

Economic Indicator — November 17, 2023

October Brings a Broad-Based Upturn in Residential Construction

Single-Family and Multifamily Construction Both Improved

Summary

Housing Starts and Permits Rise in October

Home builders and multifamily developers appeared to shrug-off higher interest rates during October. Total housing starts rose 1.9% during the month, with single-family and multifamily starts both notching improvements. A broad-based improvement was also seen in building permits, which increased 1.1% in October. The surprising gain in starts and permits easily exceeded the Bloomberg consensus. Despite rising in October, multifamily developers look to be hitting the brakes alongside more restrictive credit and softer apartment market fundamentals. Although residential construction is highly sensitive to interest rates, a lack of resale supply has boosted sales so far this year. Builders also have been able to offset higher financing costs with mortgage rate buydowns and other pricing incentives. Encouragingly, mortgage rates have trended lower over the past three weeks, although home builders still appear to be put-off by the recent volatility in interest rates and corresponding negative effect on buyer traffic. The NAHB Housing Market Index fell to 34 in November, the lowest reading since December 2022.

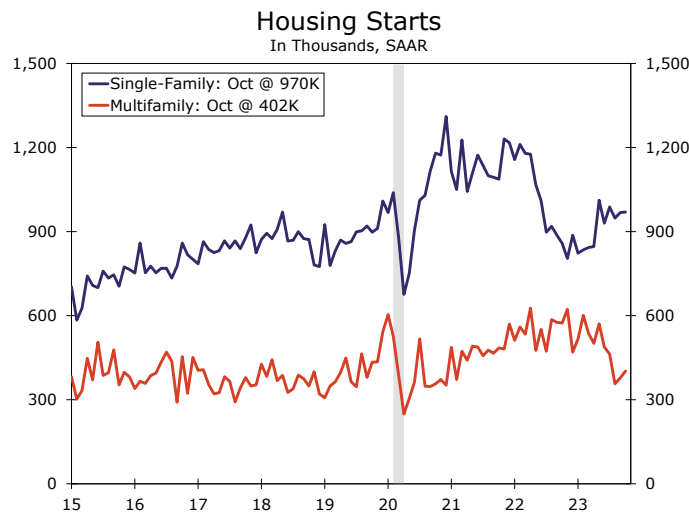
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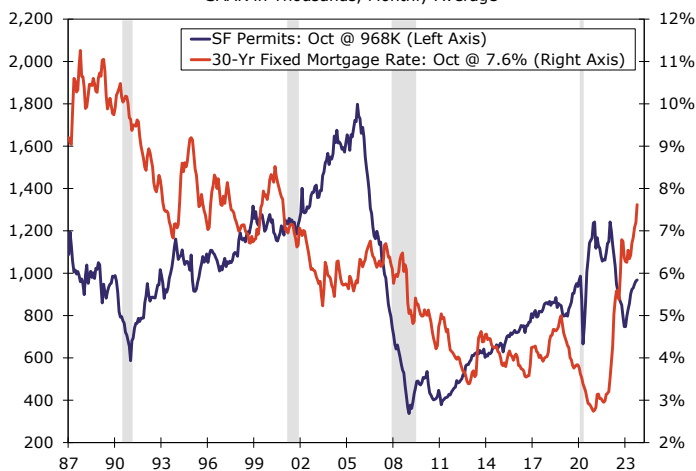


Source: U.S. Department of Commerce and Wells Fargo Economics

A Modest Gain in Single-Family Points to Construction Slowing

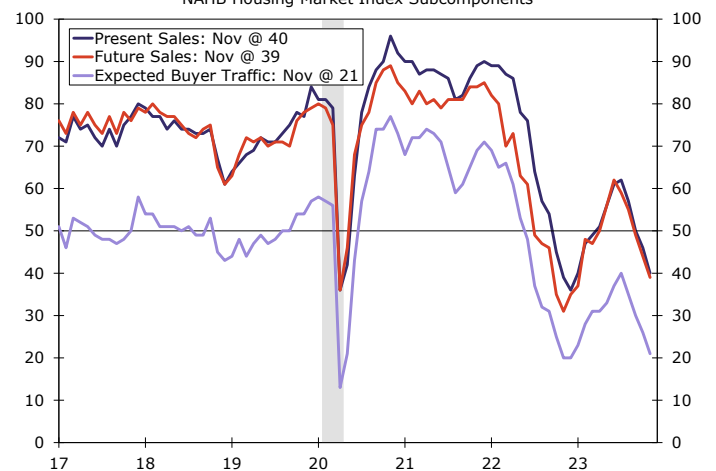
- Total housing starts rose 1.9% during the month, with single-family and multifamily starts increasing 0.2% and 6.3%, respectively, during October.
- Single-family starts improved to a 970K unit pace in October, 13.1% above the pace registered a year ago. The upturn over the past 12 months reflects resilient demand for new homes as lean resale inventories push prospective buyers to the new home market. Builders also have been able to offset higher financing costs with mortgage rate buydowns, lower prices and other incentives.
- The recent spurt higher in mortgage rates, which increased to 7.8% in the final week of October, may be testing this strategy and leading builders to throttle back production, however. In addition to the slight gain in starts, single-family permits rose just 0.5% in October, the slowest monthly rise since January.
- Encouragingly, mortgage rates have trended lower over the past three weeks, with the average 30-year commitment rate declining to 7.4% in the week ending November 16. The drop has occurred amid a string of weaker economic data and more evidence that inflation is easing, which has raised hopes that the Federal Reserve will begin to cut interest rates sooner rather than later.
- That noted, home builders still appear to be put-off by the recent volatility in interest rates and negative effects on buyer traffic. The NAHB Housing Market Index fell to 34 in November, the lowest reading this year.
- The surprise drop in builder sentiment resulted from each of the index subcomponents declining during the month. A six-point pullback in present sales was the largest drag, but future sales and prospective buyer traffic also declined by five points each.

