

Economics Group

Special Commentary

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Housing Chartbook: November 2015

Housing Is Poised for Stronger Gains in 2016

Uncertainty about the broader economic outlook appears to be increasing, even as the Fed has become more adamant that it is time to end its seven-year run of holding the federal funds rate close to zero. Data from the production side of the economy have been particularly disconcerting, with the ISM manufacturing index falling below the key 50 break-even level and the series is now at its lowest point since 2009. The weakness reflects faltering demand overseas and the continuing effect that the stronger dollar and lower commodity prices are having on producers of mining and farming equipment. While the economy is getting tougher for producers, it is largely improving for consumers. Overall employment growth is holding up relatively well and wages and salaries are growing a bit more rapidly. Consumers are also benefitting from continued low energy prices and low inflation in general.

Our forecast calls for overall economic growth to remain in line with recent growth in 2016, as the drag from federal spending cuts lessens, and consumer spending, homebuilding and commercial construction all improve. Business fixed investment in new equipment should also eke out modest gains but international trade and inventories will both subtract from growth during the year. We are looking for real GDP to rise 2.4 percent in 2016, following an expected 2.4 percent gain this past year.

Housing is once again expected to be a bright spot in the economy, but that optimism comes with a big asterisk.

Housing is once again expected to be a bright spot in the economy, but that optimism comes with a big asterisk. Both home sales and new home construction remain only a fraction of their historical norms, even after six and a half years of recovery. The housing market also remains bifurcated, much like the economy in general. The strongest recovery has taken place in markets where employment rebounded sharply, which mostly includes areas driven by the explosive growth in high technology, energy exploration and production and international trade and investment. Foreign purchases have also propelled the housing recovery in certain markets.

Figure 1

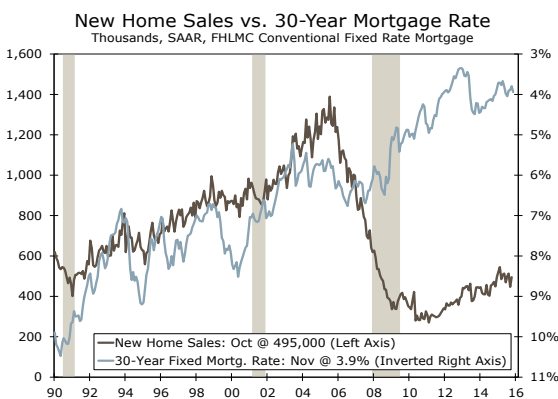
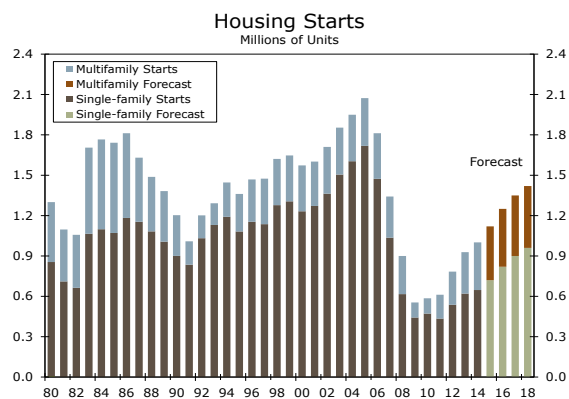


Figure 2



Source: U.S. Department of Commerce, FHLMC and Wells Fargo Securities, LLC



A More New Normal-Like Year for Housing?

Home prices have generally rebounded faster and to a greater degree in areas close to key employment centers.

Not only has the recovery in housing been highly skewed toward the relative handful of metropolitan areas where population and employment growth has grown the fastest, but there has also been a stark divide between the rebound in the cities and the suburbs and between apartments and single-family homes. Home prices have generally rebounded faster and to a greater degree in areas close to key employment centers, which has primarily been in the central cities or rapidly growing suburban nodes, which have also become much more urbanized. The traditional suburbs have recovered much more slowly and many distant suburbs have languished.

Another substantial divide has been seen in the recovery of the apartment market, and rental housing in general, relative to the recovery of for-sale housing. Both markets have improved but apartments and rental housing have had one of their best runs in recent years, while for-sale housing has seen only modest gains. We expect this mix to move more toward its historical norm in 2016; however, this shift will be hampered by rising interest rates, historically low inventories of new and existing homes, demographic changes and changes in consumer preferences for housing.

The good news is that the overwhelming majority of consumers still want to own their own home. According to Fannie Mae's National Housing Survey, attitudes toward homeownership have not changed anywhere near as much as previously thought. Most consumers still desire to own a home at some point in their lives but affordability concerns, tighter credit availability and the slow and uneven economic recovery have pushed the home-buying decision to a later point in life than in past cycles. Demographic changes, most notably the rise of the Millennials and aging of the Baby Boomers, are also influencing the rent versus buy decision. Millennials in general have taken longer to establish themselves financially and many continue to live with, or be supported by, their parents. This trend has not only kept younger households out of the housing market, but also often prevented their parents from downsizing their homes and relocating from neighborhoods chosen primarily because of their school district to other areas desired by their amenities.

We are looking for sales of new homes to rise 17.5 percent in 2016, following a 15 percent rise this past year.

The generational weights on housing will likely linger for quite some time but the winds are shifting. Stronger job growth over the past two years has led to increased household formation (Figure 4). While most of these new households have chosen to rent, home-buying has also risen, even among younger households. Rents have also increased dramatically and buying a home now makes more financial sense for persons that plan to live in a community for at least a few years. We are looking for sales of new homes to rise 17.5 percent in 2016, following a 15 percent rise this past year. Both gains come off an extremely low base. With inventories of completed new single-family homes still near record lows, any increase in sales will pull construction higher. Single-family starts are expected to rise 14 percent in 2016 following an 11 percent rise this past year. Even with these gains, single-family starts will remain well-below their historical norms.

