June 2017 Housing Commentary

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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/

June 2017
Housing Scorecard

	M/M		Y/Y	
Housing Starts	△	8.3%	△	2.1%
Single-Family Starts	△	6.3%	△	10.3%
Building Permits	△	7.4%	△	5.1%
Housing Completions	△	5.2%	△	8.1%
New Single-Family House Sales	△	0.8%	△	9.1%
Existing House Sales[1]	▽	1.8%	△	0.7%
Private Residential Construction Spending	▽	0.2%	△	9.2%
Single-Family Construction Spending	△	0.3%	△	9.0%

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

	June	May	June 2016
Total permits*	1,254,000	1,168,000	1,193,000
Single-family permits	811,000	779,000	743,000
Multi-family 2-4 unit permits	34,000	32,000	31,000
Multi-family ≥ 5 unit permits	409,000	357,000	419,000
Total starts	1,215,000	1,122,000	1,190,000
Single-family starts	849,000	799,000	770,000
Multi-family 2-4 unit starts**	7,000	12,000	18,000
Multi-family ≥ 5 unit starts	359,000	311,000	402,000
Total completions	1,203,000	1,144,000	1,113,000
Single-family completions	798,000	795,000	760,000
Multi-family 2-4 unit completions**	9,000	13,000	9,000
Multi-family ≥ 5 unit completions	396,000	336,000	344,000

* 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; 11/19/17

Housing Data

	June	May	June 2016
New single-family sales	610,000	605,000	559,000
Median price	$310,800	$324,300	$321,600
Existing sales[a]	5,520,000	5,620,000	5,570,000
Median price	$263,800	$252,000	$247,600
Private Residential Construction	$502.9 billion	$504.0 billion	$460.4 billion
SF construction	$261.3 billion	$260.6 billion	$239.8 billion
MF construction	$60.7 billion	$62.5 billion	$60.3 billion
Improvement construction[b]	$180.9 billion	$180.9 billion	$160.3 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; 07/24/17
U.S. Department of Commerce-Construction: www.census.gov/construction/nrs/pdf/newressales.pdf; 07/26/17
U.S. Department of Commerce-C30 Construction: www.census.gov/construction/c30/pdf/privsa.pdf; 08/01/17

Conclusions

Housing starts picked up a bit in June while the resale market remained flat. One problem is price. Prices are increasing faster than incomes and this, coupled with tighter loan requirements, is acting as a drag on demand. In addition, builders are having problems with construction labor shortages; lack of suitable land in parts of the country (particularly on the two coasts); and, now, rising lumber prices thanks in part to the new duties on Canadian lumber. Although first time buyers are starting to return, there is still an imbalance between demand and supply of homes. Not enough supply!

June's housing data is positive – total starts are up by 8.3% (m/m), single family homes starts are up by 6.3% (m/m), permits up by 7.4% (m/m), completions up by 5.2% (m/m), and existing home sales were down by 1.8% from the month before.

The economy grew 2.6% in the second quarter, which is an improvement over the first quarter. Inflation remains subdued due a confluence of factors including weak wage increases and slack in the economy with production capacity utilization at 77%. Thus, numerous negative macro-factors remain endangering a robust housing recovery, in particular:

1) A constrained quantity of well-paying jobs being created;
2) house price increases;
3) insufficient supply of new and existing homes on the markets;
4) strict home loan lending standards – though loosening with new programs
5) a tepid world economy; and
6) global uncertainty

May 2017
EU Housing Scorecard

		M/M	Y/Y
Production in Construction[A]	EU 28	▽ 1.1%[s]	Δ 2.5%[s]
	EU 19	▽ 0.7%[s]	Δ 2.6%[s]
	Germany	▽ 1.0%	Δ 6.4%
	France	▽ 1.2%	Δ 4.2%
	UK	▽ 0.9%[p]	Δ 0.5%[p]
	Spain	▽ 1.4%[ps]	▽ 5.8%[p]
Building permits (m^2 floor)[A]	EU 28	-.-	-.-
	EU 19	▽ 8.0%[(04)]	▽ 7.8%[s(04)]
	Germany	Δ 4.0%	▽ 0.6%
	France	Δ 12.4%[s]	Δ 17.3%[e]
	UK	-.-	-.-
	Spain	▽ 13.4[s(04)]	Δ 4.2[e(04)]

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; 08/03/17)
[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 [(04)] May data

Housing comments – June 2017

- *June starts were up 8.3% to 1.22 million (SAAR) - SF at 849,000 (SAAR) +6.3% - MF was 359,000, up 11% – MF is typically quite volatile, and is down 11%YOY. Annual basis - total starts are up 2.1% while SF up 10.3%. Making some progress, and 1st time buyers are returning! But still have problems -* lack of supply drives prices higher and out of reach, particularly for 1st time buyers. Typical supply is 6 months – today, it is 4.3 for existing homes and 5.4 for new homes. Additional problems - tight credit and, now, rising rates.
- Low rates have not helped housing much – in fact, they have created more problems – i.e., prices rising faster than incomes in the USA. Elsewhere, we have housing bubbles in Canada (Toronto, Vancouver), Australia, and on both coasts in USA. And, we have what looks like an equity bubble forming here in USA!
- *Resale market down 1.8% - 5,552,000 (annual rate) – low inventory (4.3 months) driving prices higher – prices up 6.5% YOY*
- *New home sales were up 1% to 610,000 SAAR, up 9.1% YOY*
- Job creation improved in June - +222,000,000 - unemployment to 4.4% - but, wage/income growth is lacking
- GDP grew 2.6% for 2nd Qtr 2017 - longer term prospects are not good without improved productivity and larger workforce. A smarter immigration system is best solution for short term improvement!! *And, we need more innovation!*

Comment on GDP* – we may be underestimating the contribution of technology to GDP. Traditional metrics rely on dollars to measure GDP – however, it is difficult to convert many gains from technology to "dollar equivalents". E.g., technology often improves quality of life, but how do we put a "dollar value" on this? This affects both dollar value of GDP and productivity. Here is article from "The Economist" On the subject:

(https://www.economist.com/news/briefing/21697845-gross-domestic-product-gdp-increasingly-poor-measure-prosperity-it-not-even)

Bottom line – we may be underestimating actual GDP measurement and we may be shortchanging productivity. This combination effect would significantly "underestimate current GDP" and our estimate of future GDP growth.

Remember:
GDP growth rate = (labor force growth rate)(productivity growth rate)

"The Gross Domestic Product measures the value of economic activity within a country. Strictly defined, GDP is the sum of the market values, or prices, of all final goods and services produced in an economy during a period of time (from Wikipedia)."

Why we may be underestimating GDP (and Productivity) – quotes from The Economist:

(https://www.economist.com/news/briefing/21697845-gross-domestic-product-gdp-increasingly-poor-measure-prosperity-it-not-even)

“These days it seems that a growing fraction of innovation is not measured at all. In a world where houses are Airbnb hotels and private cars are Uber taxis, where a free software upgrade renews old computers, and Facebook and YouTube bring hours of daily entertainment to hundreds of millions at no price at all, many suspect GDP is becoming an ever more misleading measure. Also, inflation measurements are flawed (e.g. performance improvement in products and services is not taken into account – we simply record price changes.”

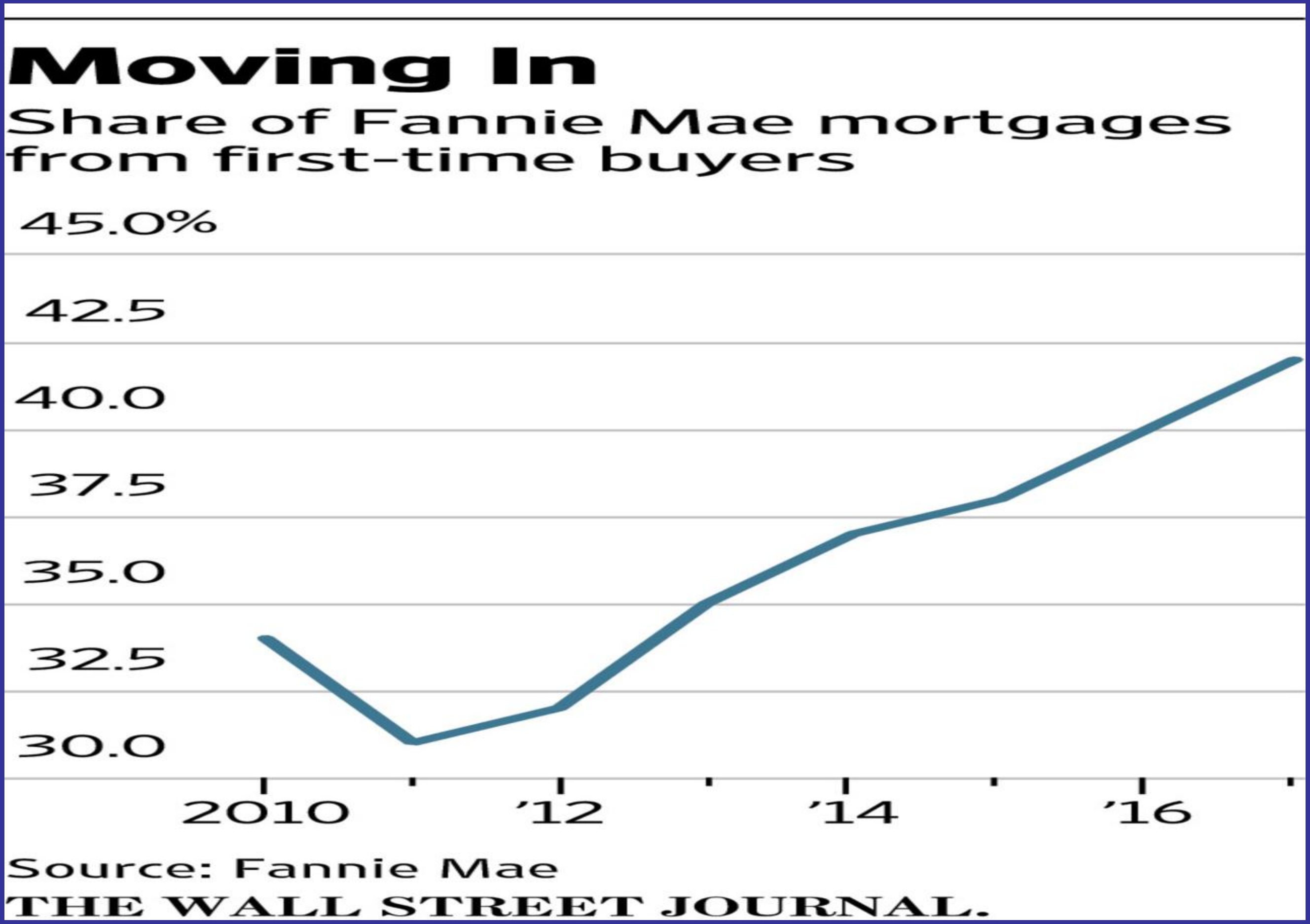
The article is sometimes hard to understand – lots of “economic jargon”. Here is the jest however – most GDP and productivity measurement techniques were developed years ago when production/manufacturing activity was more prevalent in our economy. Today, the service sector is much larger; many products/services are provided free of charge; for other products/ services, improvement in quality is not measured. For example, a new cell phone may cost more, but it does much more – but, we only measure the increase in cost.

Here is a good example of “inaccurate measurement” from housing – (from The Economist article)

“Some private-sector services are also measured indirectly. Housing services is one. This is straightforward wherever householders rent the property they live in. Rental payments capture both the value of housing services to tenants as well as the income of landlords from providing them. But in places where most people own the home they live in, a large part of the total value of housing services has to be imputed.”

OK – what does this mean? For starters, this is important because so many decisions are influenced by statements about GDP and productivity – business decisions; government decisions; Federal Reserve decisions; … You get the point – so what to do? Take the GDP and productivity measurements with a grain of salt – e.g., if you’re in business, develop your own metrics!

Good News – 1st time buyers are returning – historically, they made up about 35% of the market – that dipped to 30% during the crash. But, in QTR1 2017, they represented 38% of all SF home sales. In addition, new owner households numbered 854,000 compared with 365,000 renters in Qtr1 2017 – reversing a decade long trend.



(https://www.wsj.com/articles/the-next-hot-housing-market-starter-homes-1494495003)

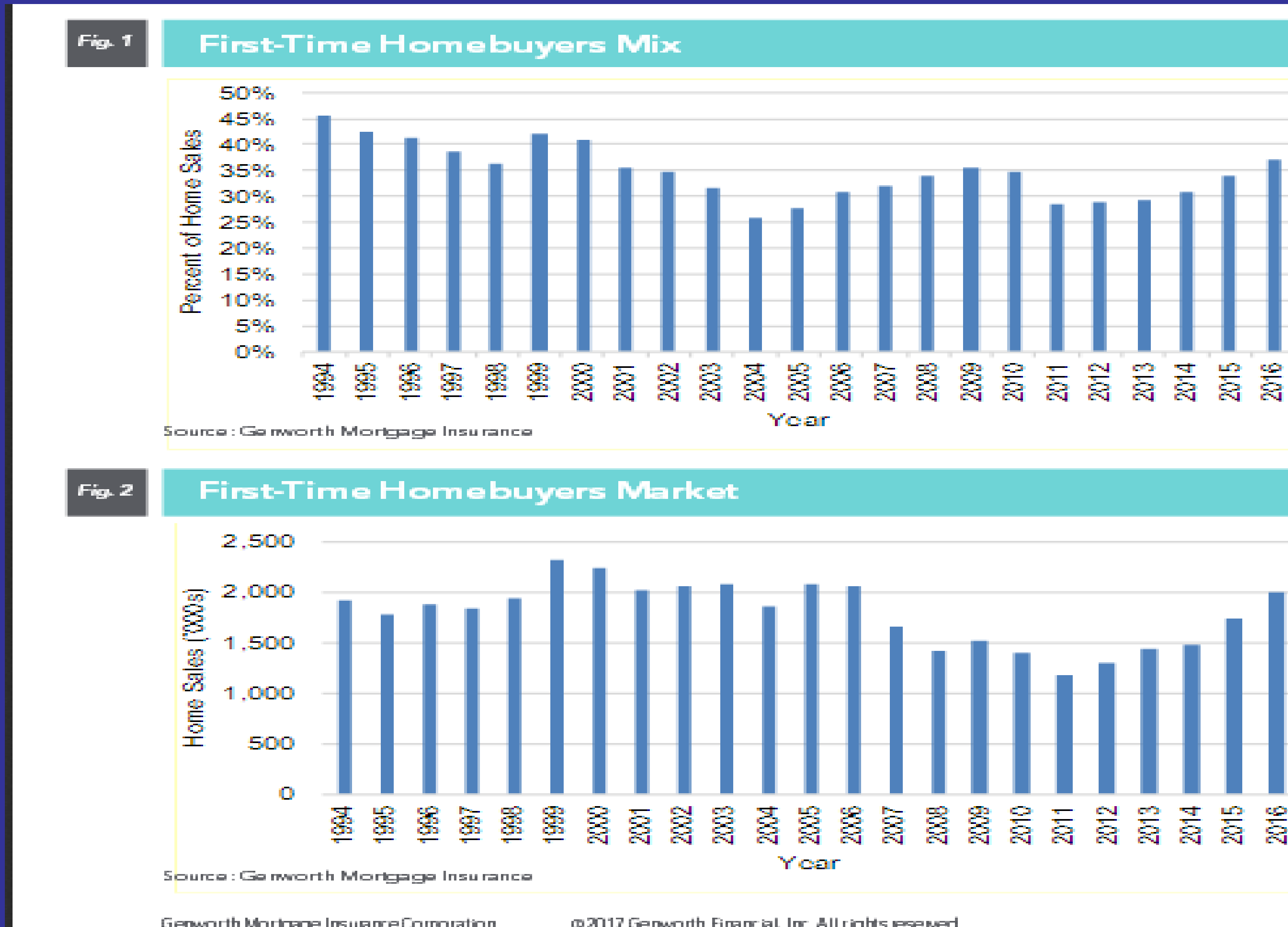
New study by Genworth Financial analyses 1st time homebuyer market - here are some excerpts:

Download the report using this hyperlink:
(https://miblog.genworth.com/first-time-homebuyer-market-report-06-17)

