

Economic Indicator — September 26, 2023

New Home Sales Pulled Back in August

Higher Mortgage Rates Start to Weigh on New Home Sales

Summary

Tailwinds for Builders Showing Signs of Fading as Mortgage Rates Edge Higher

Thus far, builders have been largely successful navigating the headwinds triggered by the Fed's monetary tightening cycle. Favorable supply dynamics and builders' use of incentives have prompted new home sales to improve on balance this year despite the rising interest rate environment. Yet, the recent surge in mortgage rates may be weighing on demand as buyers increasingly become discouraged by the prospect of higher financing costs. New home sales dropped 8.7% in August, the largest monthly decline since September 2022. Generally speaking, monthly residential sales data can be quite volatile and subject to substantial revisions. However, it seems that higher mortgage rates are starting to take a bite out of buyer demand. The median new home price dipped 1.4% in August as builders were forced to step up their use of price cuts and other incentives to reinvigorate buyer interest. In our view, the near-term outlook for new home sales has been clouded by the recent uptick in mortgage rates. Per Freddie Mac, the average 30-year fixed mortgage rate has buoyed above 7.0% for the last six weeks, which will likely test builders' abilities to bridge the affordability gap in the months ahead.

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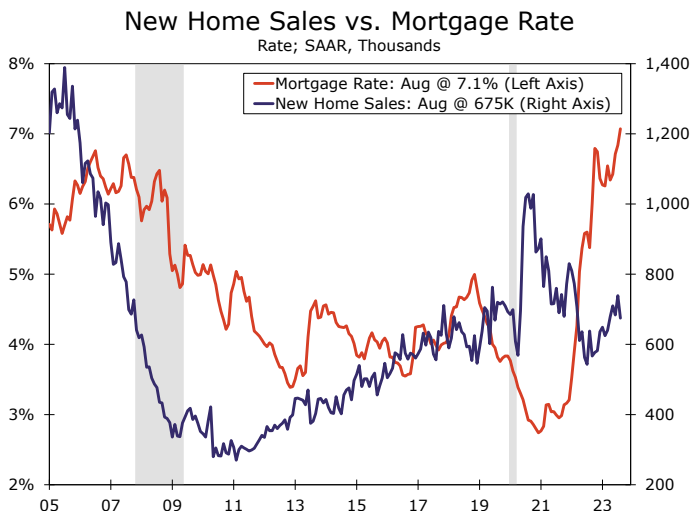
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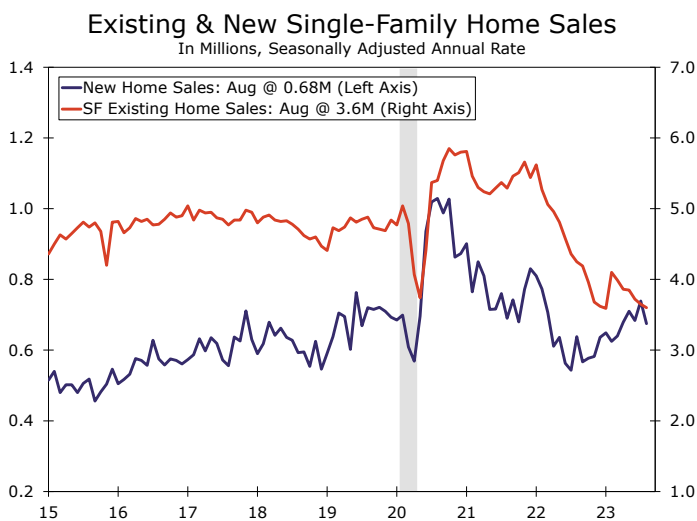
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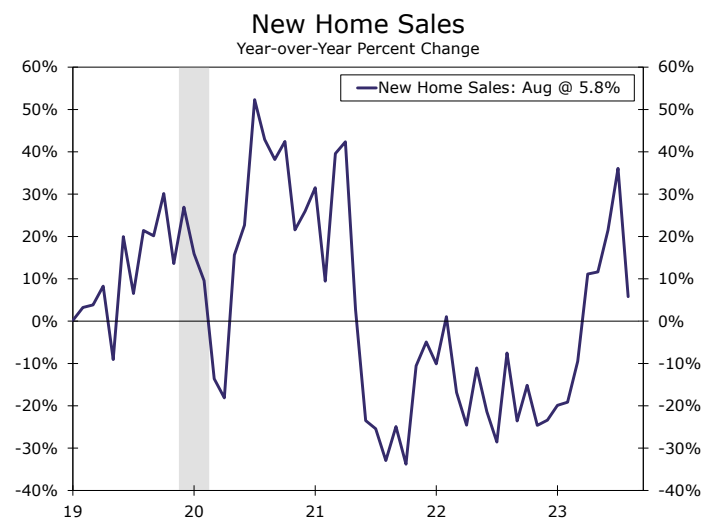
Source: U.S. Department of Commerce, Freddie Mac and Wells Fargo Economics