Single-Family Housing Permits vs. Mortgage Rate
SAAR in Thousands, Monthly Average



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

Single-Family Home Sales Outlook
NAHB Housing Market Index Subcomponents

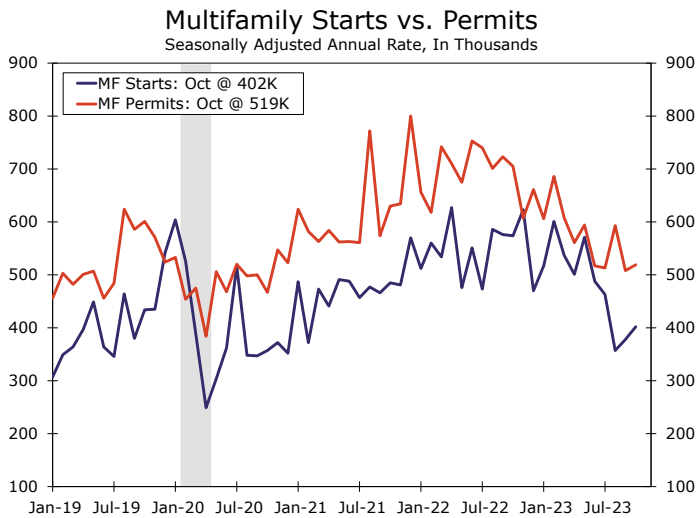


Source: NAHB and Wells Fargo Economics

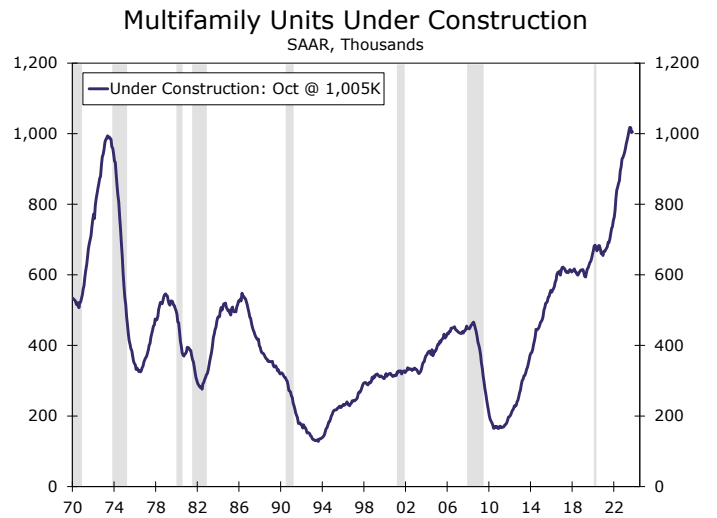
Multifamily Starts and Permits Pick Up, But More Moderation Appears on the Horizon

- Total multifamily starts rose 6.3% during October, the second consecutive monthly gain. Multifamily permits also picked up a bit and gained 2.2% during the month. Residential construction data is highly volatile and multifamily starts and permits often bounce around on a month-to-month basis.
- A downshifting trend in new multifamily development is still evident, however. Over the past year, starts have fallen 30%, while permits have declined 26%.
- Multifamily developers look to be hitting the brakes alongside more restrictive credit and softer apartment market fundamentals. Apartment vacancy rates have turned higher over the past year as normalizing demand has been overshadowed by a remarkable increase in new supply. In October, there were over one million apartment units under construction, up slightly from September's count and on par with the highs last seen in the late 1970s ([chart](#)). With a deluge of new supply on the way, multifamily construction appears set to weaken in the months ahead.
- Sentiment among multifamily developers has also worsened. Similar to the NAHB's HMI survey, the Multifamily Market Survey measures builder perception of production conditions and

occupancy. The Multifamily Production Index dipped well below the 50-point breakeven level in Q3, with high-rise builders being particularly pessimistic. The Multifamily Occupancy Index was comparatively higher at 82, reflecting solid demand for rental properties.



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



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