Figure 3

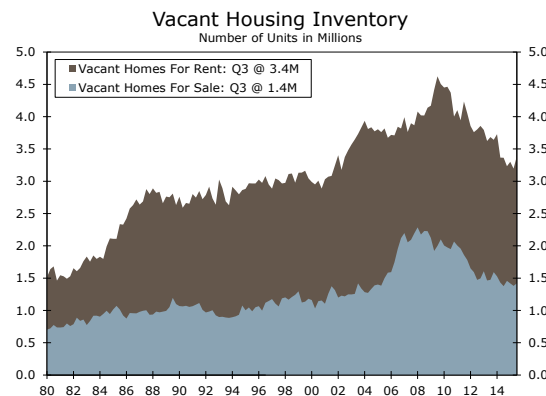
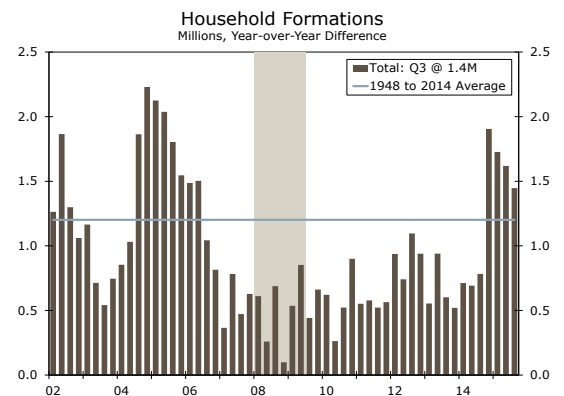


Figure 4



Source: U.S. Department of Commerce and Wells Fargo Securities, LLC

National Housing Outlook

	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
Real GDP, percent change	-0.3	-2.8	2.5	1.6	2.3	2.2	2.4	2.4	2.4	2.4
Nonfarm Employment, percent change	-0.6	-4.3	-0.7	1.2	1.7	1.7	1.9	2.1	1.7	1.5
Unemployment Rate	5.8	9.3	9.6	8.9	8.1	7.4	6.2	5.3	4.7	4.5
Home Construction										
Total Housing Starts, in thousands	905.5	553.9	586.9	608.8	780.6	924.9	1003.3	1,120.0	1,250.0	1,350.0
Single-Family Starts, in thousands	622.0	445.0	471.1	430.5	535.3	617.7	647.8	720.0	820.0	900.0
Multifamily Starts, in thousands	283.5	108.9	115.8	178.3	245.3	307.2	355.5	400.0	430.0	450.0
Home Sales										
New Home Sales, Single-Family, in thousands	485.0	374.0	321.0	305.0	369.0	429.0	437.0	502.0	590.0	670.0
Total Existing Home Sales, in thousands	4,110.0	4,340.0	4,190.0	4,260.0	4,660.0	5,090.0	4,940.0	5,220.0	5,500.0	5,625.0
Existing Single-Family Home Sales, in thousands	3,660.0	3,870.0	3,708.0	3,787.0	4,128.0	4,484.0	4,344.0	4,617.0	4,870.0	4,980.0
Existing Condominium & Townhouse Sales, in thousands	450.0	464.0	474.0	477.0	528.0	603.0	591.0	603.0	630.0	645.0
Home Prices										
Median New Home, \$ Thousands	232.1	216.7	221.8	227.2	245.2	268.9	282.8	293.3	305.0	317.0
Percent Change	-6.4	-6.6	2.4	2.4	7.9	9.7	5.2	3.7	4.0	3.9
Median Existing Home, \$ Thousands	198.1	172.5	172.9	166.1	176.8	197.1	208.3	220.8	231.4	241.1
Percent Change	-9.5	-12.9	0.2	-3.9	6.4	11.5	5.7	6.0	4.8	4.2
FHFA (OFHEO) Home Price Index (Purch Only), Pct Chg	-8.0	-5.8	-3.0	-4.1	3.2	7.4	5.5	5.6	4.8	4.5
Case-Shiller C-10 Home Price Index, Percent Change	-16.7	-12.9	2.1	-3.5	0.3	11.7	7.9	4.7	4.4	4.3
Interest Rates - Annual Averages										
Prime Rate	4.88	3.25	3.25	3.25	3.25	3.25	3.25	3.31	3.88	4.88
Ten-Year Treasury Note	3.66	3.26	3.22	2.78	1.80	2.35	2.54	2.14	2.39	2.73
Conventional 30-Year Fixed Rate, Commitment Rate	6.04	5.04	4.69	4.46	3.66	3.98	4.17	3.92	4.25	4.66
One-Year ARM, Effective Rate, Commitment Rate	5.18	4.71	3.79	3.03	2.69	2.61	2.44	2.50	2.90	3.60

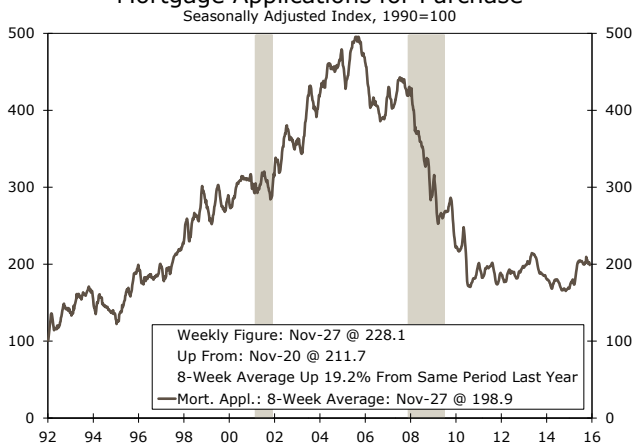
Forecast as of: December 4, 2015

Source: Federal Reserve Board, FHFA, MBA, NAR, S&P, U.S. Department of Commerce, U.S. Department of Labor and Wells Fargo Securities, LLC

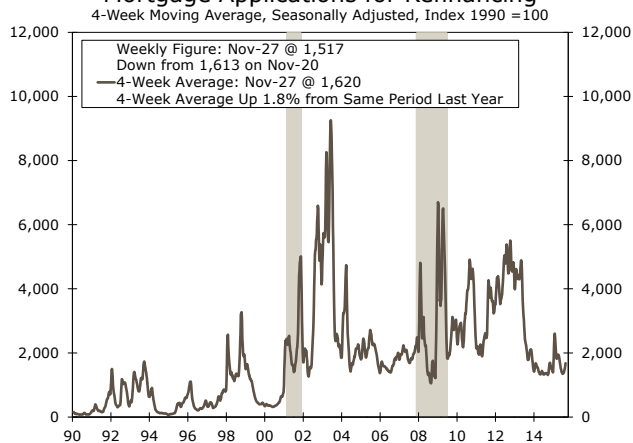
Mortgages

- Mortgage purchase applications continued to improve during the month; however, the level remains well off its January peak. With the Federal Reserve expected to increase its short-term interest rate in December, the wave of refinancing activity is behind us. Much of the consternation is now on the impact of a Fed rate hike on mortgage rates. Although mortgage rates should increase somewhat with a Fed rate hike, we are expecting a flatter yield curve, which means any increase should be relatively modest.
- Consistent with the Senior Loan Officer Opinion Survey, the Mortgage Credit Availability Index, which uses credit score, loan type, and loan-to-value ratio, continues to show a slight but persistent easing in residential lending standards.