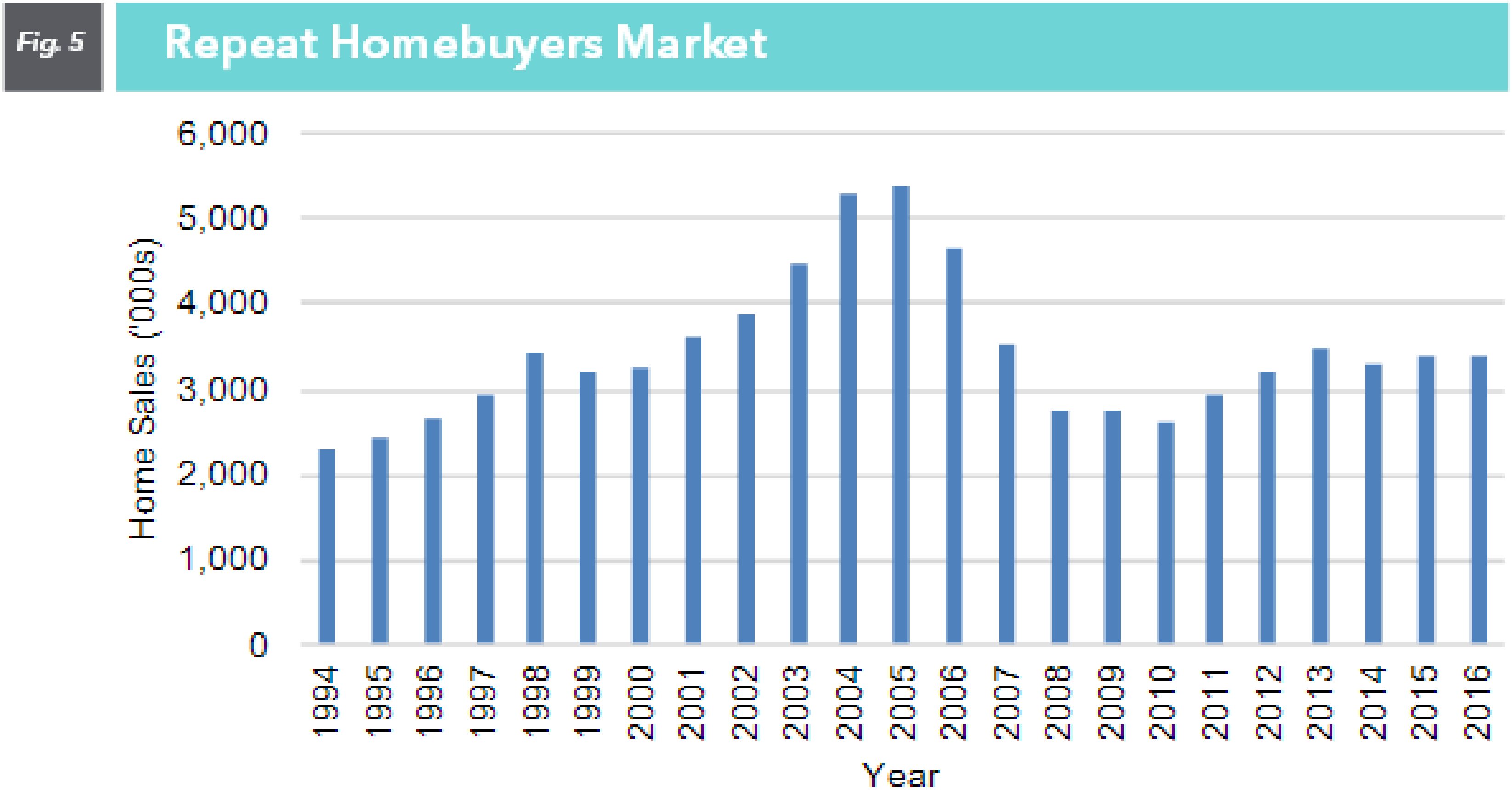
1. "During Q1 2017, first-time homebuyers bought the most single-family homes since 2005. During the first quarter of 2017, 424,000 single-family homes were sold to first-time homebuyers (38 percent of all single-family home sales), the most during that period since 2005, and an 11 percent increase from the same period in 2016.
2. From 2014 - 2016, first-time homebuyers drove 85 percent of the housing market's expansion, the fastest rate ever."

1st time home buyers are critical to a healthy housing market. Without them, the market stagnates – like today! E.g. – eventually, many first time buyers become "move up" buyers as family and incomes grow, and this allows existing homeowners to move to more upscale housing – they are a critical cog in a dynamic housing market!

Some slides from the Genworth study



More slides from Genworth



Source: Genworth Mortgage Insurance

Big problem for housing – too little supply!

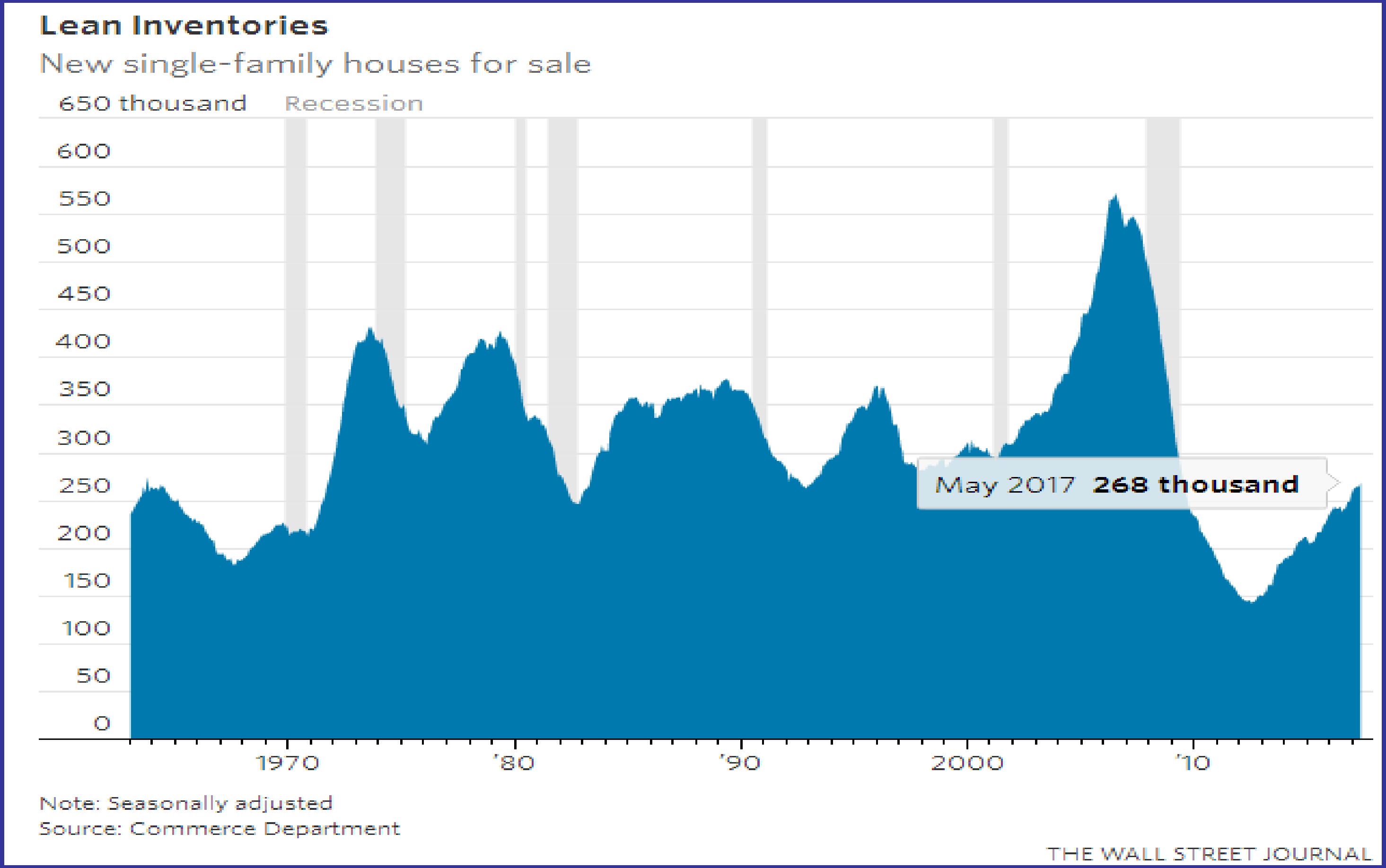
This drives prices higher and out of reach for many buyers, Especially 1st time buyers.
Typically, supply is about 6 months (time it takes to sell existing inventory at current sales rates). Today, existing Home inventory is 4.2 months while new home inventory is 5.4 months. Many homeowners are reluctant to list their homes because buying another one is expensive while builders are reluctant to build new homes due to costs, driven partly by labor and land shortages in parts of the country.

Today, prices are increasing twice as fast as incomes, so this problem is actually getting worse. Also, mortgage rates are increasing, and credit remains tight following new rules in the aftermath of the 2008 financial crisis.

Prognosis – housing could remain below par for some time!

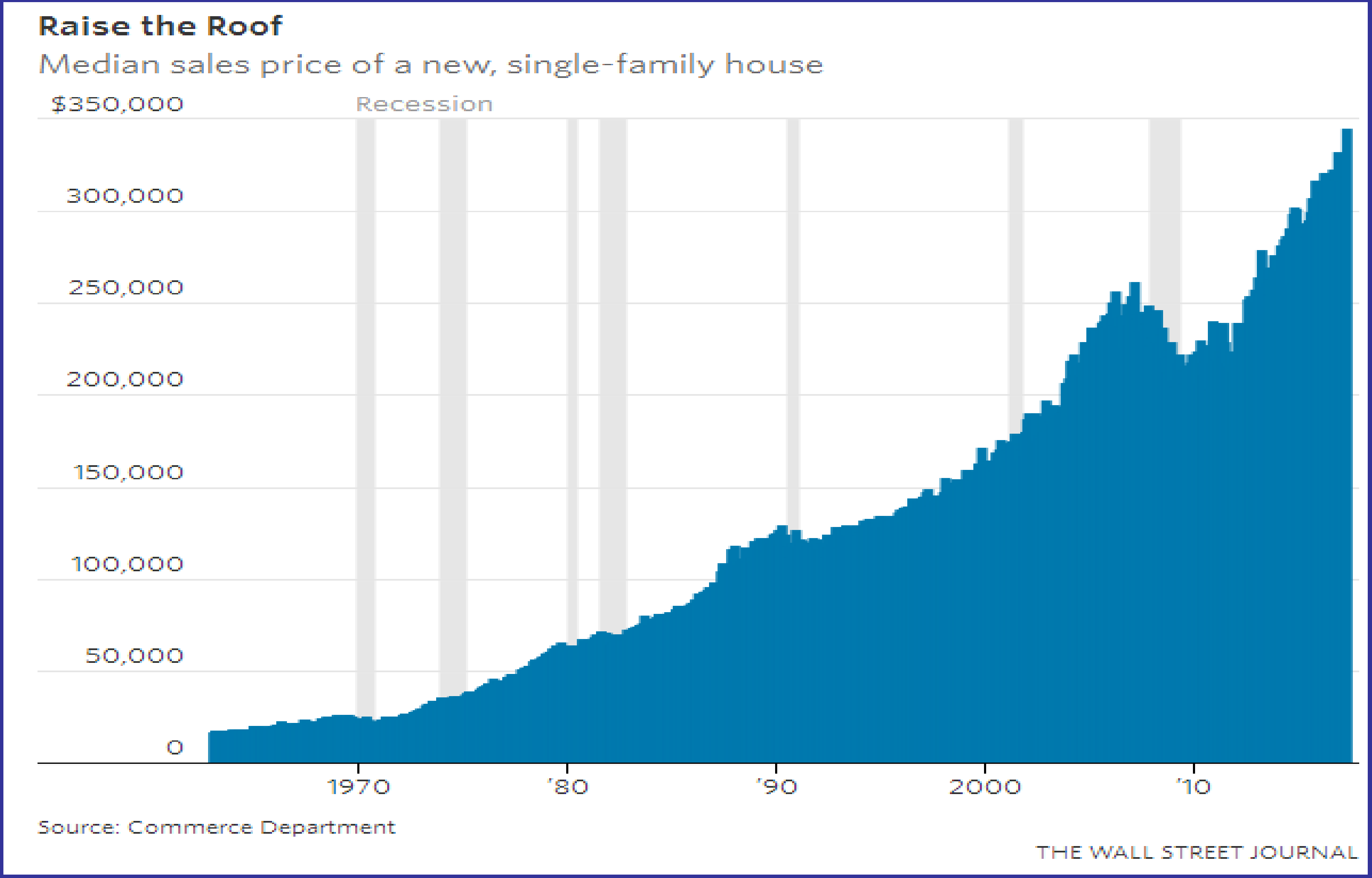
Low new home inventory (5.2 months) drives prices higher and out of reach of most 1st time buyers

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!

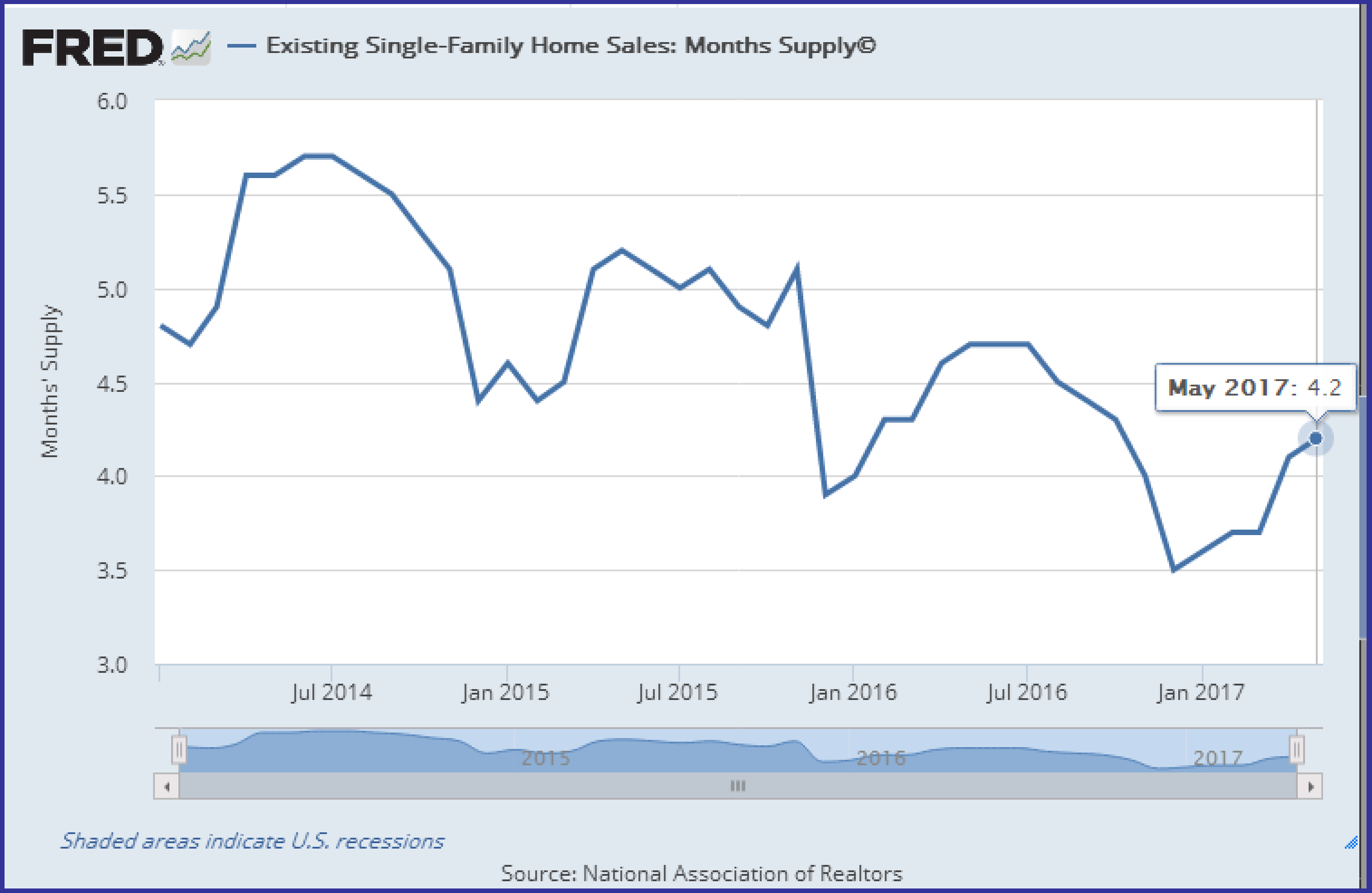


(https://research.stlouisfed.org/fred2/series/MSACSR)

