Economic Indicator — April 23, 2024

New Home Sales Bounce Back in March

Higher Rates and Rising Resale Supply Emerge as New Headwinds for Builders

Summary

New home sales jumped 8.8% to a 693K-unit pace in March, the strongest pace since September 2023. Although the report was accompanied by downward revisions to sales in February, on balance, the pace has strengthened on trend so far to start the year. New home sales should continue to gradually improve with a sturdy macroeconomic backdrop and structural affordability and availability constraints in the resale market remaining as tailwinds. That noted, higher interest rates and rising existing supply could weigh on the new home market moving forward.

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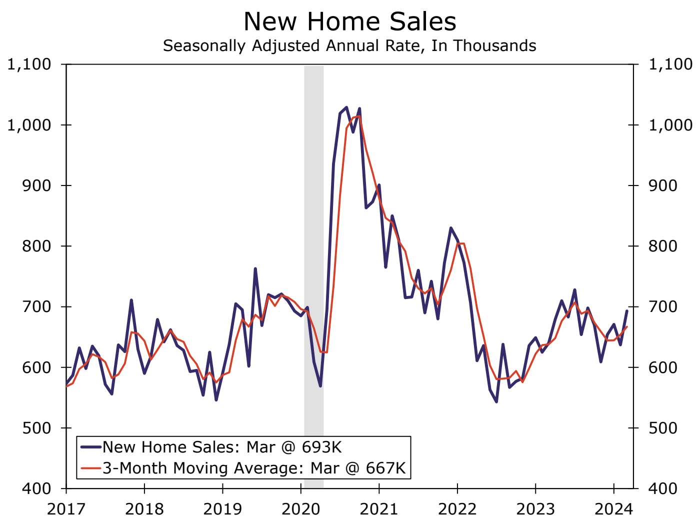
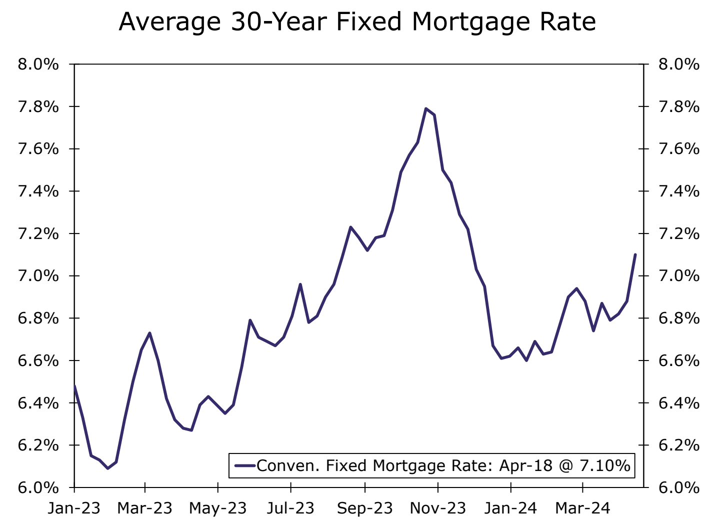
New Home Sales Rebound

- New home sales rebounded 8.8% to a 693K-unit pace during March. Even with February sales revised considerably lower, the pace of sales has averaged 667K so far this year, which represents a 4.5% improvement from the pace averaged in the same quarter last year and a 3.5% rise from Q4-2023's pace.
- The upturn in new home sales over the past year despite higher interest rates largely reflects builders' ability to offset eroding housing affordability conditions through price discounts, mortgage rate buy-downs and other incentives. A scarcity of available existing homes for sale and emergence of the "build-to-rent" market have been other factors supporting demand.
- These factors have allowed the new home market to digest the higher interest rate environment relatively well. A recent spike in Treasury yields on the back of new inflation and monetary policy uncertainty will test the mettle of both buyers and builders in the months ahead, however.
- During the week ending April 18th, the average 30-year mortgage rate stood at 7.1% according to Freddie Mac, up from 6.9% the previous week. The up-tick represents the latest step-back for housing affordability, and discouraged buyers may move back to the sidelines as a result. Larger home builders may increase the use of pricing incentives to attract buyers, but not every builder has the ability to lean on lower prices or rate-buy downs to boost sales. Higher financing costs also stand to raise the cost of construction for builders, which could also limit the use of incentives.
- Rising inventory levels in the existing market are another potential headwind. Existing supply remains tight, yet more resale options for buyers could cut into demand for new homes.