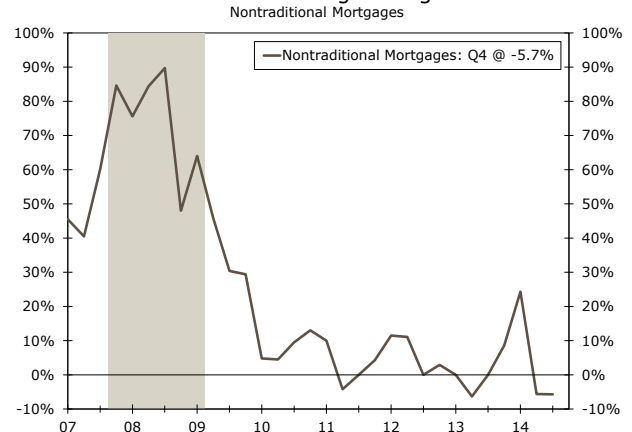
Mortgage Applications for Purchase



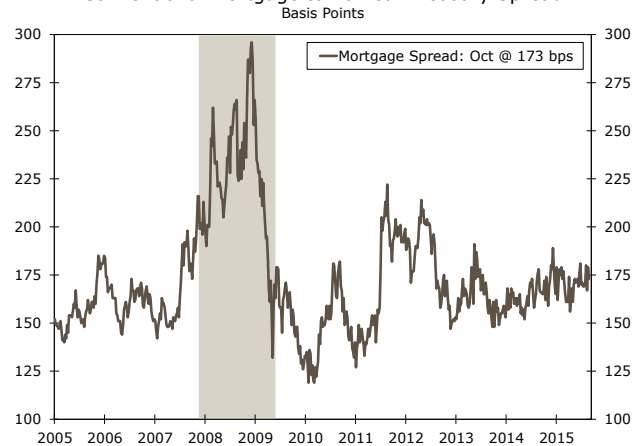
Mortgage Applications for Refinancing



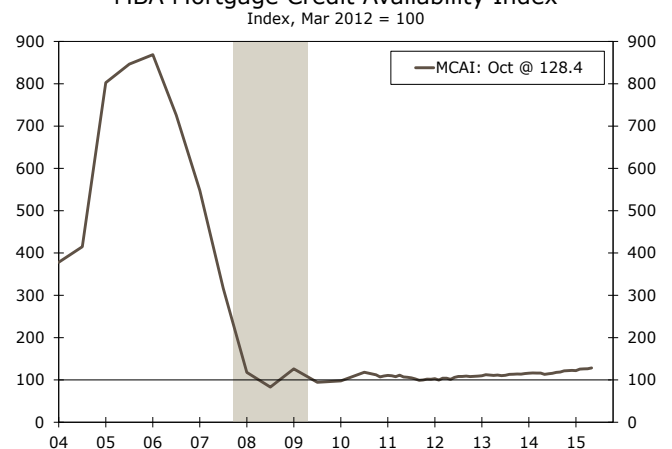
Net Percent of Banks Tightening Standards



Conventional Mortgage to 10-Year Treasury Spread



MBA Mortgage Credit Availability Index

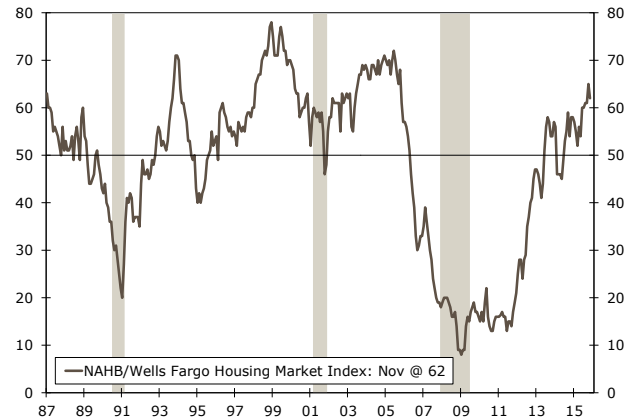


Source: Mortgage Bankers Association, FHLMC, U.S. Dept. of Commerce, Federal Reserve Board and Wells Fargo Securities, LLC

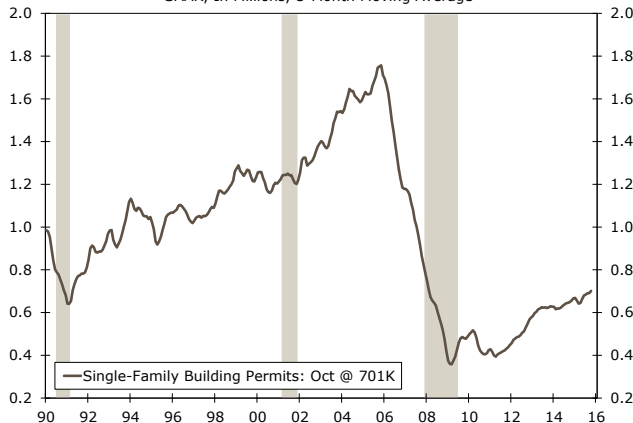
Single-Family Construction

- Single-family starts have been weak in recent months, posting negative readings in two of the past three months. Permits, which are less volatile, rose in October and continued to post strong year-over-year gains. The level of permits is now running ahead of starts, which suggests a rebound in starts is in the offing. Although much of the excess supply in the single-family market has been whittled down, the still-robust pace of apartment demand means single-family starts will remain below its pre-recession long-run trend.
- On a positive note, the level of builder sentiment remains near decade highs. Buyer traffic is now well off its cycle low, and builders' outlook for sales activity remains optimistic.

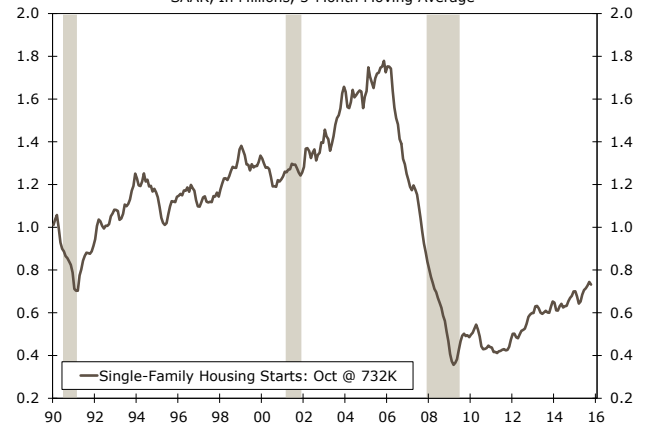
NAHB/Wells Fargo Housing Market Index
 Diffusion Index



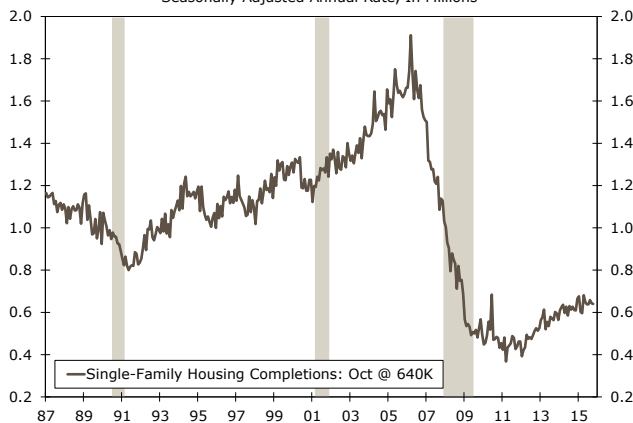
Single-Family Building Permits
 SAAR, In Millions, 3-Month Moving Average



