

Economic Indicator — September 18, 2024

Housing Starts Climb in August

Lower Mortgage Rates Improve Builder Outlooks

Summary

Fed Easing to Favor Residential Construction

Lower mortgage rates and the anticipation for substantial Fed easing in the coming months appears to be brightening the outlook for residential construction. Housing starts rose 9.6% in August, driven entirely by a surge in single-family building. August's gain prompted a 3.9% annual increase in overall starts, the first year-over-year improvement since April. As builder confidence brightens in anticipation of higher sales traffic, single-family permits also notched their second sequential uptick. Meanwhile, the multifamily market is still searching for balance. Although apartment demand has firmed notably this year, it remains below the lofty pace of new development, prompting a trend decline in new multifamily projects. Despite a notable improvement in August, multifamily starts were still down over 30% on a year-to-date basis.

As the Fed starts easing, lower financing costs should provide a boost to both the single-family and multifamily sectors. That said, elevated rates, weakening labor market conditions and substantial construction already underway will likely to limit the scope for a residential rebound.

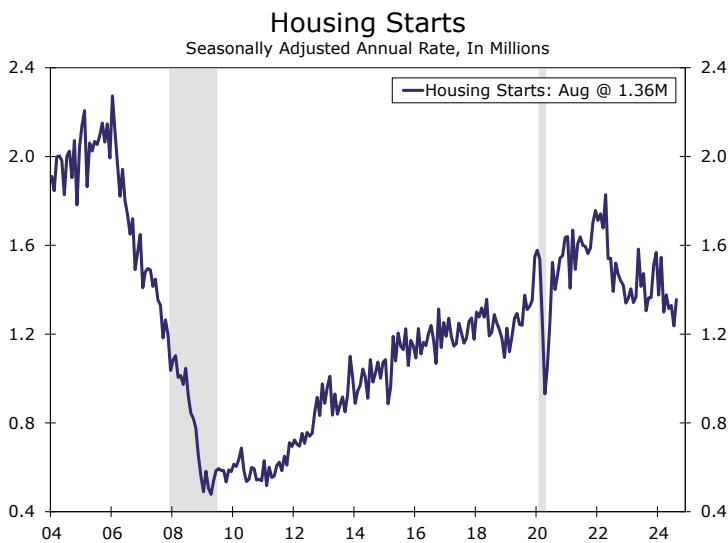
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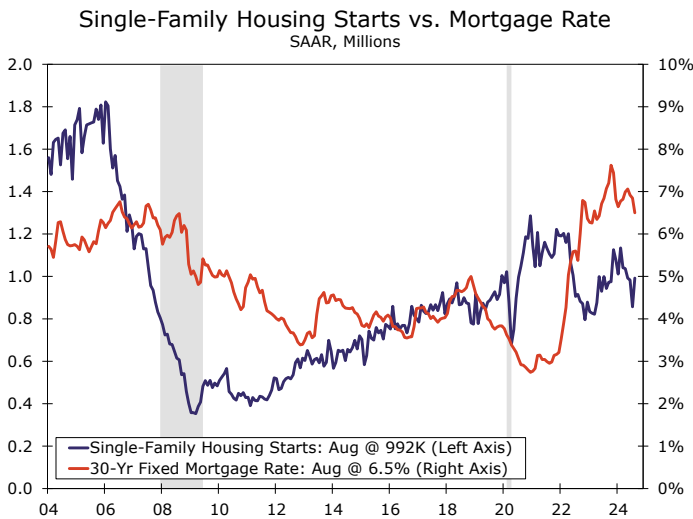


Source: U.S. Department of Commerce and Wells Fargo Economics

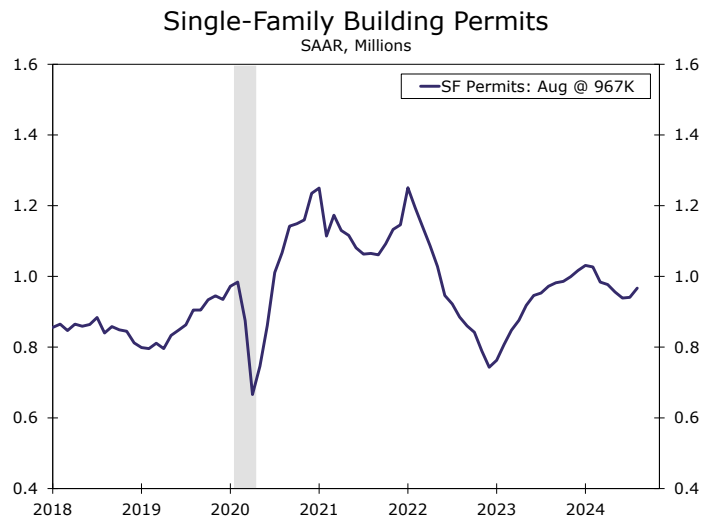
Single-Family Building Perks Up

A drop in mortgage rates appears to have sparked a bounce in both builder confidence and single-family construction. Single-family starts rose 15.8% in August, marking the first improvement in six months.

