

Economic Indicator — March 16, 2023

Housing Starts and Permits Jump in February

Multifamily Drove the Gain, but Single-Family also Improved

Summary

Residential Construction Picks Up in February

- Total housing starts jumped 9.8% to a 1.450 million-unit annual pace in February, ending a five-month streak of declines.
- February's gain is mainly owed to a 24.0% surge in multifamily construction, however, single-family starts also increased 1.1% in February.
- Multifamily starts are highly volatile month-to-month, however multifamily permits also surged in February. Permits leaped 21.1% over the month to a 747K annual pace, nearly reaching the recent cycle peak of 778K hit in December 2021.
- The surge in multifamily construction in February is likely to reignite concerns of a growing imbalance in the multifamily market. Concerns are warranted, however, the bulk of new multifamily construction is concentrated in the South and West, where strong population growth has generally led housing demand to outpace supply in recent years.
- The modest 1.1% improvement in single-family starts occurred against a backdrop of builders finding success with rate buy-downs and other incentives, as well as easing building material constraints.
- Single-family permits also notched a gain, posting their first monthly improvement in 12 months.
- The bulk of the improvement in single-family starts can be attributed to a 28.5% leap in the West, a region where housing activity has have been hit the hardest by rising interest rates.
- The gain in single-family permits was largely owed to a boost in activity in the South. A 9.8% jump in single-family permits in the South was responsible for roughly three-fourths of the total monthly gain.
- The National Association of Home Builders/Wells Fargo Housing Market Index (HMI) rose for the third straight month, jumping two points to 44 in March. Strengthening new home sales, low existing inventories, and successful incentive programs seem to be fueling the recent rise in builder optimism.

Economist(s)

Charlie Dougherty

Senior Economist | Wells Fargo Economics
Charles.Dougherty@wellsfargo.com | 212-214-8984

Jackie Benson

Economist | Wells Fargo Economics
Jacqueline.Benson@wellsfargo.com | 704-410-4468

Patrick Barley

Economic Analyst | Wells Fargo Economics
Patrick.Barley@wellsfargo.com | 704-410-1232

Single-Family Starts Improve Alongside Brightening Builder Sentiment

A jump in housing construction adds to the evidence that residential activity is starting to stabilize. Total housing starts jumped 9.8% in February, easily besting market expectations and reversing a five-month streak of declines. The upside surprise was mainly driven by a surge in multifamily starts, however, single-family starts also posted a 1.1% monthly gain.

The modest improvement in single-family starts occurred against a backdrop of builders finding success with rate buy-downs and other incentives, as well as easing building material constraints. The gain was also likely aided by seasonal factors, with much of the country experiencing abnormally warm weather in both January and February.

The bulk of the improvement in single-family starts can be attributed to a 28.5% leap in the West, which is the largest monthly increase in the region since May 2020. Housing activity in the West has been hit especially hard by the move higher in interest rates. Despite the monthly gain, single-family starts in the West are running 45.1% below the pace registered in February 2022. The Northeast was the only other region to register an increase, with starts rising 8.6% month-over-month. The South and Midwest recorded 4.7% and 8.1% declines in single-family starts, respectively.

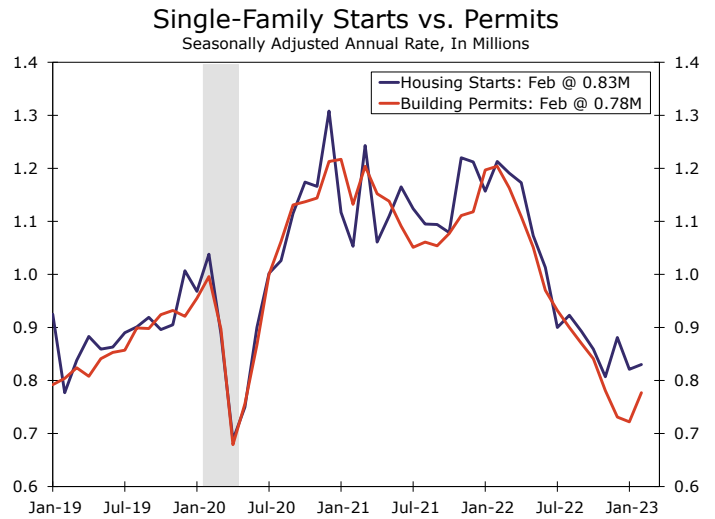
The recent uptick in builder confidence seems to have stopped the slide in single-family permits. Single-family permits posted their first monthly gain in 12 months, surging 7.6% in February. A 9.8% monthly increase in the South was responsible for roughly three-fourths of the total jump. The West and Midwest also registered notable gains of 7.6% and 10.9%, respectively. The Northeast was the only region to record a decline, where single-family permits dropped 14.5% over the month.

Multifamily Construction Continues to Run at Robust Pace

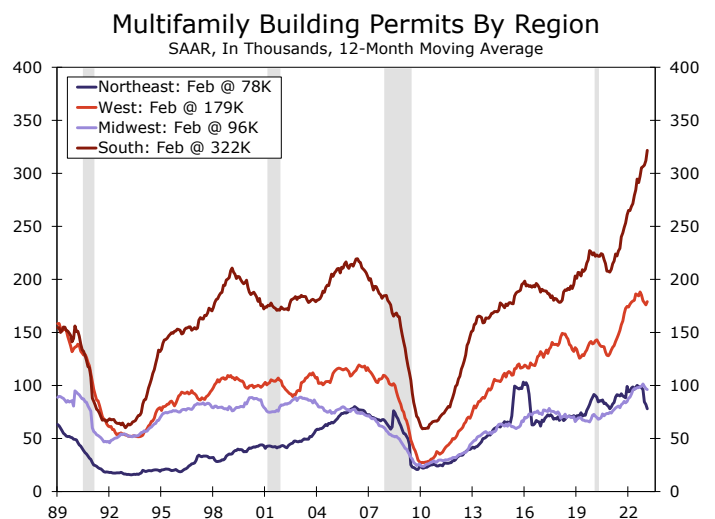
The modest gain in single-family activity is encouraging. However, the gain in overall activity during February appears to be owed to a jump in multifamily construction. Multifamily starts jumped 24% to a 620K-unit pace during the month, the strongest pace since April 2022. Multifamily construction is highly volatile on a monthly basis. For example, starts rose sharply in the Midwest region after plunging in January. Meanwhile, the South and West posted solid gains and the Northeast registered a decline.