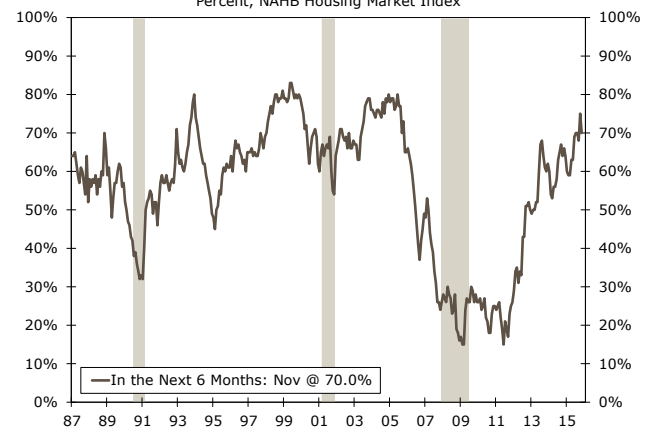
Single-Family Housing Starts
 SAAR, In Millions, 3-Month Moving Average



Single-Family Housing Completions
 Seasonally Adjusted Annual Rate, In Millions



Expected Single-Family Home Sales
 Percent, NAHB Housing Market Index

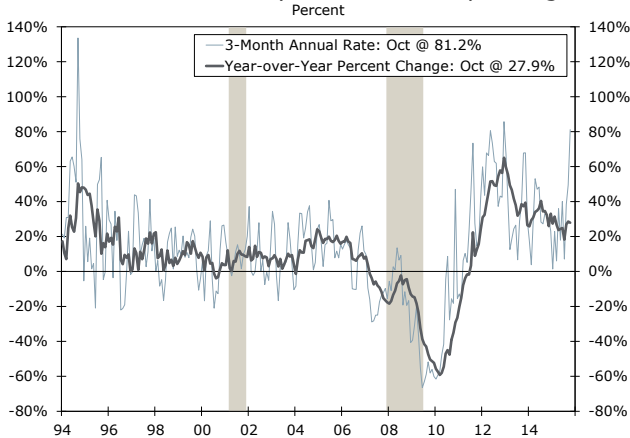


Source: U.S. Department of Commerce, NAHB and Wells Fargo Securities, LLC

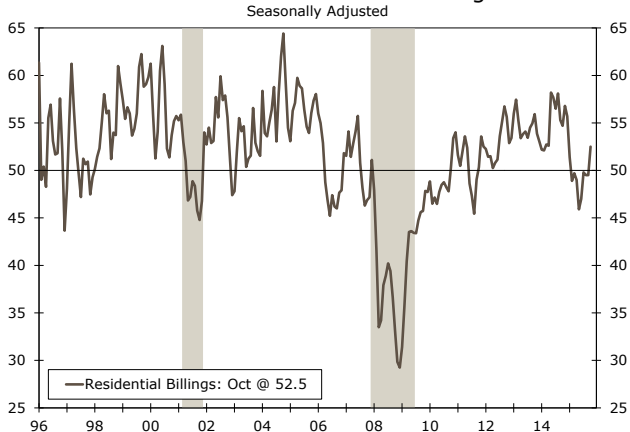
Multifamily Construction

- Firming labor market conditions and rising household formations, which are still heavily tilted toward renter-occupied units, will continue to underpin solid gains in multifamily starts. The pace, however, is slowing as supply in many markets outpaces demand. Permits have fallen sharply in recent months, but with the level still running significantly ahead of starts, we expect to see additional gains.
- Following eight months of negative readings, residential architecture billings increased in October. Although the long string of lackluster readings appears ominous, we expect activity in the multifamily sector to remain solid given the favorable demographics; however, the pace of growth will likely moderate.

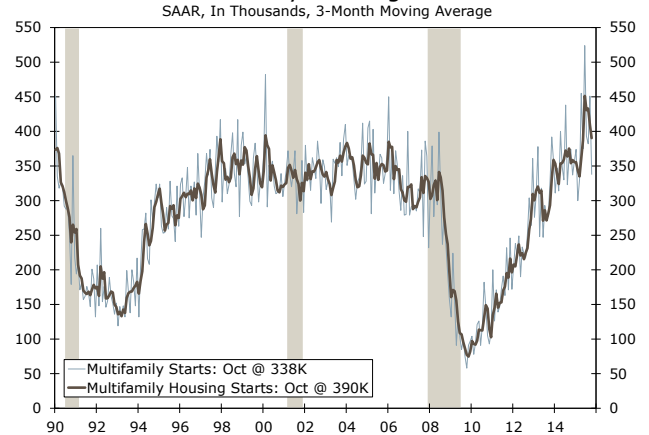
Private Multifamily Construction Spending



