Economic Indicator — March 1, 2024

Construction Spending Slipped in January

Residential Gain Not Enough to Offset Drop in Nonresidential

Summary

Construction Spending Weakened to Start 2024

Total construction spending declined 0.2% during January. The drop appears partially owed to harsh winter weather that much of the nation experienced during the month. That noted, January's weakness was concentrated in the nonresidential category. Although manufacturing project spending once again rose, educational, retail, warehouse and lodging construction all declined notably. Considering commercial construction starts have downshifted sharply over the past year alongside uncertain demand prospects, higher interest rates and reduced credit access, further declines in nonresidential spending in the months ahead would not be surprising. By contrast, residential spending rose solidly in January thanks in large part to another gain in single-family outlays. Home builders look to be increasingly encouraged by low resale supply as well as the prospect for a soft landing and lower financing costs on the horizon. Meanwhile, the recent downturn in multifamily starts now appears to be weighing on spending.

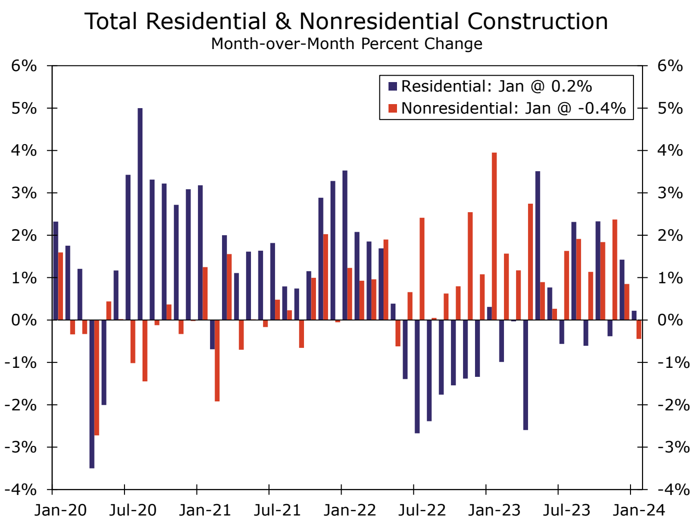
Economist(s)

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

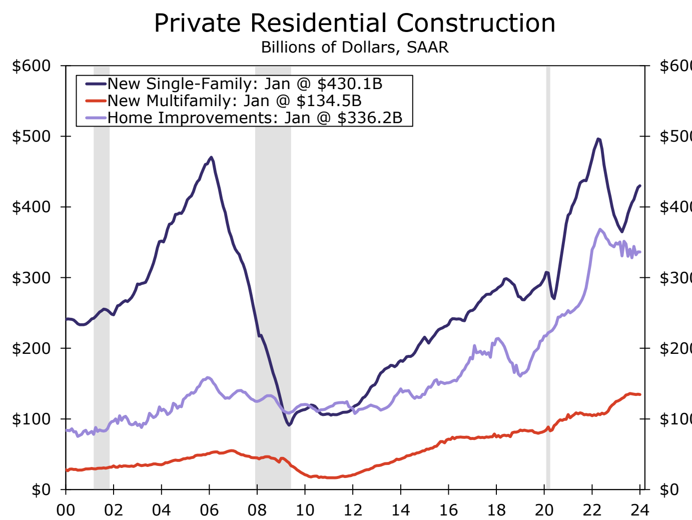
Patrick Barley
Economic Analyst | Wells Fargo Economics
Patrick.Barley@wellsfargo.com | 704-410-1232

Single-Family Continues to Carry Residential Spending

- Total construction surprised to the downside, falling 0.2% in January as winter weather suppressed activity across the country. The monthly slowdown stemmed from weaker nonresidential and multifamily outlays.
- Residential outlays ticked up 0.2%, driven entirely by a pick-up in single-family spending which rose 0.6% over the month. Single-family spending has improved for nine consecutive months as home builders look to fill the home supply gap left by a tight resale market.
- Multifamily spending slipped 0.6%, the fourth decline in the past five months. Multifamily construction has pulled back in the face of rising apartment vacancy rates and a near-record number of apartment units under construction. We suspect multifamily outlays will continue to soften going forward as the count of new projects dwindles and builders work through and complete existing projects.
- Home improvement outlays were essentially flat over the month but are down 3.7% year-over-year. Higher interest rates has chilled spending on home renovation. Reflected in consumer spending, retail sales for building and gardening materials are down 8.3% year-over-year as of January.



