

Economic Indicator — September 19, 2023

# Housing Starts Declined in August

## Higher Interest Rates Intensify the Headwinds for Residential Construction

### Summary

#### Single and Multifamily Starts Both Fell Sharply in August

Total housing starts dropped 11.3% to a 1.28 million-unit pace in August. The monthly decline was broad-based, with single-family and multifamily starts falling by 4.3% and 26.3%, respectively. The surprising pull-back in starts stands in contrast to a strong gain in both single-family and multifamily building permits.

The below-consensus housing starts number is a reminder of the month-to-month volatility of residential construction data and is likely more noise than signal. That said, the drop in August should not be completely written off. The recent leg-up in borrowing costs will certainly test builders' ability to lean on incentives to sell homes. Builders have thus far navigated the higher rate environment relatively well, mostly thanks to greater pricing flexibility. As mortgage rates have risen, many builders have successfully offered rate buy-downs and price discounts to incentivize affordability-crunched buyers. However, not every builder has the ability to offer such incentives and thus are more sensitive to upward changes in mortgage rates.

A second consecutive pullback in builder sentiment suggests builders may be starting to reassess plans to scale up production in light of the recent rise in 30-year mortgage rates, which are now hovering above 7%. The NAHB Housing Market Index fell to 45 in September, the lowest reading since April.

Economist(s)

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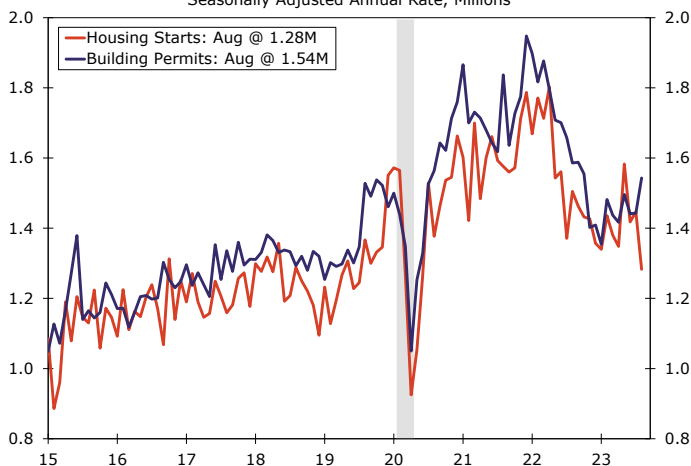
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### Housing Starts and Building Permits

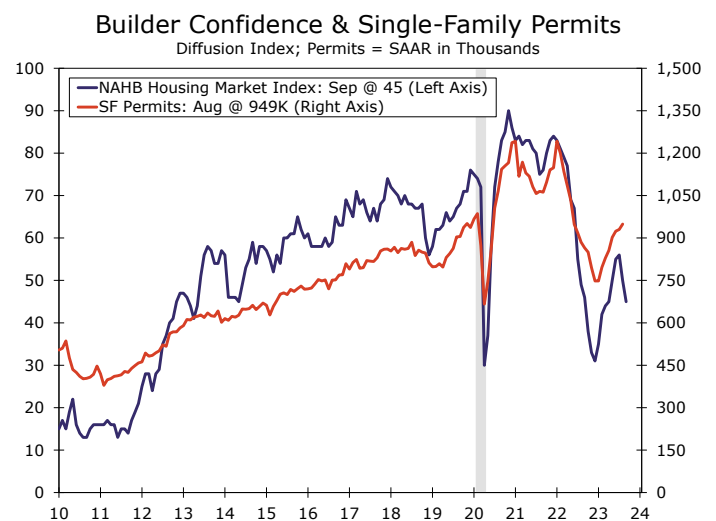
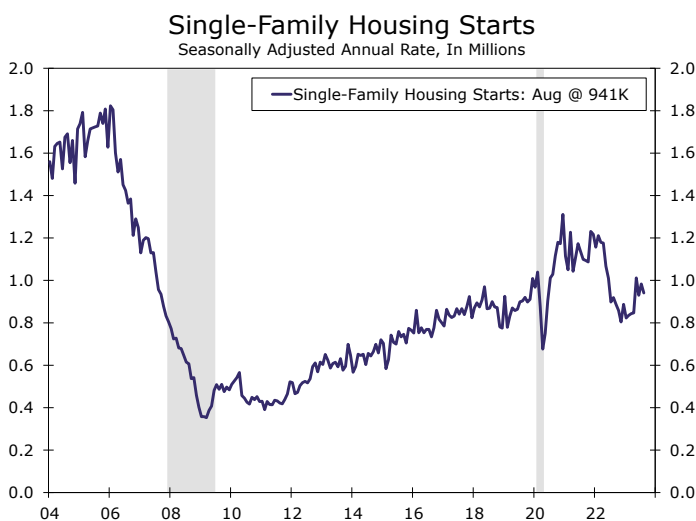
Seasonally Adjusted Annual Rate, Millions



