October 2016 Housing Commentary

Urs Buehlmann
Department of Sustainable Biomaterials
Virginia Tech
Blacksburg, VA
540.231.9759
buehlmann@gmail.com

and

Al Schuler
Economist (retired)
Princeton, WV

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This report is a free monthly service of Virginia Tech. Past issues can be found at: http://woodproducts.sbio.vt.edu/housing-report/

October 2016
Housing Scorecard

	M/M	Y/Y
Housing Starts	Δ 25.5%	Δ 23.3%
Single-Family Starts	Δ 10.7%	Δ 21.7%
Building Permits	Δ 0.3%	Δ 4.6%
Housing Completions	Δ 5.5%	Δ 7.2%
New Single-Family House Sales	∇ 1.9%	Δ 17.8%
Existing House Sales[1]	Δ 2.0%	Δ 5.9%
Private Residential Construction Spending	Δ 2.8%	∇ 1.6%
Single-Family Construction Spending	Δ 0.1%	Δ 2.9%

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

Source: U.S. Department of Commerce-Construction; [1]National Association of Realtors® (NAR®)

Housing Data

	October	September	Oct. 2015
Total permits*	1,229,000	1,225,000	1,175,000
Single-family permits	762,000	742,000	725,000
Multi-family 2-4 unit permits	28,000	36,000	35,000
Multi-family ≥ 5 unit permits	439,000	447,000	415,000
Total starts	1,323,000	1,054,000	1,073,000
Single-family starts	869,000	785,000	714,000
Multi-family 2-4 unit starts**	9,000	14,000	11,000
Multi-family ≥ 5 unit starts	445,000	255,000	347,000
Total completions	1,055,000	1,000,000	984,000
Single-family completions	749,000	721,000	640,000
Multi-family 2-4 unit completions**	6,000	13,000	9,000
Multi-family ≥ 5 unit completions	300,000	266,000	355,000

* All data are presented at a seasonally adjusted annual rate (SAAR).
** US DOC does not report 2-4 multi-family starts and completions directly, this is an estimation.
Source: U.S. Department of Commerce-Construction: www.census.gov/construction/nrc/pdf/newresconst.pdf; 11/17/16

Housing Data

	October	September	Oct. 2015
New single-family sales	563,000	574,000	478,000
Median price	$298,700	$314,100	298,700
Existing sales[a]	5,600,000	5,490,000	5,290,00
Median price	$232,200	$235,300	$219,100
Private Residential Construction	$466.2 billion	$458.8 billion	$445.4 billion
SF construction	$243.5 billion	$236.8 billion	$243.5 billion
MF construction	$63.7 billion	$61.9 billion	$57.2 billion
Improvement construction[b]	$159.1 billion	$159.9 billion	$140.7 billion

[a] NAR®

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

Sources:
NAR® www.realtor.org/topics/existing-home-sales; 11/22/16
U.S. Department of Commerce-Construction: www.census.gov/construction/nrs/pdf/newressales.pdf; 11/23/16
U.S. Department of Commerce-C30 Construction: www.census.gov/construction/c30/pdf/privsa.pdf; 12/01/16

Conclusions

Housing is gaining some strength. Latest numbers show 10% increase in total starts in October, but that was driven primarily by the 75% increase in multifamily numbers. Interest rates are heading up as the labor market tightens. Hopefully, the new administration will turn things around, investment has been lagging as has productivity. Without productivity, the economy stagnates, as do incomes, standard of living, and, of course, housing activity. Without housing activity, wood product prices remain weak.

October's housing data is positive – total starts are up by 25.5% (m/m), single family homes starts are up by 10.7% (m/m), permits up by 0.3% (m/m), completions up by 5.5% (m/m), and existing home sales were up by 2.0% from the month before.

With meager economic growth (average growth since 2009 2.1%, slowest recovery since WWII) and with 51% of all worker's in the U.S. making less than $30,000/year, it's hard to envision a scenario where the U.S. housing market returns to "normal" anytime soon. Slowing economies in China, Brazil, among others, and continuing problems in Europe's banking sector all add up to numerous negative macro-factors endangering a robust housing recovery, in particular:

1) A constrained quantity of well-paying jobs being created;
2) a tepid economy;
3) declining real median annual household incomes;
4) strict home loan lending standards – though loosening with new programs
5) slow world economy; and
6) global uncertainty

September 2016
EU Housing Scorecard

		M/M	Y/Y
Production in Construction[A]	EU 28	∇ 0.3%[s]	Δ 1.8%[s]
	EU 19	∇ 0.9%[s]	∇ 0.2%[s]
	Germany	∇ 0.4%	Δ 1.7%
	France	∇ 1.7%	Δ 0.7%
	UK	Δ 0.9%[p]	Δ 2.6%[p]
	Spain	Δ 1.5%[ps]	Δ 4.5%[p]
Building permits (m² floor) [A]	EU 28	-.-	-.-
	EU 19	Δ 8.3%[(07)]	Δ 19.5%[s(07)]
	Germany	Δ 3.8%	Δ 10.8%
	France	Δ 0.2%[s]	Δ 16.6%[e]
	UK	-.-	-.-
	Spain	Δ 0.4[s(07)]	Δ 71.8[e(07)]

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

Source: Eurostat (http://ec.europa.eu/eurostat/web/short-term-business-statistics/data/main-tables; 12/14/16)

[A] see http://ec.europa.eu/eurostat/web/short-term-business-statistics/overview/sts-in-brief

[e] estimate, [s] Eurostat estimate, [p] provisional, [-.-] no data available, [(08)] August data

Housing comments – October 2016

- *October starts were up 25% to 1.323 (SAAR) - SF at 869,000 (SAAR) – up 10% - MF was up 75% (yes, 75%) – that was the driver!*
- **Home ownership rate down to 63.5% in QTR3 2016 – *lowest ownership rate in 50 years!*** **Financing problems; changing *preferences (to renting); and rising home prices - problem for 1st time buyers***
- *Resale market dropped 1% - 5,330,000 (annual rate) – low inventory (4.6 months) driving prices higher – major impediment to sales*
- *New home sales were down 1.9% to 574,000 SAAR, but up 18% YOY*
- **Job creation is improving – October +161,000 - unemployment at 4.9% - – However , 51% of all workers make less than $30,000/year – can't buy a house on that! (https://www.ssa.gov/cgi-bin/netcomp.cgi?year=2014)**
- **30 year fixed rate mortgage inched up to over 4% this week – will impact some prospective buyers.**
- **Looks like the FED will raise rates next month – about time.**
- **RE: the election. Glad it is over (despite Jill Stein's Green party's pathetic attempt at recounts in Michigan, Wisconsin, and PA). The people have spoken – we want change. Not sure Trump is the best vehicle, but nothing would have changed with Hillary so at least we're moving forward (my opinion).**

OK – let's look at the economy ---

Want to fix the U.S. Economy? Start with the broken political System – new report from Porter et. al. (we start this November)

Political dysfunction has become the biggest economic stumbling block for the U.S., according to a Harvard report.

Here is the hyperlink to the Porter et al. study
(http://www.hbs.edu/competitiveness/Documents/problems-unsolved-and-a-nation-divided.pdf)

Interesting report from experts on competitiveness. Slow reading, but lots of good analysis, charts, and recommendations from some of America's leading thinkers on competitiveness.

Here are suggestions from the Porter study on how to fix America's economy – however, to accomplish this, we need a functioning government, which we don't have.

FIGURE 1: THE EIGHT-POINT PLAN FOR WASHINGTON

1	Simplify the corporate tax code with lower statutory rates and no loopholes
2	Move to a territorial tax system like all other leading nations
3	Ease the immigration of highly skilled individuals
4	Aggressively address distortions and abuses in the international trading system
5	Improve logistics, communications, and energy infrastructure
6	Simplify and streamline regulation
7	Create a sustainable federal budget, including reform of entitlements
8	Responsibly develop America's unconventional energy advantage

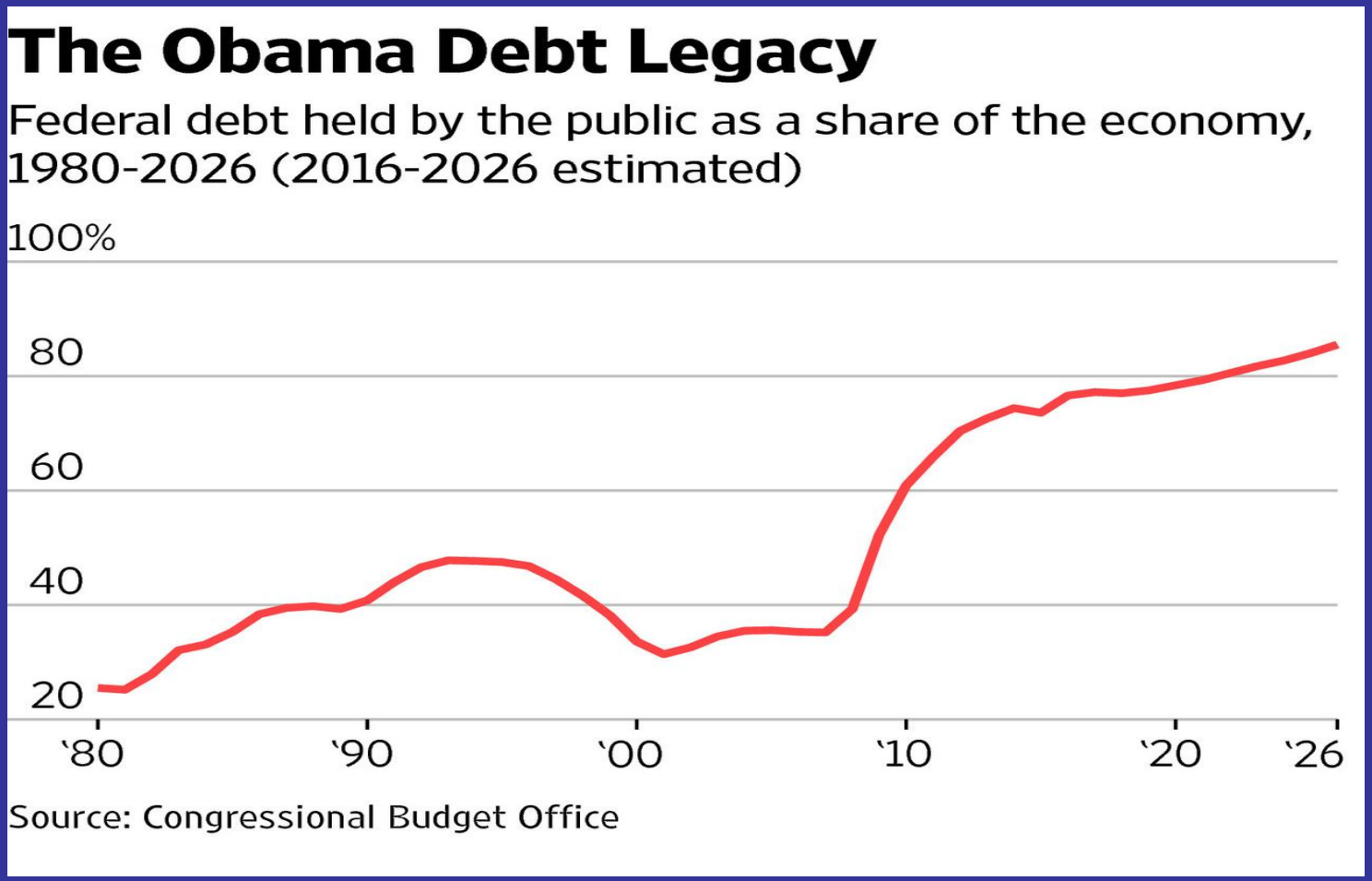
Source: Michael Porter and Jan Rivkin. "An eight-point plan to restore American competitiveness." The Economist: The World in 2013. (Nov 2012).

MY Comments on the economy – it continues to sputter – propped up by low interest rates, compliments of the FED –
business investment remains weak as Washington gridlock and uncertainty discourages investment needed to create jobs.
Also, businesses don't invest when they see excess capacity –
i.e., they don't invest into a weak economy that shows little sign of improving beyond 1% - 2% GDP growth.

I believe we, Europe, and many other countries are following Japan into a prolonged period of weak growth, low inflation, and low interest rates. Central banks can't fix our problems – when will we learn?

Debt - Innovation – Productivity

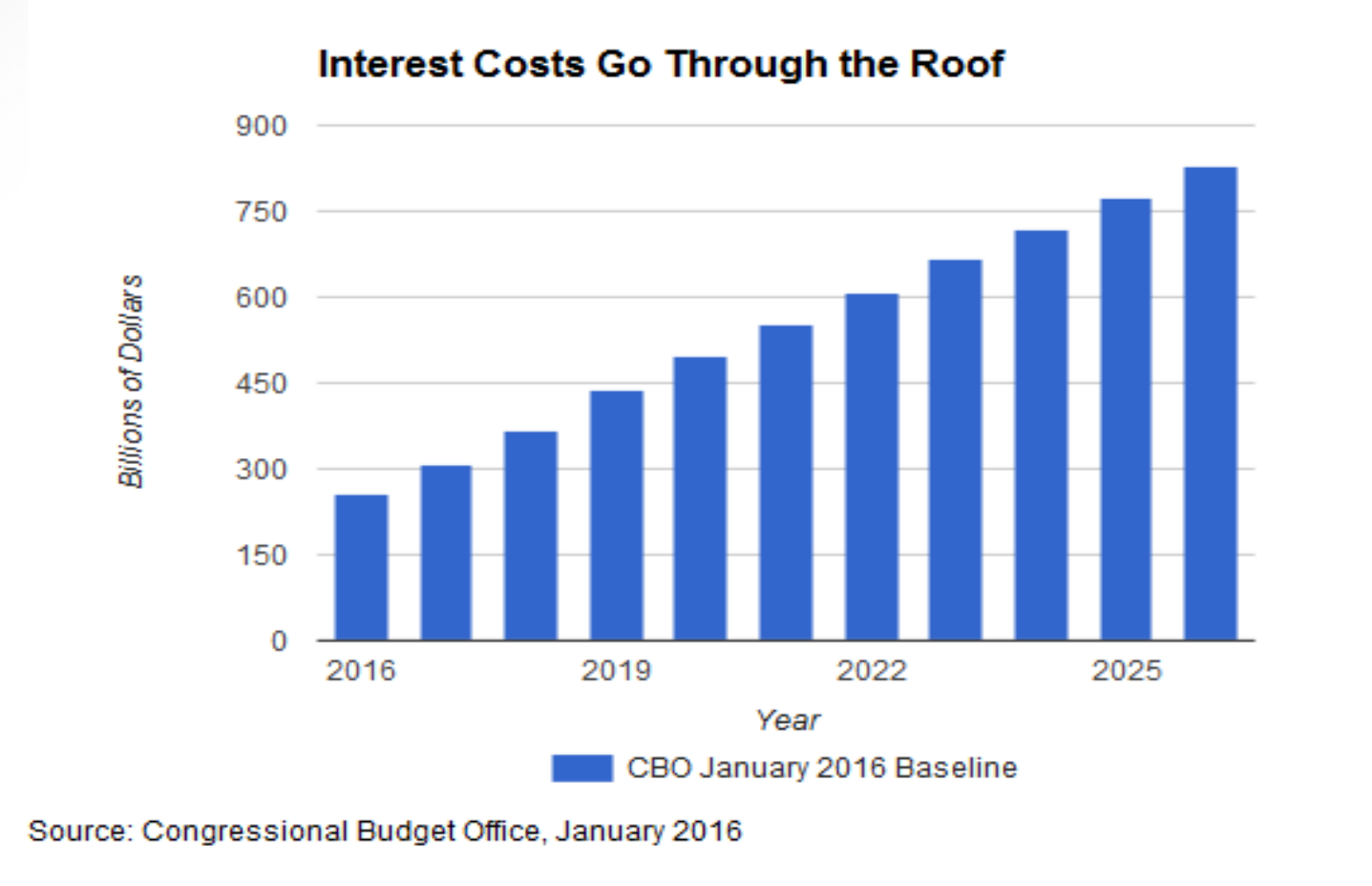
Huge problem facing this country is public debt – that's the debt that has to be repaid. Total debt today ~ $20 trillion, of which $14 trillion is "public debt". The $6 trillion ("borrowed") by the Treasury from the Social Security, Medicare, and highway trust funds is gone/spent. Here is link to real time debt clock (http://www.usdebtclock.org/) - a scary picture! PS: Public debt now equals 75% of GDP – we're getting very close point of no return – where principal plus Interest payments exceed our capacity to pay, and lenders refuse to lend – that's when "the shit hits the fan" – the USA of Greece!



