1st time buyers share down
To 30% from historical average of 40% - this problem "cascades"
Over time (fewer 1st time buyers = delayed "move up" buyers, etc.)



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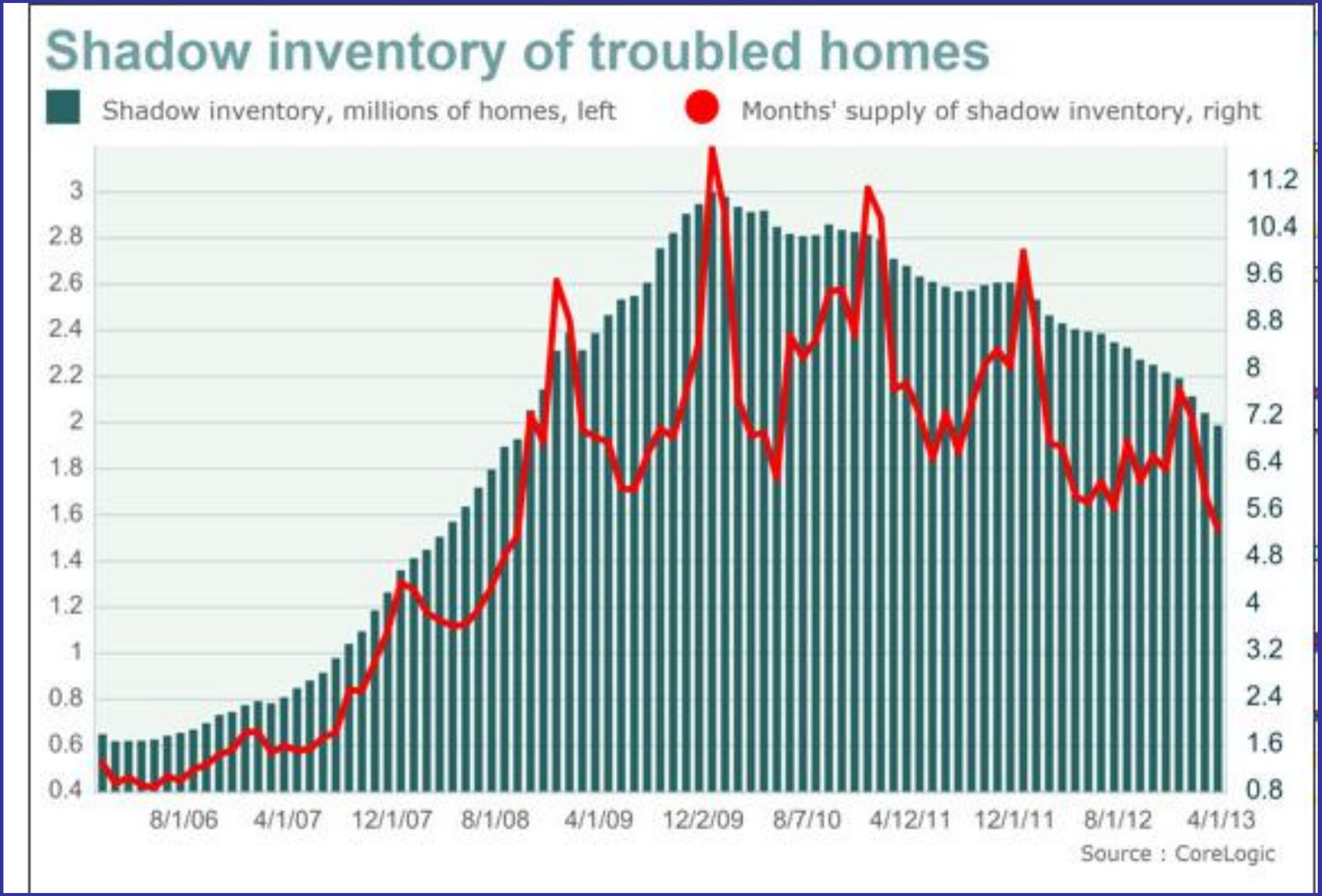
Shadow inventory coming down – a good sign



(http://www.marketwatch.com/Story/story/print?guid=9E9C304A-EF17-11E2-922F-002128040CF6)

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Latest Housing Forecasts – and change from forecast
Six months ago – multi family is leading the way

The Forecasts of the Analysts

2013 Housing Starts (thousands)

	Single-Family	Multi-family	Total
APA - The Engineered Wood Assn	645	330	975
Forest Economic Advisors	639	332	971
National Assn of Home Builders	644	311	955
Mortgage Bankers Assn	635	325	959
Fannie Mae	659	318	977
Average	644	323	967
% change from average of the analysts' projections for 2013 in January	+0.3	+12.5	+4.1

Source: Random Lengths, July 12

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Good News - -

(1) Household formations are key to the housing recovery
- - - there is a growing “pent up demand”

(2) Formations are improving – but, further improvement depends on a stronger economy

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Good news is that household formations exceed starts - -
Plus, when you include demolitions, there is considerable
"pent up demand" for shelter – again, demand exceeds supply –
A good thing

Source: WSJ (http://online.wsj.com/article/SB10001424127887324069104578531040339867974.html)

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Household (HH) formations Shortfall*

Facts:
(1) 1995 - 2007: 1.5 million HH formed per year
2008 – 2010: 500,000 HH formed per year (*1/3 of normal*)

(2) During 1995 – 2007, population increased 2.9 million annually
2008 – 2010, the increase was 2.7 million annually