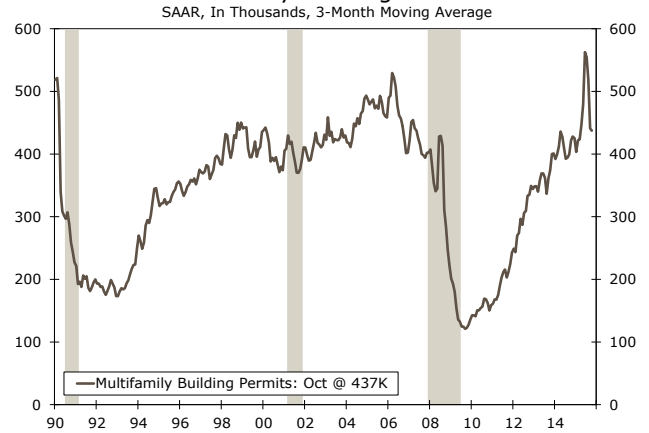
Residential Architecture Billings



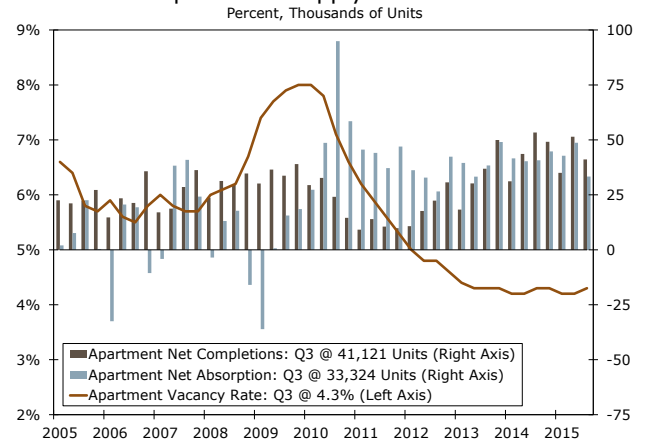
Multifamily Housing Starts



Multifamily Building Permits



Apartment Supply & Demand

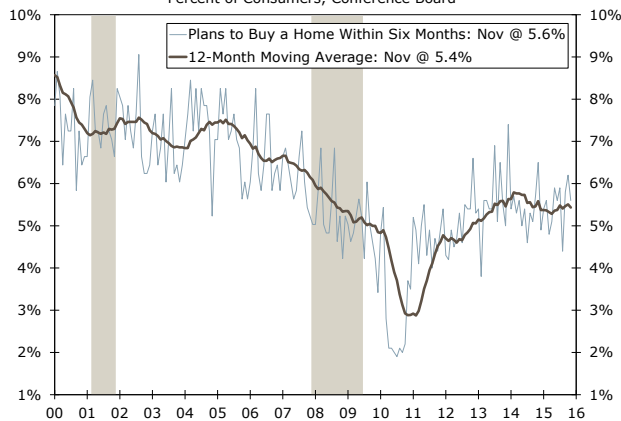


Source: U.S. Dept. of Commerce, REIS Inc. and
Wells Fargo Securities, LLC

Buying Conditions

- Buying conditions remain favorable, but prices have escalated at a much faster pace than incomes, which means affordability is moderating. Much of the increase in home prices is due to non-traditional buyers, namely resident foreign buyers in the United States for school or business; and, nonresident buyers who are purchasing U.S. single-family properties as a vacation home or investment property.
- According to the NAR, roughly 4 percent of total existing home sales were to foreign buyers over the past year, split evenly between resident and nonresident buyers. The average home purchased by foreign buyers was almost \$500,000, with about half of the purchases occurring in Florida, California, Texas and Arizona.

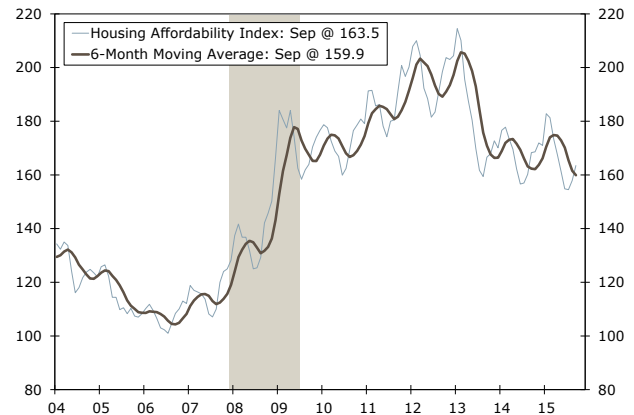
Confidence: Plans to Buy a Home
Percent of Consumers, Conference Board



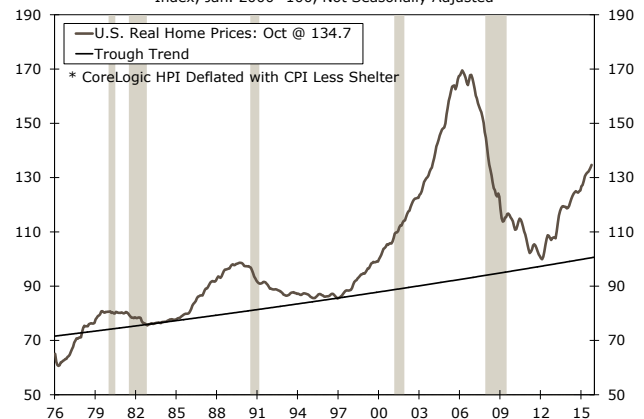
Existing Home Sales to International Clients
Top 5 Countries, In Billions of Dollars, Previous 12 Months



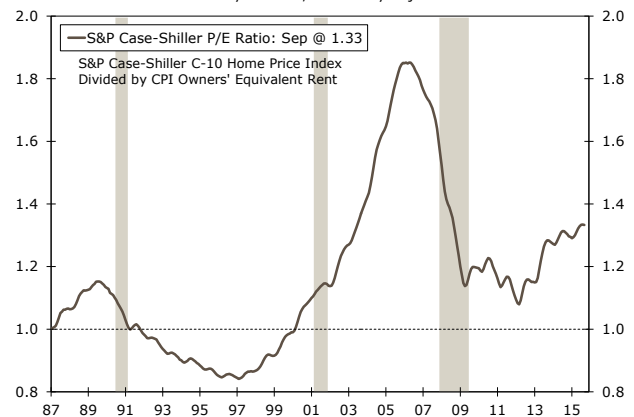
Housing Affordability, NAR-Home Sales
Base = 100