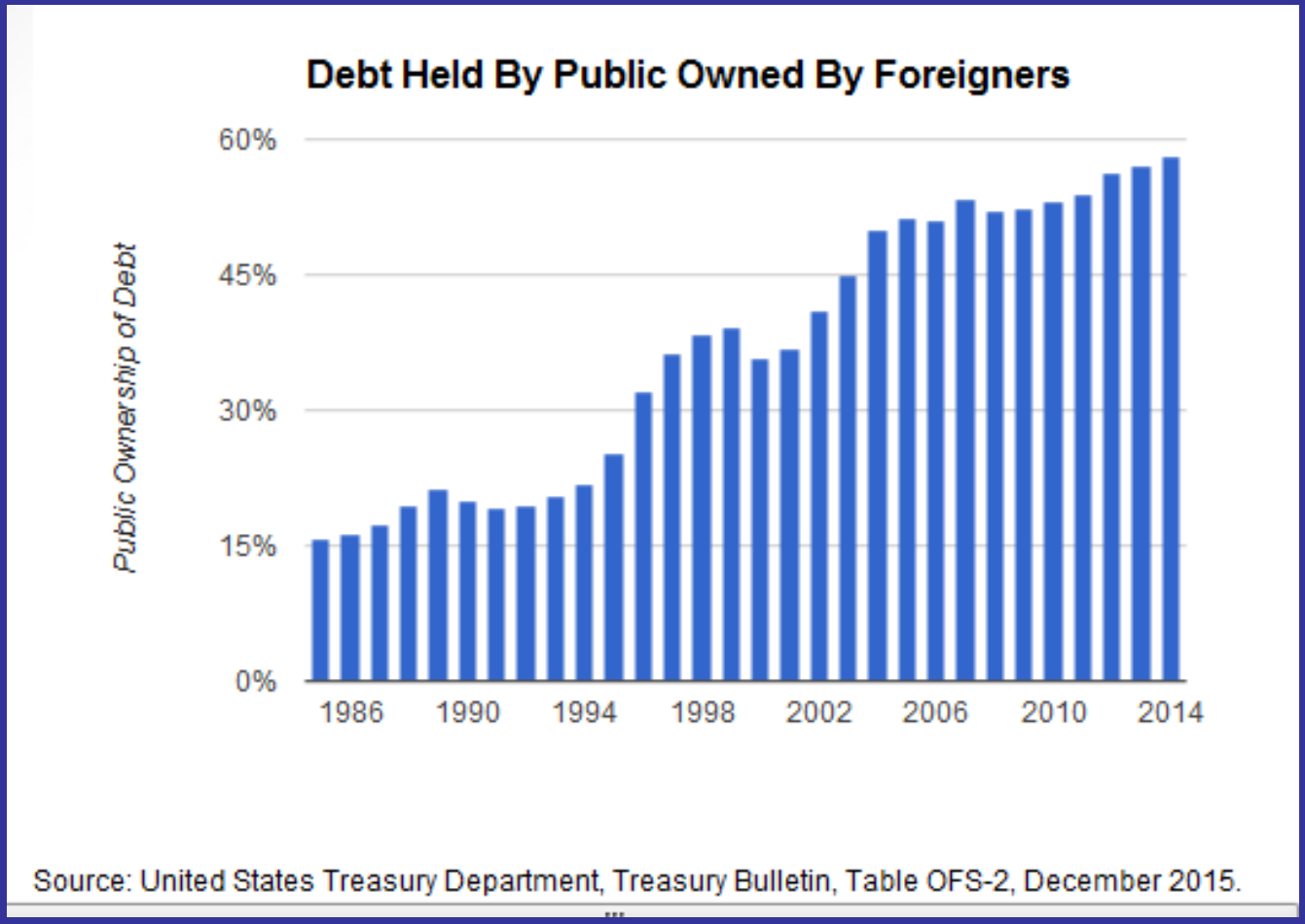
Main problem with $20 trillion debt is that paying down that debt (including interest) will reduce government spending on social programs, including Social Security, Medicare/Medicaid, housing allowances for the poor, food stamps. Furthermore, investments in technology, research/development, education, infrastructure, will suffer, hurting productivity even more. And, defense spending will suffer as well.
These investments and social programs are critical to future growth, GDP, standard of living, and security of our nation. And, yes, a return to a healthy housing market.

Not sure why we don't see this as a major threat to our future – Probably because we don't understand the magnitude of the Problem. Also, the politicians do a great job in "passing the Buck" – i.e., delaying the 'day of reckoning, promising that we'll tax the Rich, the banks, etc. – i.e., someone else will Pay for the fixes!!!! Guess what – that won't work – they are not main problem – as a country, we consume too much, save too little, and don't invest enough in our future. We are the problem, and we are the ones who must fix the problem.

Problems with too much debt – servicing costs will squeeze social programs (Social Security, Medicare Medicaid, food stamps, ..), R&D, education spending, infrastructure investments, ...

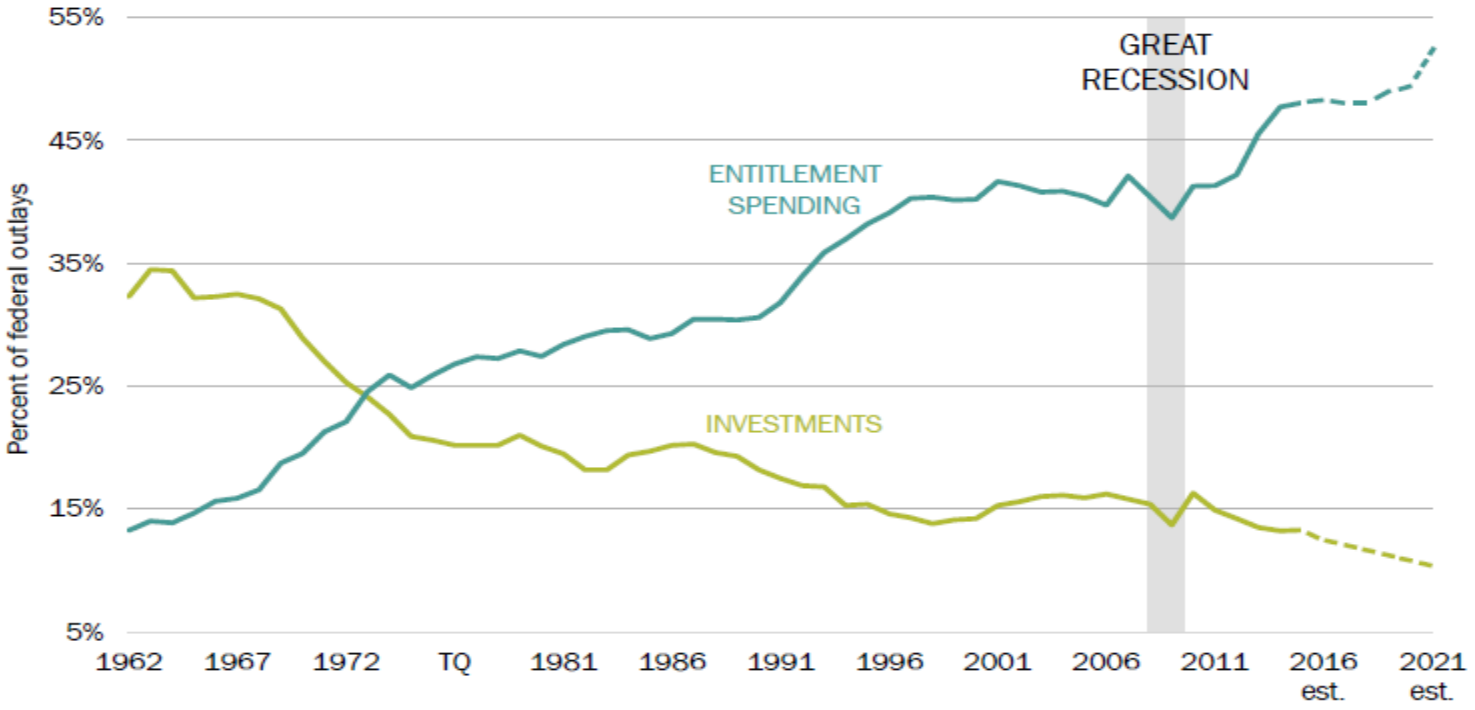


Big problem when foreigners question our ability to repay our debts – they will demand higher rates, etc., and eventually, refuse to buy our debt. When the proverbial "shit hits the fan".
Total debt = $20 trillion, of which $14 trillion is public and $6 trillion Is intergovernmental debt (i.e., what government owes itself).
Foreigners hold about $8 trillion of our debt which is 57% of the public debt.



Going into debt is OK if you're investing for the future - but, we're not!
For decades, we, as a nation, have been living a fantasy life. Entitlement spending is now approaching 50% of the federal budget while investment spending (critical to maintain our competitiveness) has been declining for the past 60 years. (from Porter et al. study)

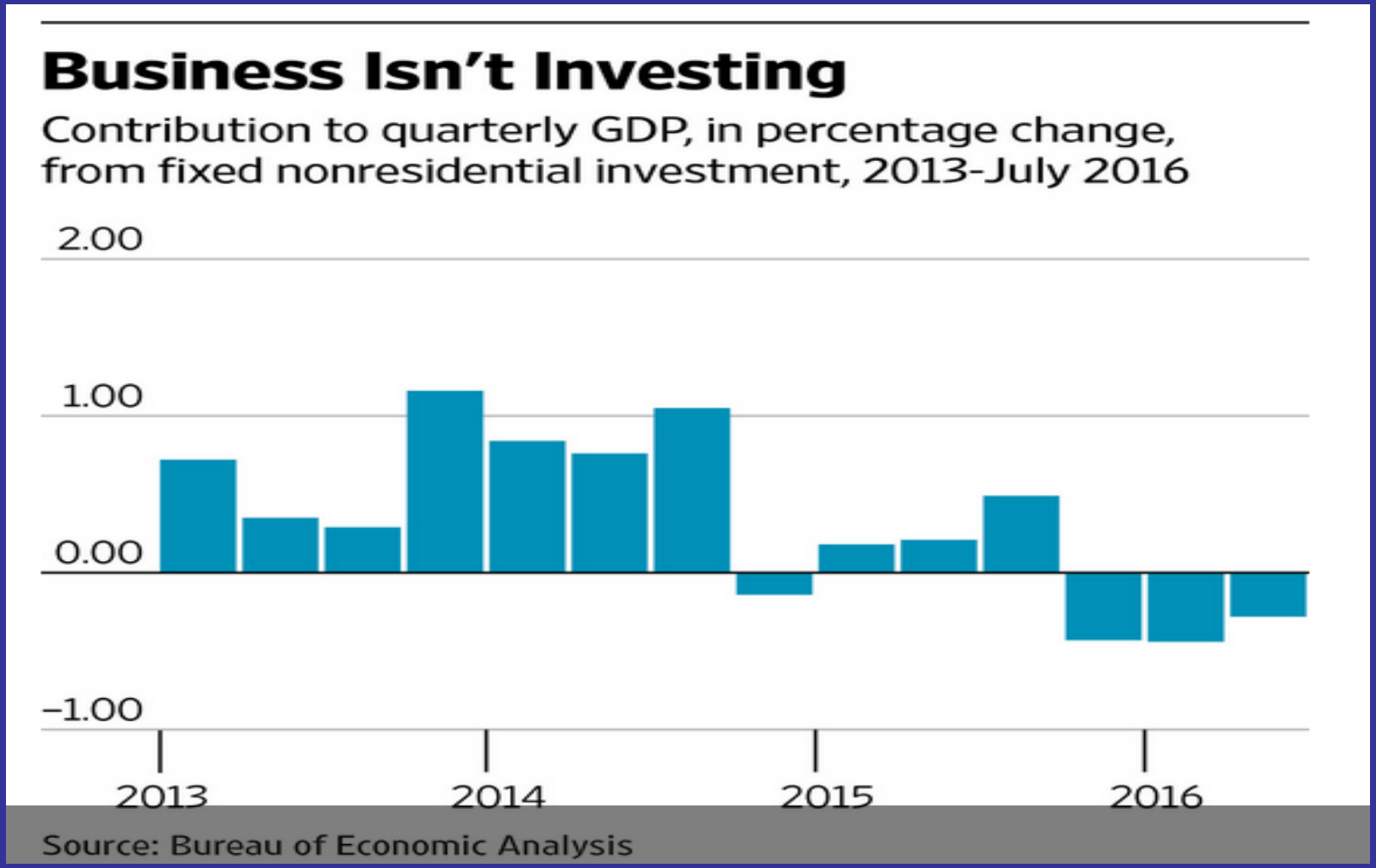
FIGURE 9: SHIFTING COMPOSITION OF FEDERAL SPENDING



Note: Entitlement spending includes outlays for Social Security, Medicare, Medicaid, CHIP, and Affordable Care Act Subsidies. Investments includes outlays for infrastructure, R&D (both defense and non-defense), and education. 2016-2021 figures are Office of Management and Budget estimates. TQ refers to the Transition Quarter from July 1, 1976 to September 30, 1976, after which the federal government changed its fiscal year. Dotted line is a forecast based on previous Office of Management and Budget estimates. Shaded area indicates the recession of December 2007 to June 2009 as defined by the National Bureau of Economic Research.

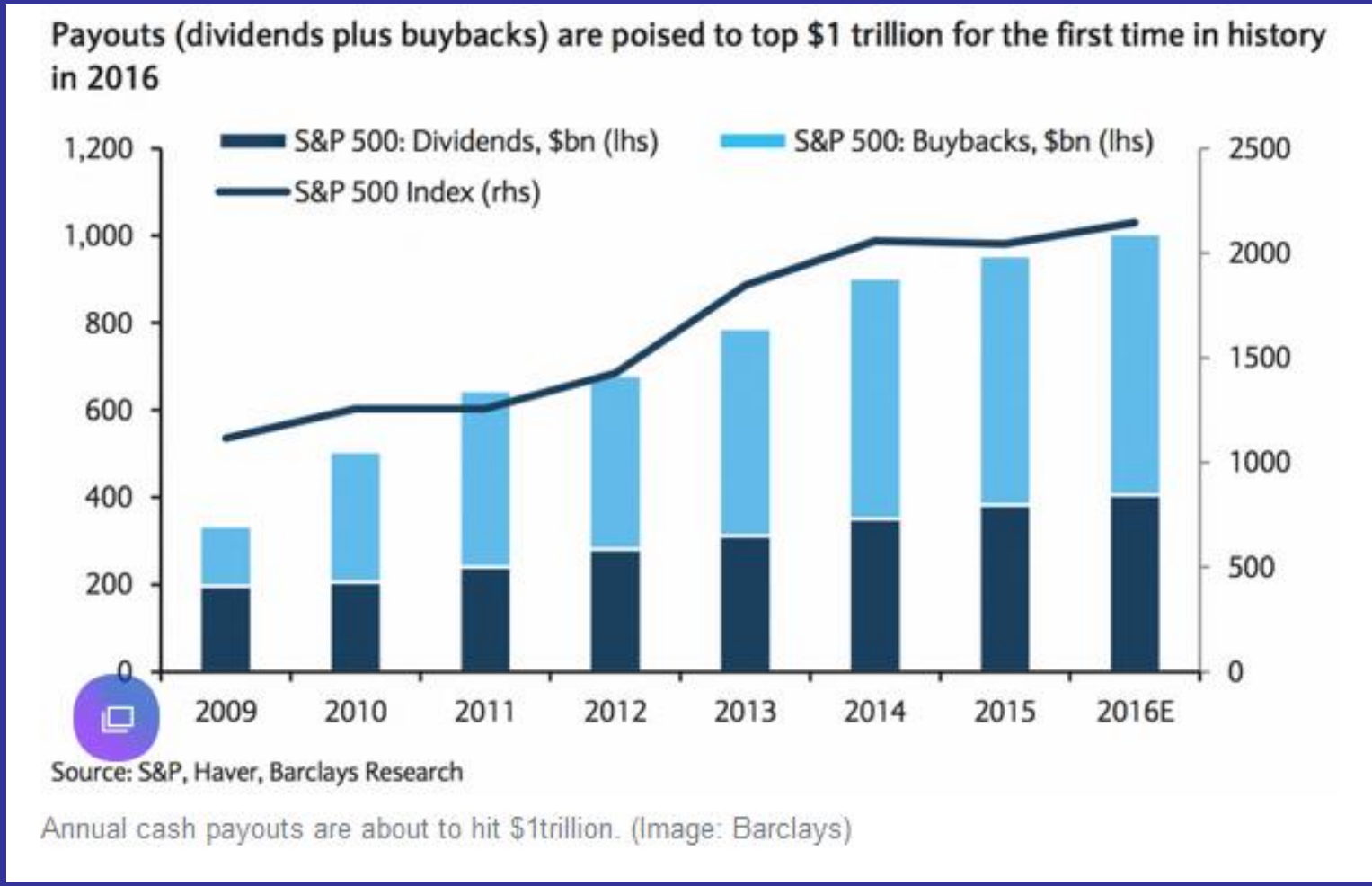
Source: Office of Management and Budget; author's calculations.

Business isn't investing either --- has been trending lower for the past several years. That's why GDP growth remains weak. That means income growth will remain weak and housing will continue to underperform, and creation of good paying jobs will remain an elusive goal.