That said, there was also surge in multifamily permits during the month. Multifamily permits soared 21.1% in February, rising to a 747K-unit pace. The pace in permits in February is close to the recent cycle peak of 778K, reached in December 2021. The overall gain in multifamily permits was attributed to a step-up in the South and West regions, where permits are now running at the strongest pace on records dating back to 1991.

Monthly volatility aside, the bounce in multifamily construction during February will certainly reignite concerns that the multifamily market is in danger of becoming unbalanced with new supply outstripping demand. During February, the count of new multifamily units currently under construction rose to 957K, the highest level since 1973. As noted above, however, the increase in



Source: U.S. Department of Commerce and Wells Fargo Economics



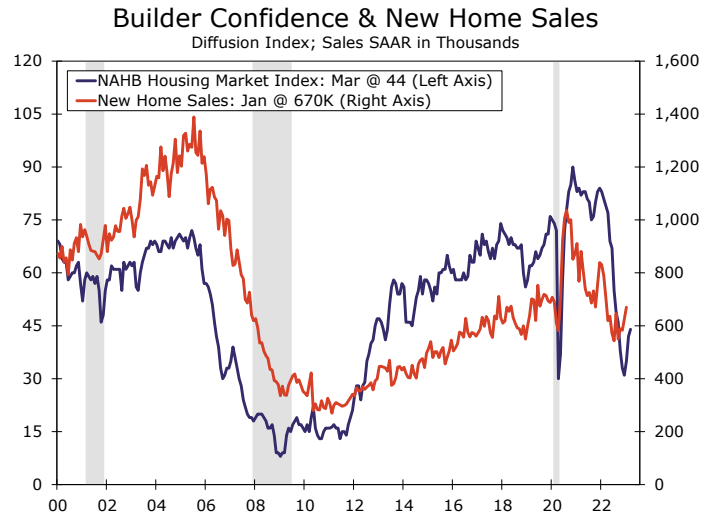
Source: U.S. Department of Commerce and Wells Fargo Economics

new multifamily construction is mostly centered in the South and West, regions where new demand has outpaced supply in recent years thanks to migration inflows and generally strong population growth.

Builder Sentiment Improves as Buyer Traffic Returns

Builder sentiment continued to improve in March. The National Association of Home Builders/Wells Fargo Housing Market Index (HMI) rose for the third straight month, increasing to a reading of 44 from 42 the month prior. The trend improvement suggests home builders are regaining confidence as buyer traffic returns. The improvement in the headline index was driven by the present sales component rising two points to 49 and prospective buyer traffic rising three points to 31.

The outlook remains uncertain, however. The future sales component, which measures sales expectations six months from now, inched down one point to 47. An uptick in new home sales seems to be fueling builder optimism as low inventories of existing homes as well as successful use of incentives and discounts has shifted demand towards new construction. Although high construction costs continue to pose an issue, price growth has slowed substantially. The Producer Price Index for residential construction inputs turned negative for the first time since May 2020, falling to -2.2% in February on a year-over-year basis.



Source: NAHB, U.S. Department of Commerce and Wells Fargo Economics

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Economics Group

Jay H. Bryson, Ph.D.	Chief Economist	704-410-3274	Jay.Bryson@wellsfargo.com
Sam Bullard	Senior Economist	704-410-3280	Sam.Bullard@wellsfargo.com
Nick Bennenbroek	International Economist	212-214-5636	Nicholas.Bennenbroek@wellsfargo.com
Tim Quinlan	Senior Economist	704-410-3283	Tim.Quinlan@wellsfargo.com
Sarah House	Senior Economist	704-410-3282	Sarah.House@wellsfargo.com
Azhar Iqbal	Econometrician	212-214-2029	Azhar.Iqbal@wellsfargo.com
Charlie Dougherty	Senior Economist	212-214-8984	Charles.Dougherty@wellsfargo.com
Michael Pugliese	Senior Economist	212-214-5058	Michael.D.Pugliese@wellsfargo.com
Brendan McKenna	International Economist	212-214-5637	Brendan.Mckenna@wellsfargo.com
Jackie Benson	Economist	704-410-4468	Jackie.Benson@wellsfargo.com
Shannon Seery	Economist	332-204-0693	Shannon.Seery@wellsfargo.com
Nicole Cervi	Economic Analyst	704-410-3059	Nicole.Cervi@wellsfargo.com
Jessica Guo	Economic Analyst	212-214-1063	Jessica.Guo@wellsfargo.com
Karl Vesely	Economic Analyst	704-410-2911	Karl.Vesely@wellsfargo.com
Patrick Barley	Economic Analyst	704-410-1232	Patrick.Barley@wellsfargo.com
Jeremiah Kohl	Economic Analyst	704-410-1437	Jeremiah.J.Kohl@wellsfargo.com
Coren Burton	Administrative Assistant	704-410-6010	Coren.Burton@wellsfargo.com

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