*HH formation Shortfall(cumulative)**

2008 – 600,000
2009 – 1.7 million
2010 – 2.5 million
2011 – 2.6 million - this is the shortfall

* Shortfall based on model developed by Tim Dunne of the Cleveland Fed
Based on historical relationship between economy, headship rates, population increase, Social norms, etc. (http://www.clevelandfed.org/research/commentary/2012/2012-12.cfm)

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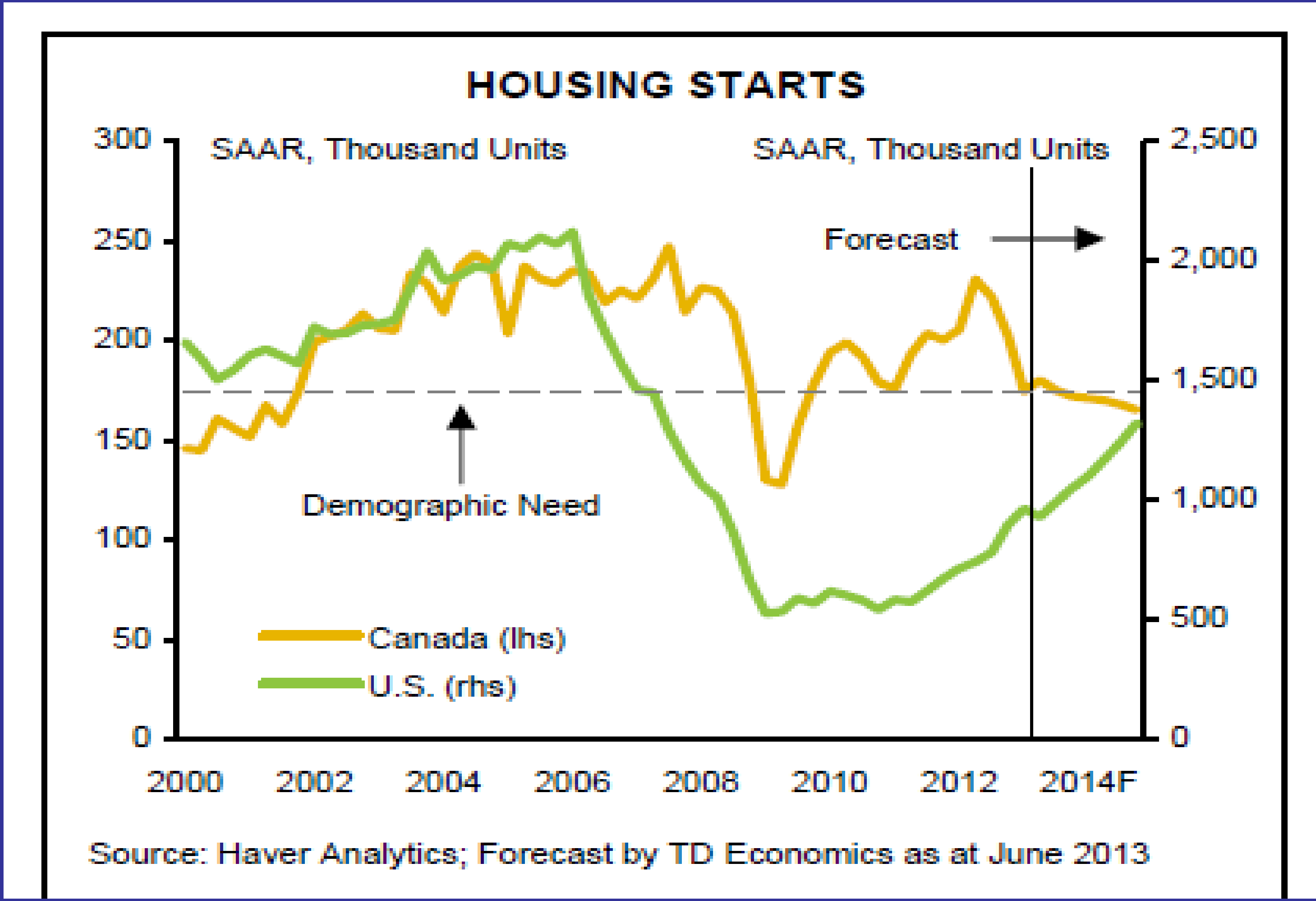
North American Housing outlook from TD Bank



Source: TD Economics (http://www.td.com/document/PDF/economics/special/LumberPriceCorrectionWillNotLast.pdf)

Bottom line – when economy returns to normal,
Demand for shelter will strengthen.

Question – what will the mix be between detached single
Family and multi family housing and what are the
Implication for the wood products industry? Also, implications
If house size gets smaller??

Most of you have seen this article by Craig Adair and
Myself and it is three years old, but there is some material
There that addresses the question posed above as it
Relates to the wood products industry
(http://www.nxtbook.com/nxtbooks/naylor/EWAB0110/index.php?startid=16#/16)

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Some conclusions – housing continues to improve – will Multifamily continue to gain share – will house size shrink?

(1) Economy will muddle along until 2015? Depends on world economy, China, Europe, ….. Question – can the economy "stand on its own"?
(2) What will housing look like in the future? My guess – smaller homes; higher percentage of renters; and more people moving back to the city
(3) We're in "uncharted waters" territory right now (i.e., massive money printing) to date, it has helped prevent worsening of economy, but, certainly hasn't had the impact the FED had hoped for (i.e., jump start the economy)
(4) Housing will continue to improve, albeit more slowly than hoped for
(5) Problems going forward are higher interest rates and continuing uncertainty. We have headwinds, but we're making good progress

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