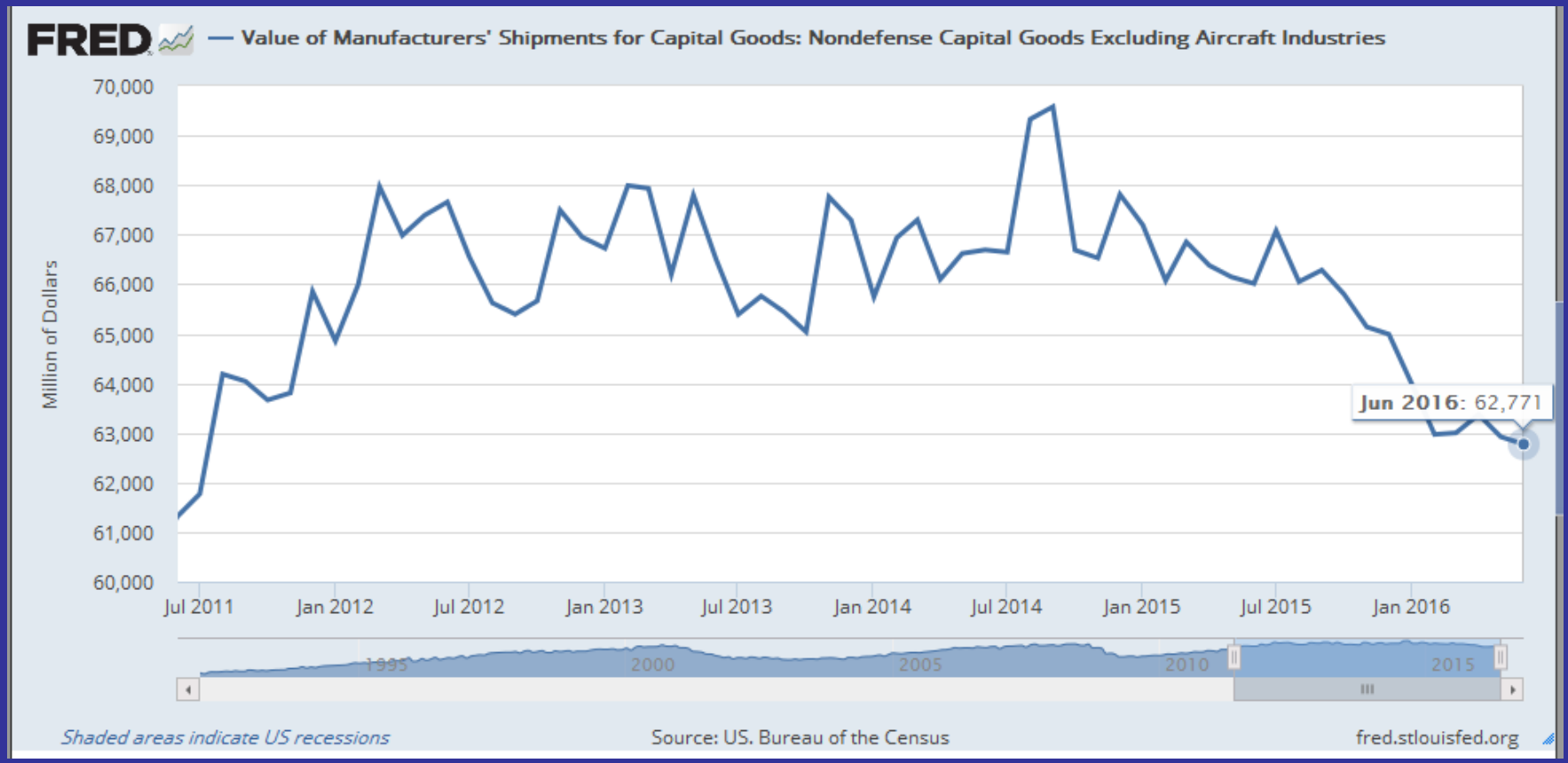


(http://www.wsj.com/articles/make-america-grow-again-1469831784)

This is what businesses do when they don't see much growth - instead of investing in plant, equipment, technology, they buy back stock and increase dividends. Good short term strategy, but does little to make the company/business more competitive.

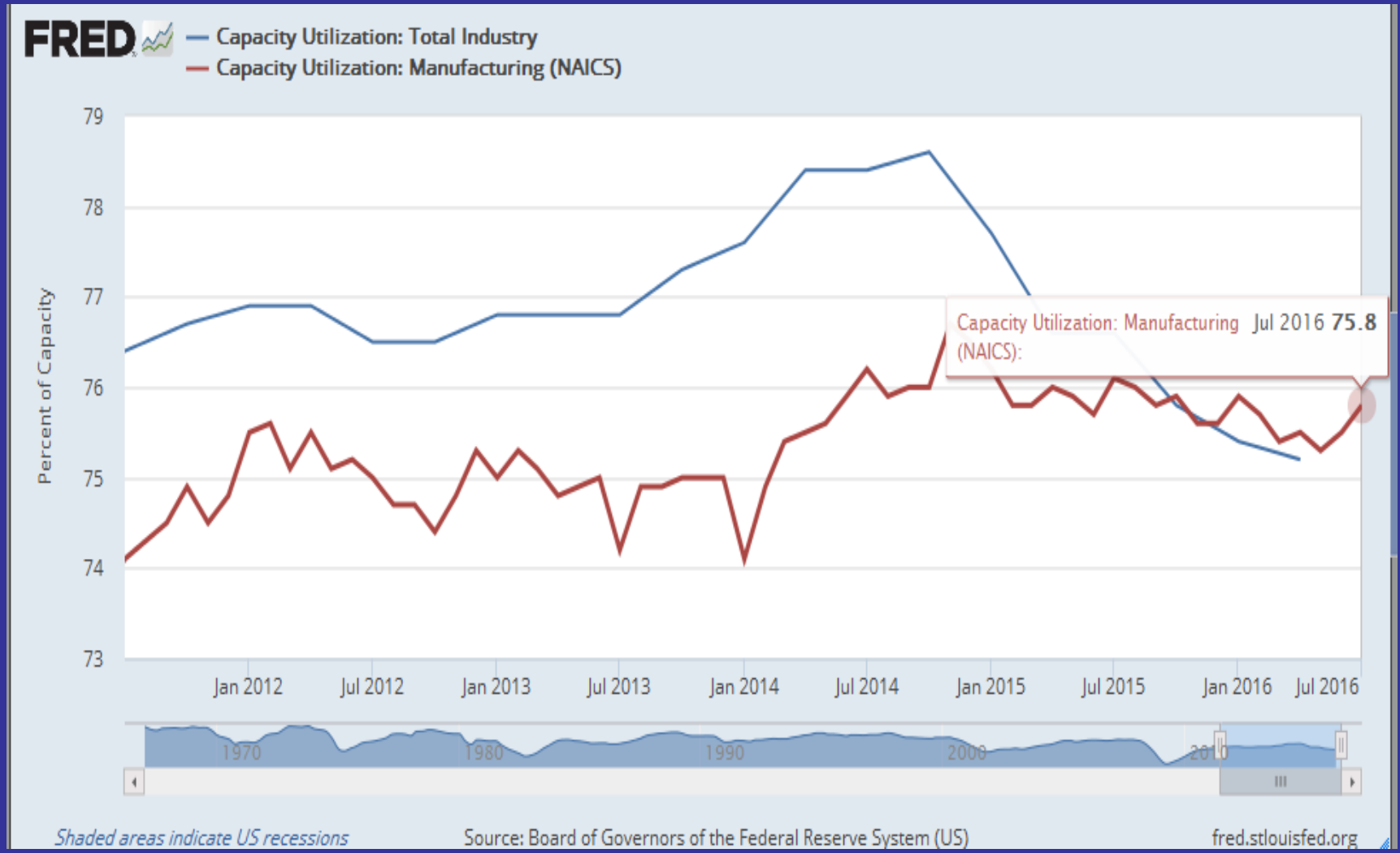


Capital spending has been trending lower for past 4 years
Why? Companies not confident of future – uncertainty re: Tax code, regulations; Washington grid lock!



(http://www.wsj.com/articles/u-s-durable-goods-orders-fell-2-2-in-may-1466771610)

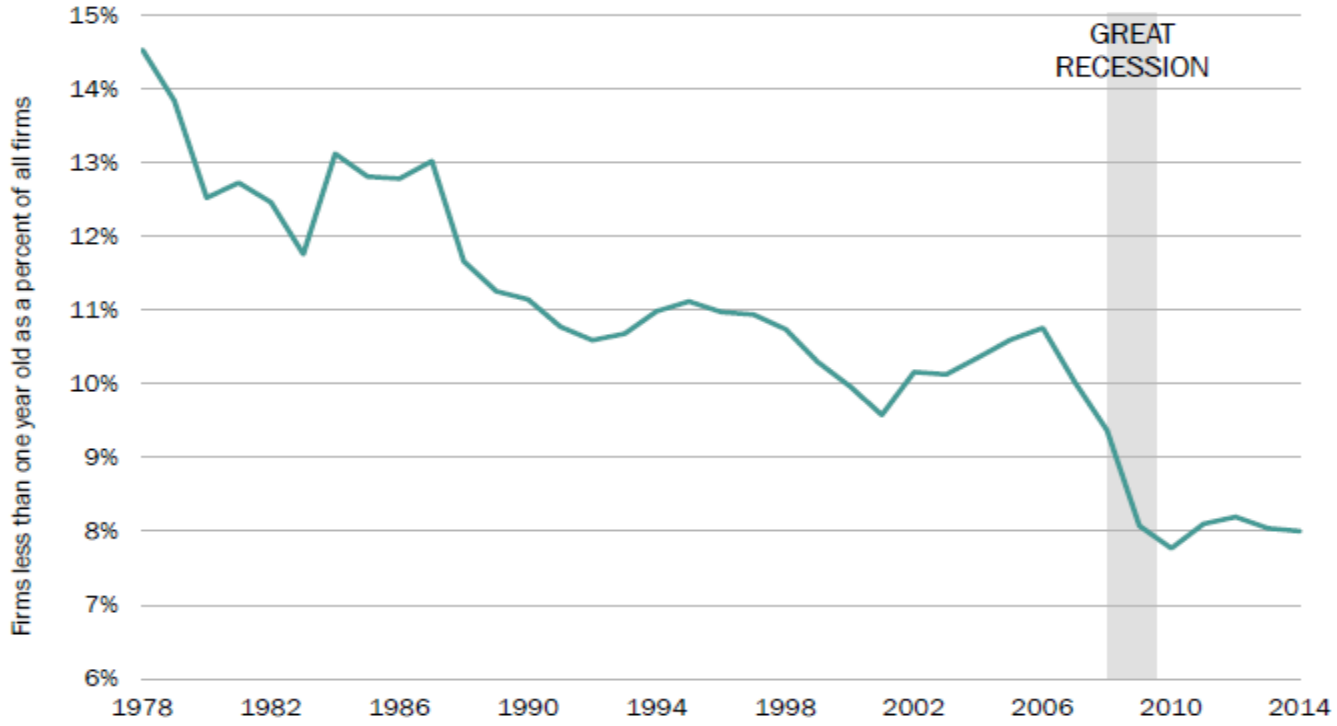
Business won't invest (and create jobs) when there is excess capacity – capacity Utilization below 80% suggests "excess capacity" exists – we've had 2 years of falling capacity utilization – my guess the culprit is the weak economy!



Another structural problem – new business formations are down significantly (from the Porter et al. study)

FIGURE 12: SLOWDOWN IN NEW BUSINESS FORMATION

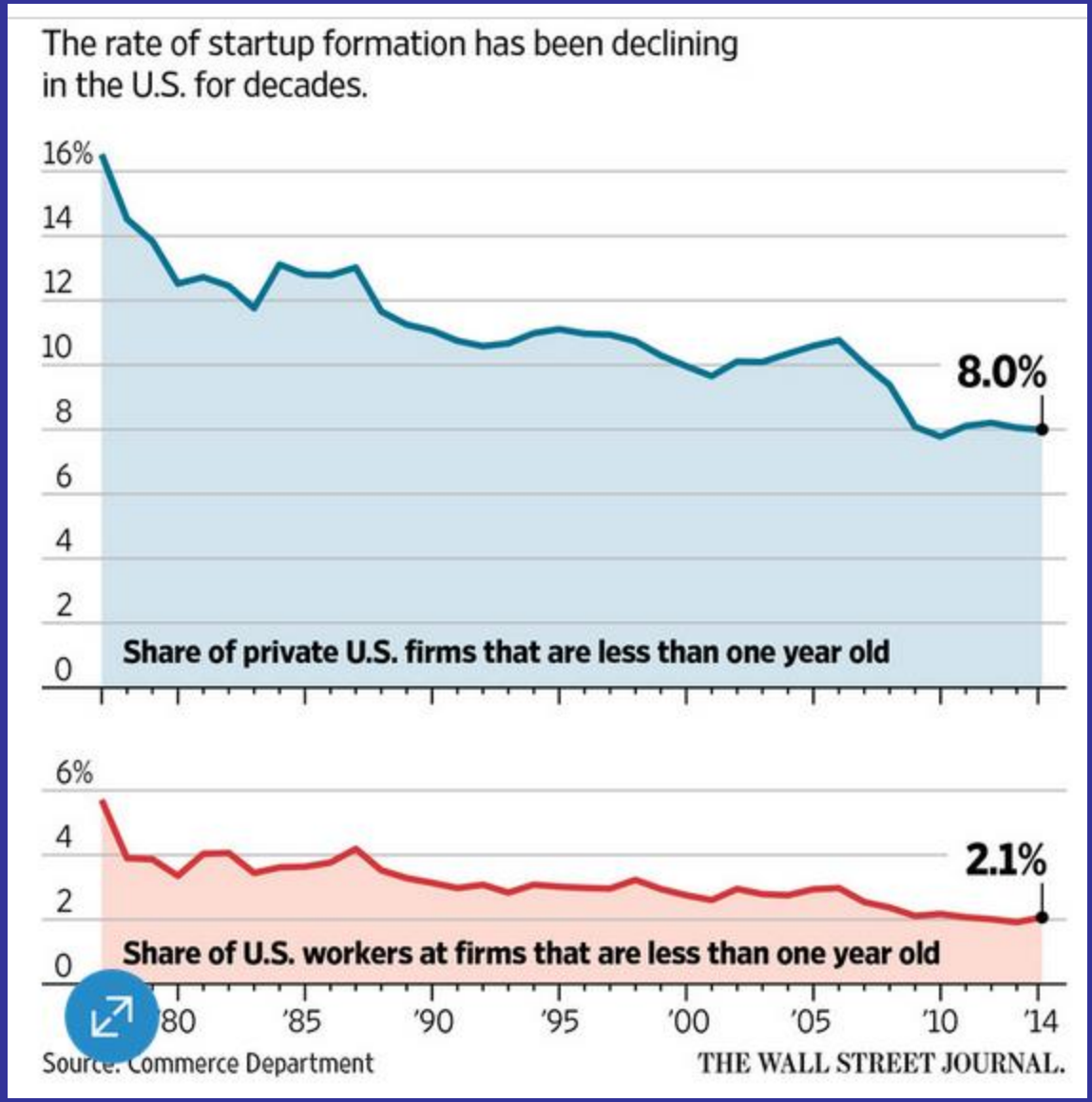
Start-ups as a portion of all U.S. firms, 1978–2014



Note: Shaded area indicates the recession of December 2007 to June 2009 as defined by the National Bureau of Economic Research.

Source: U.S. Census Bureau Business Dynamics Statistics. Chart adapted from Ian Hathaway and Robert E. Litan, "Declining Business Dynamism in the United States: A Look at States and Metros," Economic Studies at Brookings, May 2014.

Slowdown in entrepreneurship is one reason economy remains mired in slow growth mode!



WSJ (http://www.wsj.com/articles/sputtering-startups-weigh-on-u-s-economic-growth-1477235874)

What happens when innovation is missing!

Dismal productivity growth - - worst Performance for US economy since the 1980's when we experienced back to back recessions.

(PS – I understand that productivity measurement is a problem as new products/services quality is difficult to measure so maybe we are underestimating real productivity?)

