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July Residential Construction: Single Family Not "Done" Just Yet . . .

- > Total housing starts rose to an annualized rate of 1.168 million units; total housing permits rose to an annualized rate of 1.311 million units.
- > Single family starts rose to 862,000 units while single family permits rose to 869,000 units (annualized rates).
- > Multi-family starts rose to 306,000 units and multi-family permits rose to 442,000 units (annualized rates).

Total housing starts rose to an annualized rate of 1.168 million units in July, falling short of our below-consensus forecast of 1.238 million units, while total housing permits rose to an annualized rate of 1.311 million units, shy of our above-consensus forecast of 1.331 million units. The soft headline starts number fits right in with the "housing is done" story line that has become quite the rage, and anyone intent on clinging to this story line can stop reading now. For anyone willing to listen, however, the real story in the data on residential construction is told by the not seasonally adjusted data. The quick summary of that story is that single family permits and starts continue to grind higher, even if at a frustratingly slow pace, while the multi-family continues to march to the beat of its own drummer, with a growing divergence between starts (tailing off) and permits (still oddly strong). We see nothing to suggest the single family story will change any time soon. Given what remains a massive backlog of units under construction, it makes sense that multi-family starts are tailing off, so the question is when will permits do the same.

The not seasonally adjusted data show total starts of 110,400 units in July, short of our forecast of 115,900, with total permits of 114,000 units, slightly ahead of our forecast of 112,100 units. The 82,900 single family starts topped our forecast of 81,800, but at 28,600 units, multi-family starts came in well below our forecast of 33,000. As for permits (not seasonally adjusted), the 77,600 single family permits were slightly ahead of our forecast of 75,400, while the 36,400 multi-family permits were trivially below our forecast of 36,700. Multi-family starts in the West region fell to 5,900 units in July, and while it could be activity in the region was held back by the widespread fires, single family activity in the West was in line with both recent trends and our forecast for July.

On a year-to-date basis through July, single family permits and starts are each up 7.2 percent, so if housing really is done someone should perhaps inform the single family segment of the market. Single family starts are down slightly in the Midwest region on a year-to-date basis

but up sharply in the other three broad Census regions, led by a 15.7 percent increase in the West region. The running 12-month total of not seasonally adjusted single family starts stands at 884,800 units as of July, and while the rate of increase has slowed a bit over the past two months this still reflects the highest 12-month total since May 2008.

On a year-to-date basis through July, multi-family permits are up 1.9 percent and multi-family starts are up 3.7 percent. It is the South and West regions, however, that are responsible for the increase in multi-family activity. The growing divergence between multi-family permits and starts is best seen by looking at the running 12-month totals; as of July there had been 466,900 multi-family permits issued over the past 12 months, but multi-family starts have totaled 361,800 units over that same period. It is not at all uncommon for multi-family permits to run ahead of starts – over 20 percent of multi-family permits never progress to an actual start – but the gap between the two has widened steadily over the past several months. While we cannot account for the continued high level of multi-family permit issuance, the tailing off of multi-family starts reflects, at least to us, the reality of what remains a massive backlog of under-construction multi-family units. As of July, there were 603,900 multi-family units under construction, the 25th consecutive month above the 600,000 unit mark. As we have been noting for some time now, one has to go back to the mid-1970s to see a backlog this large for this long. As our second chart below illustrates, this backlog is spread out across the four broad Census regions. While multi-family completions did pick up a bit in July, the pace at which multi-family units are being finished ensures the supply backlog will be with us for some time to come, which to us suggests that there is considerably more room for multi-family starts to fall.

To be sure, the market could easily digest for single family construction but constraints on lots and labor make it unlikely that the pace of single family activity will pick up to any material degree. There is, however, a long way between that and housing being "done."