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

## Starts Pull Back as Permits March Forward

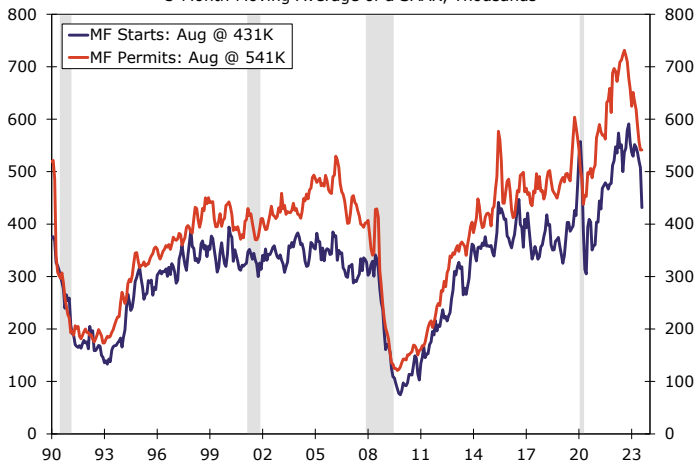
- Total housing starts dipped 1.3% to a 1.28 million-unit pace in August. The monthly decline was broad-based, with single-family and multifamily starts both slipping during the month.
- Single-family starts dropped 4.3% to a 941K-unit pace. The decline reverses some of the gains registered over the prior two months, but the pace of single-family activity was still up 2.4% on a year-over-year basis in August.
- The improvement over the past year generally reflects easing supply-side constraints and resilient buyer demand. Many builders have successfully offered rate buy-downs and price discounts to incentivize affordability-crunched buyers as mortgage rates have risen. Furthermore, the new home market is relatively replete with supply, in contrast to the existing market where inventories are remarkably lean.
- Single-family permits rose 2.0% during August. The monthly gain indicates that a relatively deep pool of potential buyers who have been boxed out of the resale market are leading builders to press ahead despite higher mortgage rates.
- Not every builder has the ability to maintain pricing flexibility, and the recent dip in builder confidence, which we write about below, is a sign that some may be starting to reassess plans to scale up production in light of the recent rise in 30-year mortgage rates, which are now hovering above 7%.



## Multifamily Construction Downshifting Amid Supply Concerns and Higher Financing Costs

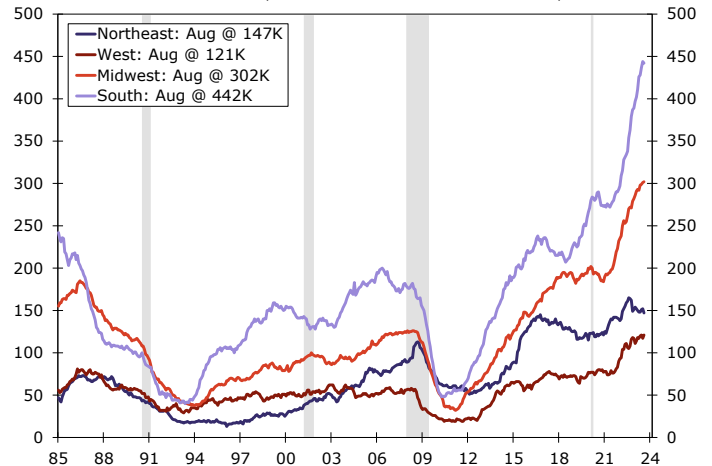
- Meanwhile, multifamily construction continues to shift to a lower gear. Multifamily starts declined 26.3% during August. The 342K-unit pace hit during the month was 41.6% below the same pace registered a year ago.
- Multifamily permits picked up 15.8% during August. Multifamily data tends to be highly volatile, and substantial monthly swings in starts and permits are not unusual. On balance, however, multifamily construction has trended significantly lower this year as apartment vacancy rates have moved higher, financing costs have increased and lending has become more restrictive.
- Higher mortgage rates are exerting renewed pressure on single-family affordability, which could help bolster rental demand in the months ahead. While not quite as robust as recent years, apartment demand has partially bounced back from the drop-off seen in 2022.
- Supply is the main issue in the multifamily market. During August, there were just over 1 million units under construction, down slightly from July, but higher than at any period since 1970.
- Approximately 44% of multifamily construction currently underway is in the South region. Miami, Austin, Nashville, Raleigh and Charlotte all have high counts of units under construction as a share of total inventory. Although concerning, these markets also rank high in terms of population growth, which should help partially allay fears of a significant supply overhang.