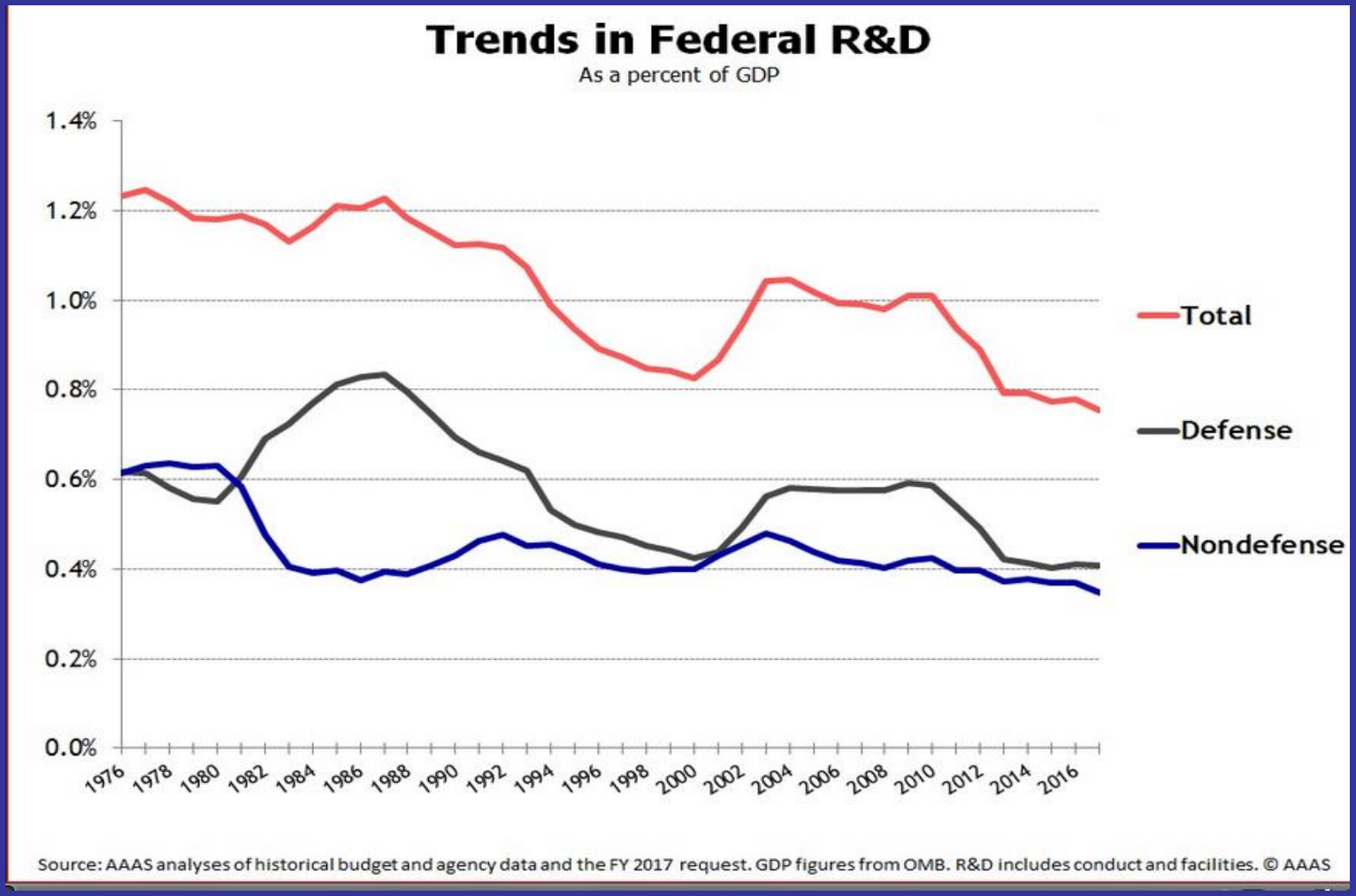
Source: WSJ (http://www.wsj.com/articles/u-s-productivity-dropped-at-0-5-pace-in-the-second-quarter-1470746092)

Waning productivity is major cause of our economic problems. Weakening trend over past 60 years needs to change if wages/standard of living are to improve. According to recent study by Porter et al., competitiveness is key. Solution is infrastructure reform, tax reform, and immigration reform. Political paralysis keeps us from implementing the right solutions according to Porter et al.

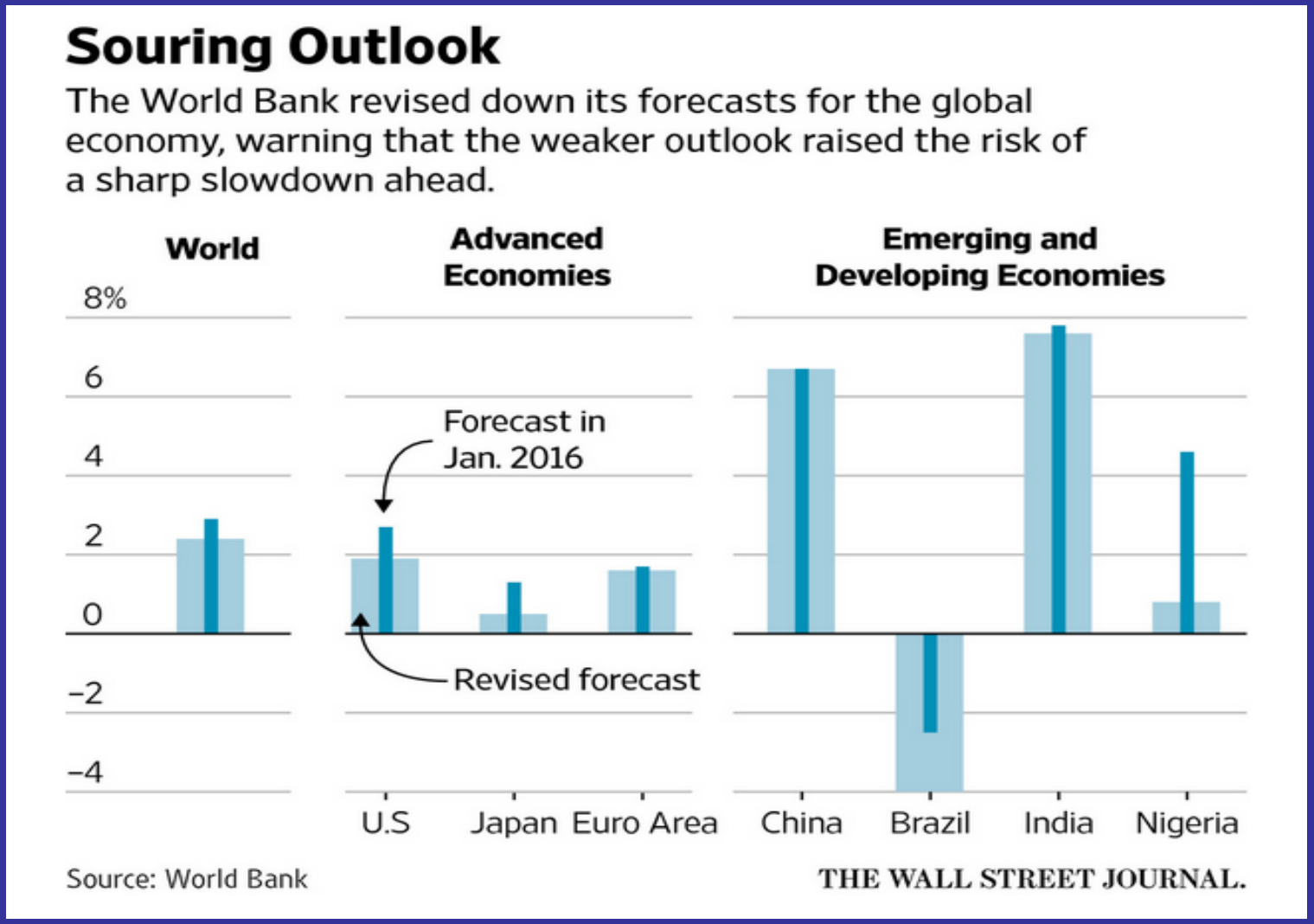
(http://finance.yahoo.com/news/us-competitiveness-project-harvard-business-school-hbs-michael-porter-030021739.html)

Falling R&D - - Not a good trend!

Currently, Federal R&D is 0.78% of GDP – non defense spending is .36%
Federal government funds basic research – which is critical to development of new technology and innovation in science and engineering - critical to economic growth, job growth, and productivity growth.



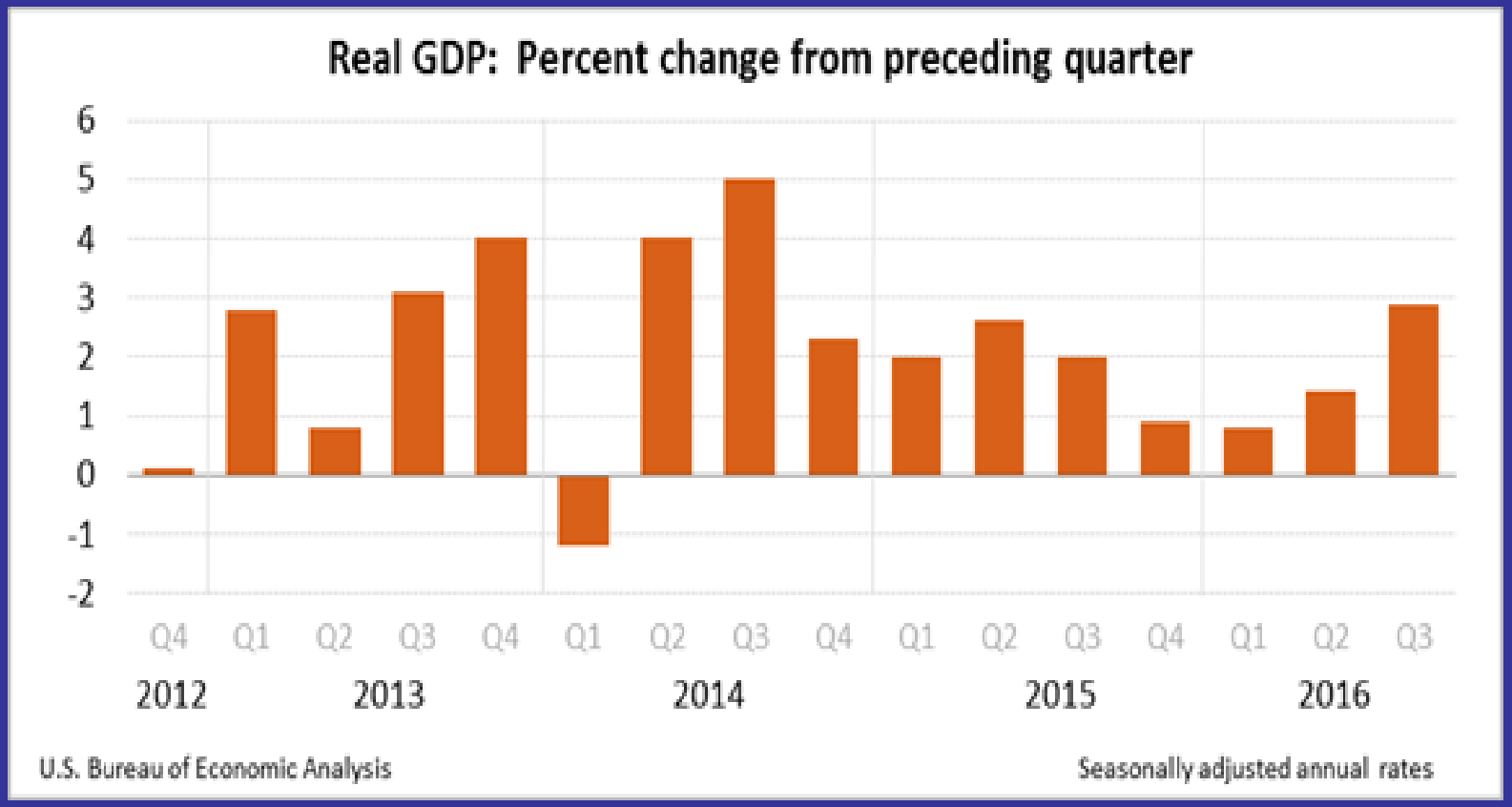
World Bank downgrades growth (again) in 2016 to 2.4% as problems in developed and developing world mount



Source: WSJ (http://www.wsj.com/articles/world-bank-cuts-global-growth-outlook-1465329662)

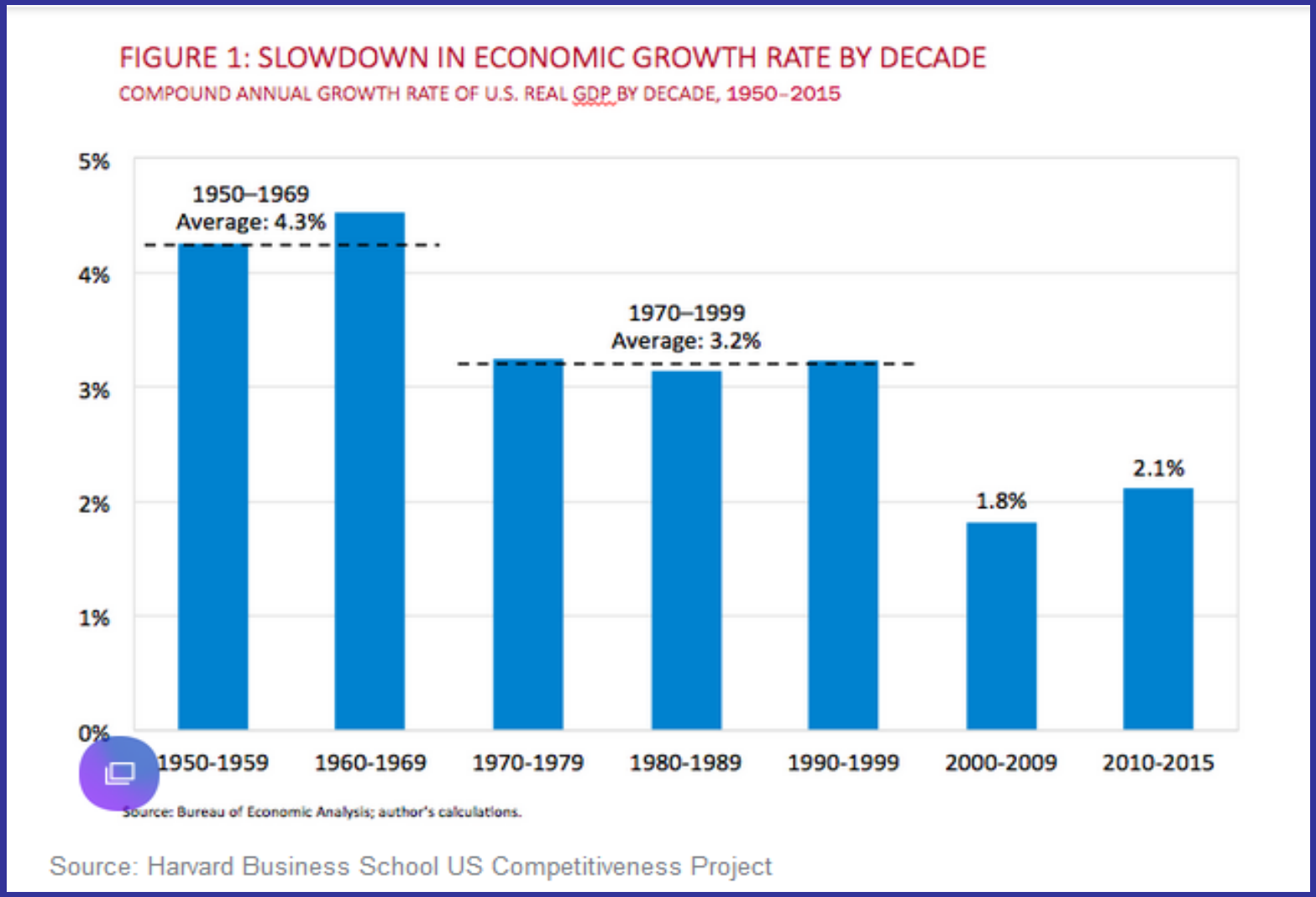
U.S. 3rd Qtr 2016 Economic growth nice surprise 2.9% - but since last September, the economy has averaged only meagre growth!

(1) Slowing world economy (weaker China , European, and South American growth)
(2) Stronger dollar will reduce exports and increase imports – negative impact on manufacturing jobs which is key to income growth in USA
(3) Political stalemate/weak leadership, terrorism, currency wars, growing national debt, …
(4) Weak income growth and continuing high "real unemployment"



Source: BEA (http://www.bea.gov/newsreleases/national/gdp/gdp_glance.htm)

Weak growth means weak incomes and weak housing numbers in the future unless we address our competitiveness issues.



Source: Harvard Business School US Competitiveness Project

(http://finance.yahoo.com/news/us-competitiveness-project-harvard-business-school-hbs-michael-porter-030021739.html)

Here are a few slides on labor market conditions – problems persist, but there are solutions

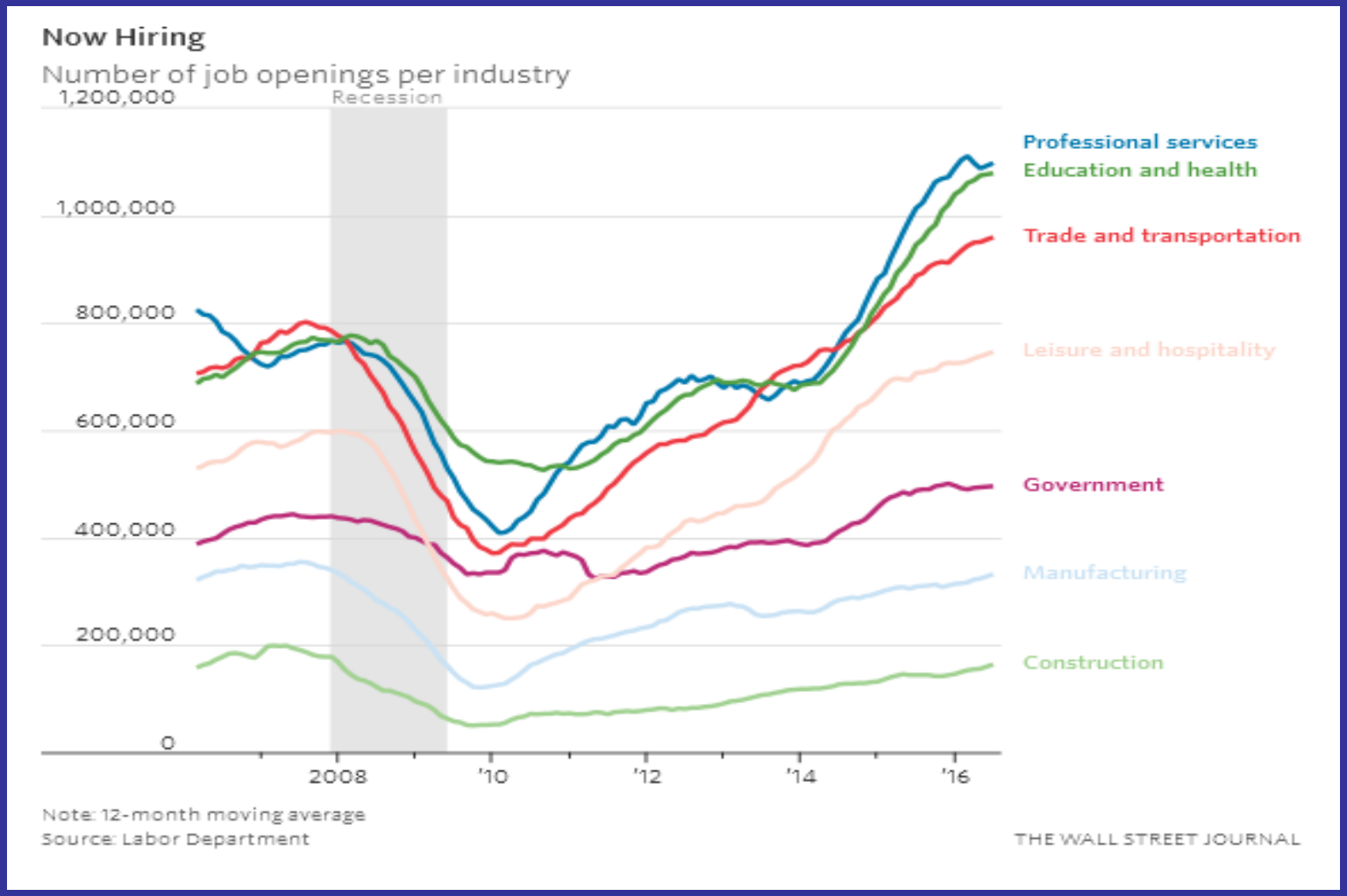
Not a good trend for the economy – employment to population ratio keeps decreasing.
Too much welfare, plus many people don't have the required job skills?