Rising Borrowing Costs Start to Weigh on New Home Sales

- New home sales dipped 8.7% to a 675K-unit pace during August. Although the monthly drop was below consensus estimates, upward revisions show a slightly stronger pace of sales during July. Despite the monthly decline, new home sales have trended higher over the past year, with the pace of sales up 5.8% on a year-over-year basis in August.
- The improvement in new home sales over the past year stands in stark contrast to the existing market where higher mortgage rates continue to weigh heavily on activity. Home builders have successfully employed incentives such as mortgage rate buy-downs to help improve affordability for prospective buyers.
- However, the prospect for higher mortgage rates for longer might be discouraging buyers from even starting the search for a home. The NAHB Housing Market Index for September showed a drop in buyer traffic in both August and September.



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



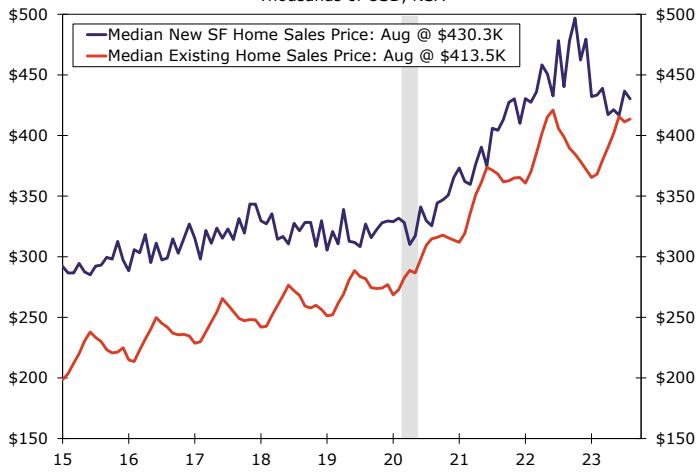
Source: U.S. Department of Commerce and Wells Fargo Economics

Builders Use Price Cuts to Spark Demand

- In order to reinvigorate buyer interest, builders may be furthering the use of price discounts. As of August, the median new home price has declined 2.3% on a year-over-year basis. The September NAHB homebuilder survey found 32% of builders reported offering price discounts, up from 25% in August and the highest share since December 2022.
- Price discounting on the part of builders has narrowed the difference between new homes prices and existing home prices, which are now back on the rise following a brief slump in the second half of 2022. Separately reported, the S&P CoreLogic CS 20-City home price index rose 0.9% during July, the fifth consecutive monthly gain. Higher mortgage rates have led to a decline in existing home sales, but lean resale inventories are exerting upward pressure on home prices.
- Compared to the existing market, there is a relative abundance of new homes available for sale. At the end of August, there were 436K units for sale, up 1.2% during the month and equivalent to 7.8 months supply. Since peaking at 9.7 months late 2022, months supply has trended lower over the past year, although the slower pace of sales yielded a slight increase during August.
- Second quarter data from the Census's Quarterly Starts and Completions report was released last month and revealed that newly built homes are getting smaller. The median square footage of a newly started single-family home fell to 2,191 feet, over 100 sq ft smaller than a year ago and the lowest level since late 2010. These smaller homes may provide a more affordable alternative for prospective buyers who have been priced out of larger properties.

New vs. Existing Median Home Sales Price

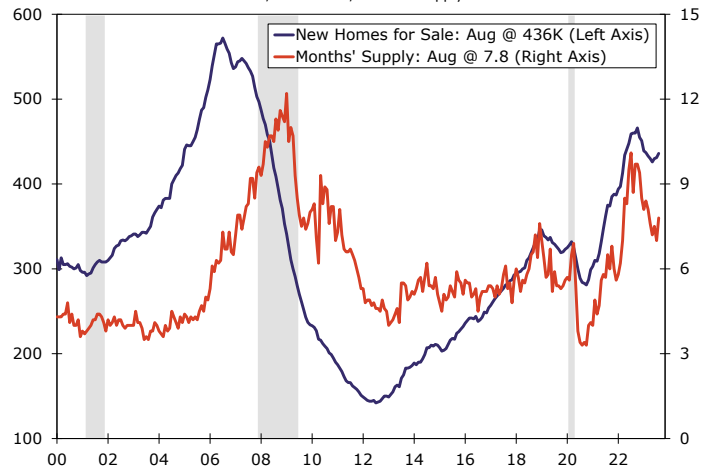
Thousands of USD, NSA



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

Inventory of New Homes for Sale

For Sale at End of Month, Thousands; Months' Supply at Current Sales Pace



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

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