U.S. Real Home Prices
Index, Jan. 2000=100, Not Seasonally Adjusted



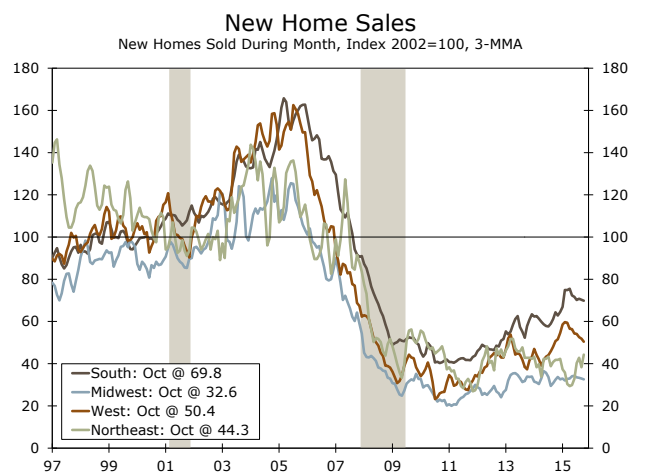
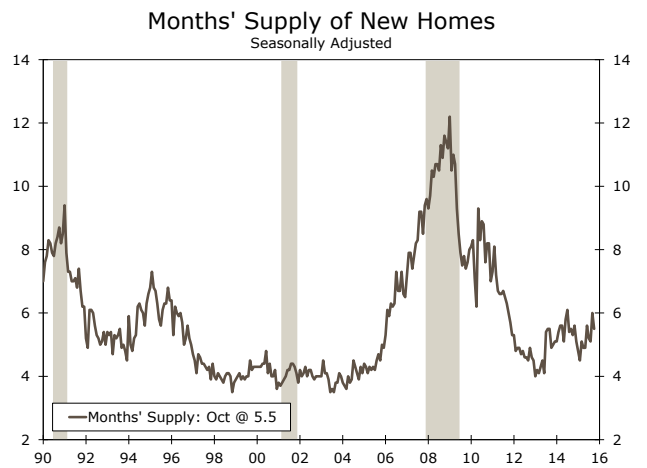
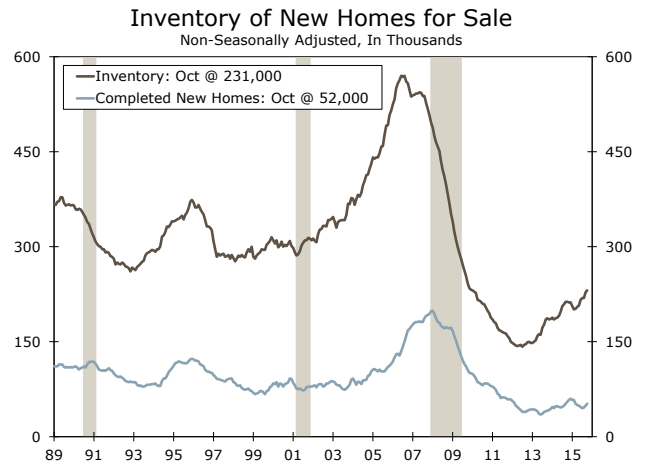
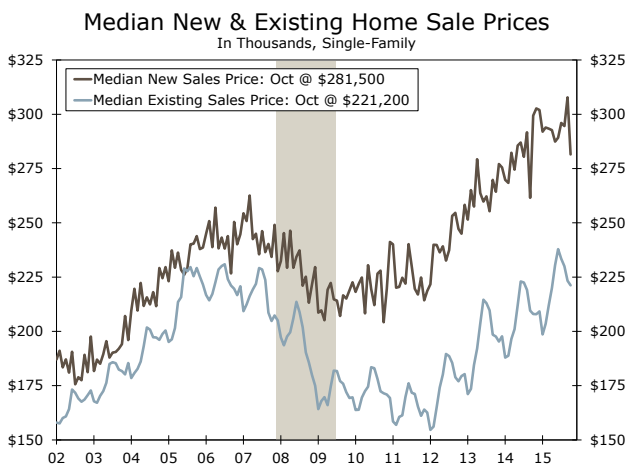
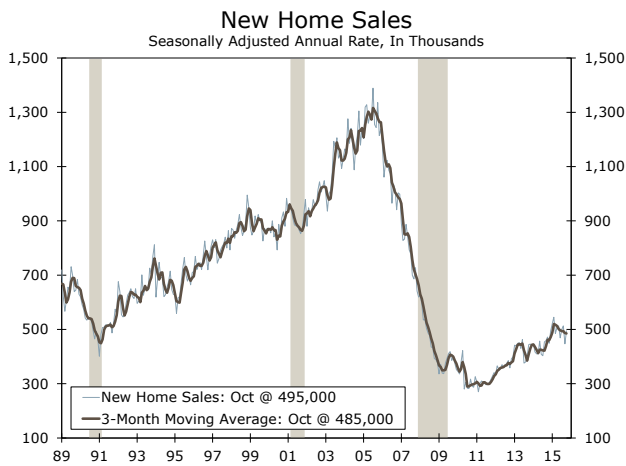
S&P Case-Shiller Home Price Index P/E Ratio
January 1987=1, Seasonally Adjusted



Source: CoreLogic, S&P, Conference Board, NAR, U.S. Dept. of Commerce and Wells Fargo Securities, LLC

New Home Sales

- New home sales rose sharply in October, but monthly figures tend to be more volatile than existing home sales. On a three-month moving average basis, sales activity downshifted during the month to the lowest level since December 2014. That said, the level of new home sales remains low by historical standards but is expected to post another double-digit annual gain in 2016.
- Inventories of completed new homes also remain near historical lows, at just 231,000 homes in October. The low level of completed new home inventory means that just about any incremental boost to sales will provide a lift to starts. The level of new home sales in the South rose sharply in October but has remained relatively steady since May, possibly reflecting some slowing in Texas.

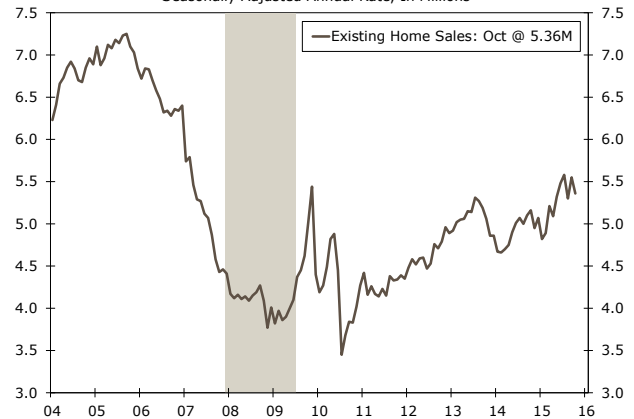


Source: U.S. Department of Commerce, National Association of Realtors and Wells Fargo Securities, LLC

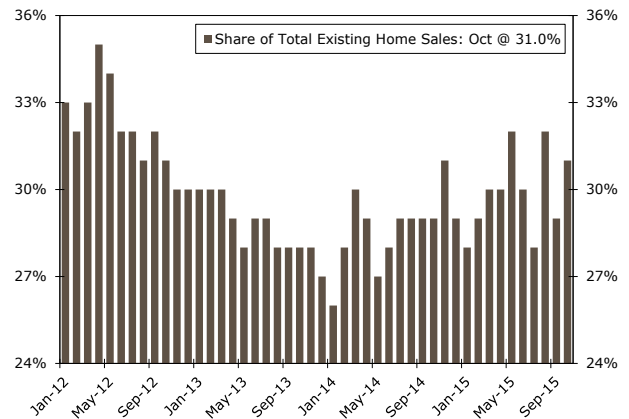
Existing Home Sales

- Existing home sales fell in October to a 5.36 million-unit annual pace. Overall sales continue to be restrained by the low-level of inventories. Sales activity for lower-priced homes remains slow while mid- to higher-priced homes continue to show improvement. The share of homes sold for less than \$250,000 reached a high of more than 62.3 percent earlier in the year but has since fallen to 57.8 percent in October.
- The share of first-time home buyers remains historically low. Although residential lending standards are gradually easing, first-time home buyers are more sensitive to increases in the mortgage rate. In anticipation of a Fed rate hike, the 30-year fixed-rate mortgage has risen roughly 20 bps since early October to 3.94 percent.