(http://www.wsj.com/articles/the-idle-army-americas-unworking-men-1472769641)

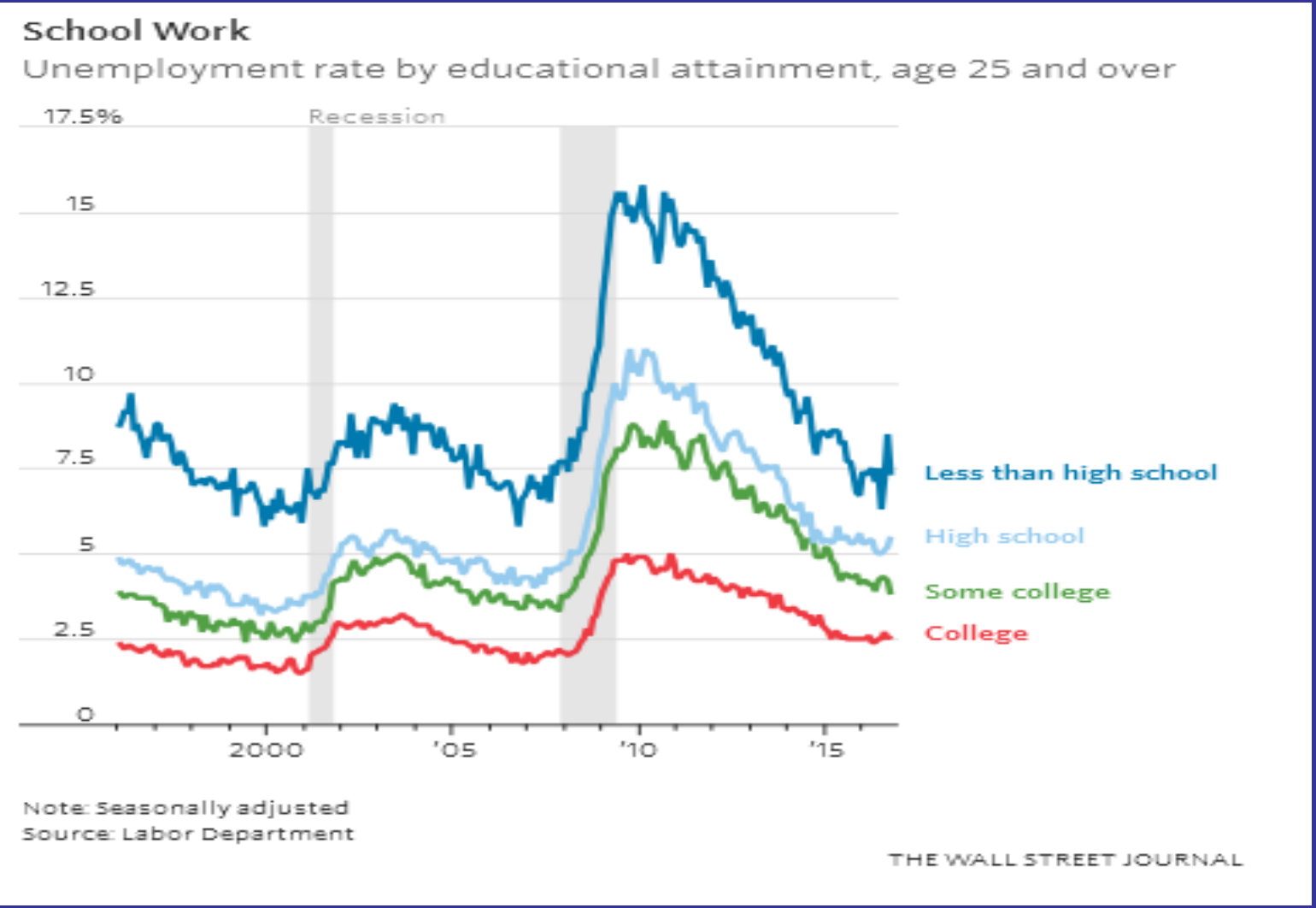
Here's the problem – there are lots of jobs, but too many job seekers don't have the required skills!

(http://blogs.wsj.com/economics/2016/09/07/a-new-record-for-job-openings-deepens-mystery-over-lack-of-hiring/)

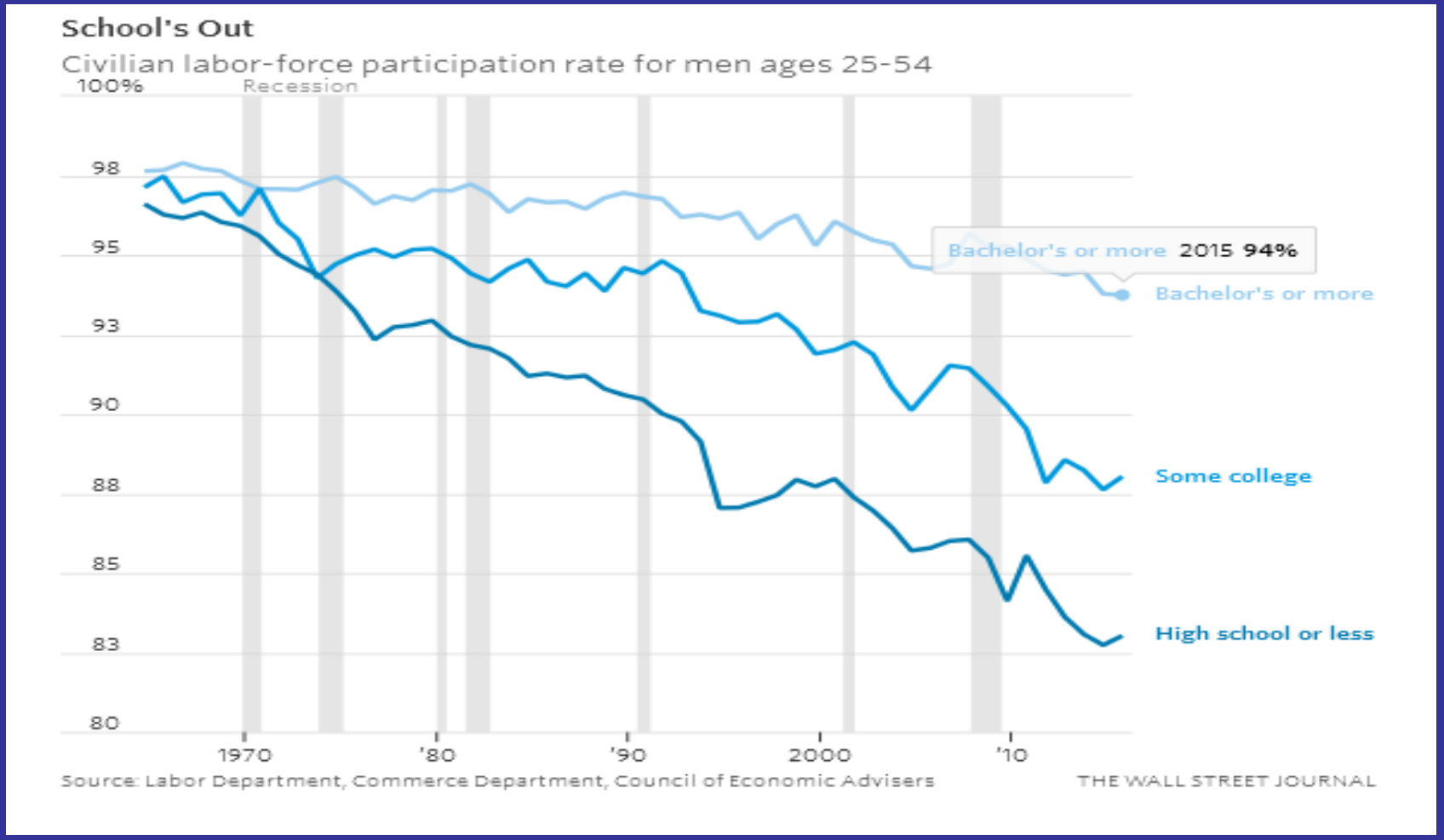
Here's where the jobs are – but lack of skills means many of these positions go unfilled!



Education will help keep you out of the unemployment line



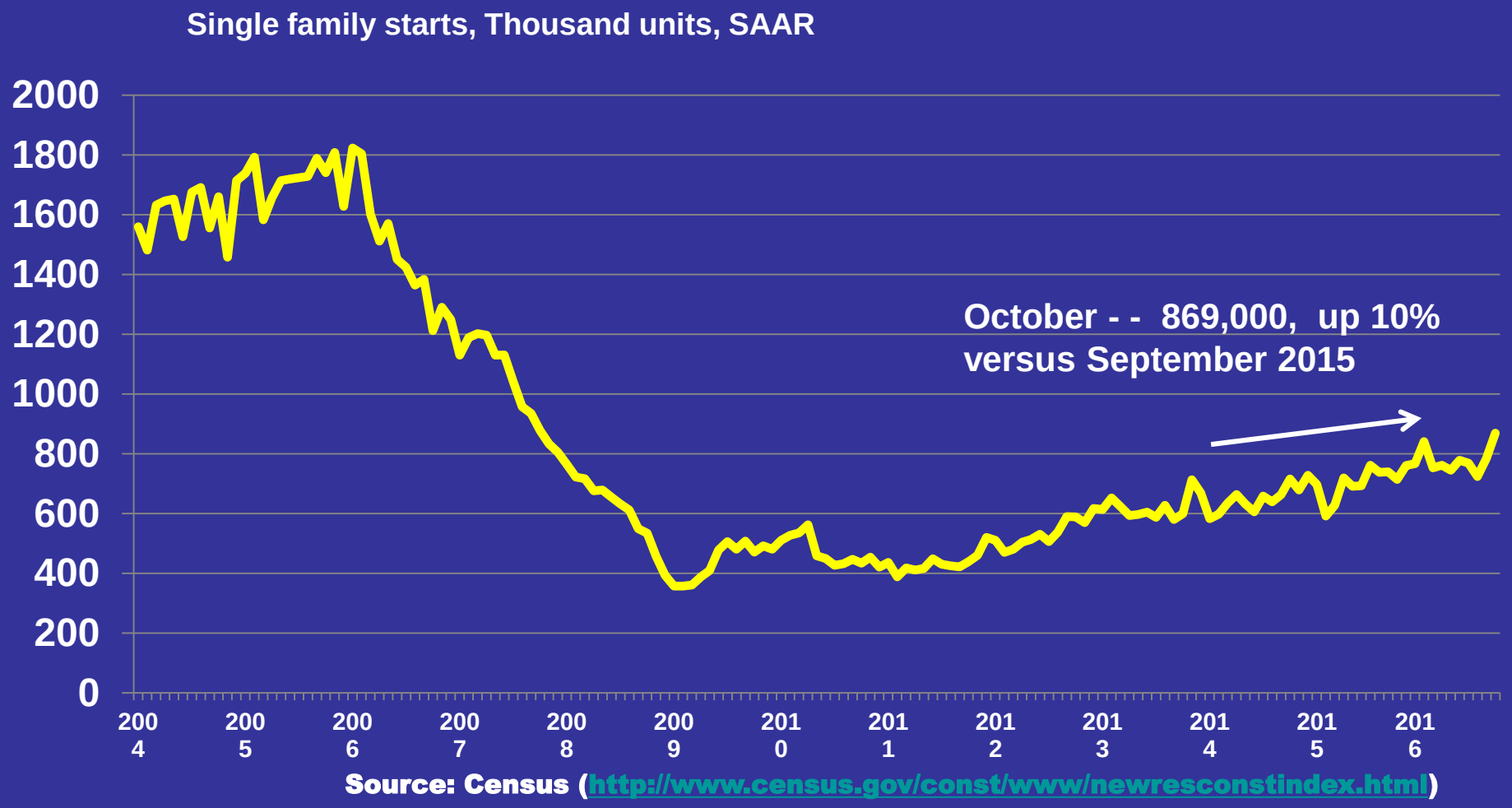
Getting an education will get you back into the labor force



Housing comments

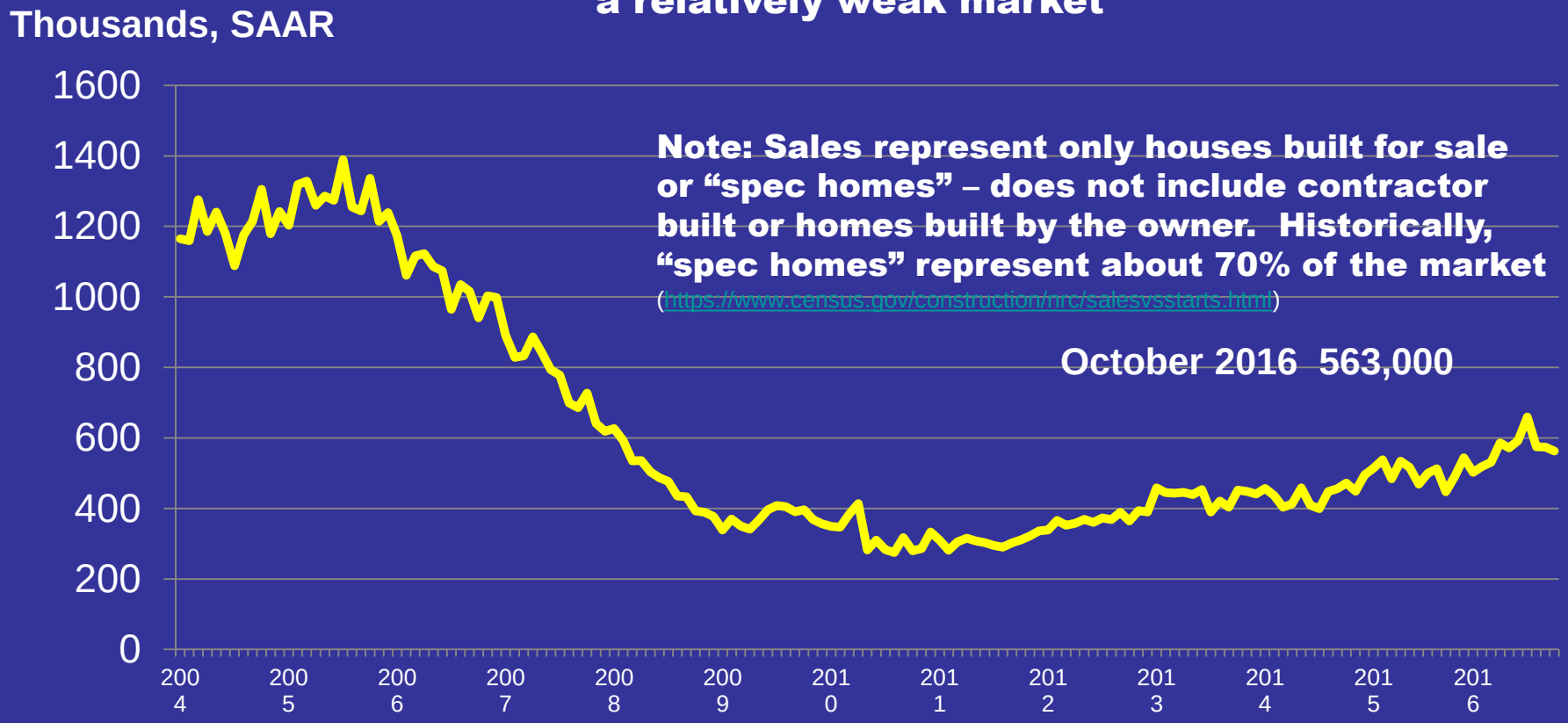
Starts are inching forward – But, ***low interest rates can't fix housing!***

This is basically a two tiered market – healthy upper end versus weak entry level housing - not sustainable.