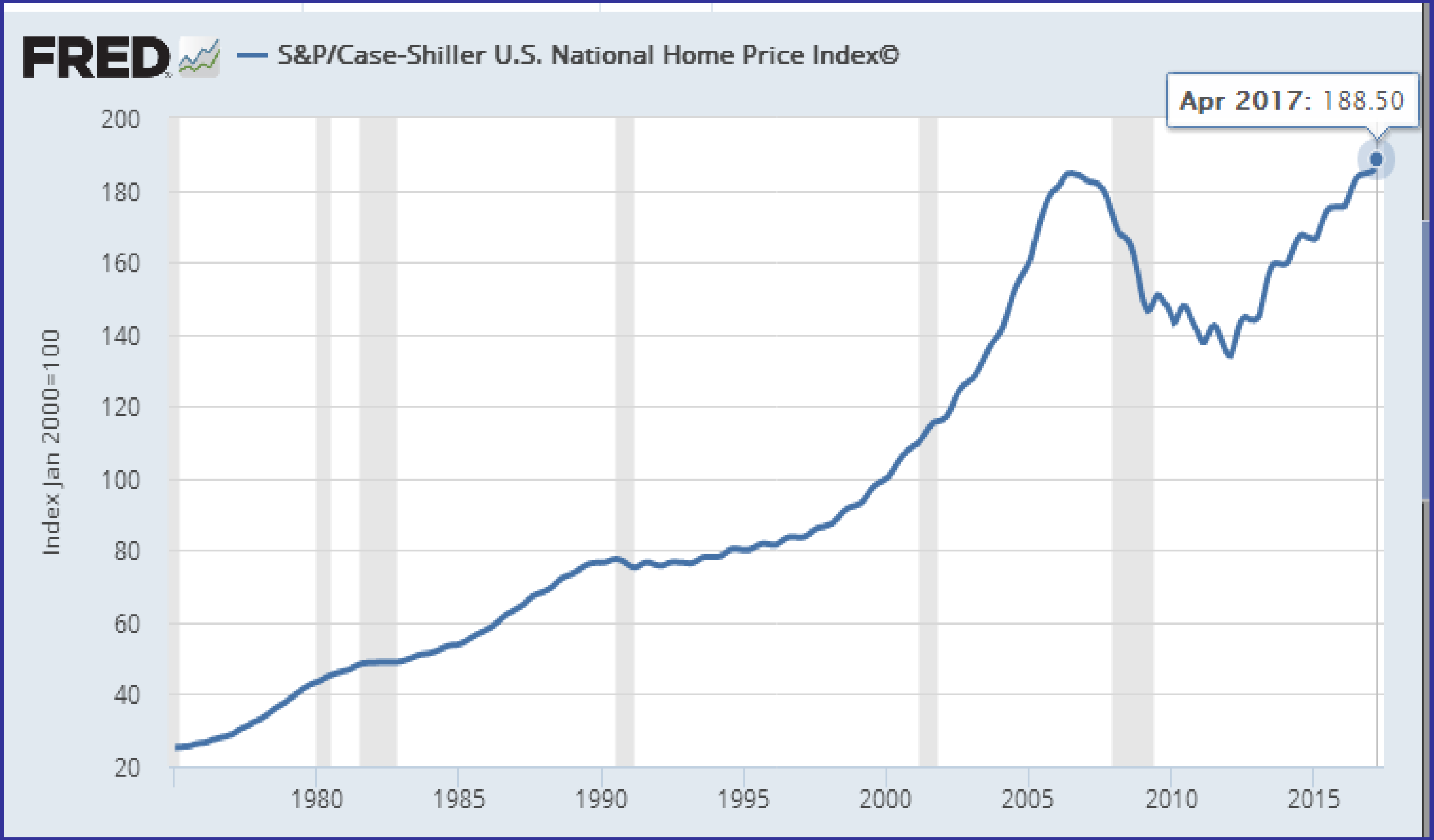
New Home sales prices: Imbalance between demand and supply driving prices to record levels – same story with existing home sales. Price increase also due to weakness in entry level/lower end housing coupled with strength in upper end housing.



Low Existing home inventory (4.2 months) drives prices higher - out of reach to most 1st time buyers.

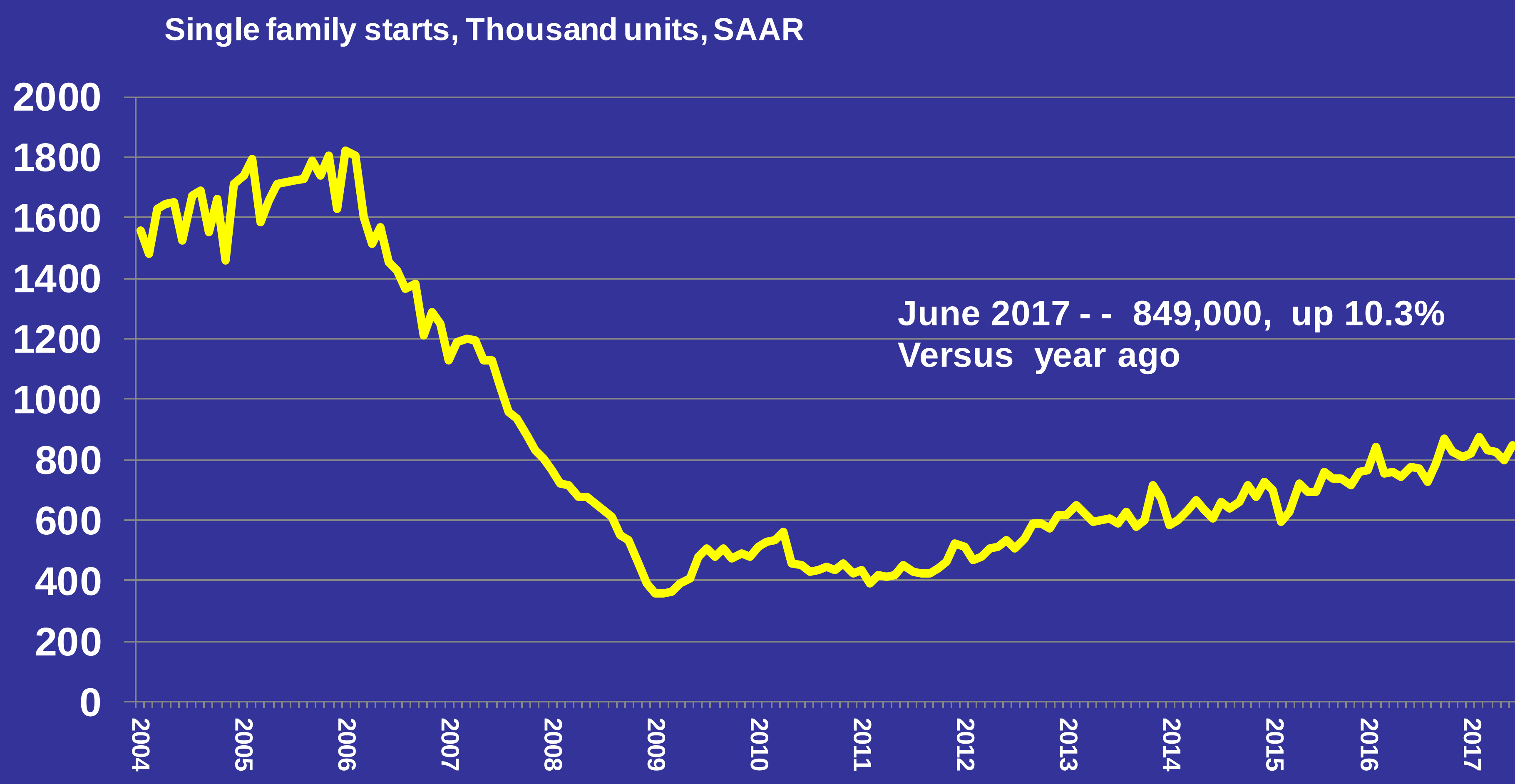


Case Shiller National existing home prices – up 41% in past 5 years – driven primarily by short supply and demand for upscale homes



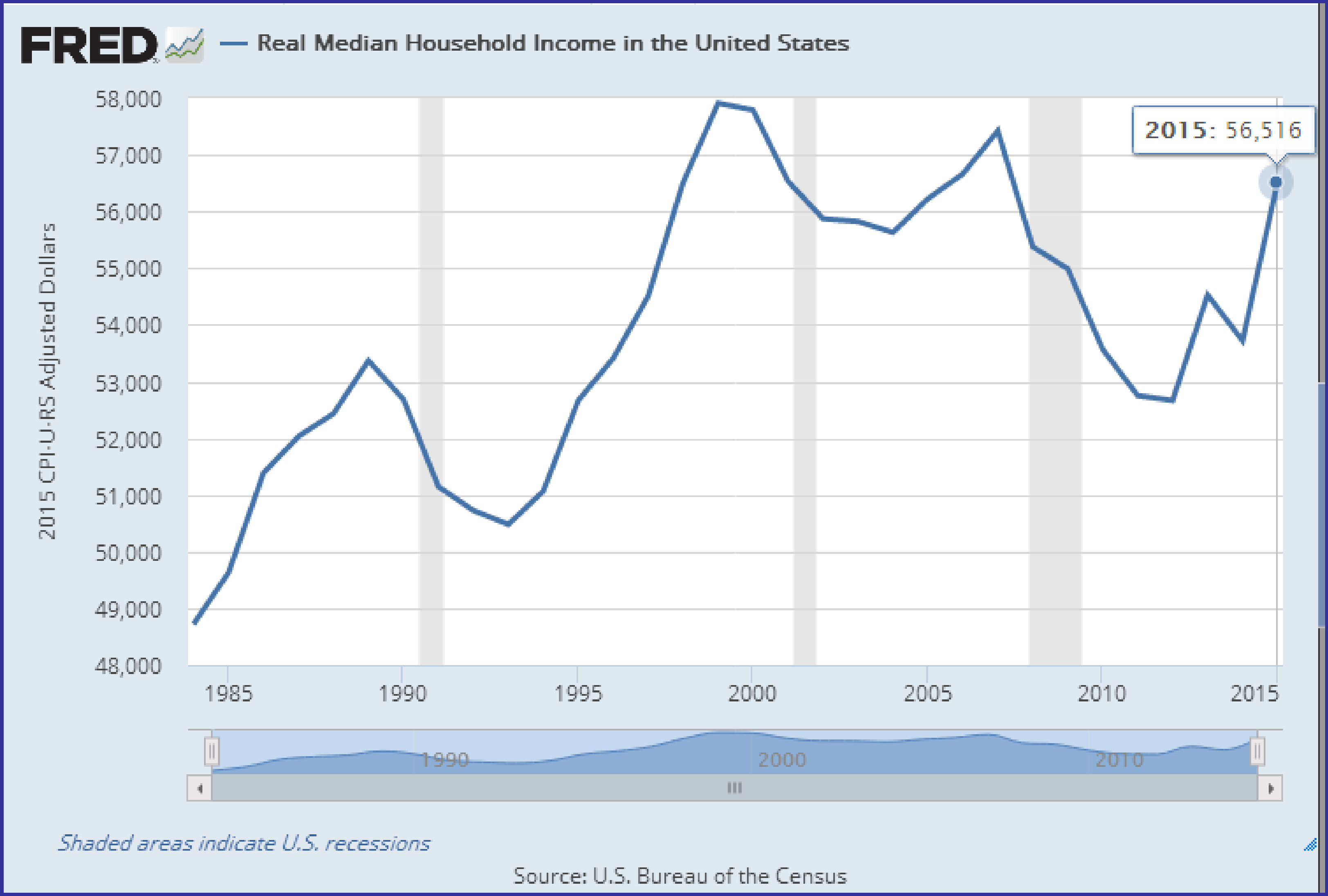
(https://fred.stlouisfed.org/series/CSUSHPINSA)

Weak housing starts contribute to the supply shortage and *drive prices higher*

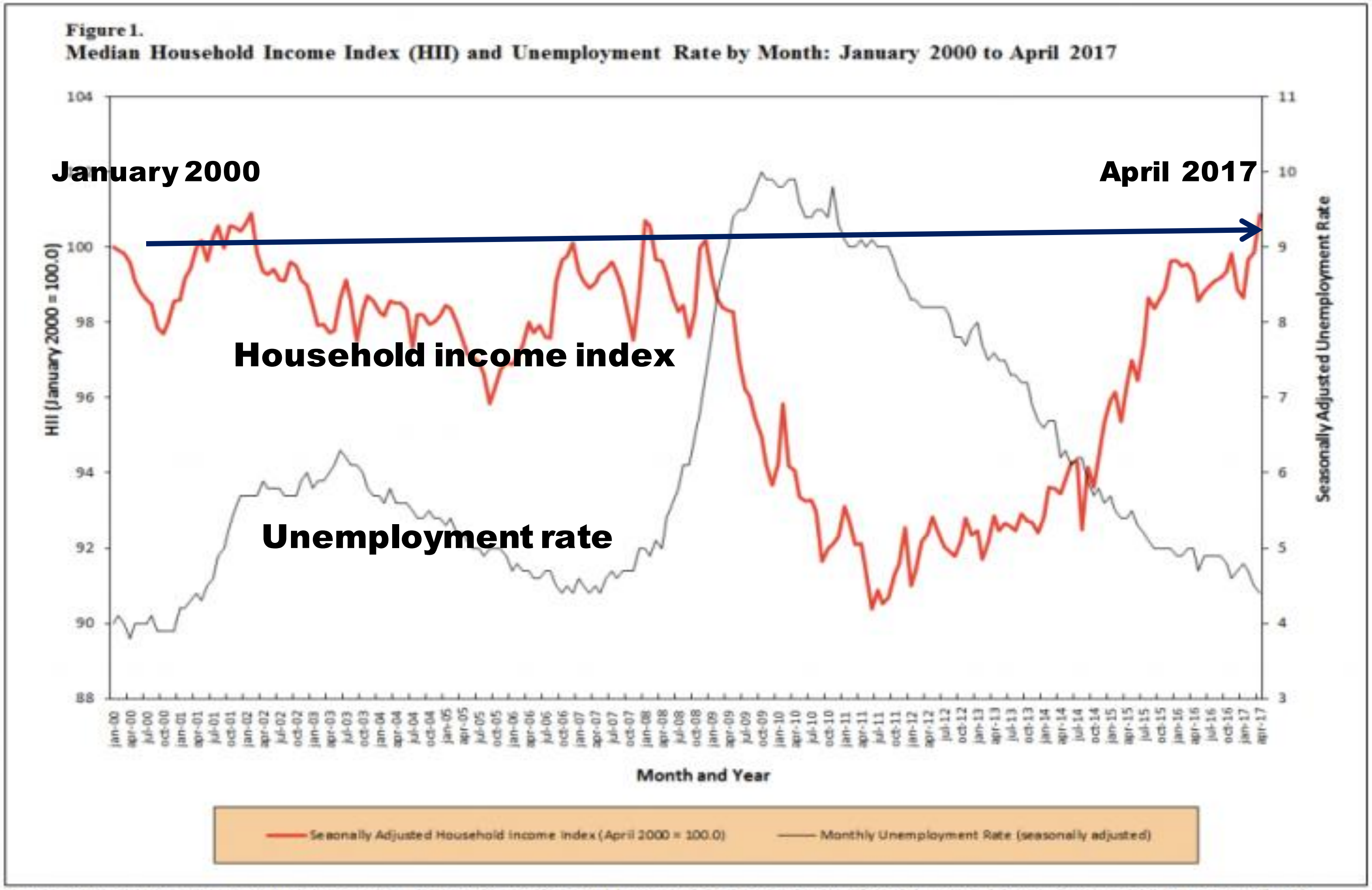


Source: Census (http://www.census.gov/const/www/newresconstindex.html)

Real Incomes today same as 1998 – i.e., little progress in two decades – unemployment at record low levels, yet wage growth has lagged.



