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October Existing Home Sales: Inventories, Or Lack Thereof, Still The Main Story Line

- Existing home sales rose to an annualized rate of 5.220 million units in October from September's sales rate of 5.150 million units
- Months supply of inventory stands at 4.3 months; the median existing home sale price rose by 3.8 percent on a year-over-year basis

Existing home sales rose to an annualized rate of 5.220 million units in October, falling short of our above-consensus forecast of 5.310 million units. At 4.3 months in October, the months supply metric continues to point to a significantly undersupplied market, and what relief there is on the inventory front is coming at a frustratingly slow pace. The median existing home sales price was up 3.8 percent year-on-year in October, slower than the gains seen over the past several months, but affordability nonetheless is a growing concern in light of higher mortgage rates. Though NAR offered no specific guidance, it is likely that the data for the South region were impacted by Hurricane Michael, just as the September data for the South region were impacted by Hurricane Florence. At the same time, however, sales in the West region have softened, and it is in this region that lack of inventory and diminished affordability have been bigger constraints on sales. All in all, we continue to think sales will remain fairly range bound over coming months though there will likely be a high degree of noise in the data in the near term.

On a not seasonally adjusted basis, there were 446,000 existing home sales in October, below our forecast of 462,000 sales. Our miss here was entirely due to the South region, where sales of 182,000 units fell short of our forecast, with sales in the other three broad regions matching our forecasts. There is reason to suspect Hurricanes Florence and Michael have held down sales activity in the South region over the past two months though the effects from Michael should be less severe than those from Florence. What isn't clear, however, is the extent to which the hurricanes simply delayed closings (recall that existing home sales are booked at closing) or led to sales being canceled, which is a question that will be answered over coming months. As it is, October's sales leave the running 12-month total of not seasonally adjusted existing home sales, which we see as the most reliable gauge of the underlying sales trend, at 5.412 million units, down from 5.424 million units as of September. As our middle chart shows, the running 12-month total of not seasonally adjusted sales as of October is higher in the South region than was the case last October but is down in the three remaining regions, with the total in the West region the lowest of any October since 2014.

Listings of existing homes for sale fell to 1.850 million units in October from 1.880 million in September, but keep in mind that we are in the time of the year in which listings typically decline (the NAR inventory data are not seasonally adjusted). Of more significance than the seasonal decline in October is that inventories are up 2.78 percent year-on-year. October is the third consecutive month in which inventories of existing homes for sale are up on a year-on-year basis which, granted, may not sound like all that noteworthy of an achievement, but keep in mind that this follows a run of 37 consecutive months of year-on-year declines. In other words, inventories are beginning to come back, but they are coming back off of a very low base and 2018 will go down as the fourth consecutive year in which the seasonal top in inventories was lower than that of the prior year. This goes to our earlier point that any improvement on the inventory front will come at only a grudging pace.

If we are correct on this point, this will support further price appreciation, but at a slower pace than what we have seen over the last couple of years. Further price appreciation and higher mortgage interest rates will hit prospective first-time buyers the hardest, and this group will continue to be underrepresented in the market for existing homes. First-time buyers accounted for 31 percent of all existing home sales in October, in line with recent months but well below historical norms. That said, builders of new single family homes are making increased efforts to target first-time buyers, which supports our contention that, higher mortgage rates notwithstanding, the demand for home purchases is still there.

We remain constructive on the demand side of the market, even allowing for higher mortgage rates, and continue to see soft existing home sales as more of a supply story.

