



The Ripple Effect of Housing on Our Economy

Housing starts down, construction jobs way down and lumber prices are up?

As states begin to ease stay-at-home orders, communities across the county are starting to see “For Sale” signs planted in neighbors’ lawns again, after a dearth of signs since late February. And as we head into Memorial Day and fire up our barbecues, the conversations will inevitably turn towards the local real estate market, with topics ranging from:

- Will there be more buyers or sellers this summer?
- Will house prices decline given COVID or go back to their pre-COVID levels?
- Will the average time to sell go up or down?
- Can you believe how much so-and-so is asking?

We love to discuss the local real estate market and everyone has an opinion and a prediction as to where the local market might be headed. But investors would be wise to understand the effect that nationwide housing data has on our economy, the markets and by extension, our investments. Let’s explore the latest housing data.

Housing Starts

The U.S. Census Bureau and the U.S. Department of Housing and Urban Development compile new residential construction statistics every month and separate the data by Building Permits, Housing Starts and Housing Completions.

While each of those data sets is important to understanding the housing sector, Housing Starts is one of the most closely watched reports because it reflects a very direct commitment by a builder to build.

Think of it this way: as a general rule, home builders don’t start building a house unless they can sell it shortly before or upon its completion. And once a local home builder is confident enough to start building, local employment goes up and money is pumped back into the local economy as landscaping is purchased, furniture is bought, appliances are installed and people are put to work.

Now multiply that effect hundreds of thousands of times across the country and you can see the impact that housing has on our economy.

Here is what was reported on May 19th:

- Privately-owned housing starts in April were 30.2% below the March rate and 29.7% below the April 2019 rate
- Single-family housing starts in April were 25.4% below the revised March rate

Home Builders Index

There are other data sets that monitor the housing sector and one of them is an index that asks home builders to rate housing conditions and the general economy. Compiled by the National Association of Home Builders, this index is a weighted average of many sub-indexes, including:

- Present sales of new homes;
- Sales of new homes expected in the next six months; and
- Traffic of prospective buyers in new homes.

According to the latest from the NAHB, builder confidence for newly-built single-family homes increased seven points to 37 in May (50 is considered breakeven). This increase in builder confidence follows the largest single monthly decline in the history of the index recorded last month.

In addition, the index reflecting builder confidence about current sales conditions increased, as did the builders' confidence index measuring prospective traffic of home buyers.

The Ripple Effect of Housing

While the Home Builders Index data sets might be considered glimmers of hope, the housing industry in general brings a significant ripple effect throughout the rest of the economy. Here are a few examples:

- On the same day that the NAHB reported on home builders' optimism, the Bureau of Labor Statistics reported that there were 618,000 layoffs in the construction sector in March – triple the amount for the month before. And that number is supposed to increase next month when April's numbers are released;
- On March 15th, it was reported that prices paid for goods used in residential construction decreased 4.1% in April, which was the largest monthly decline on record; and
- The year-to-date decline of -5.4% in residential construction inputs prices is more than three times larger than the previous record (-1.3% in 2009).

The reason for the decline in prices? Supply and demand. The demand for construction materials has dropped and when the demand for a commodity drops, so does its price (usually).

But economists are quick to point out that the supply of construction materials has also dropped given COVID-19 restrictions on certain businesses, so it's possible that the average prices for construction materials might have dropped more if not for the supply decrease.

But It's Not All Negative

To summarize, Housing Starts were down significantly, home builders are more optimistic this month versus last month and construction materials have come down in price. But guess what prices are up this month?

If you guessed lumber, you're right. On the exact same day that the NAHB reported on home builders' optimism, it was reported that lumber prices have increased by 13% since May 1st, the largest two-week increase in over 10 years.

Why have lumber prices increased? Well, there is now a lot more work being done by the do-it-yourselfers during COVID lockdowns. And they're buying more lumber. Plus lumber mills have been operating at restricted capacity. More demand, less supply means higher prices.

It's a lot easier and way more fun to gossip about how much so-and-so is trying to sell their house for, isn't it?