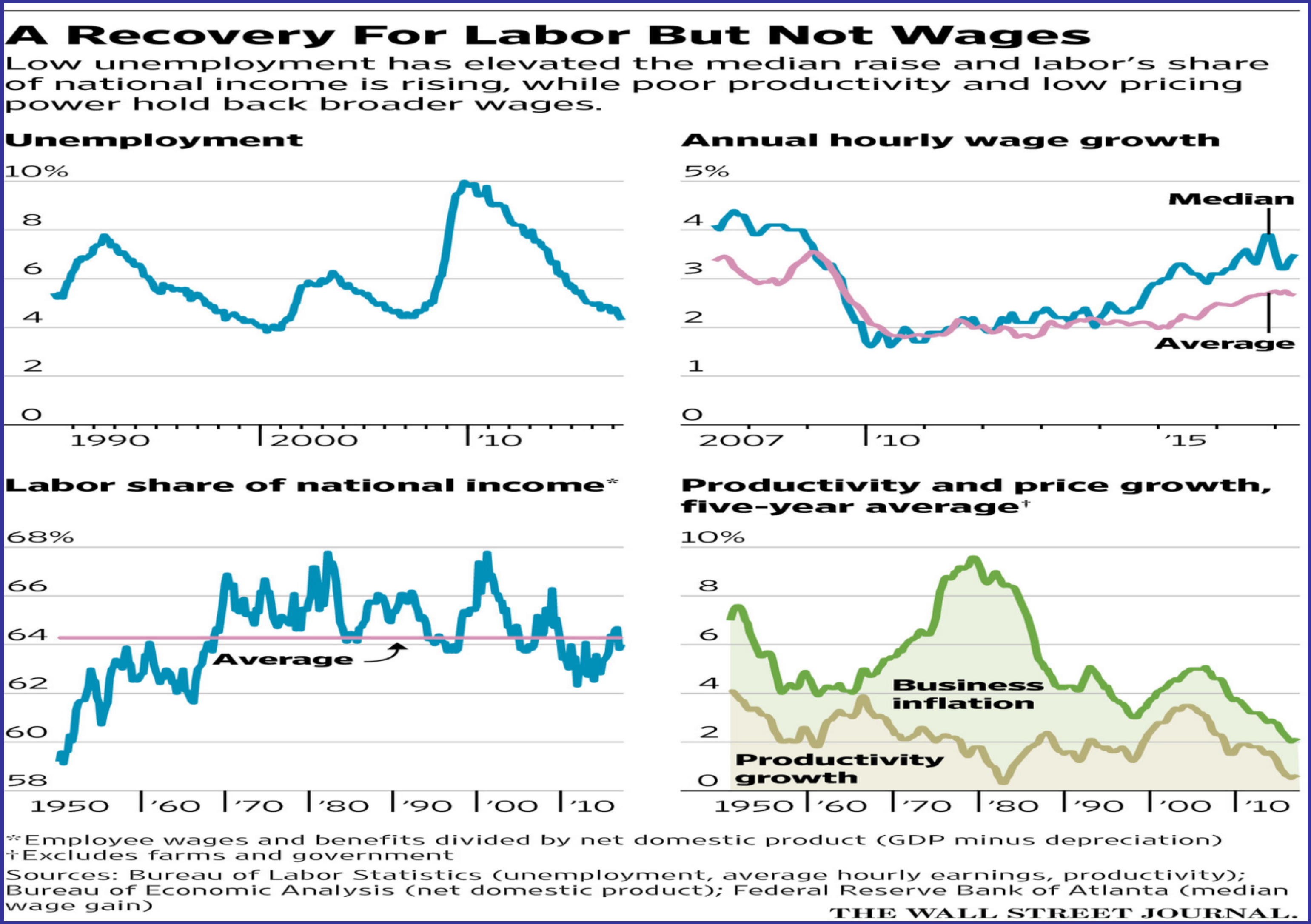
Long term trend - a disconnect between unemployment rates and incomes. Problem - many of new jobs created are low paying with little or no benefits. This is a structural problem with many high paying jobs that go unfilled because applicants don't have the required skill set!



Sources: For income data: Sentier Research, LLC estimates of annual household income derived from the monthly Current Population Survey (CPS) conducted by the U.S. Census Bureau; for the unemployment rate and the CPI-U: the U.S. Bureau of Labor Statistics.

Low productivity, aging work force, and weak corporate pricing power suggest that wage growth could remain weak for some time. Despite low unemployment, wage growth has been lackluster *– bad news for housing*

G. Ip, WSJ (https://www.wsj.com/articles/why-the-tight-labor-market-isnt-generating-better-pay-1497441272)



Solution to fixing the economy – get housing back to trend levels – yes, this is a "chicken and egg type issue", but as the chart on the next page shows, spending on housing is an important contributor to GDP. E.g., total expenditures on housing related activities (appliances purchases, real estate agent jobs, …) has averaged 19% of GDP over past 60 years, but today it is 15.6%!

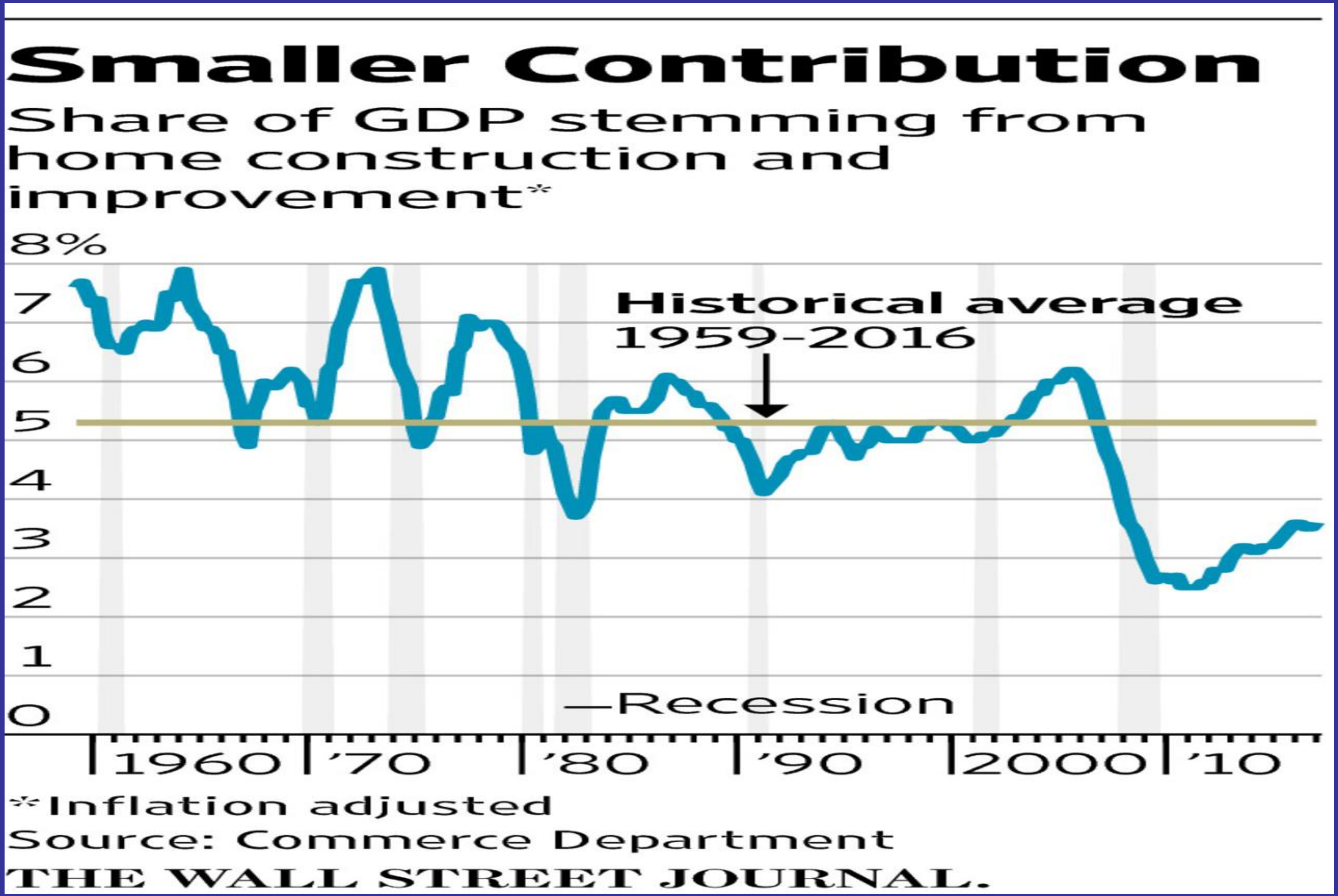
Tight credit also big problem, especially for 1st time buyers.

Now, we have the "lumber tax" on Canadian lumber to deal with. That will only increase construction costs and make housing less affordable.

An interesting comment on the U.S. economy by Greg Ip WSJ (https://www.wsj.com/articles/the-economy-needs-amazons-but-it-mostly-has-ges-1498037403)

“Housing serves as an economic engine through home construction as well as ancillary activities such as appliance purchases, spending on home renovations and jobs for real-estate agents.” “Total spending on housing fell to 15.6% of GDP in 2016, compared with 19% over past 60 years. A more specific measure - Spending on new construction and remodeling fell to 3.6% of GDP” – see chart below.

Source: WSJ (https://www.wsj.com/articles/sluggish-housing-recovery-took-300-billion-toll-on-u-s-economy-data-show-1490526643)



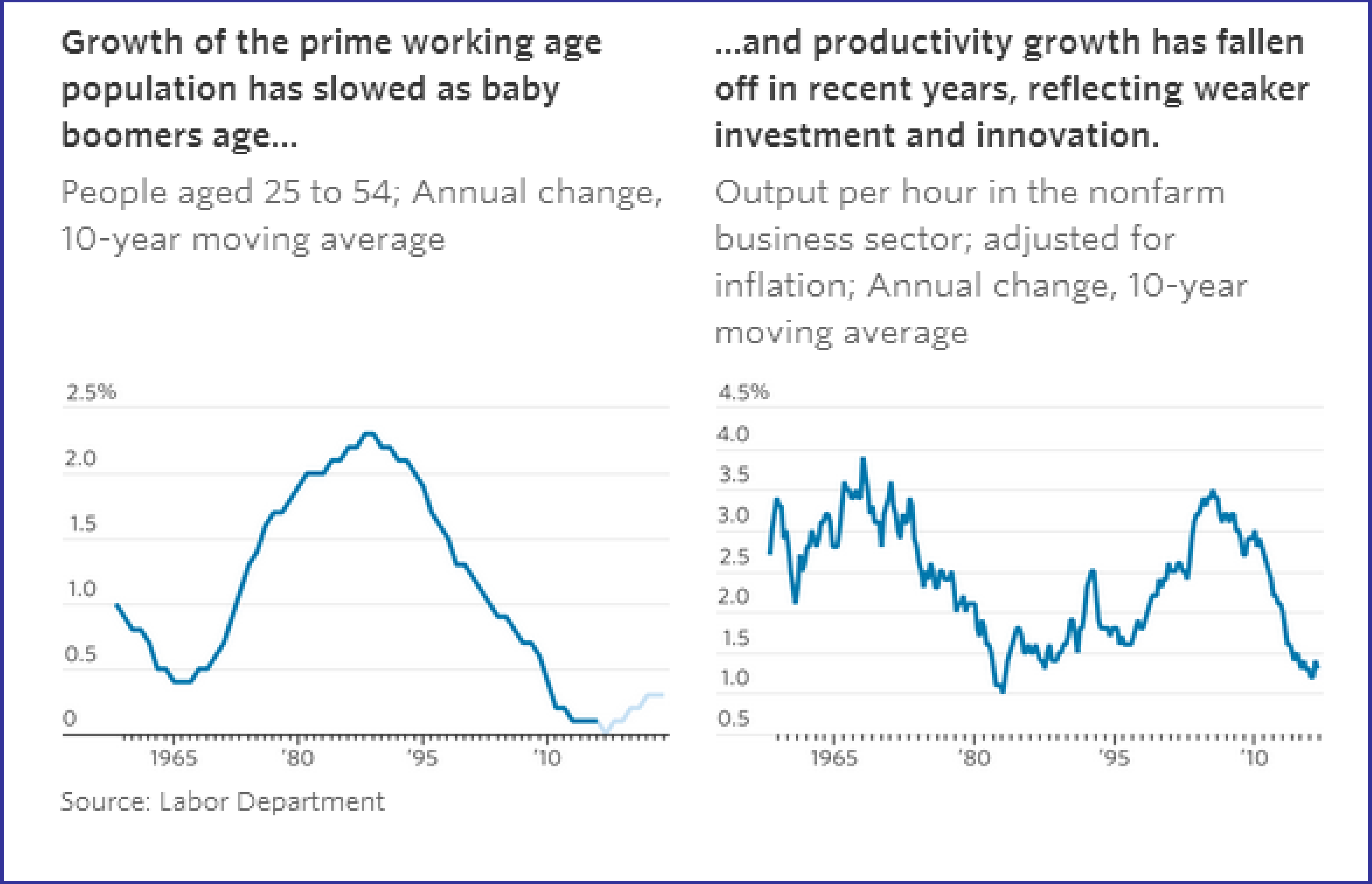
Here is another suggestion on how to fix the economy – a "no brainer" .

GDP = (labor force) (productivity)
"Economics 101"
We have an aging work force and our fertility rate has been falling for decades. That means slow growing labor force. Productivity growth has been weak for decades too. Yes, We need to invest for the future – R&D; Infrastructure spending; less regulation; fix K-12 system;.... But, we also need immigrants.

Solution – develop a smart immigration system that brings in educated, hard working people with technical skills that will support better productivity growth., and address our shrinking labor force too.

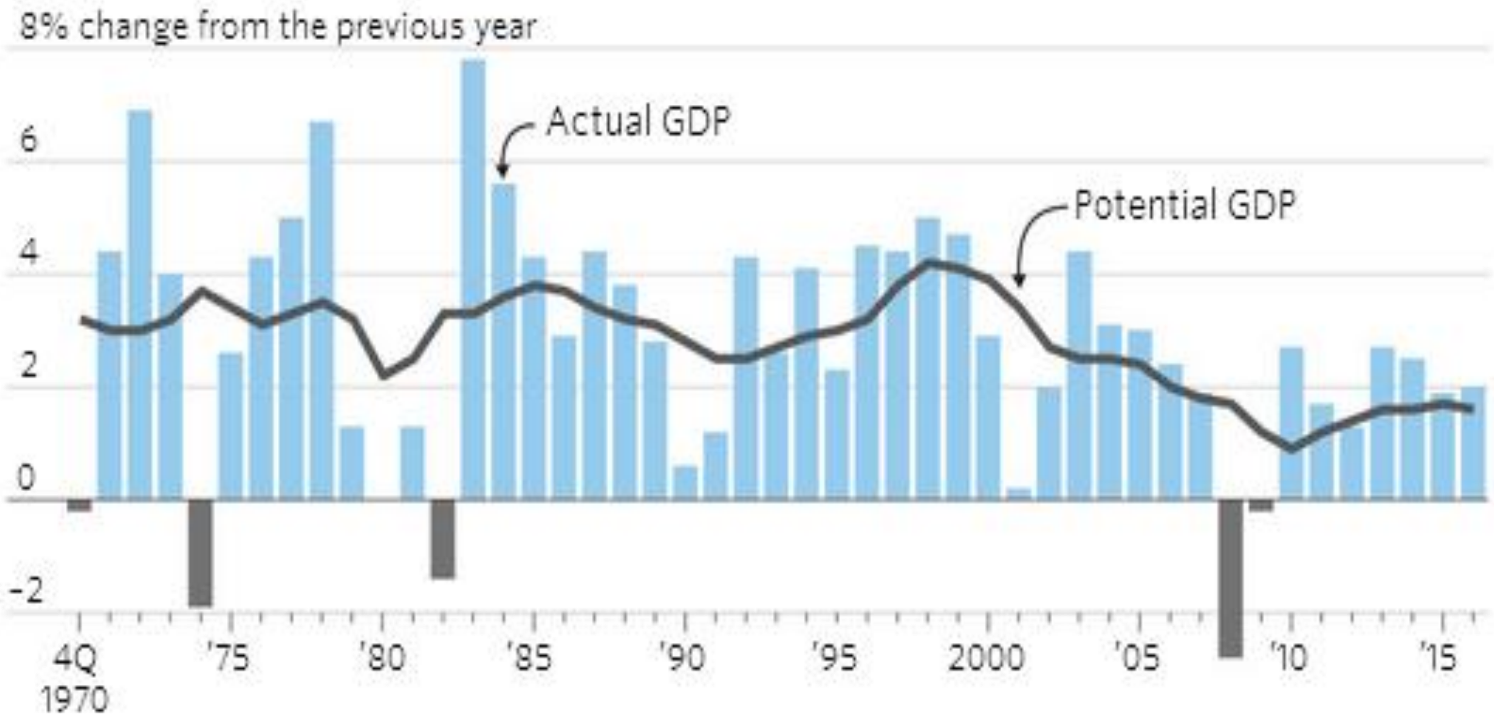
Yes, we still need to bring in refugees too – that is the mark of a compassionate country. But, the focus today needs to be highly educated, English speaking (doesn't have to be perfect, but workable) people with technical skills and a strong work ethic.