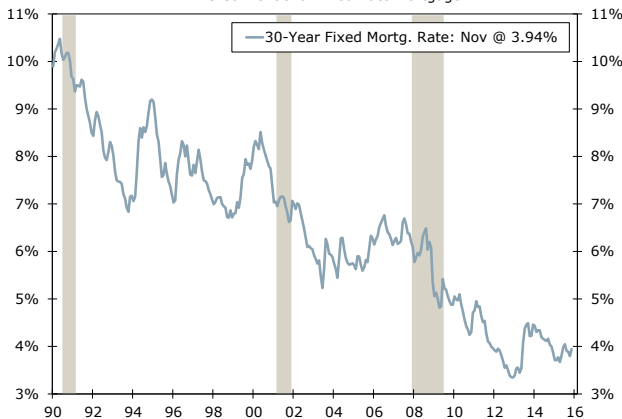
Existing Home Sales
Seasonally Adjusted Annual Rate, In Millions



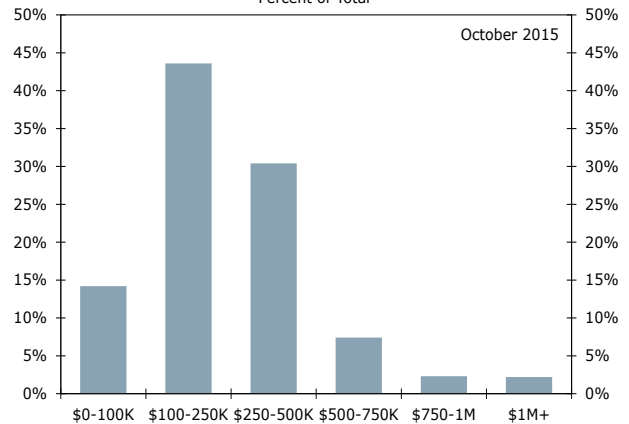
First-Time Home Buyers
Share of Existing Home Sales



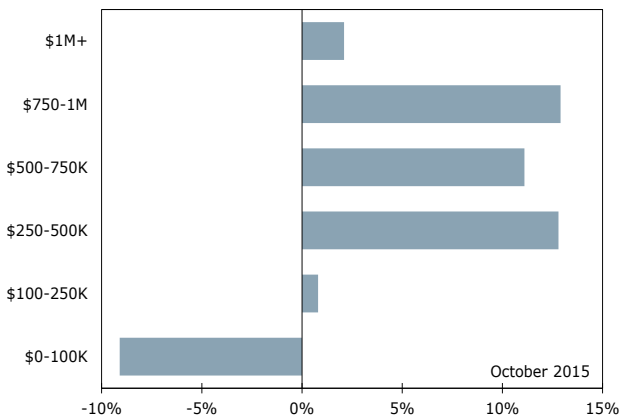
30-Year Mortgage Rate
FHLMC Conventional Fixed Rate Mortgage



Distribution of Existing Home Sales by Price
Percent of Total



Change in Existing Home Sales by Price
Year-over-Year Percent Change

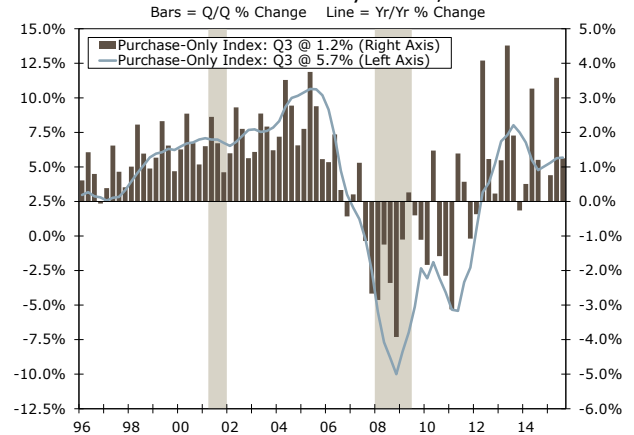


Source: NAR, U.S. Department of Commerce and Wells Fargo Securities, LLC

Home Prices

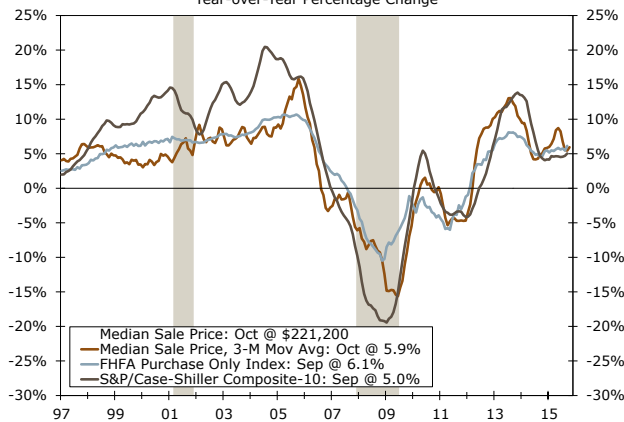
- Home price appreciation has been fairly steady in recent months, with most measures pointing to a roughly five percent year-over-year increase. According to the S&P/Case-Shiller National Composite Index, prices grew roughly 4.9 percent in September, with high-tech intensive markets continuing to see the strongest gains. On the other hand, metros with slower labor market gains and population growth such as Chicago and Washington, D.C, showed the slowest gains.
- Some of the most recent gains in home prices stems from heightened levels of foreign buying and a low level of inventories. We are also beginning to see some firming in prices due to a gradual increase in underlying demand, particularly in parts of the South and West.