**Multifamily Starts vs. Permits**  
3-Month Moving Average of a SAAR, Thousands



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

**Multifamily Units Under Construction by Region**  
Thousands of Units, Under Construction at End of Period, SA

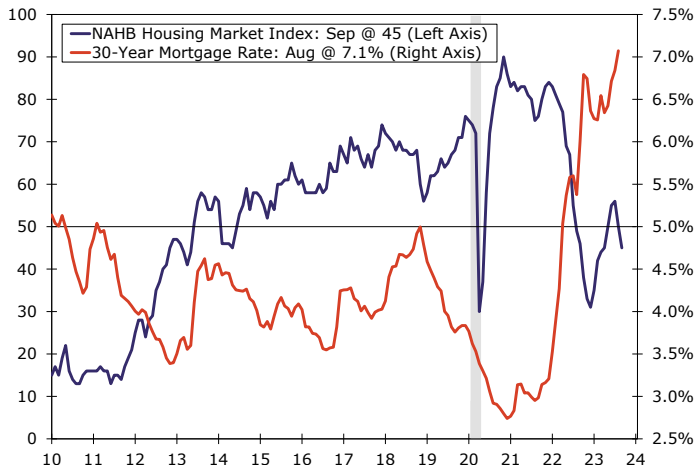


Source: U.S. Department of Commerce and Wells Fargo Economics

**Home Builder Confidence Slides for Second-Straight Month**

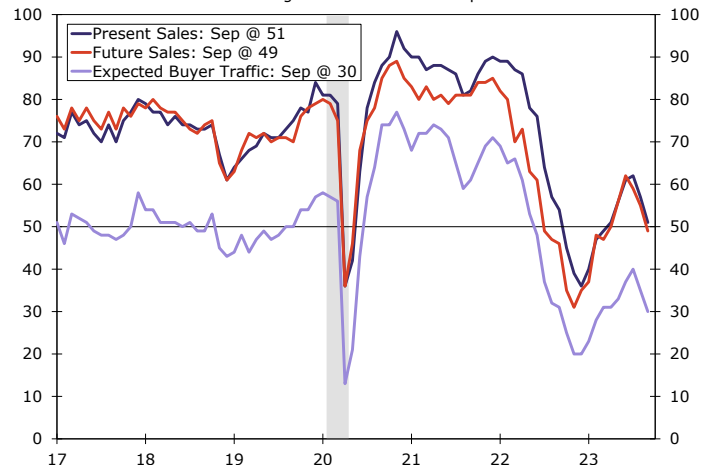
- The National Association of Home Builders/Wells Fargo Housing Market Index (HMI) fell to a five-month low of 45 in September, below consensus expectations and the second-straight monthly drop.
- The two-month decline in builder confidence coincides with mortgage rates moving above 7% for the first time since November 2022. The HMI has declined 11 points over the past two months as rising mortgage rates continue to erode affordability and bruise builder confidence.
- All three HMI subcomponents declined over the month. The present sales index fell six points to 51, just barely above the 50-point breakeven level. The future sales index also fell six points to 49 and prospective buyer traffic fell five points to 30—a seven-month low.
- Home builders are increasingly employing price cuts to attract buyers and drive sales. In September, 32% of builders reported offering price discounts, up from 25% in August, and the highest share since December 2022.

**NAHB Home Builder Confidence vs. Mortgage Rate**  
Diffusion Index



Source: NAHB, Freddie Mac and Wells Fargo Economics

**Single-Family Home Sales Outlook**  
NAHB Housing Market Index Subcomponents



Source: NAHB and Wells Fargo Economics

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