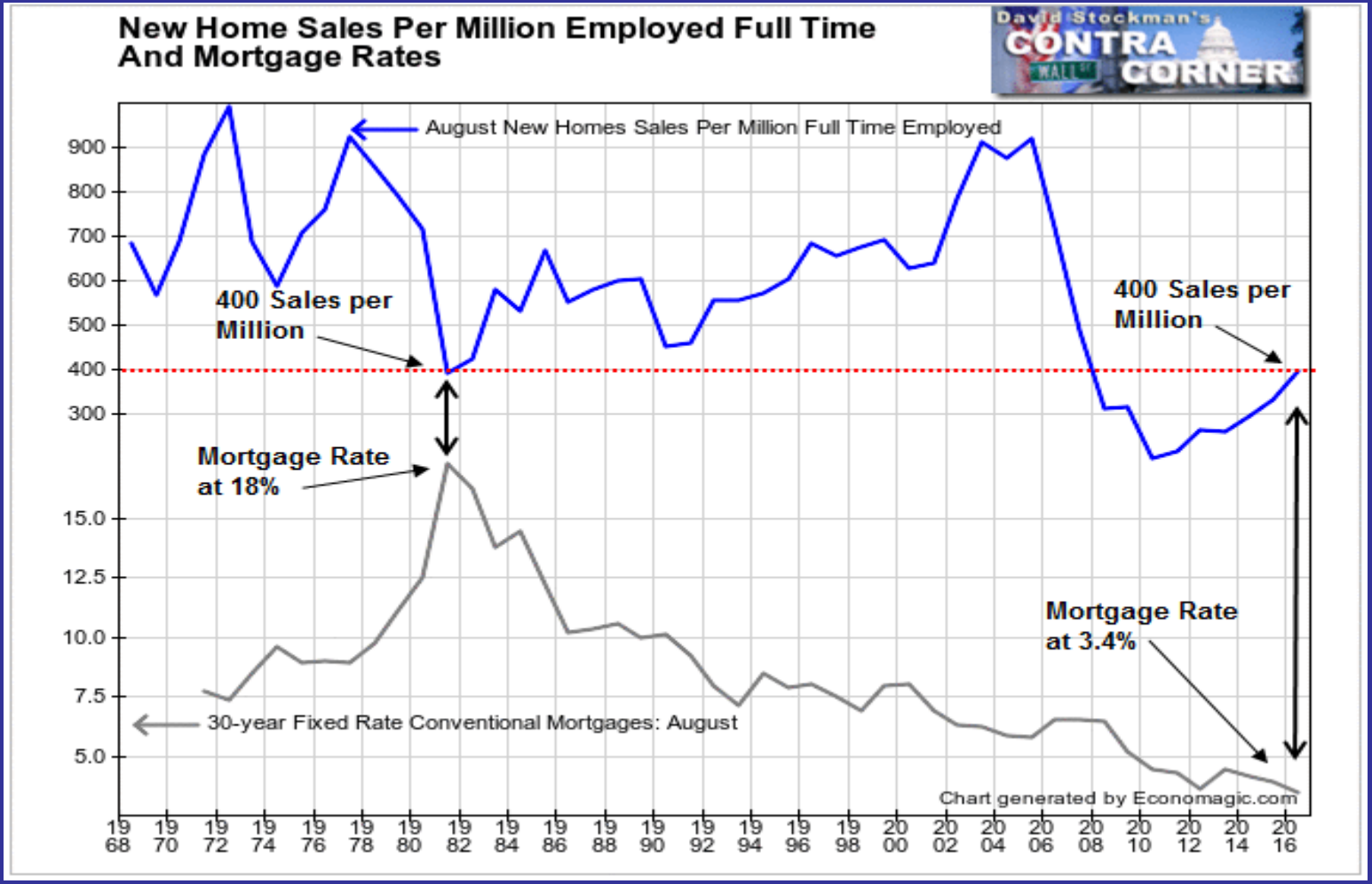
New Single Family Home sales are the key statistic to watch for wood products demand – sales drive housing starts – this drives demand for wood products!

up 18% versus October 2015
OK. We're making progress, but still a relatively weak market

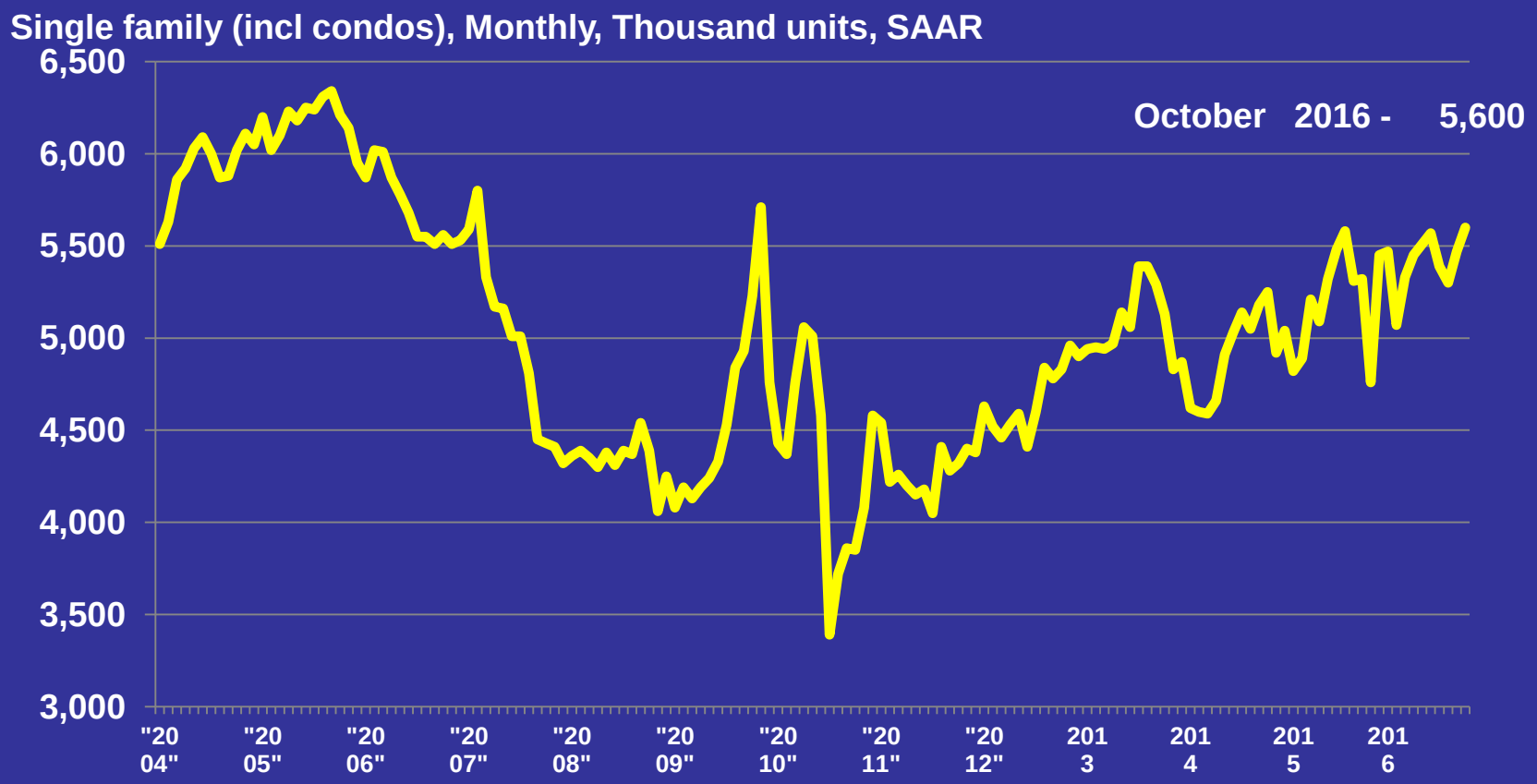


Source: Census (http://www.census.gov/const/www/newressalesindex.html)

Interesting chart showing new home sales versus population – despite lowest mortgage rates in history, today's new home sales per million are no better than back in 1980 when mortgage rates were almost 20%. Tells me that low mortgage rates are not the answer – people need good jobs and a belief in their future – today, both are in jeopardy!

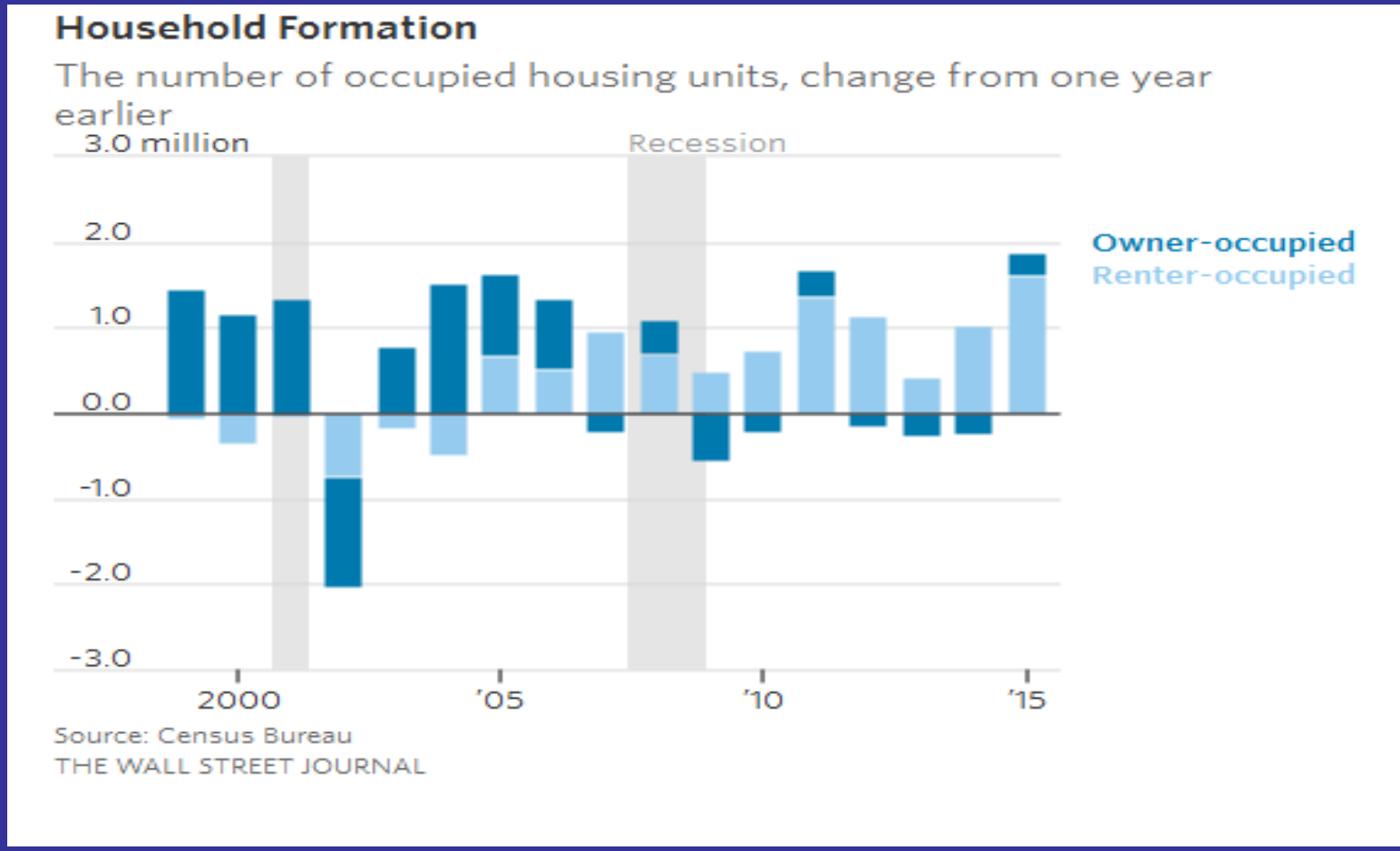


Resale market continues to improve - however, tight supply (which drives prices), currently at 4.3 months, remains a problem. Healthy market is about 6 months supply. ***Median prices are up 6.0%, annual basis - 54th consecutive monthly increase.***



Source: NAR (http://www.realtor.org/news-releases/2015/06/existing-home-sales-bounce-back-strongly-in-may-as-first-time-buyers-return)

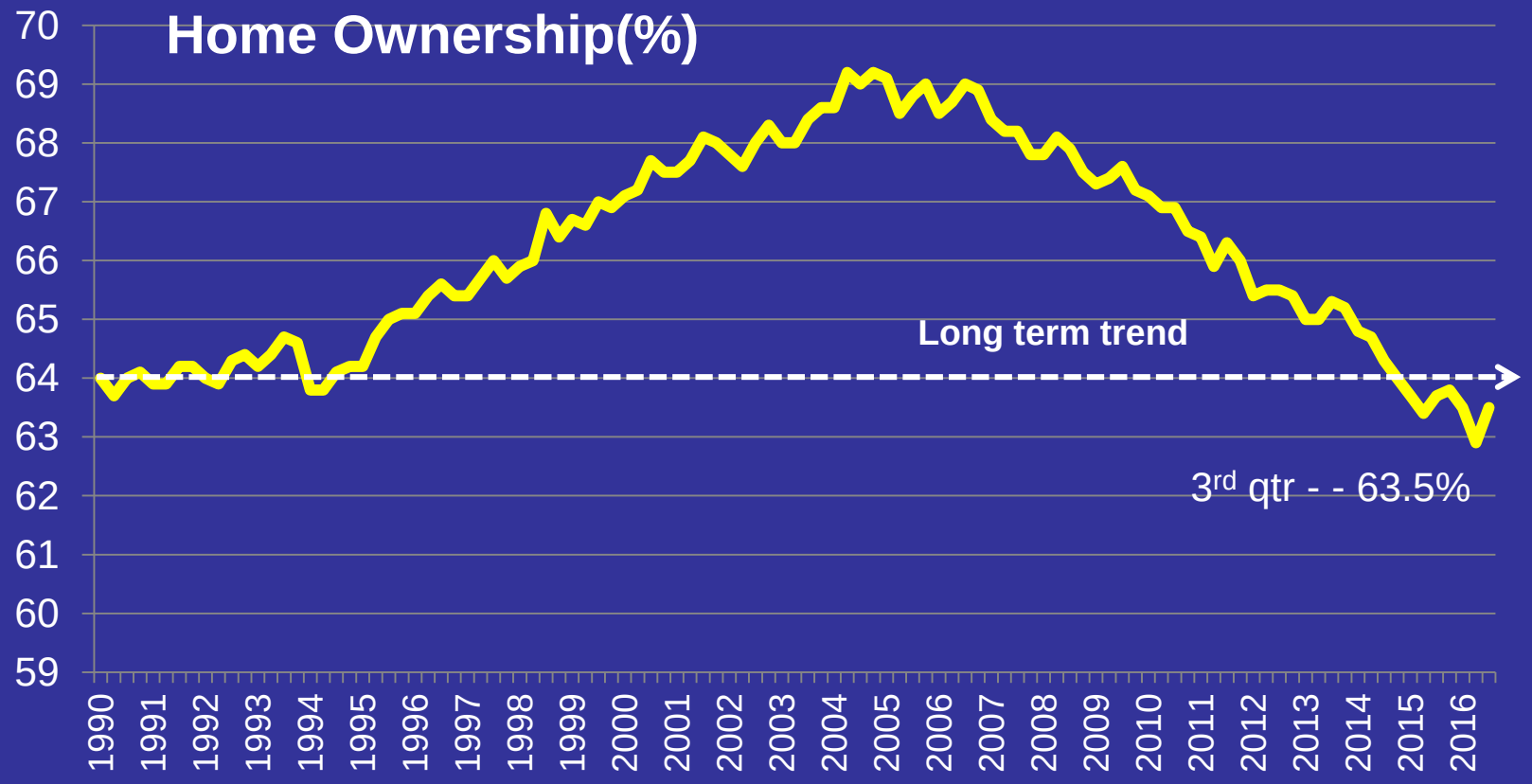
Household formations (HH) are starting to pick up, but since 2007, the bulk of new HH are renting!