- A notable upshift in permits also signals the beginnings of a potential turnaround in single-family construction. Single-family permits rose for the second consecutive month in August following a five-month string of declines. The 2.8% uptick in permits marked the largest monthly increase in over a year.
- The Federal Reserve has signaled that it will begin easing policy this afternoon. As markets price in a greater probability of substantial interest rate cuts on the horizon, mortgage rates have retreated in kind. The 30-year fixed mortgage rate averaged 6.2% the week ending September 12, down 75 bps from early July and the lowest rate in 19 months.
- Mortgage rates likely have further to fall this easing cycle. Conditions appear favorable for residential construction to improve next year as buyers reemerge in search of lower financing costs. That said, significant headwinds remain. Mortgage rates remain historically elevated even as they claw back from recent highs, and elevated new home supply is another factor that may hold back new construction in the coming months.
- Labor market deterioration will also likely pose a challenge. If job growth slows and the unemployment rate rises through year-end like we currently expect, weaker income growth may limit the scope for a residential rebound.
- September's NAHB Housing Market index increased two points in September following four consecutive months of decline. All three components of the index increased, with sales expectations over the next six months rising the most. This improvement suggests that builders are generally optimistic about lower mortgage rates revitalizing buyer interest.



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



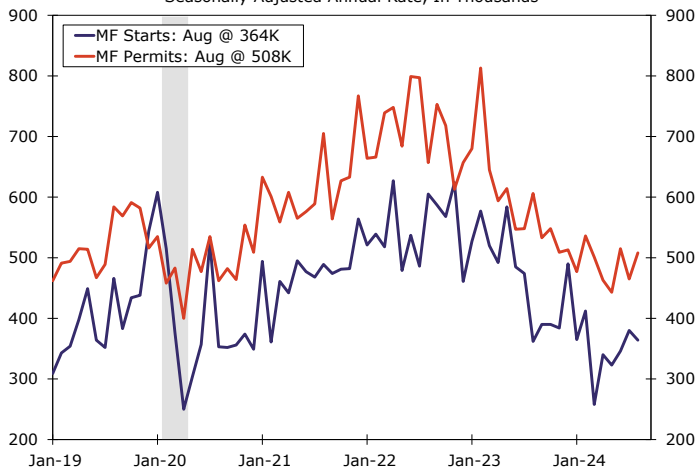
Source: U.S. Department of Commerce and Wells Fargo Economics

Multifamily Conditions Still Soft

- Multifamily starts dipped 4.2% in August, partially reversing the prior month's robust gain. Through the monthly volatility, the pace of multifamily development remains rather tepid with starts down over 30% on a year-to-date basis through August.
- Multifamily permits posted the second improvement over the last three months in August but similarly remain weak overall, a byproduct of substantial multifamily supply already under construction. Multifamily completions in August rose to their highest level on record dating back to 1985, most of which were delivered in the South.
- Although still elevated, the count of multifamily units under construction continues to slowly recede as builders pull back on new projects, dropping to 867K in August.
- Looking ahead, lower financing costs also appear likely to incentivize more multifamily building. Firmer apartment demand spurred by poor affordability conditions in the housing market is another tailwind. Although we expect the pace of multifamily construction to improve over the next couple of years, the elevated construction pipeline will likely keep a lid on new development.

Multifamily Starts vs. Permits

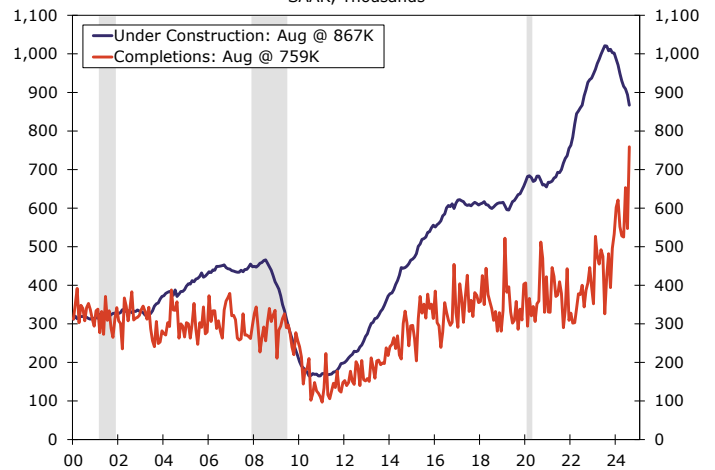
Seasonally Adjusted Annual Rate, In Thousands



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

Multifamily Construction & Completions

SAAR, Thousands



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

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