

US HOUSING MALAISE TO CONTINUE EARLY NEXT YEAR WITH JUMP IN RATES

**Housing starts declined 19% to an annualized 1090k in November and has been volatile in recent months due to swings in multifamily building activity*

**New residential construction has moved mostly sideways in 2016*

**The jump in mortgage rates will likely weigh on housing activity early next year*

Housing starts declined 19% to an annualized 1090k in November, continuing on the extreme volatility of the last few months due to swings in the multifamily sector. Looking past these recent swings, the six-month moving average of housing starts is 1177k, only slightly better than a year ago as starts have moved sideways over the last year. The housing market has disappointed in 2016, but it is still well below potential with plenty of room for improvement.

The recent surge in interest rates has already begun to push up mortgage rates and will likely hinder new home sales early next year. In May 2013, after the jump in interest rates with Taper Tantrum, new residential construction stalled for a few months (See Chart 1).

There is the possibility of a near-term surge in housing activity as persons try to lock in rates due to fear of further increases. Indeed, the mortgage applications for home purchases volume index has increased since the elections (see Chart 2).

To be sure, mortgage rates are still historically low and household balance sheets are better than they were a few years ago as incomes are starting to pick up, the labor market tightened and rising equity prices. So the drag on housing activity may be less intense than 2013 following the surge in rates.

Sentiment among businesses and home builders is improving. The National Association of Home Builders housing market index joined the group of other optimistic sentiment indicators post-election, jumping 7 points to the highest since mid-2005 in December (see Chart 3). According to the NAHB:

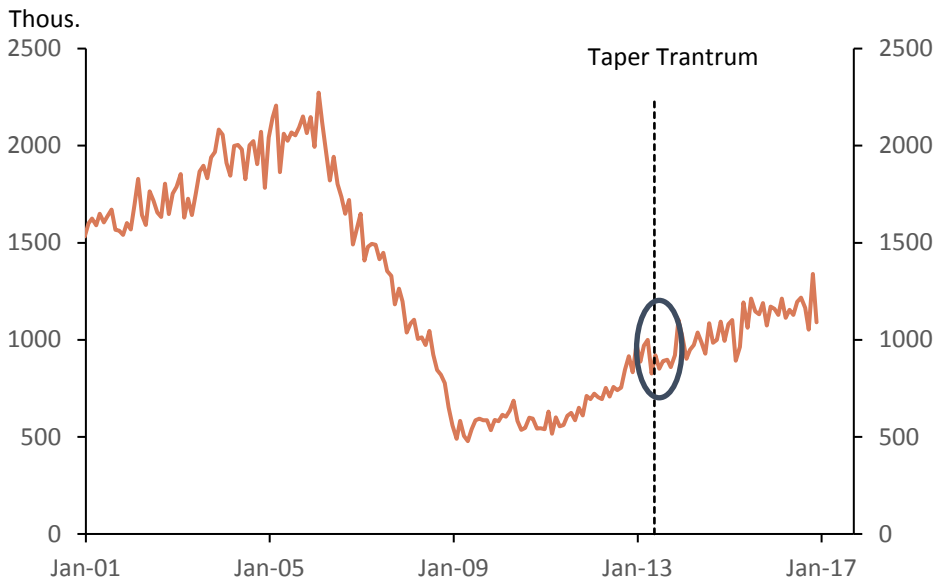
“This notable rise in builder sentiment is largely attributable to a post-election bounce, as builders are hopeful that President-elect Trump will follow through on his pledge to cut burdensome regulations that are harming small businesses and housing affordability... This is particularly important, given that a recent NAHB study shows that regulatory costs for home building have increased 29 percent in the past five years.”

The excessive regulatory burden on businesses and its adverse impact on business capex is something we have discussed extensively (see [“Resetting Fed Policy”](#) and [“How the Fed should reset monetary policy”](#)).

The expectation is to see a solid gain in residential investment this quarter - which won't be too hard following the very slow pace of activity over the last two quarters - then for activity to slow early next year due to the higher rates. Further out, strong household fundamentals, robust economic growth and the dearth of for-sale homes should overcome headwinds.