Growth comes from workforce and productivity – can't increase very fast over the long term unless we deal with declining workforce and weak productivity growth.



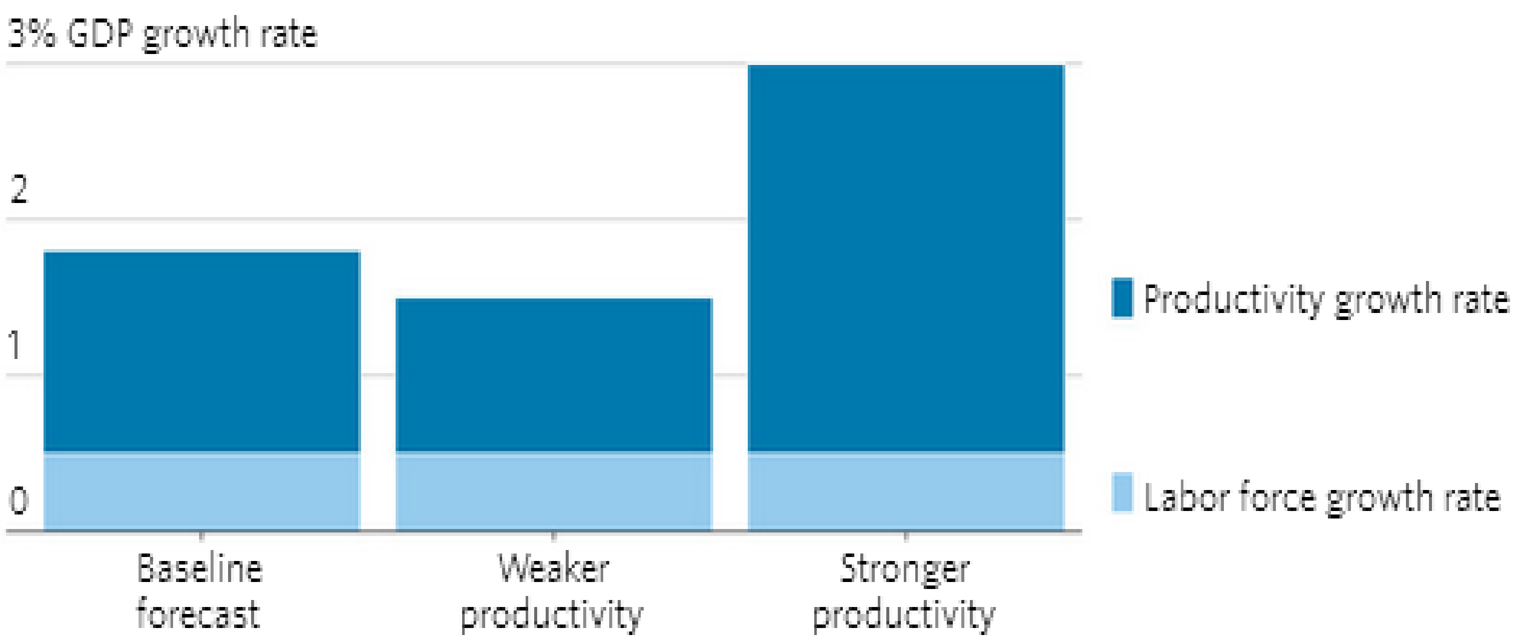
(https://www.wsj.com/articles/labor-force-stands-in-way-of-trumps-3-growth-goal-1494861153)

The economy's "speed limit" :
GDP Growth = (growth in labor force)(Growth in Productivity)
Chart below shows projections from CBO



Sources: Commerce Department (actual figures); Congressional Budget Office (potential GDP)

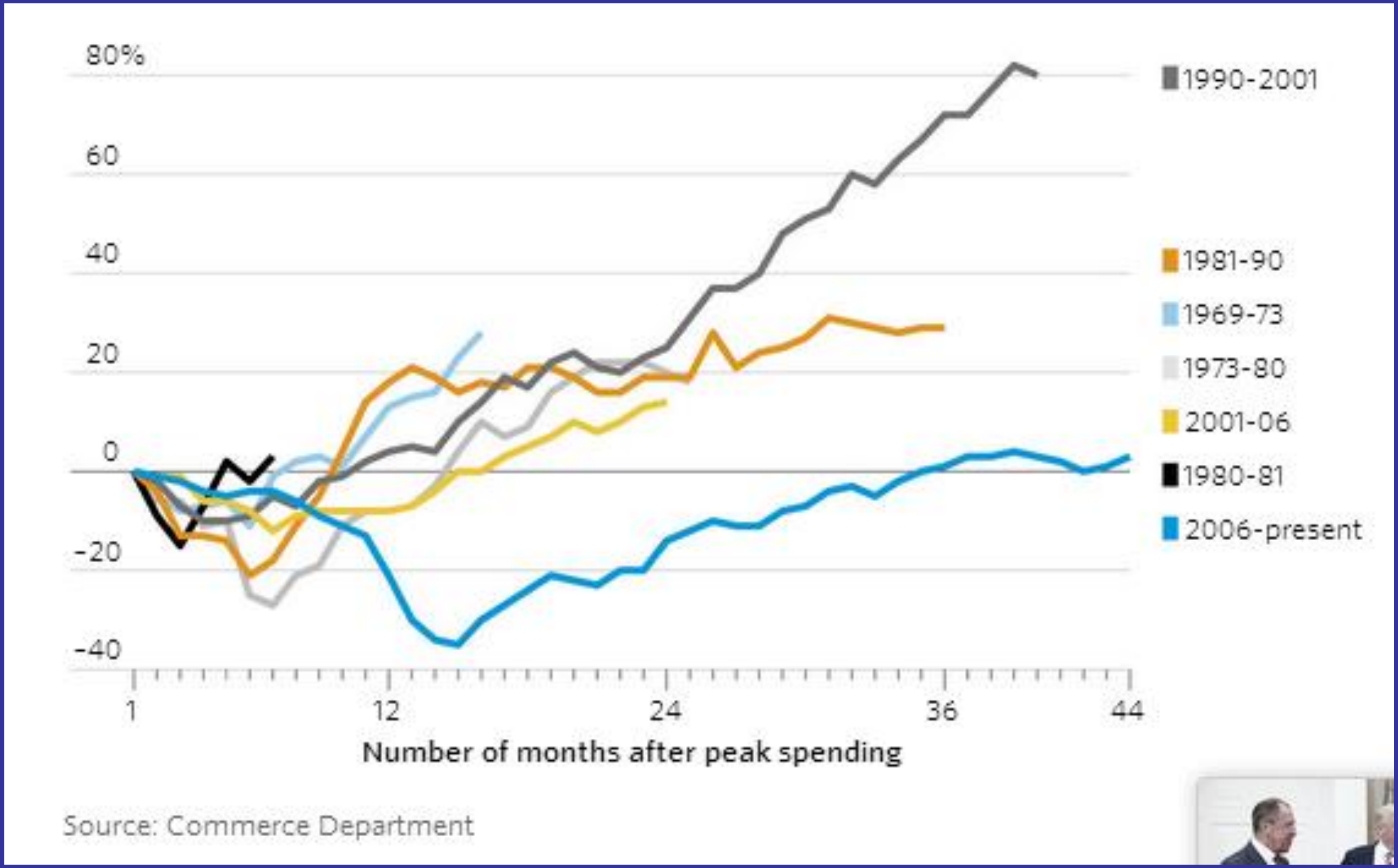
Some (CBO) projections of GDP growth with weaker productivity versus stronger productivity – but, for better productivity we need to invest, and we are not doing so!



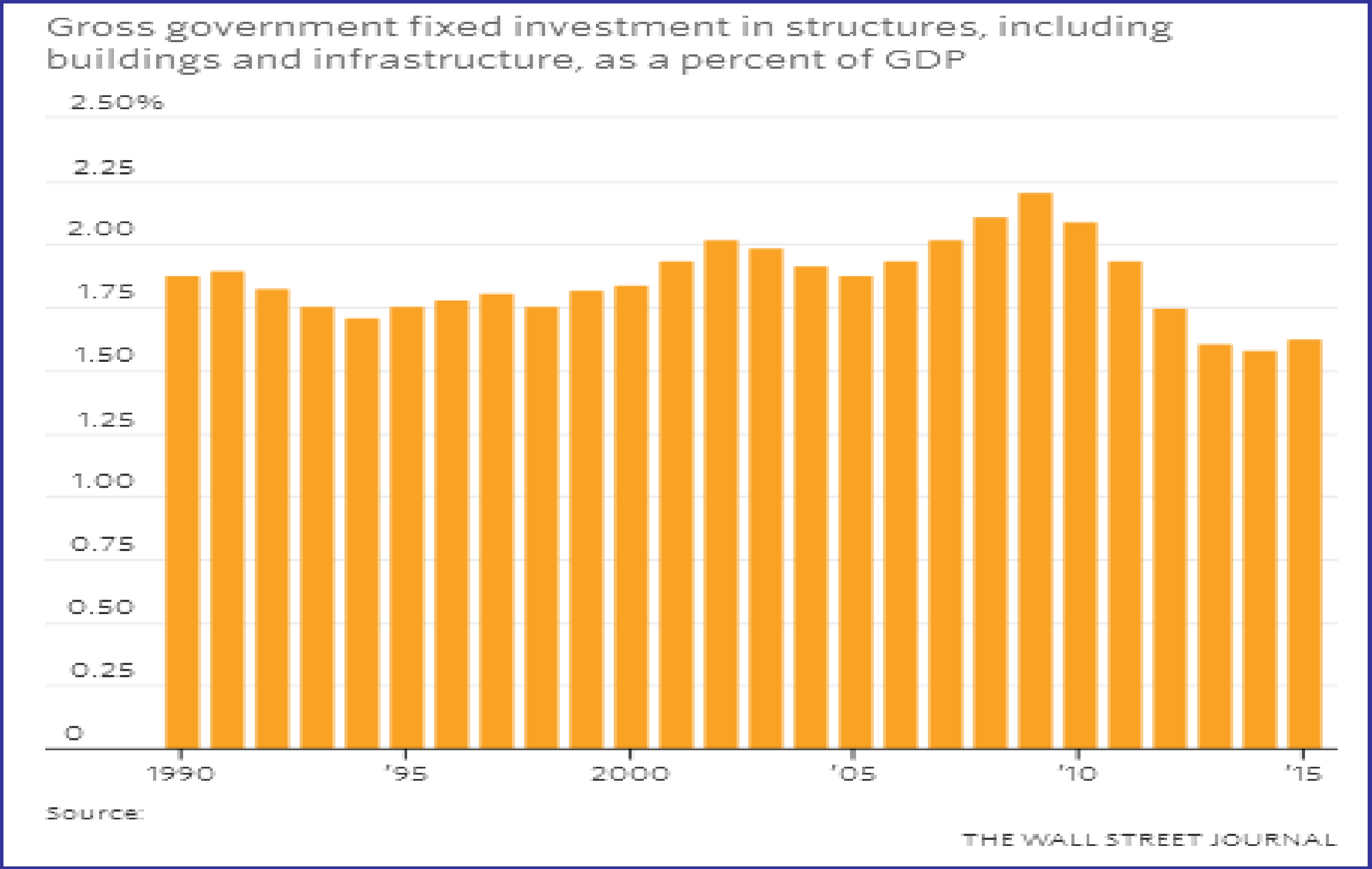
*Forecast from the Congressional Budget Office †Since 1958

Sources: Congressional Budget Office (baseline forecast, workforce projections); Jason Furman of the Peterson Institute for International Economics (productivity projections)

Gross private investment spending over the last three decades - chart compares recovery in investment following recessions. Latest recovery is pathetic! Why? Many individuals are not excited about the future – can’t blame them with current political climate!



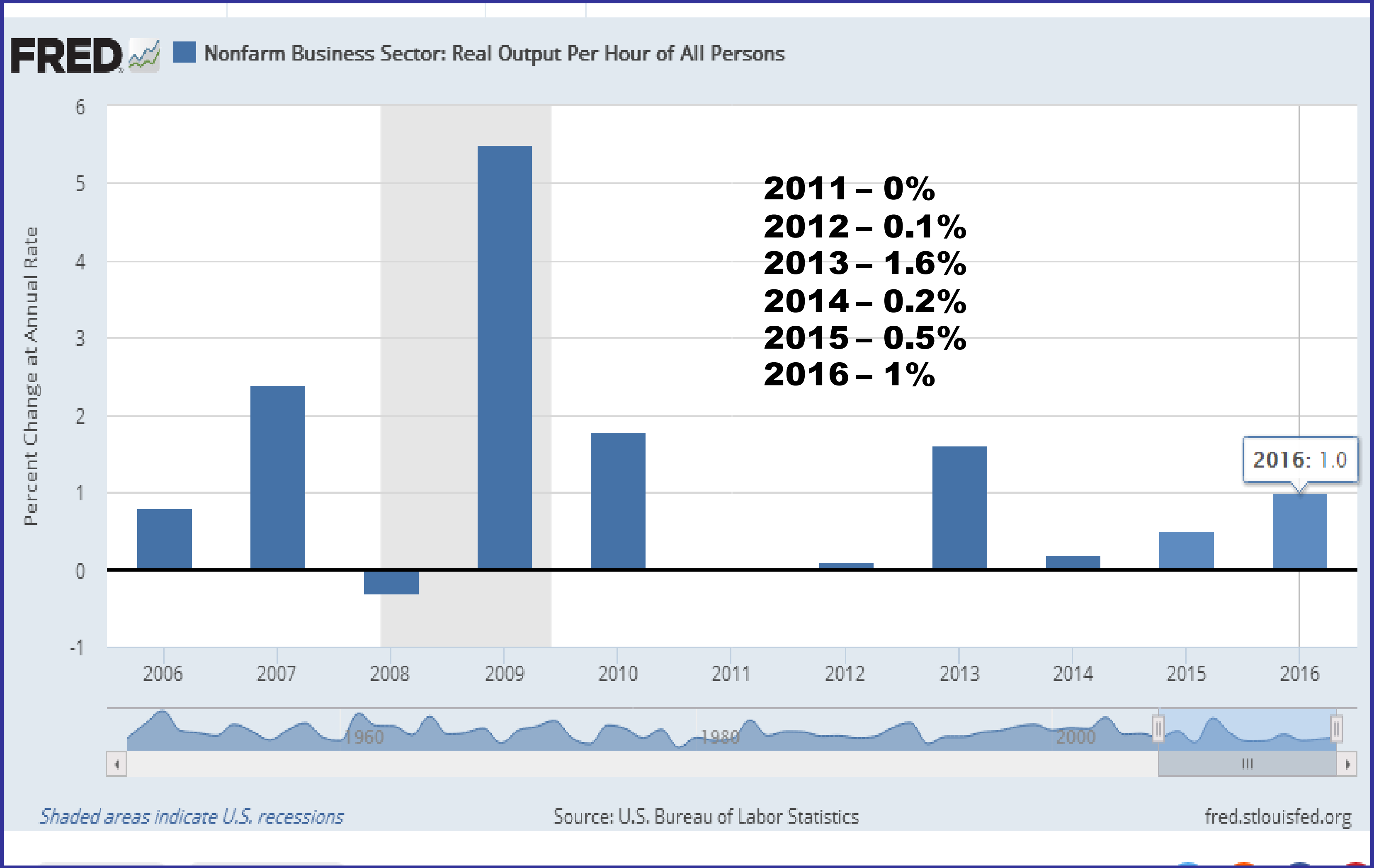
Public infrastructure investments have been falling for a decade - hinders any improvement in productivity



What happens when innovation/investment are 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?)