FHFA Purchase-Only Index, NSA



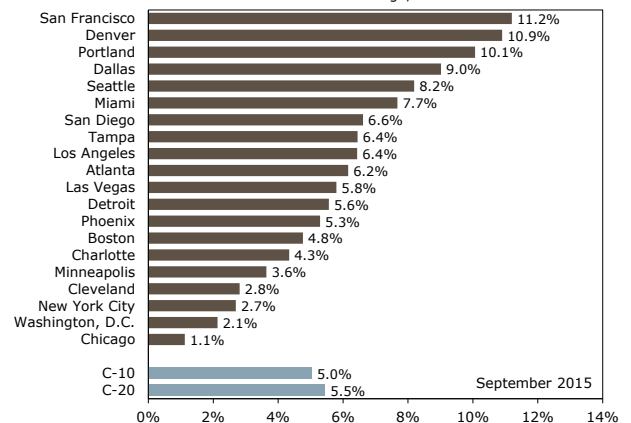
Home Prices

Year-over-Year Percentage Change



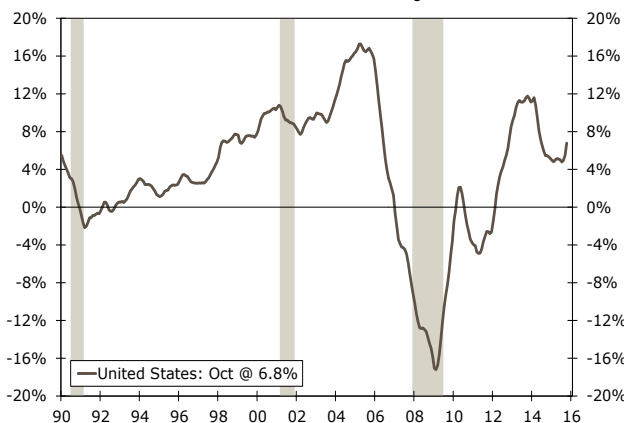
S&P/Case-Shiller Home Prices

Year-over-Year Percent Change, NSA



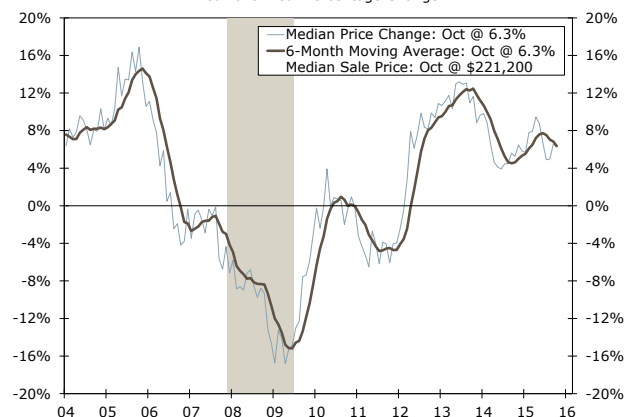
CoreLogic HPI: United States

Year-over-Year Percent Change



Median Single-Family Existing Home Price

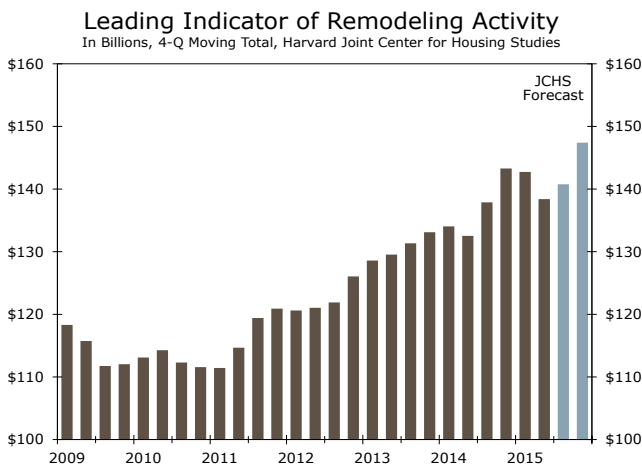
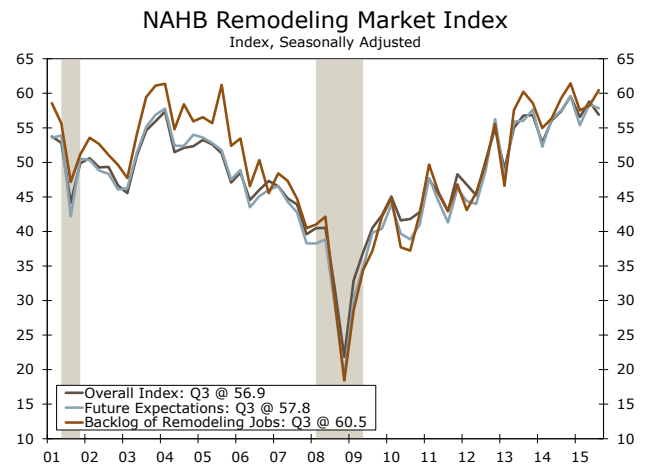
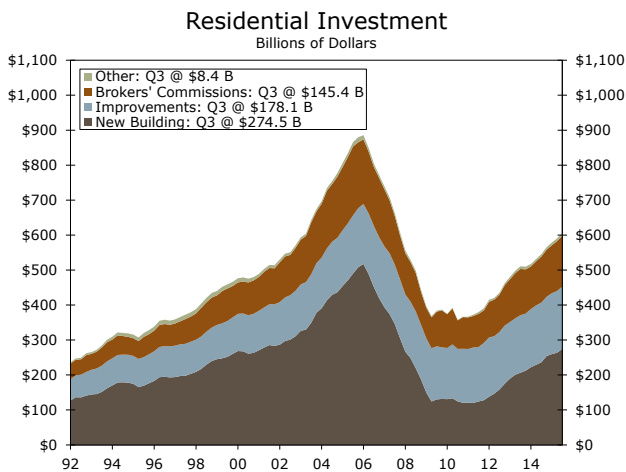
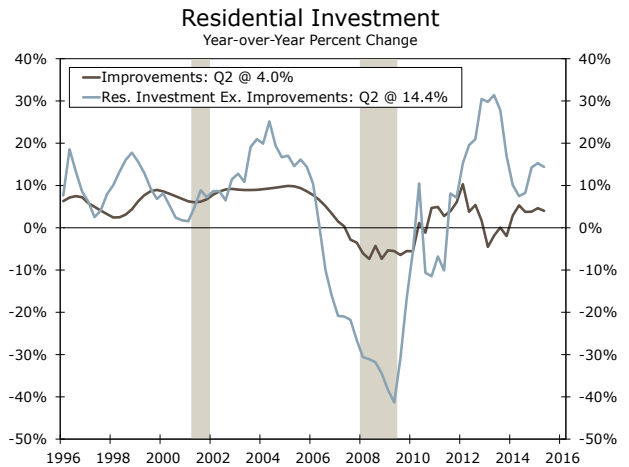
Year-over-Year Percentage Change



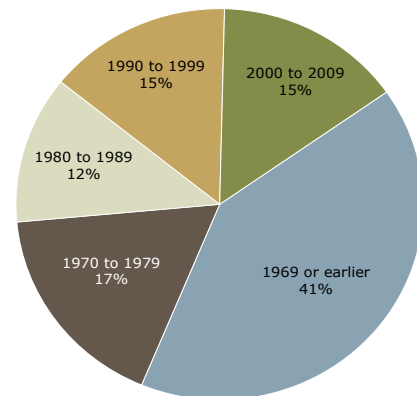
Source: CoreLogic, NAR, S&P, FHFA, U.S. Department of Commerce and Wells Fargo Securities, LLC

Renovation and Remodeling

- Along with the pickup in sales activity during the home buying season, home improvement spending continued to rise during the quarter by most measures. Studies done by the Joint Center for Housing Studies show owners are investing in more discretionary home improvements, such as kitchen and bath remodeling and room additions. Consistent with the larger share of older homes in the United States, roofing and siding outlays are also rising.
- The wave of refinancing activity in recent years suggests many households will be reluctant to put their homes on the market, especially as the Fed begins raising rates. The Leading Indicator Remodeling Activity projects annual spending growth will continue to accelerate in 2016.



Share of Owner-Occupied Housing
Year Structure Built - 2013



Source: Joint Center for Housing Studies, U.S. Department of Commerce, NAHB and Wells Fargo Securities, LLC

Wells Fargo Securities, LLC Economics Group

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