Household formations and shift to renting - - Falling Homeownership rate for millenial's - used to be 43% - now it is 33% - young people are renting

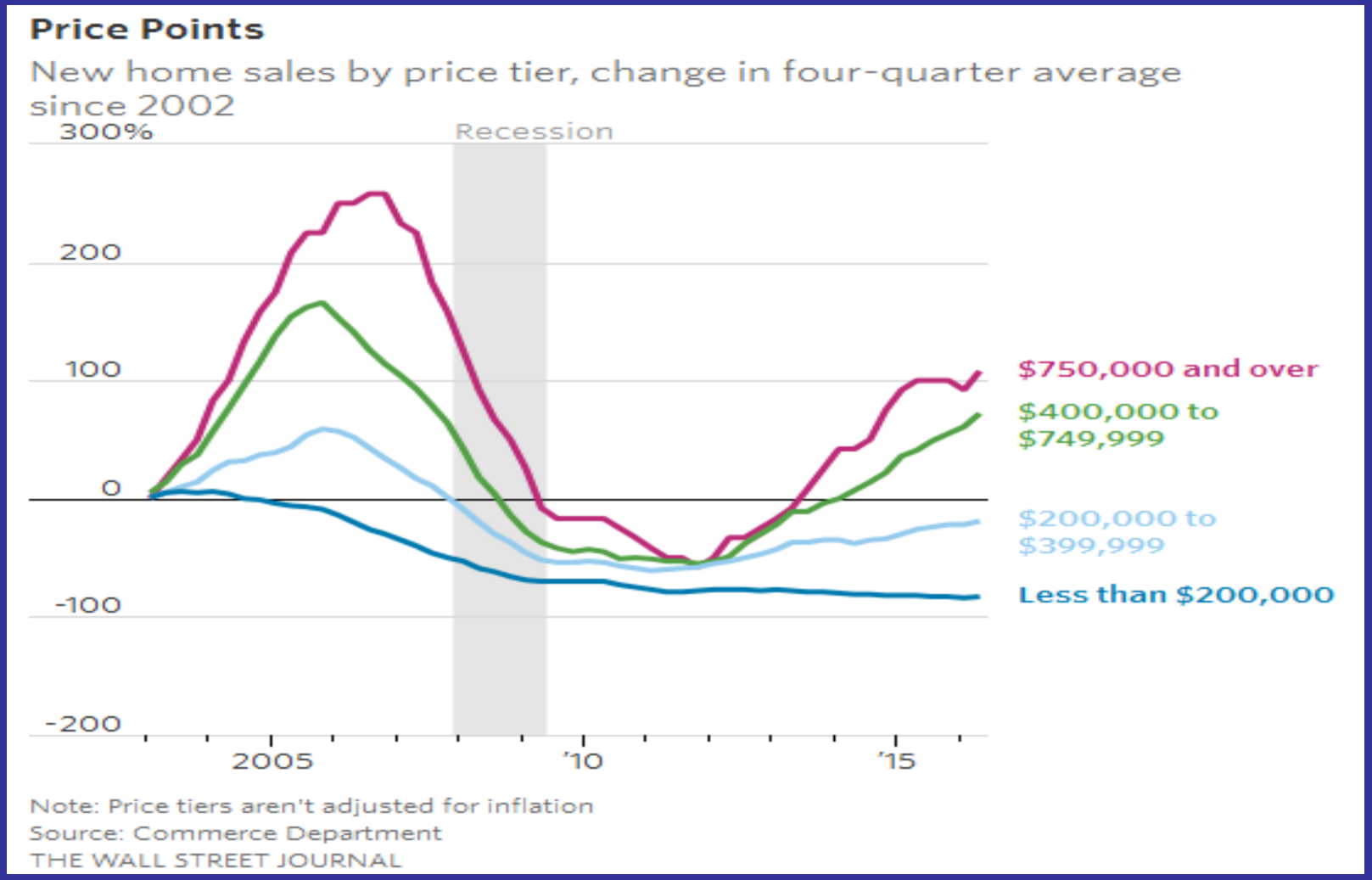
Recent study shows that people with college degree takes 5 years to save enough for down payment for starter home (with student debt – 10 years), No college – 16 years (http://www.wsj.com/articles/homeownership-elusive-for-young-adults-without-college-degrees-1463909402)

Homeownership rate lowest in 50 years

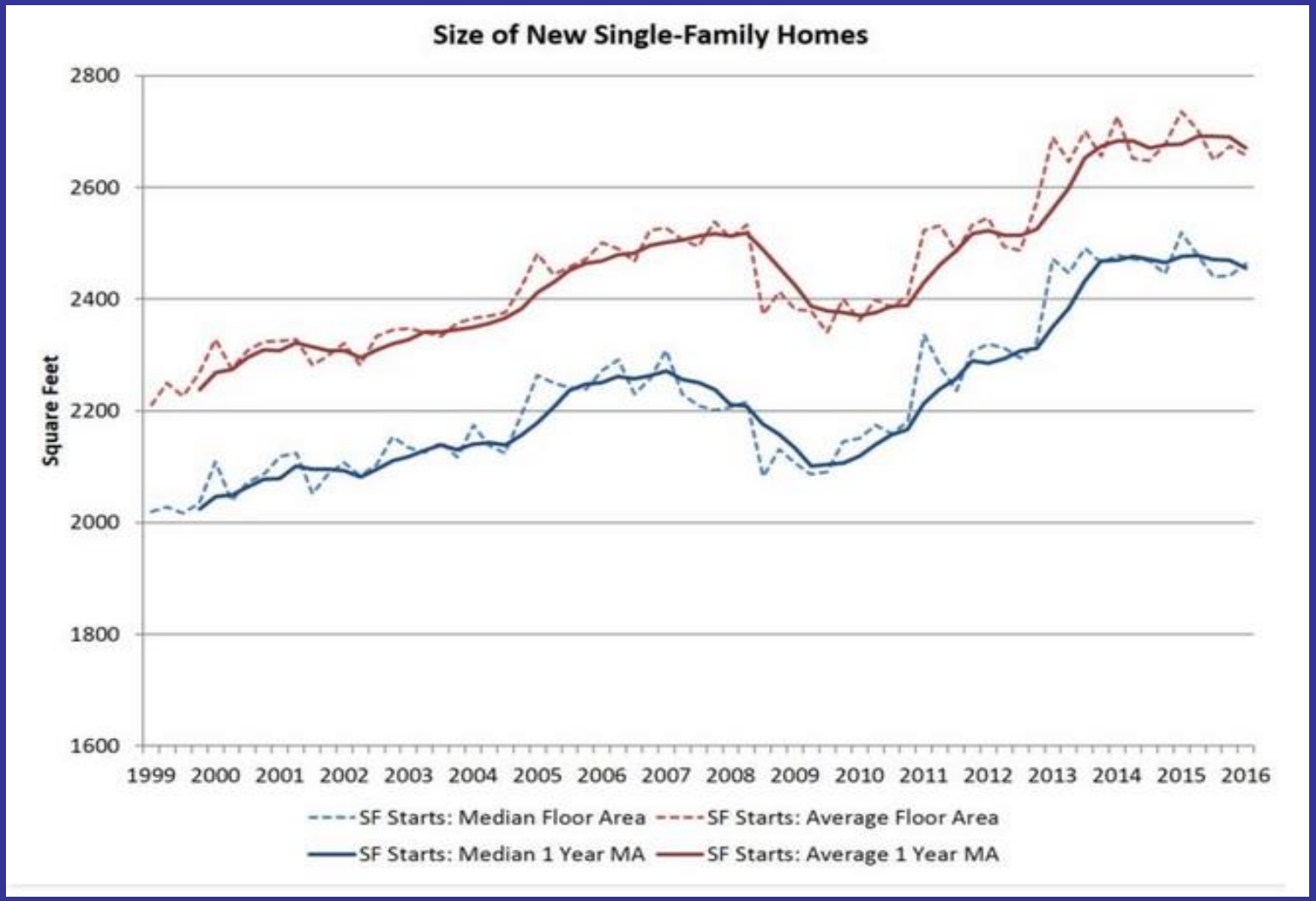


Source: Census (https://www.census.gov/housing/hvs/data/q413ind.html)

The supply of new homes is only 4.3 months – 6 months is considered healthy. The median price in July was $295,000 – but the chart below shows this is heavily skewed to larger homes. 1st time buyers are missing so builders are building larger, more expensive homes

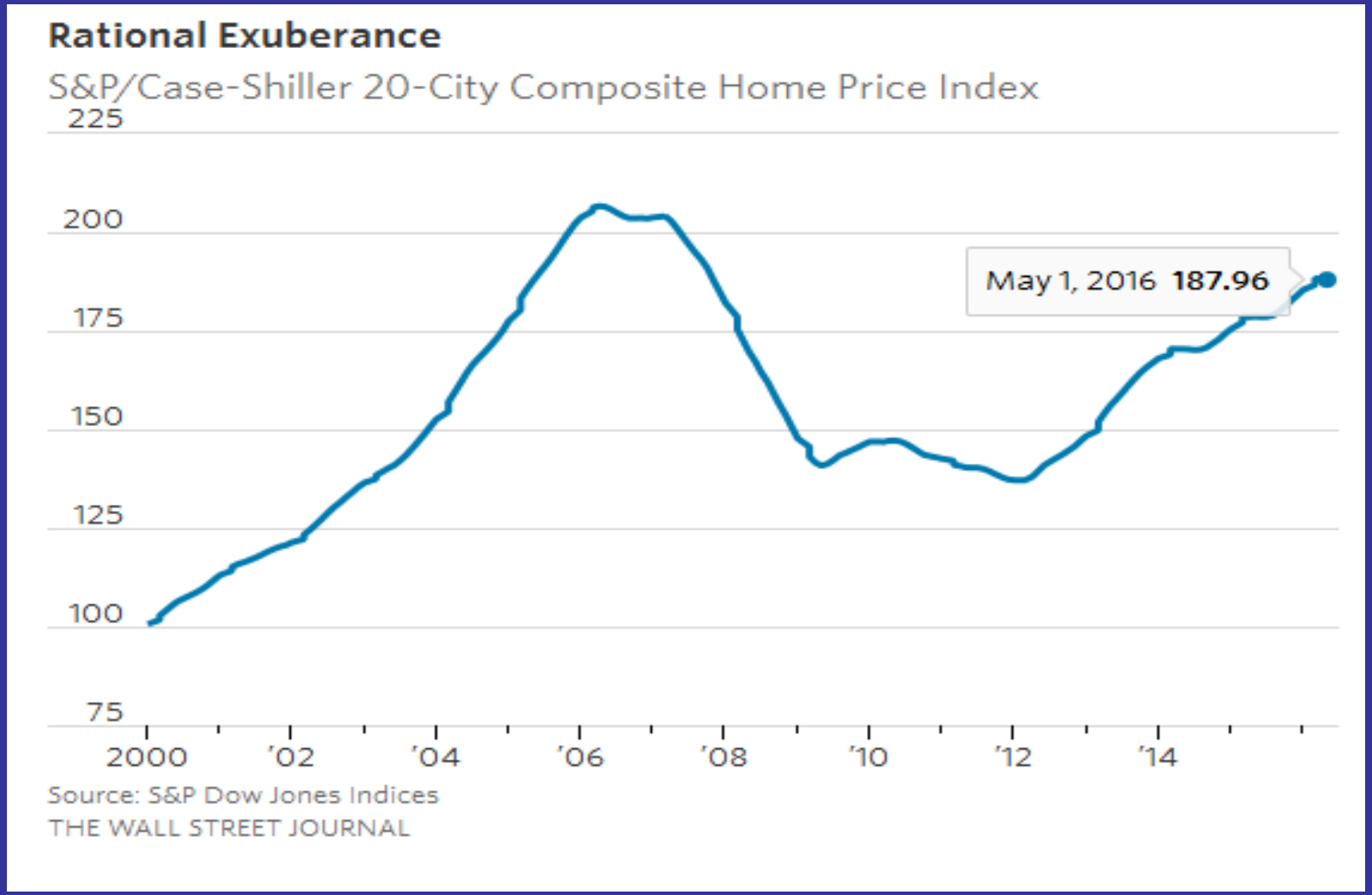


Builders are building bigger homes in response to weaker demand from millennials who buy starter homes



(http://eyeonhousing.org/2016/05/flat-trends-continue-for-new-single-family-home-size/http://eyeonhousing.org/2016/05/flat-trends-continue-for-new-single-family-home-size/)

Existing home prices almost back to pre recession levels good for existing homeowners, but a deterrent to millennial's and other potential buyers



Rental demand versus single family housing ---

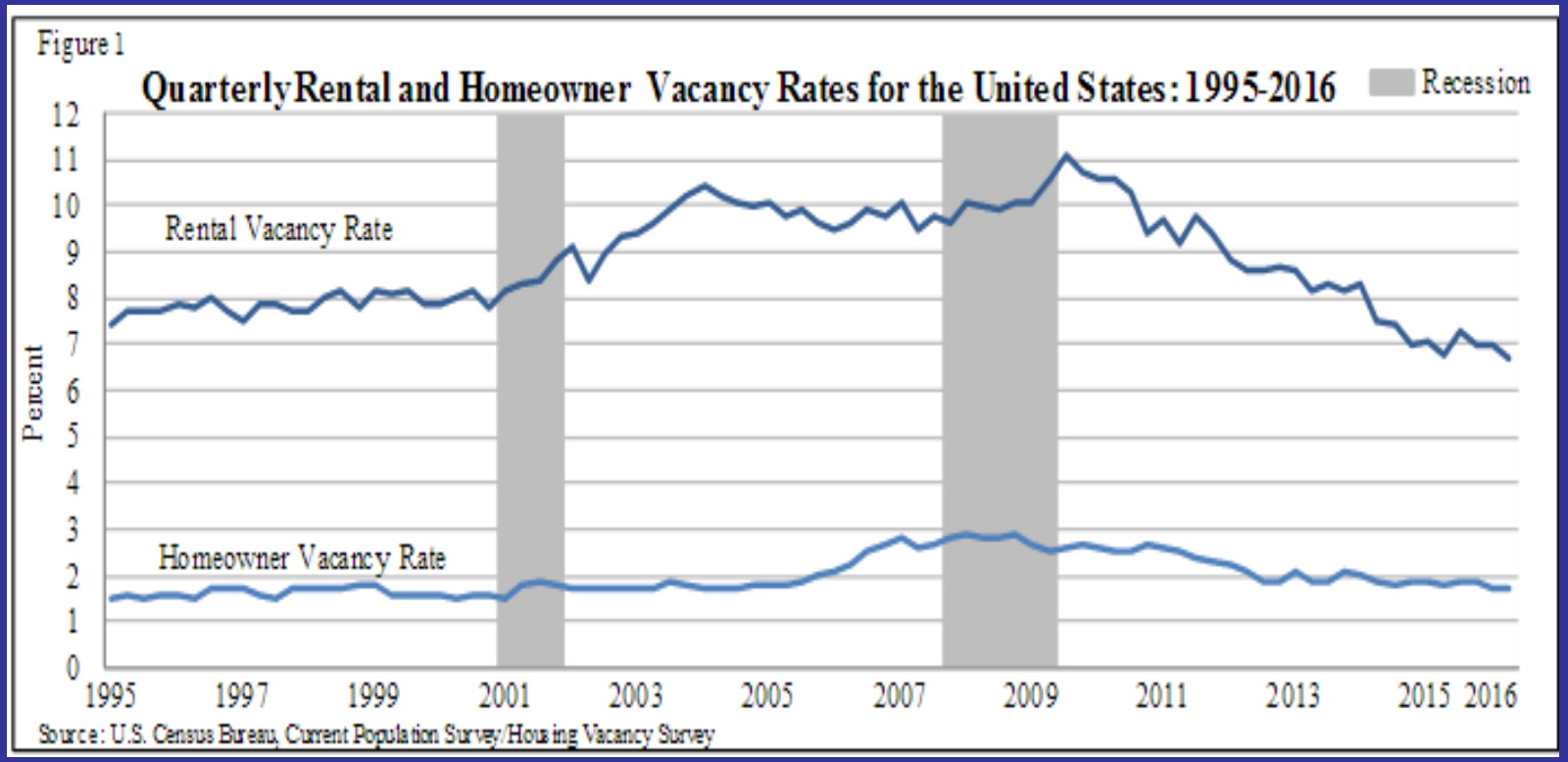
Rental demand will continue to increase for years – a recent study by the Urban Institute suggests it may continue for another decade or two
(http://www.wsj.com/articles/new-housing-crisis-looms-as-fewer-renters-can-afford-to-own-1433698639)

Why - - demographics; growing minority population; student debt; weak income growth; …. E.g., Minorities (nonwhite) will make up 75% of net household growth over the next 10 years, and 85% during 2020 - 2030. They are less likely to own homes (lower incomes is main reason) so home ownership continues to fall toward 60% by 2030. During this time, rental demand will increase dramatically. Although this is just one study, it provides food for thought. One potential question with the study, however, is other studies show that although immigrants, for example, rent initially, but, over time they purchase homes at a rate equal to or higher than native born Americans. Why – people come to the U.S. to improve their quality of life, and for most, this means homeownership. This suggests that the U.S. has to find solutions to immigration issues like "illegal immigrants" while encouraging legal immigration. This country was founded by immigrants seeking a better life, and they are key to our future. And, incomes for all minorities has to improve if home ownership is to return to "good old days"
(http://www.engineeredwood.org/Data/sites/3/documents/EngWoodJournal/EWJ_Spring2010.pdf)

Anyway, this has potential implications for home ownership; single family construction; and demand for wood products – lots of variables and scenarios.