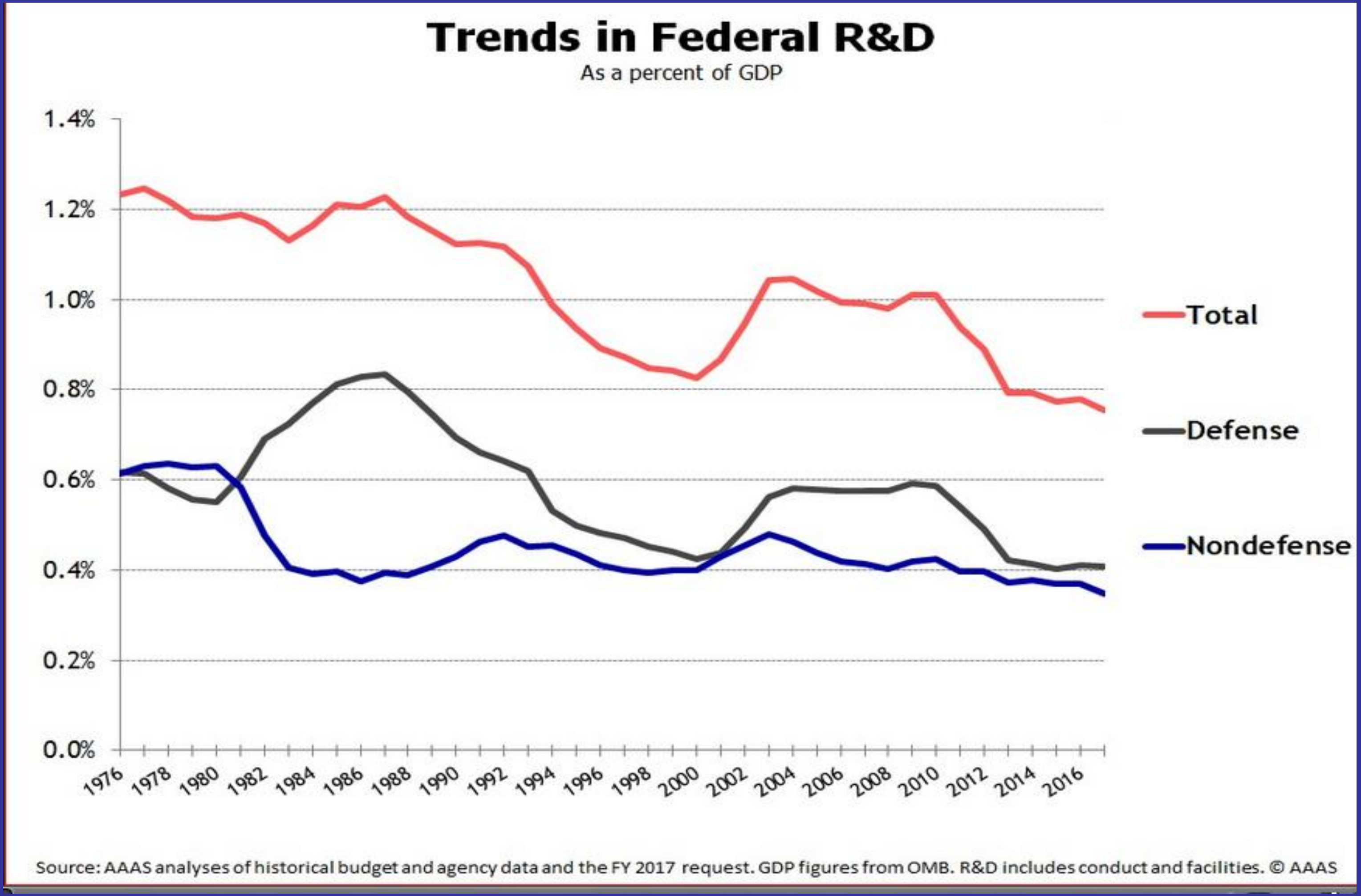
Source: WSJ (http://www.wsj.com/articles/u-s-productivity-dropped-at-0-5-pace-in-the-second-quarter-1470746092)

Declining productivity is a major problem – has averaged 0.6% annually since 2011 – this plus declining work force means weak GDP and declining standard of living



Falling basic R&D - - funding basic science is declining – big problem that needs fixing

Federal government funds basic research while industries fund applied research – basic research is critical to development of new technology and innovation in science and engineering - critical to economic and job growth, and productivity
(http://www.wsj.com/articles/the-dividends-of-funding-basic-science-1480982516?mod=rss_opinion_main)



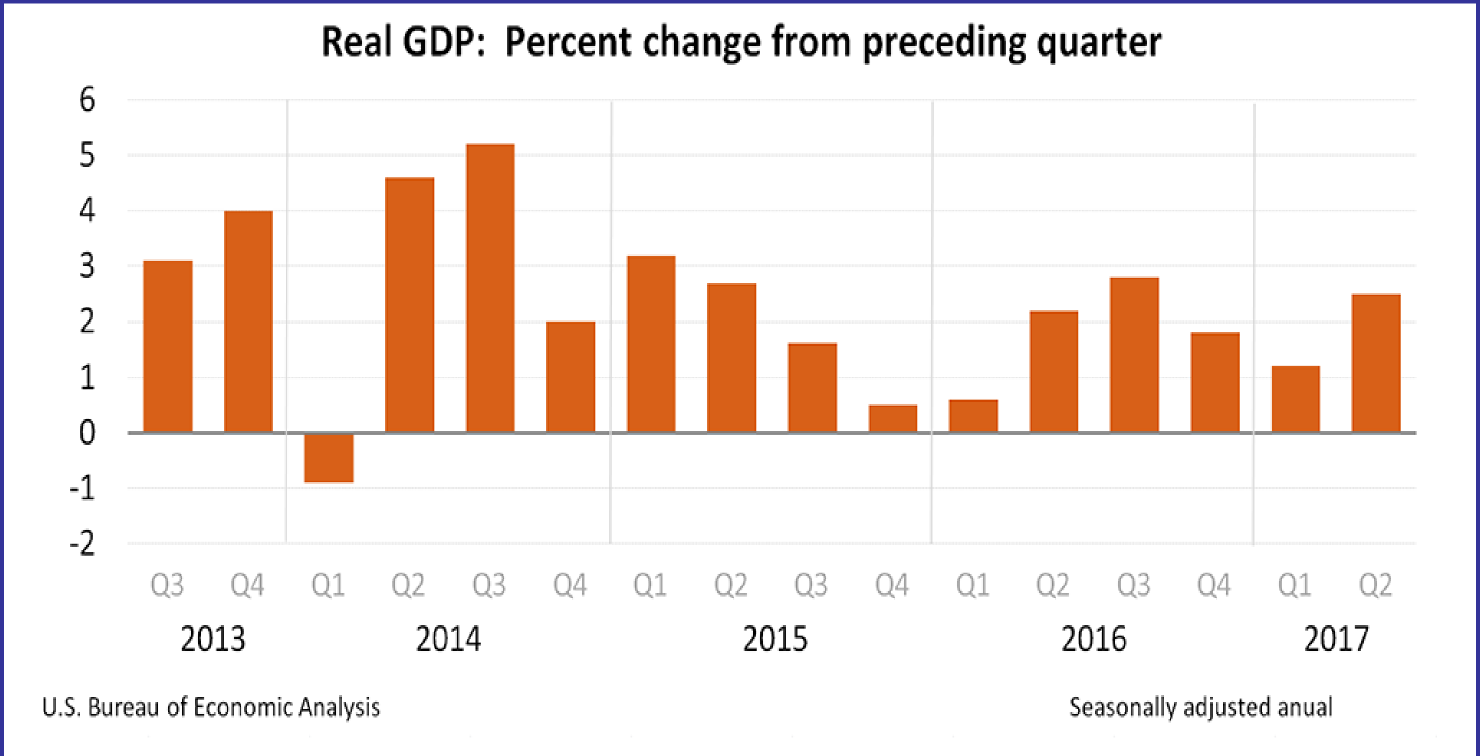
U.S. 2nd Qtr 2017 Economic growth 2.6% - - - 1.6% for 2016 - terrible The slowest expansion since WW11.

(1) Slowing world economy (weaker China , European, and South American growth)

(2) Weaker dollar will support exports and decrease imports – positive impact on manufacturing jobs which is key to income growth in USA – good news!!!!

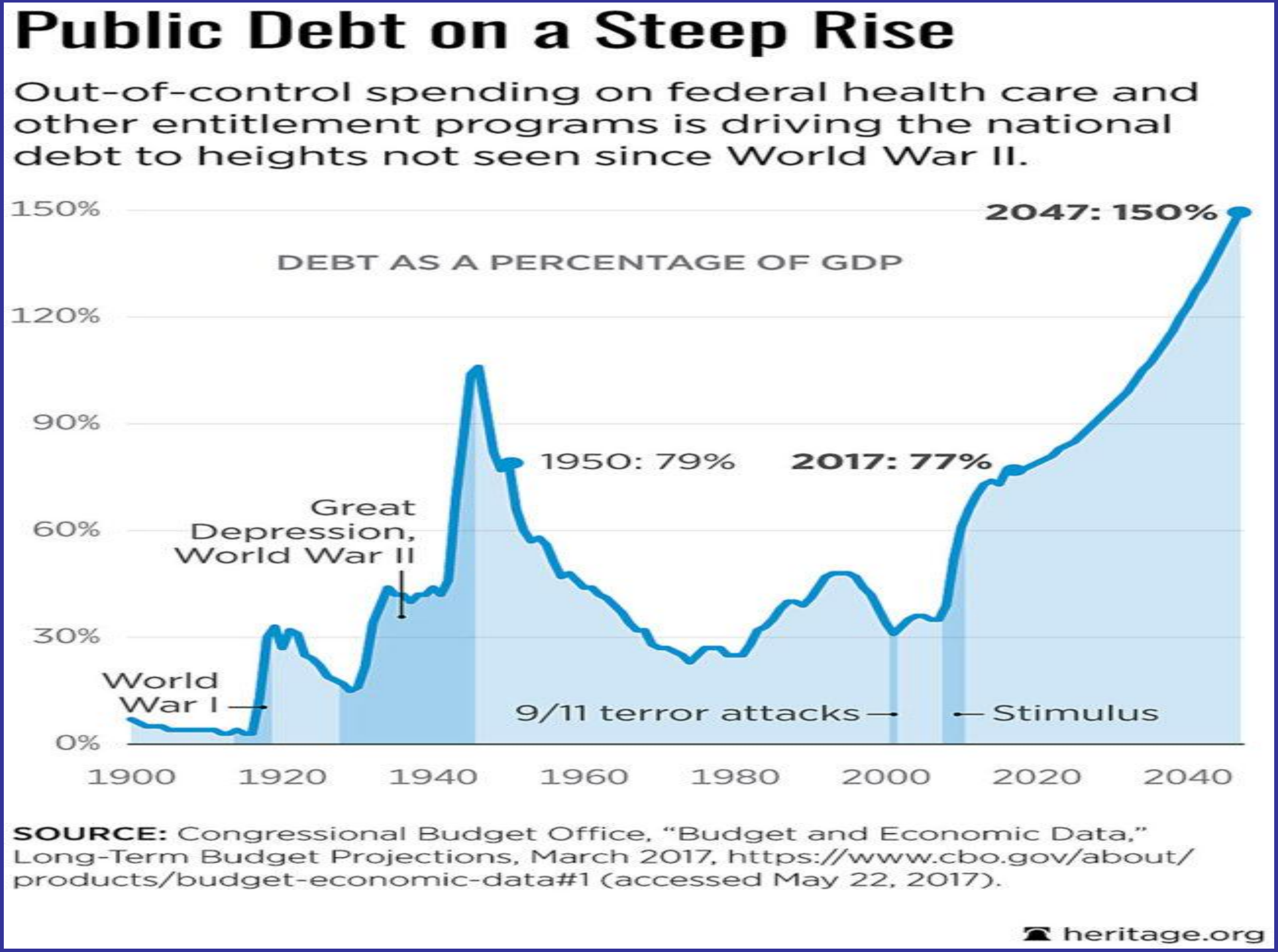
(3) Political stalemate/weak leadership, terrorism, currency wars, growing national debt, …

(4) Weak income growth and continuing high "real unemployment"

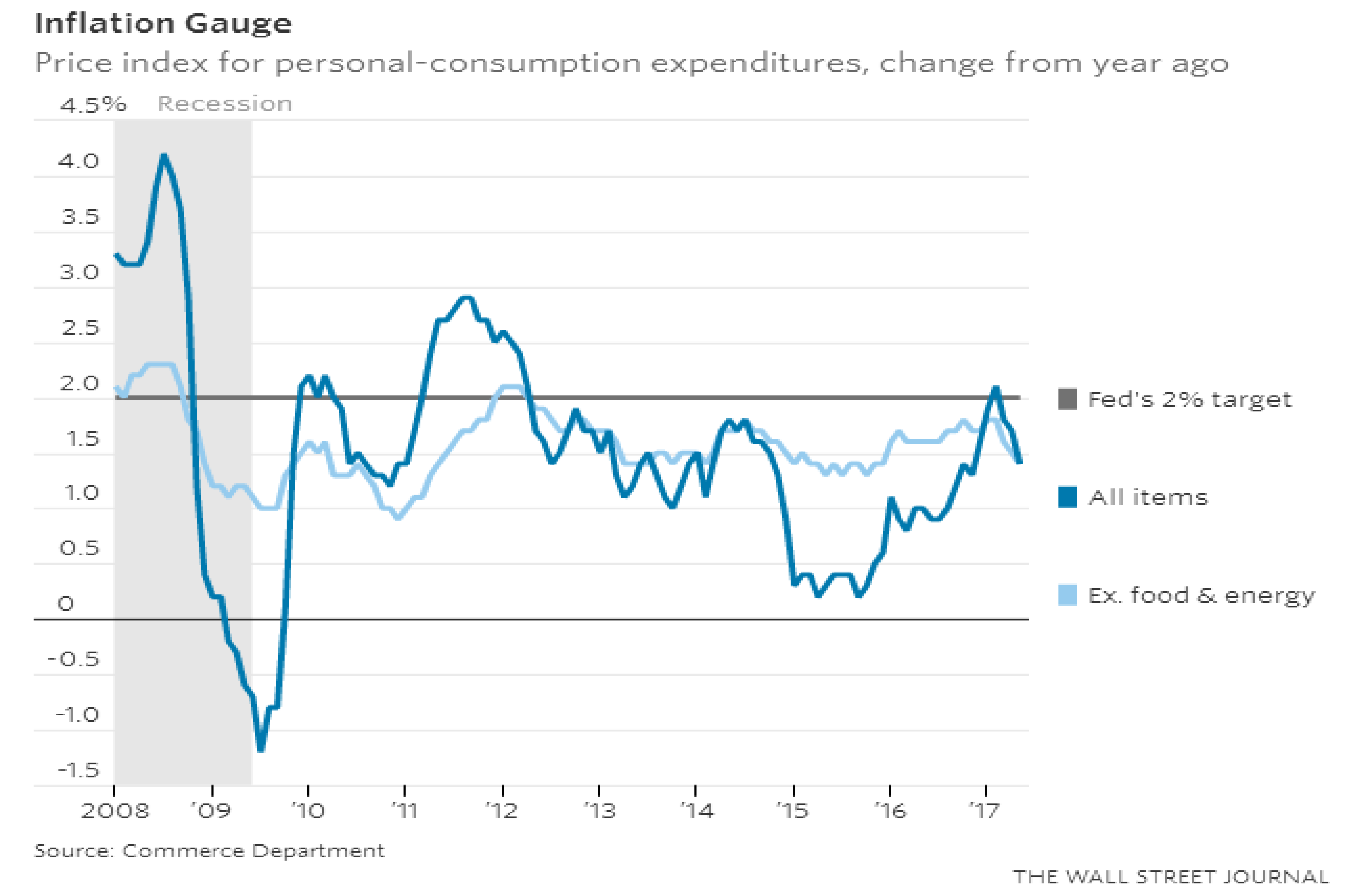


Source: BEA (http://www.bea.gov/newsreleases/national/gdp/gdp_glance.htm)