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

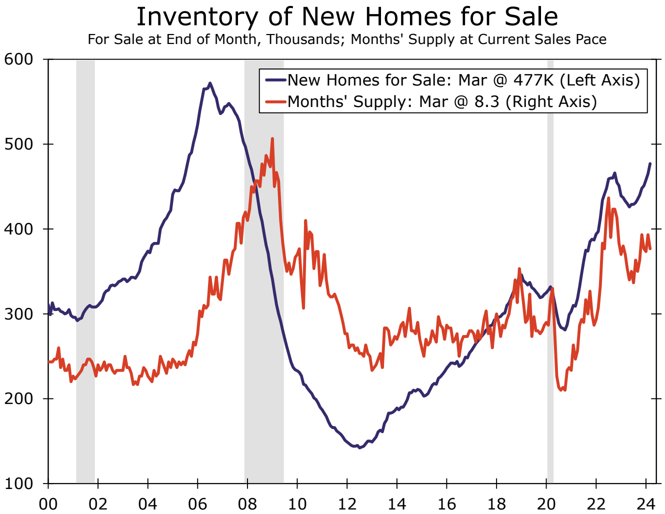


Source: Freddie Mac and Wells Fargo Economics

New Home Supply Pipeline Remains Robust

- Looking ahead, economic growth appears poised to remain resilient in the near-term, which should foster a gradually improving pace of new home sales this year. What's more, despite recent shifts, new home demand is likely to remain solid given structural affordability and availability constraints in the resale market.
- Ample inventory remains a key advantage for the new home market. The count of new homes for sale at the end of March rose to 477K from 465K, the eighth consecutive monthly increase. Month's supply of inventory fell to 8.3 from 8.8 on account of the faster overall sales pace.
- Completed homes are accounting for an increasing share of new home inventory. After falling to an all-time low 8% share in 2022, the share of new homes completed in inventory has climbed back to 19% as of March. This is still below the pre-COVID average of 29% but is indicative of builders having more completed inventory on hand which is helping to drive inventory growth.
- If mortgage rates continue to creep up, builders may be forced to step up the use of incentives. Builders pulled back from offering price cuts earlier this year as mortgage rates seemed to stabilize below 7%, but as of April, average lending rates have once again breached the 7% mark. According to the NAHB, just 22% of builders reported cutting prices in April, down from 24% in March and 36% in December.

- The pullback on price cuts is one likely factor that contributed to the jump in the median new home sale price in March, which rose 6% over the month to reach $430,700. The median sale price is sitting at a seven-month high and is down just 1.9% over the year.



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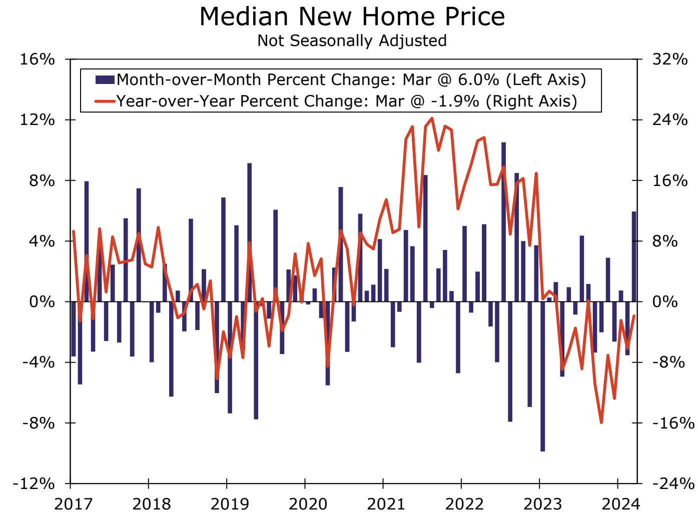

Source: U.S. Department of Commerce and Wells Fargo Economics

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