Rental vacancy rates lowest in 20 years

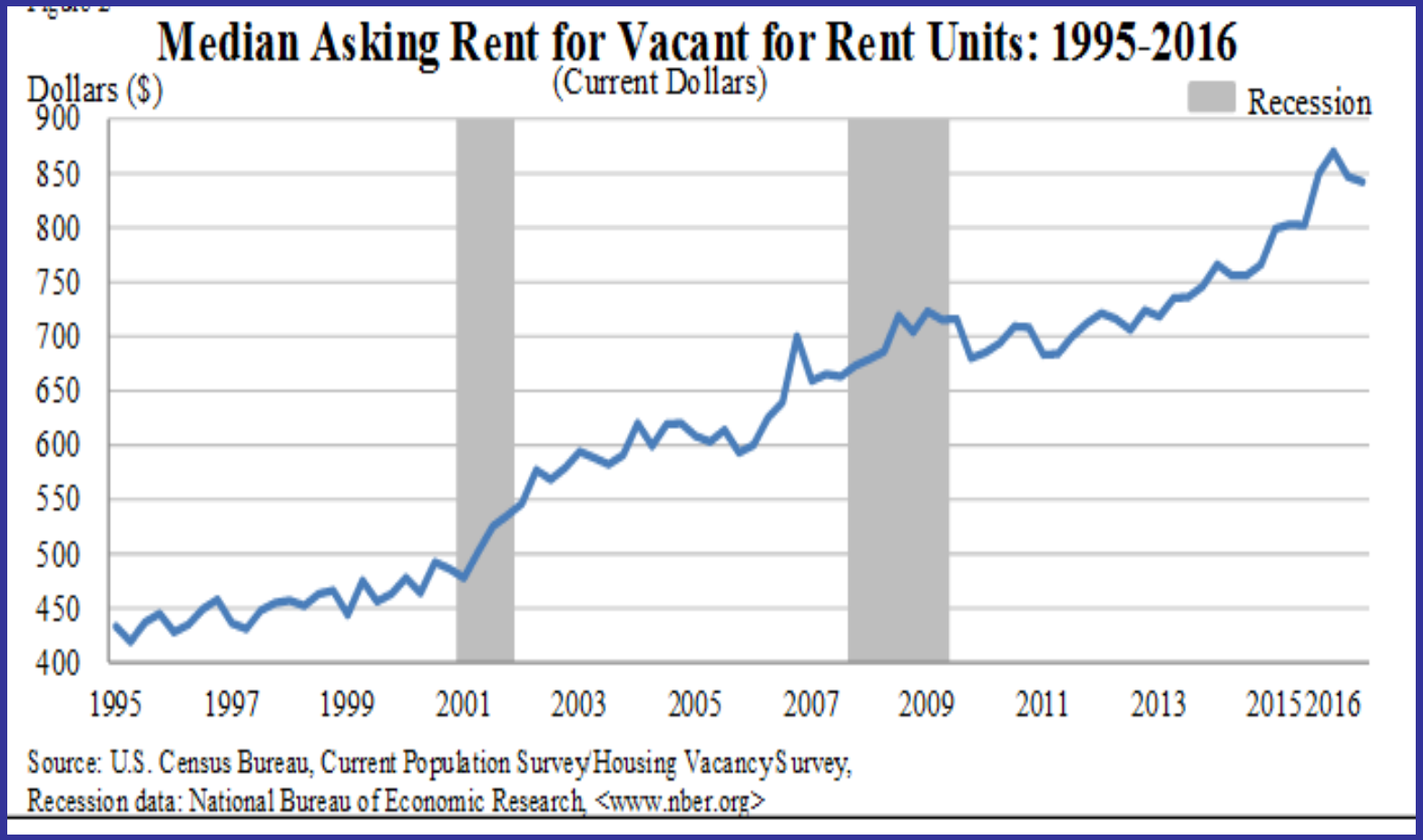
Falling rental vacancy rates will drive rental prices higher and this will drive multi family construction – Economics 101 – *if I were a builder, I would focus on rental construction*



Source; Census (http://www.census.gov/housing/hvs/files/currenthvspress.pdf)

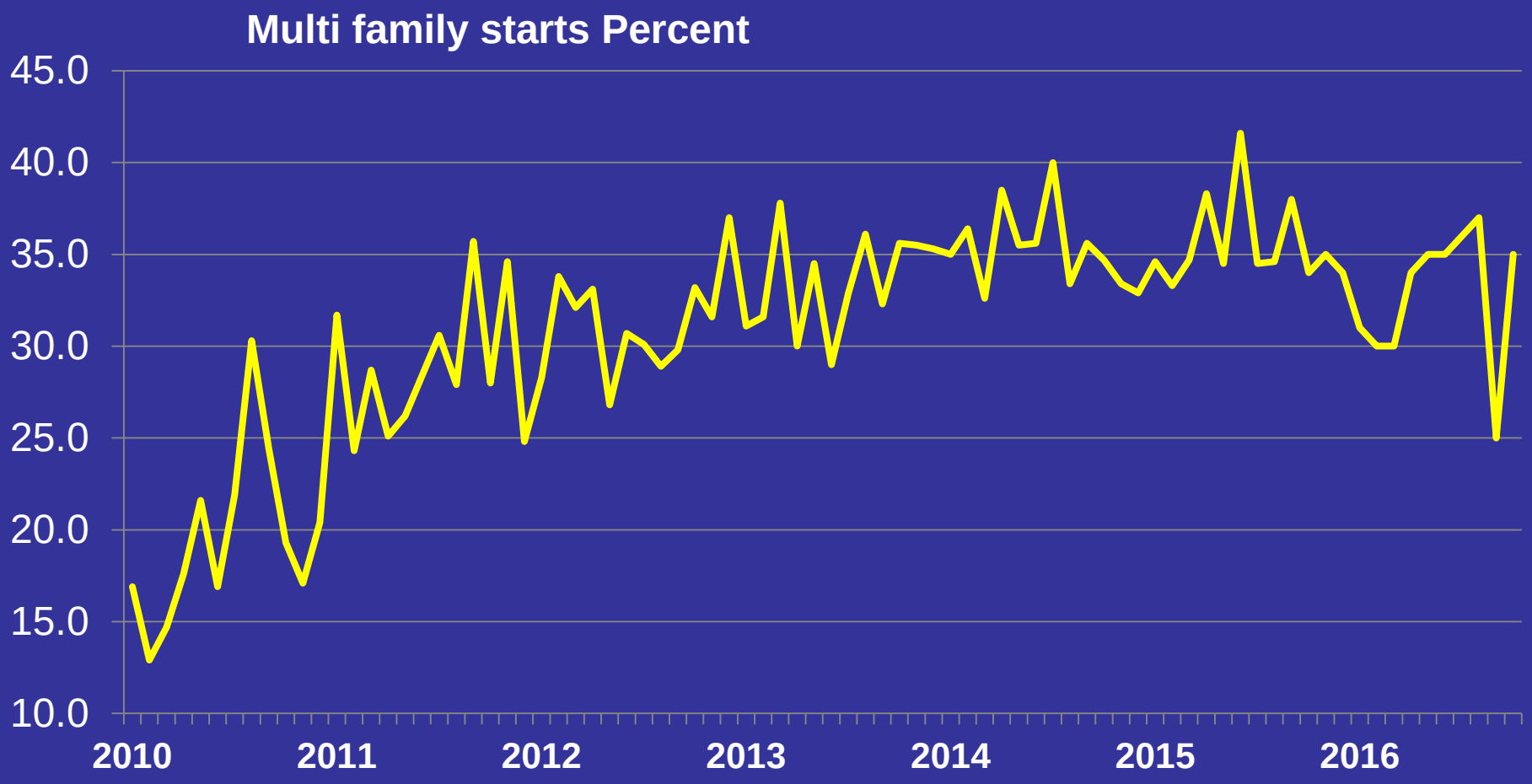
Increasing rents are slowing housing starts - -

more difficult for renters to save for down payment for house purchase



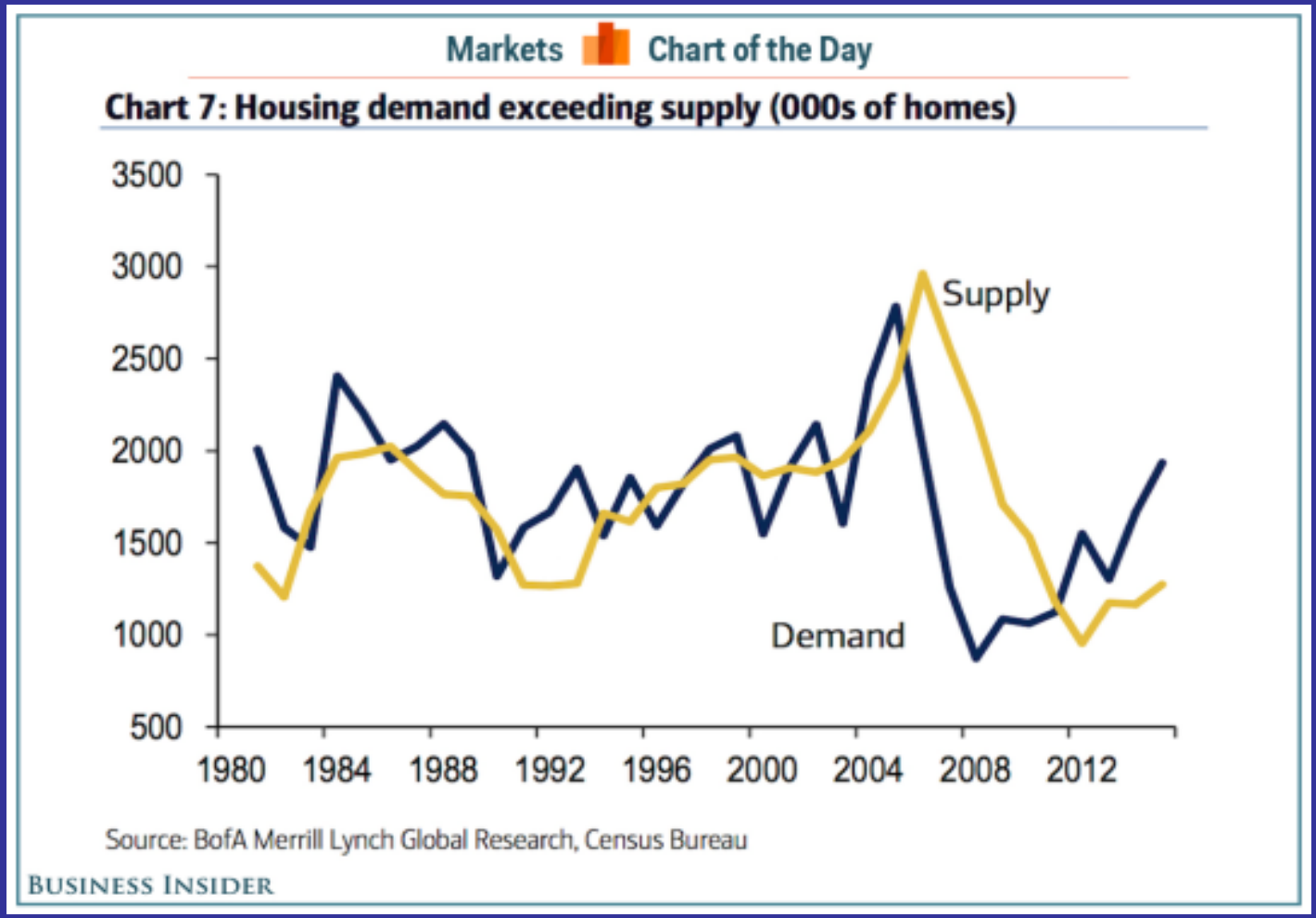
Source: Census : (http://www.census.gov/housing/hvs/files/currenthvspress.pdf)

Multi family share of housing starts – upward trend expected to continue for some time. Also, since the housing crash in 2008, single family rentals have now reached 13% of overall housing stock, up from 9% in 2005 (http://blogs.wsj.com/economics/2015/07/20/signs-of-overheating-in-the-single-family-rental-market/)



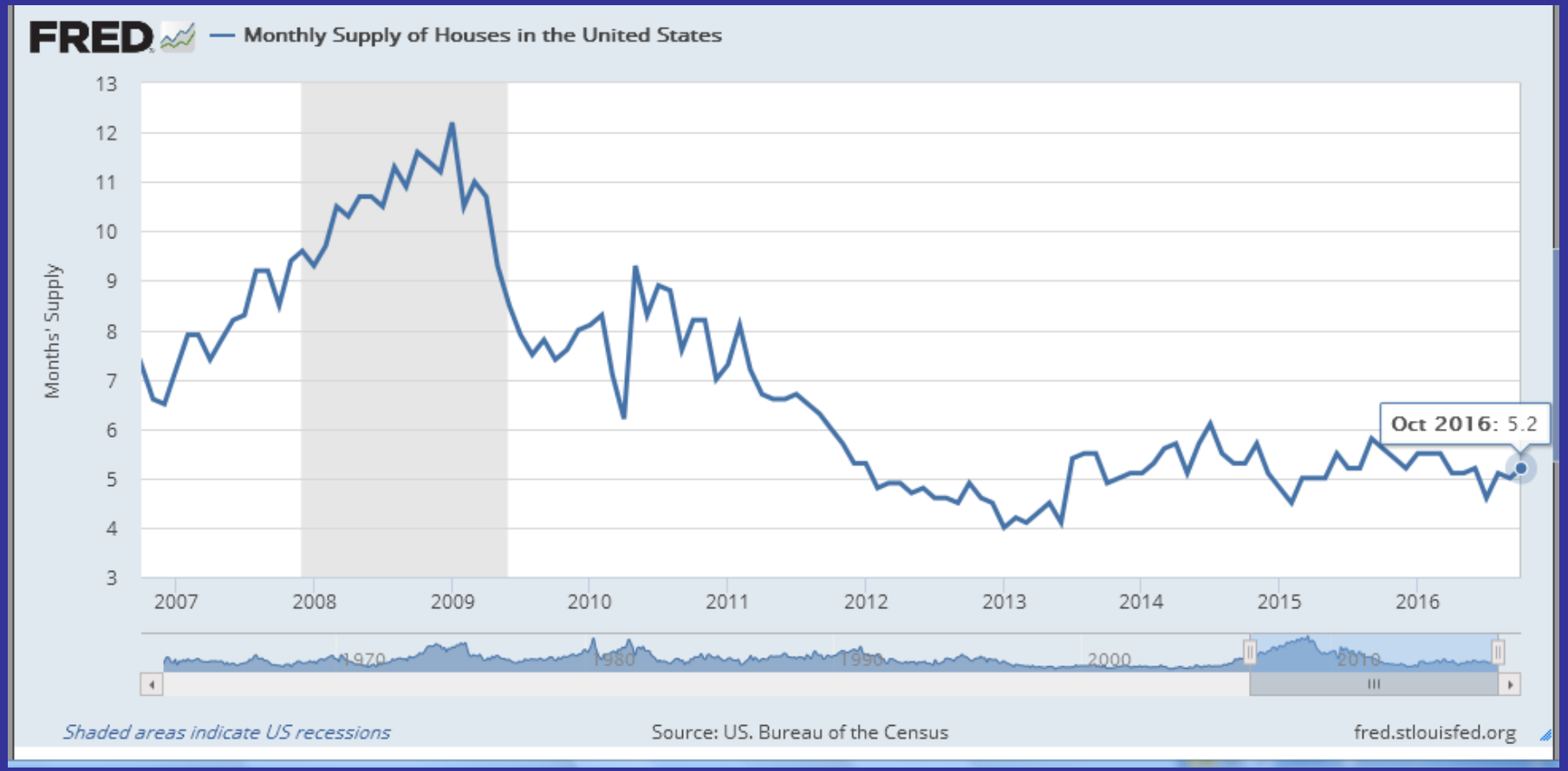
Source: Census

Tight supply drives up prices – existing homes at 4.7 months supply – normal supply is 6 months



Low new home inventory drives prices higher and out of reach to most 1st time buyers

But, builders can't find enough carpenters, masons, electricians, etc. So construction costs keep escalating = this exacerbates the inventory problem – also, land shortages in parts of the country drive costs higher!



(https://research.stlouisfed.org/fred2/series/MSACSR)

More News on the labor front

Employment situation - our biggest problem – stuck near 200,000, and many of these jobs are part time with little or no benefits – not conducive to driving housing demand higher - *need to encourage innovation and investment in future - that means less government*

Net change in non farm payrolls – monthly, thousands

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

Unemployment rate keeps coming down – but, nearly 7 million remain "underemployed" – working part time, but want full time jobs

There are about 16 million people either unemployed, underemployed, or stopped looking – **Key reason why wage increases are stagnant!

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

Labor force participation rate is shrinking – demographics is one reason – another reason – bloated welfare system – 130 million people on some form of welfare (food stamps, long term disability, housing allowances, Medicaid, …) - - we'll see skilled labor shortages increase over the next decade - we're already seeing construction related shortages with brick layers, masons, electricians, plumbers, etc.

Excellent article (http://finance.yahoo.com/news/should-i-go-to-a-trade-school-162413337.html#)

Some conclusions – housing continues to improve albeit very slowly and this will not change soon for the reasons listed below:

(1) Economy will continue to sputter -- 2016 growth expected to be about 2.0%

(2) Housing market not healthy - 1st time buyers (31% today) are below trend (45%) - household formations are improving, but more people will continue to rent

(3) Productivity a major problem for U.S. economy – real GDP driven by population (number of workers) and real GDP/worker or productivity. During past 7 years, productivity has grown 1.7% annually whereas the average over previous 17 years was 2.4%.

(4) "QE" not working – bulk of "printed money" hoarded by the banks to shore up capital positions – not being loaned out to the economy - GDP languishes - we need a new and more effective approach to our competitiveness problems!

(5) *Weak/no leadership from current administration and Congress,*
- our biggest problem – hopefully the new administration will fix our problems

(6) The fed will probably increase rates in December, finally. Low rates are not the solution to our weak economy.
Innovation, investment, tax reform, is the solution, but that will be challenging with $20 trillion (and counting) federal debt and 41% of the population on some form of welfare. Many business leaders have lost confidence in where the country is headed so they are not investing.

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