Long term problem that needs fixing – public debt (gross debt minus what the government owes itself (Medicare and social security trust funds, etc.) has reached 77% of GDP or about $15 trillion. Total debt is 104% of GDP, or $20 trillion

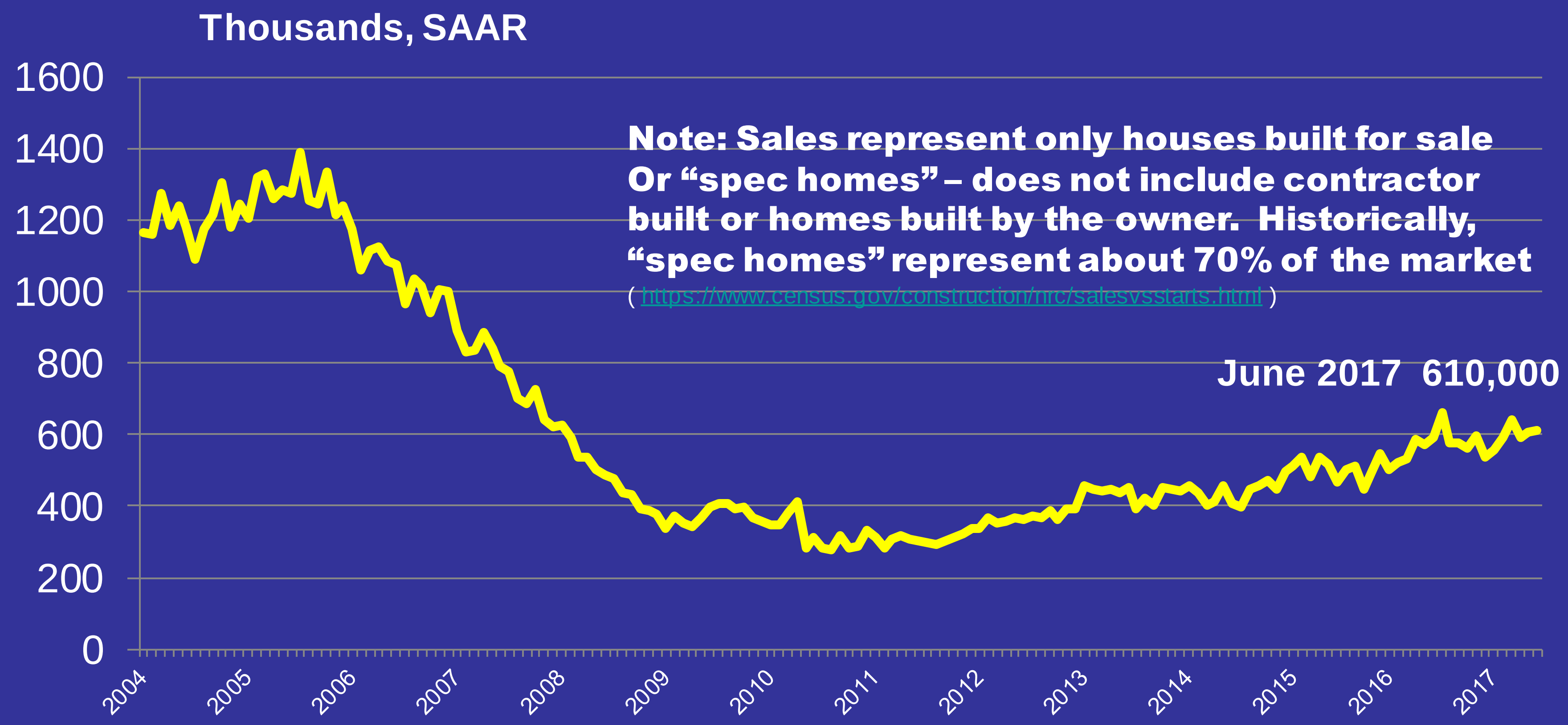


Little inflation despite "free money" for a decade. Why – weak demand and weak income growth – this is an indication of an economy in trouble – another possibility – traditional inflation metrics incorrectly measure impact of technology (e.g., cost reduction and/or benefits) -- i.e., maybe technology is keeping inflation down despite good economic growth?



Additional housing comments

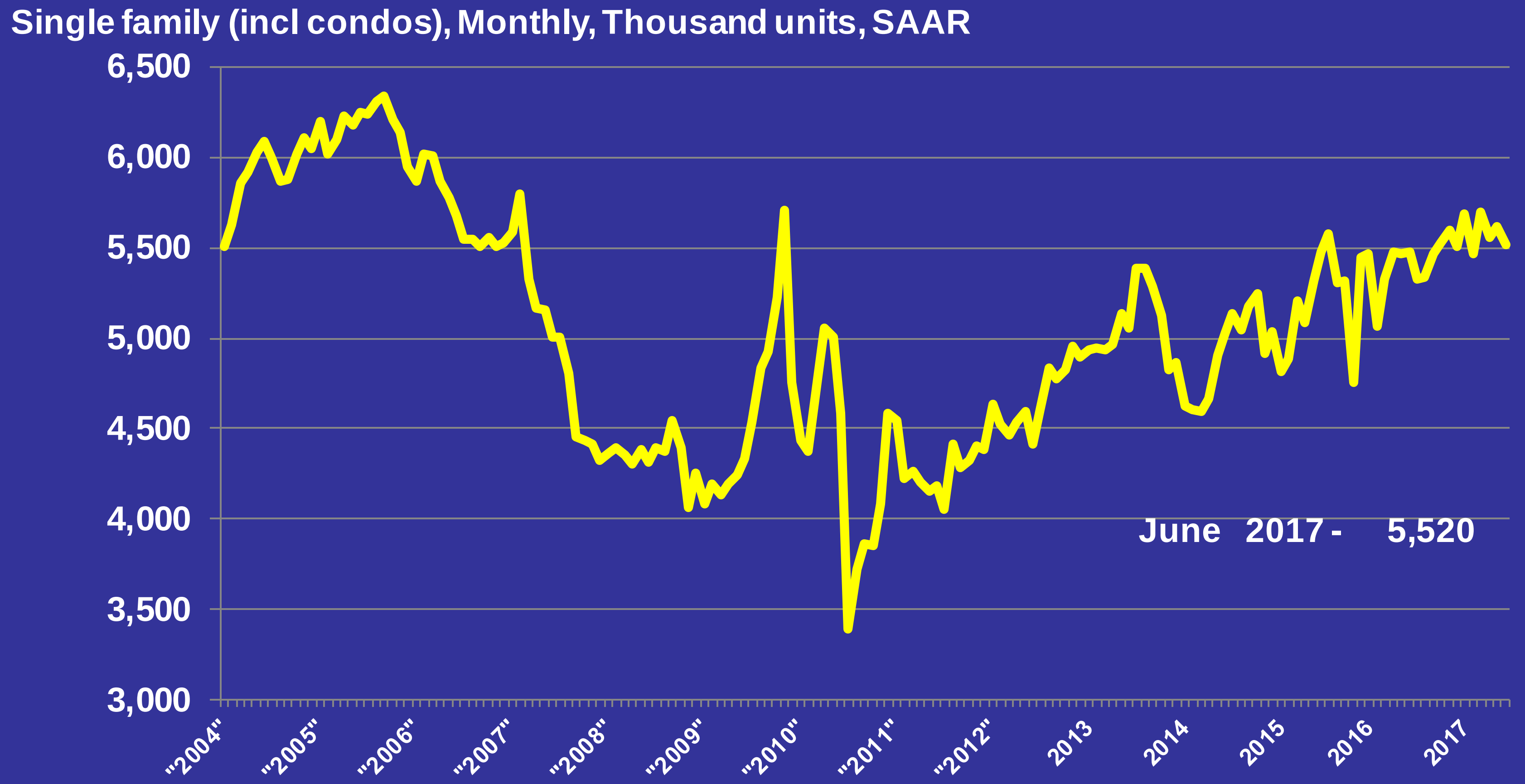
New Single Family Home sales are the key statistic to watch for wood products demand – Sales drive housing starts – this drives demand for wood products!



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

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 6.5%, annual basis - 62st consecutive monthly increase. Here is good report from NAR on 2016 totals***

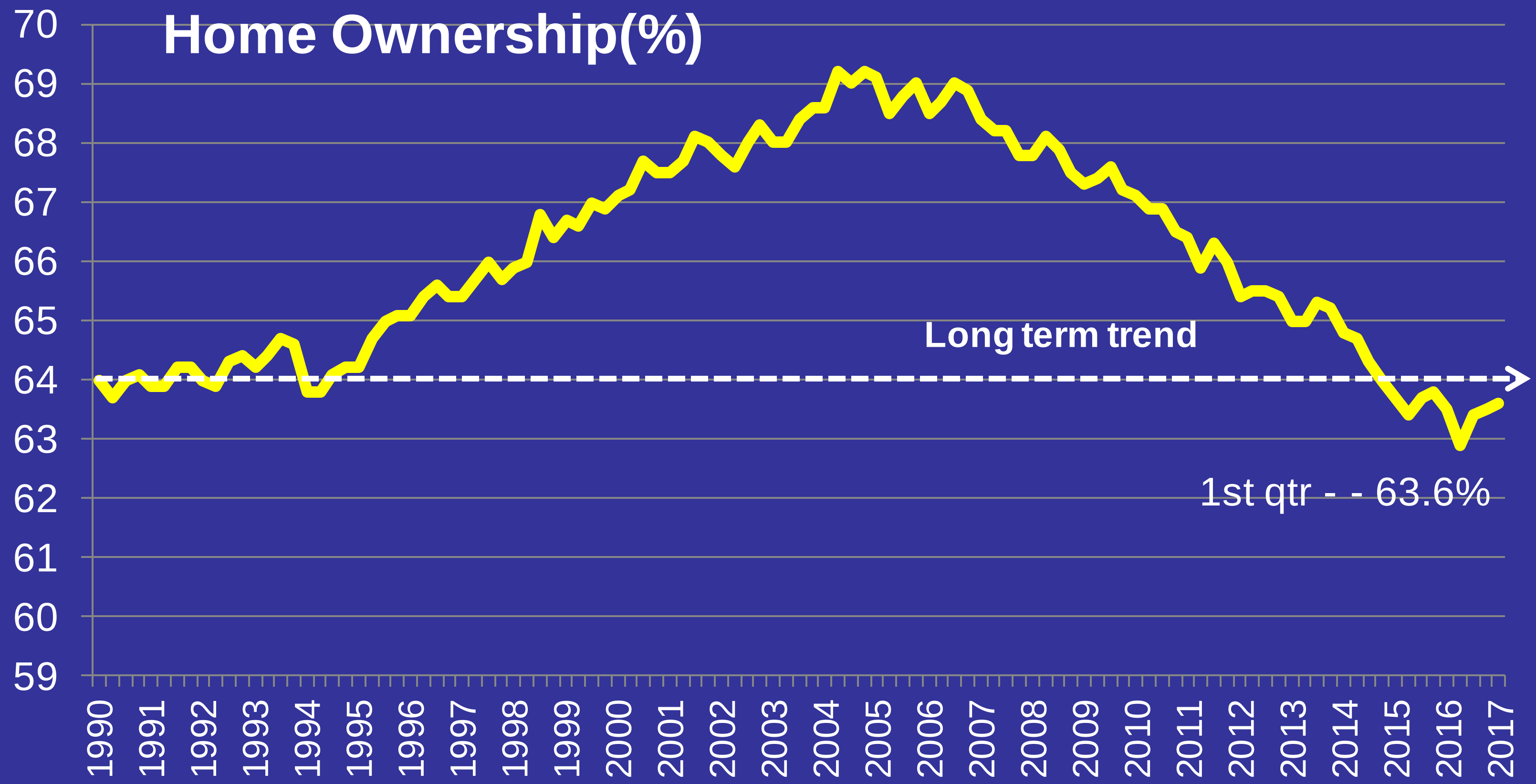
(https://www.nar.realtor/news-releases/2017/01/existing-home-sales-slide-in-december-2016-sales-best-since-2006)



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

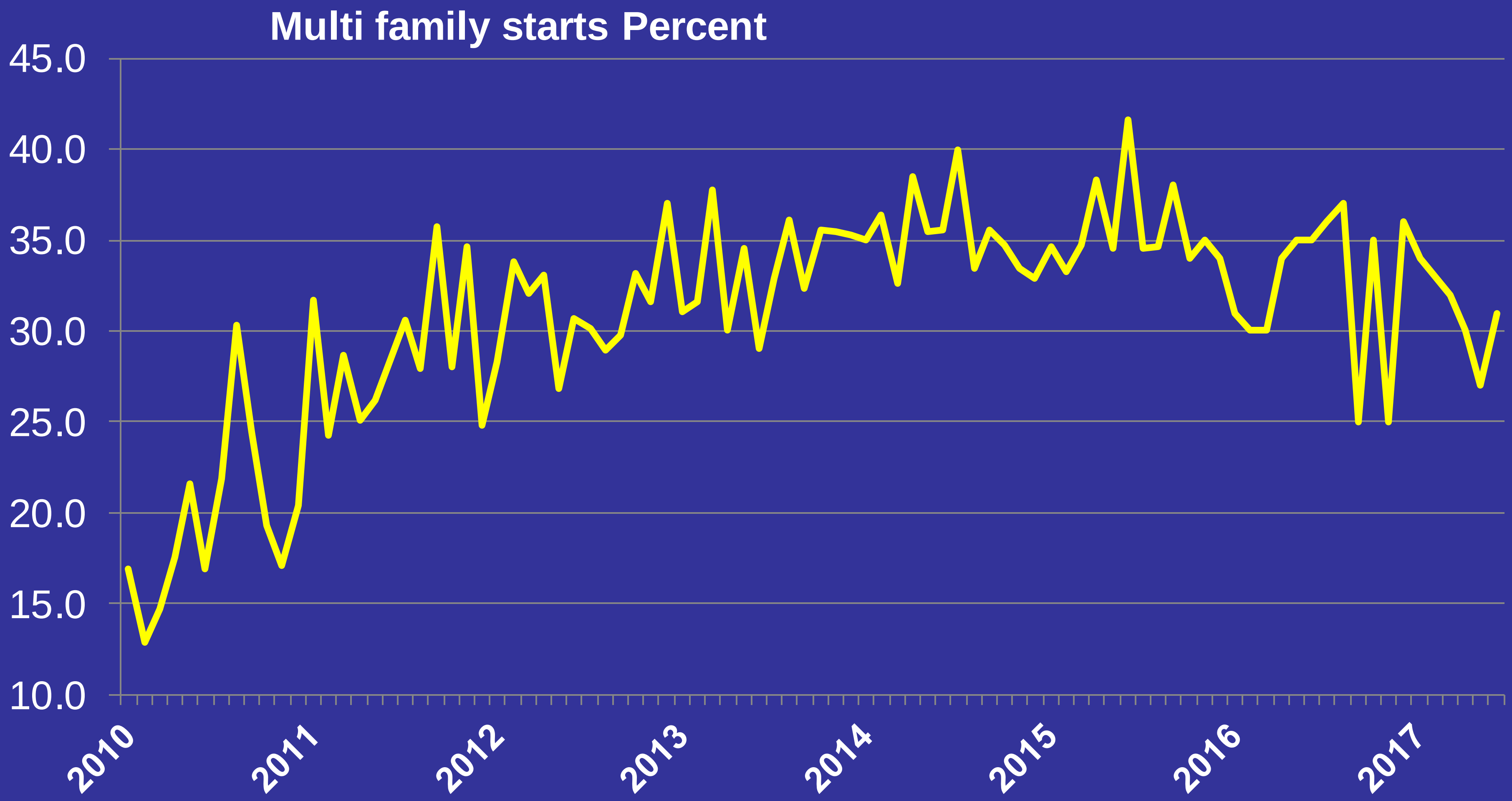
Falling homeownership rate has bottomed (?) – 1st qtr, new owner HH were 854,000 compared with 365,000 renters – reversing a decade long trend.

Homeownership lowest in 50 years



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

Multi family share of housing starts – upward trend has leveled off.