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

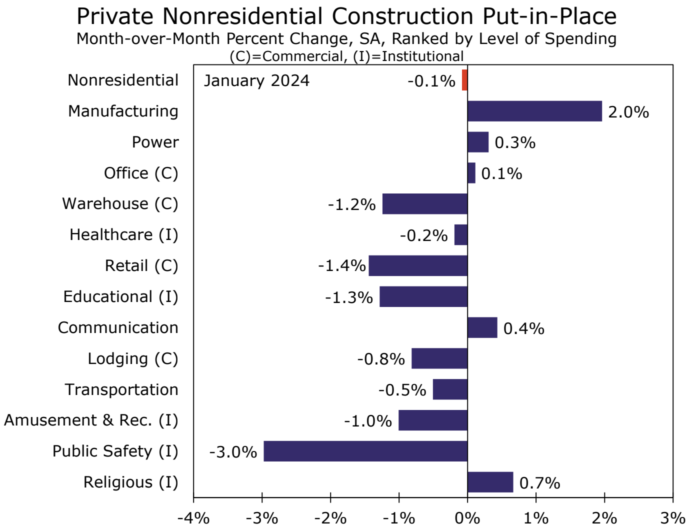


Source: U.S. Department of Commerce and Wells Fargo Economics

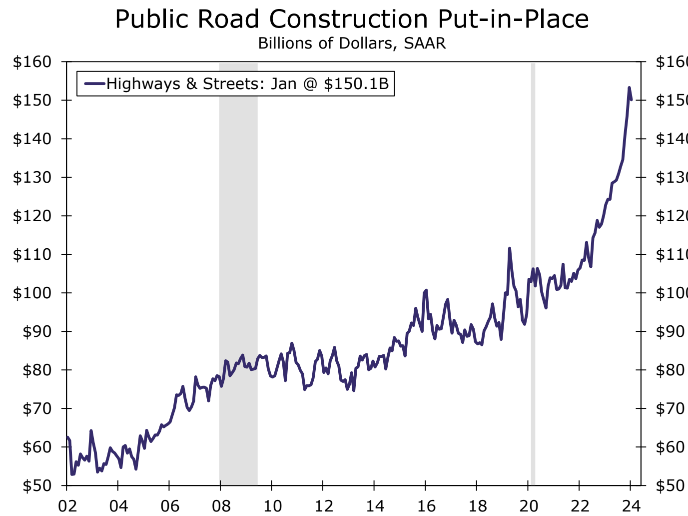
Nonresidential Looks to be Losing Momentum

- Total nonresidential spending declined 0.4% during January. Public and private nonresidential outlays both fell during the month, although the drop in the public category was more pronounced. On balance, total nonresidential spending has moderated in recent months. The 17.1% year-over-year gain posted in January marks the softest annual gain since February 2023.
- Commercial construction looks to be pulling back and dragging down overall spending. As displayed in the below chart, private retail, warehouse and lodging outlays registered declines during January. The pullback is mostly owed to tighter bank lending, higher financing costs and uncertain demand prospects.
- Private office spending rose slightly in January. Considering the acute drop in new office construction since the pandemic and rise of hybrid work, the improvement was likely owed to rising data center construction, which the Census includes as part of the office category.
- Private educational and healthcare outlays also declined to start off 2024. On trend, however, both of these spending categories have risen strongly over the past few years alongside the need to update and expand existing facilities in the wake of the pandemic.
- Although the pace has moderated, manufacturing project outlays rose another 2% in January. The robust gain was the result of upturns in the computer/electronic/electrical and transportation equipment sectors, which reflect the ongoing build out of electric vehicle supply chains and semiconductor plants. Given the support from federal spending packages such as the Chips and Science Act and the Inflation Reduction Act, manufacturing project outlays are likely to rise in the years ahead.

- Public spending should continue to rise as projects stemming from the Infrastructure and Jobs Act roll out over the next few years. That said, public spending pulled back 0.9% in January. The large highway and street category, where projects are more easily disrupted by unfavorable weather conditions, dipped 2.1% during the month. Most other public works categories declined to start the year.



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



Source: 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 Grein	Economist	704-410-0369	Shannon.Grein@wellsfargo.com
Nicole Cervi	Economist	704-410-3059	Nicole.Cervi@wellsfargo.com
Patrick Barley	Economic Analyst	704-410-1232	Patrick.Barley@wellsfargo.com
Jeremiah Kohl	Economic Analyst	212-214-1164	Jeremiah.J.Kohl@wellsfargo.com
Aubrey George	Economic Analyst	704-410-2911	Aubrey.B.George@wellsfargo.com
Delaney Conner	Economic Analyst	704-374-2150	Delaney.Conner@wellsfargo.com
Anna Stein	Economic Analyst	212-214-1063	Anna.H.Stein@wellsfargo.com
Coren Burton	Administrative Assistant	704-410-6010	Coren.Burton@wellsfargo.com

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