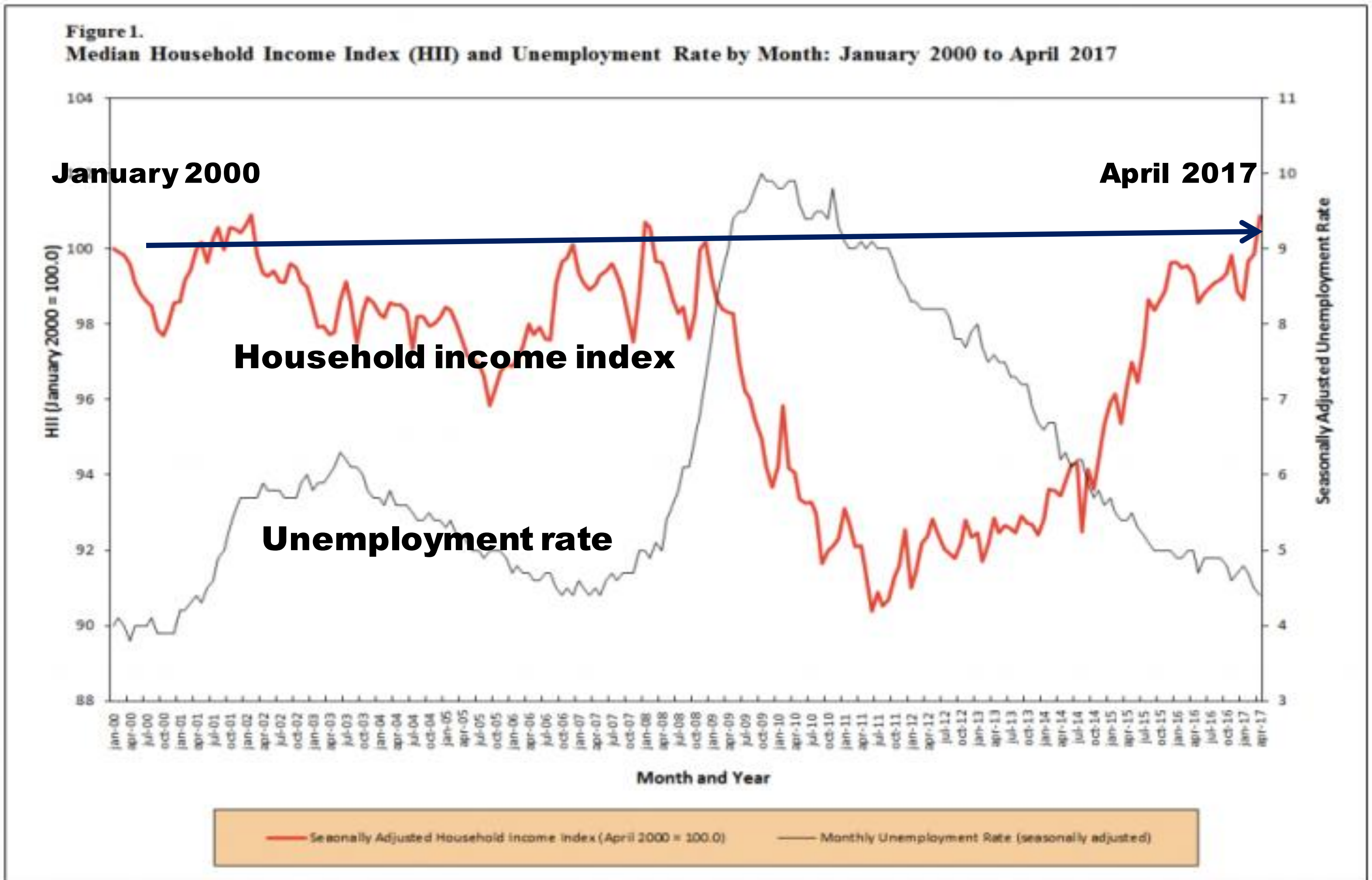


Source: Census

More News on the labor front

**Unemployment coming down,
but wages are not coming up.
That causes problems with housing affordability with house prices increasing faster than incomes!**

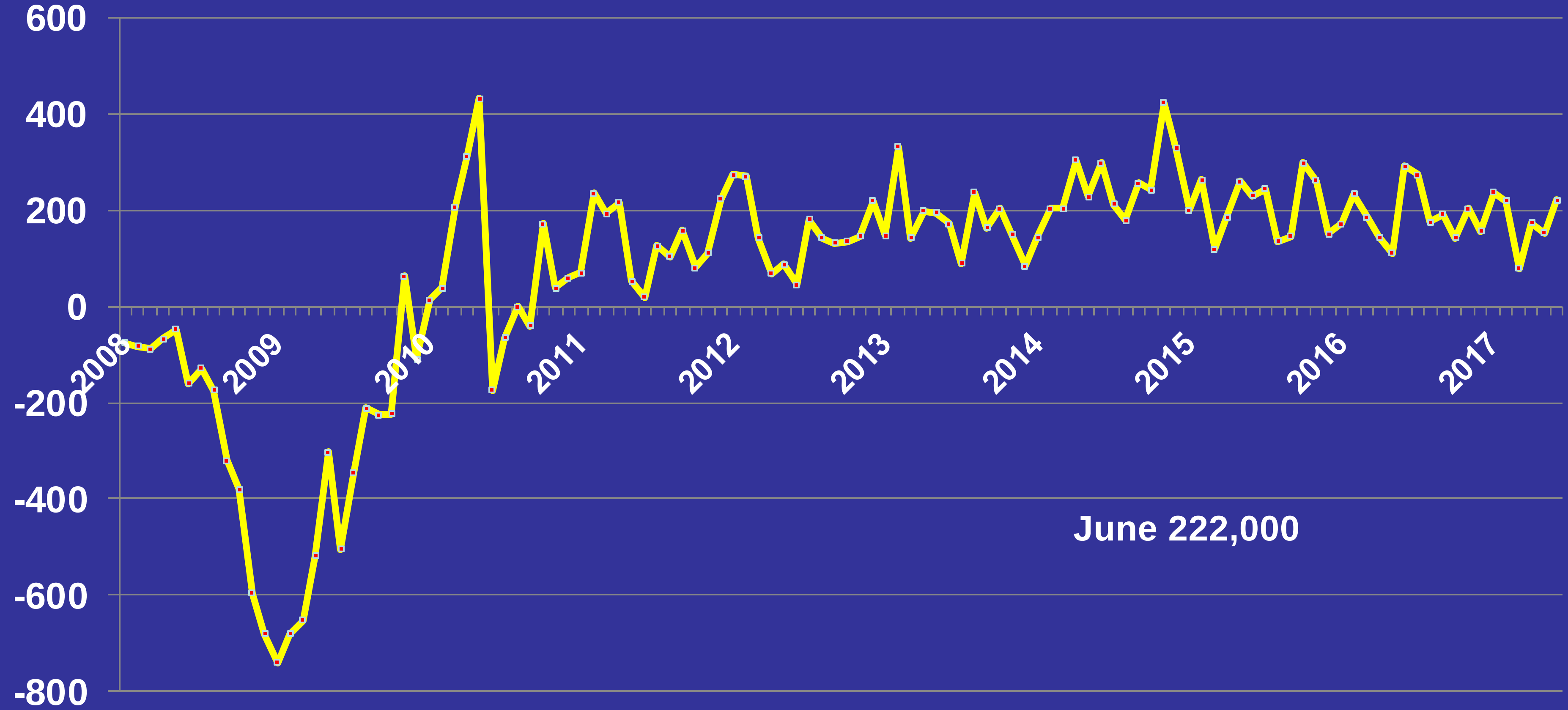
Long term trend - a disconnect between unemployment Rates and incomes. Problem - many of new jobs created Are low paying with little or no benefits. This is a structural problem with many high paying jobs that go unfilled Because applicants don't have the required skill set!!!!



Sources: For income data: Sentier Research, LLC estimates of annual household income derived from the monthly Current Population Survey (CPS) conducted by the U.S. Census Bureau; for the unemployment rate and the CPI-U: the U.S. Bureau of Labor Statistics.

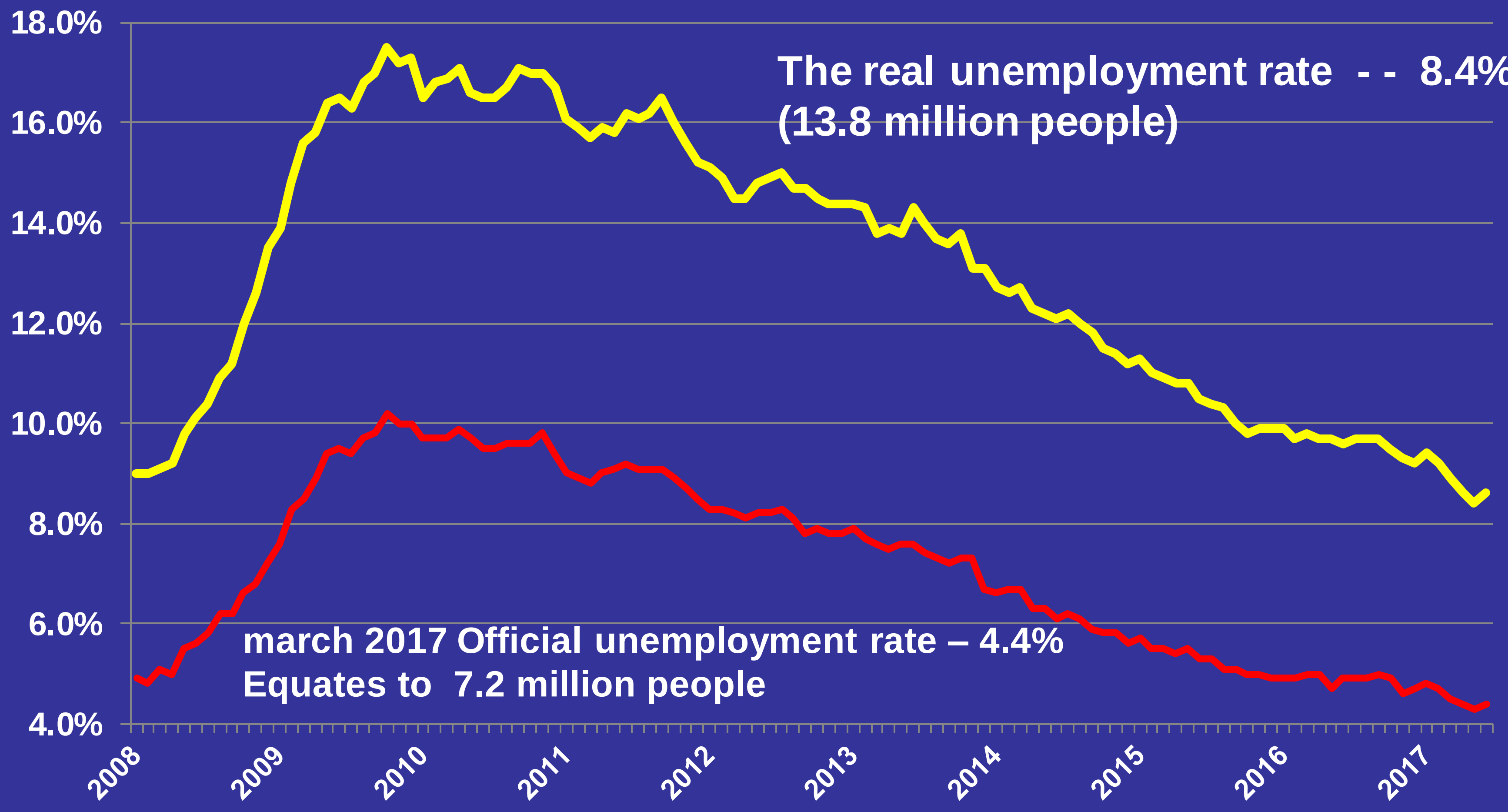
Employment situation – stuck around 200,000, and many of these jobs are part time with little or no benefits – not conducive to driving housing demand higher - *need to encourage innovation and investment in future - that means less government and more research*

Net change in non farm payrolls – monthly, thousands



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

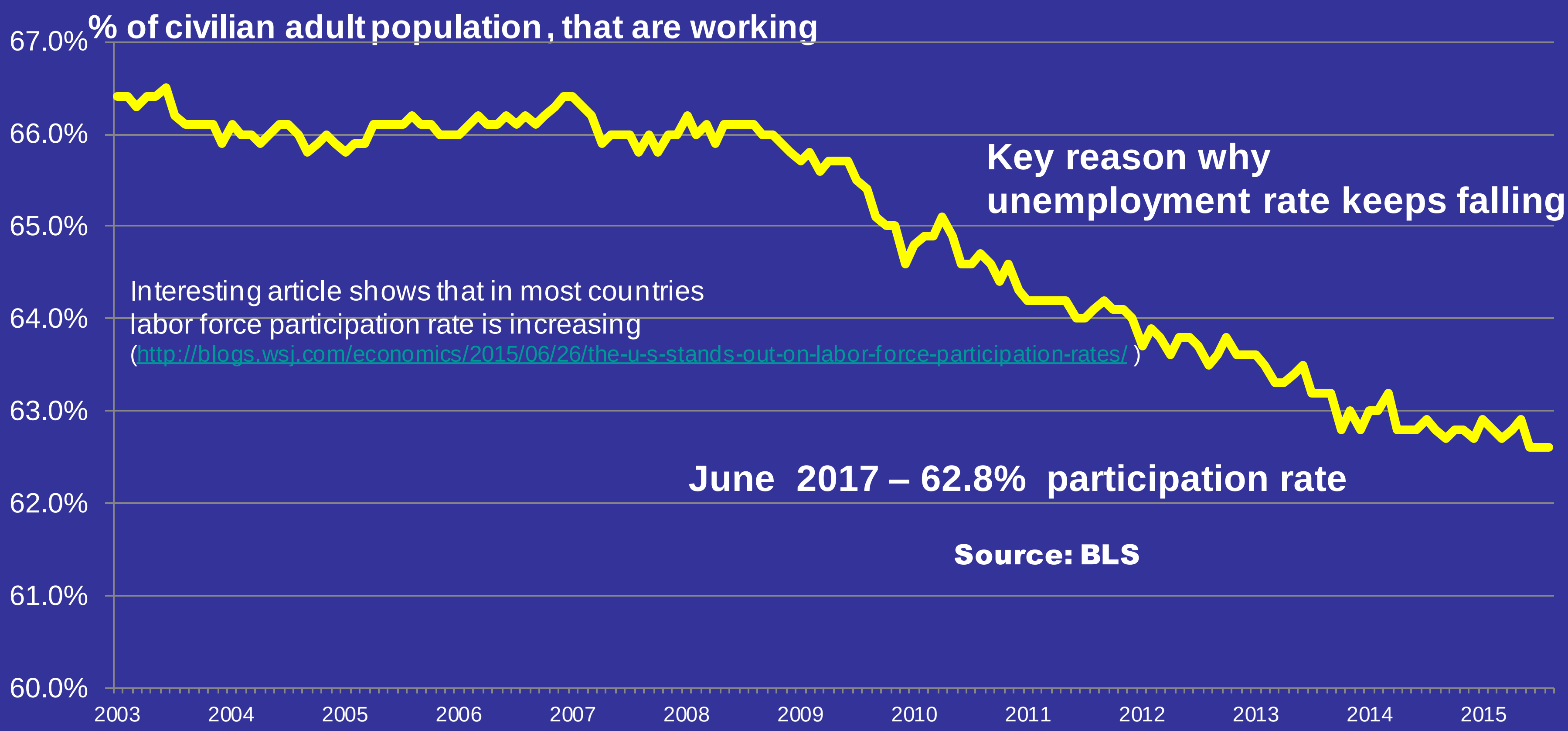
Unemployment rate keeps coming down – but, 5.2 million remain "underemployed" – working part time, but want full time jobs – another 1.6 million are "marginally attached" including 514,000 discouraged – total = 13.8 million including official 7 million unemployed



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 is improving (slowly) -- 2016 growth was 1.9% while 2017 expected to be about the same.

(2) Housing market is improving - 1st time buyers are returning – 1st Qtr 2017 percentage back to 42%, up from 30% in 2008! Will it continue?

(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

(5) Low rates have created housing bubbles in Canada, Australia, and equity bubbles here in USA - I hope the central banks have a solution?

(5) Leadership is a serious problem for our country – 2016 elections changed nothing – we're more divided than ever – little progress on key issues and this probably won't change until we realize that "we're all in this together"

(7) The fed finally increased rates in December, with two more in 2017. Low rates are not the solution to the 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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