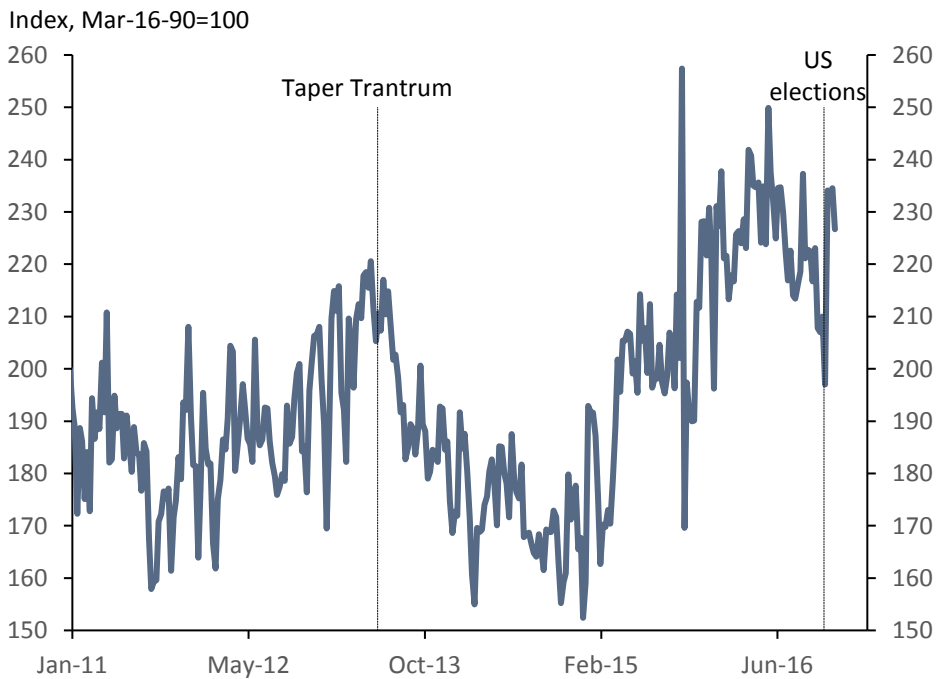
16 December 2016

Chart 1: Housing Starts



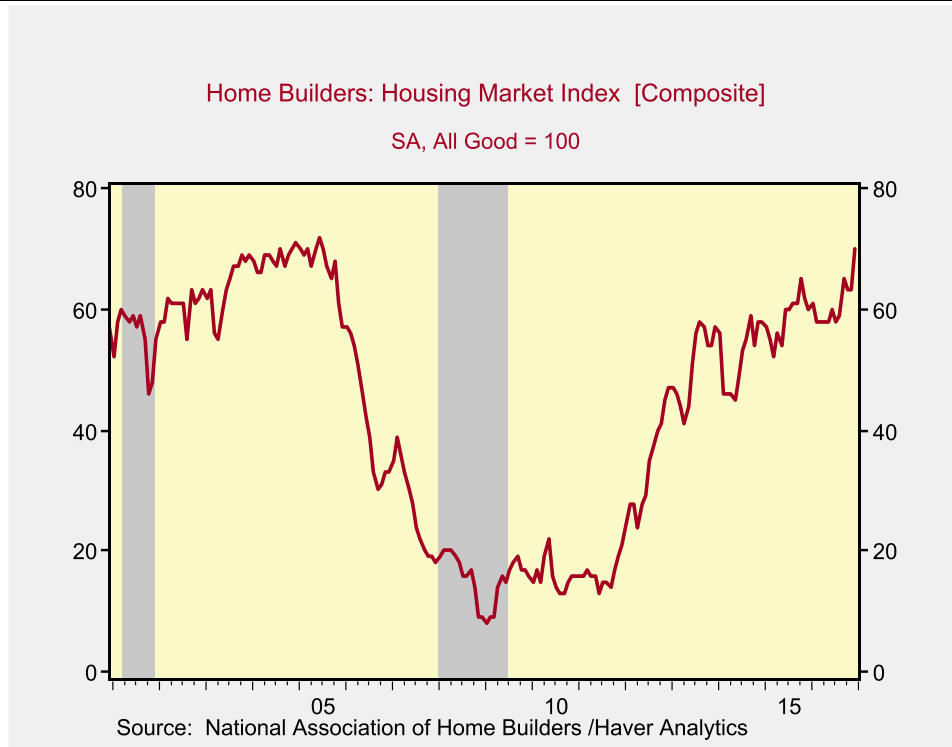
Source: Monthly data. Source: Census Bureau and Berenberg Capital Markets

Chart 2: Mortgage Applications for Purchase Volume Index



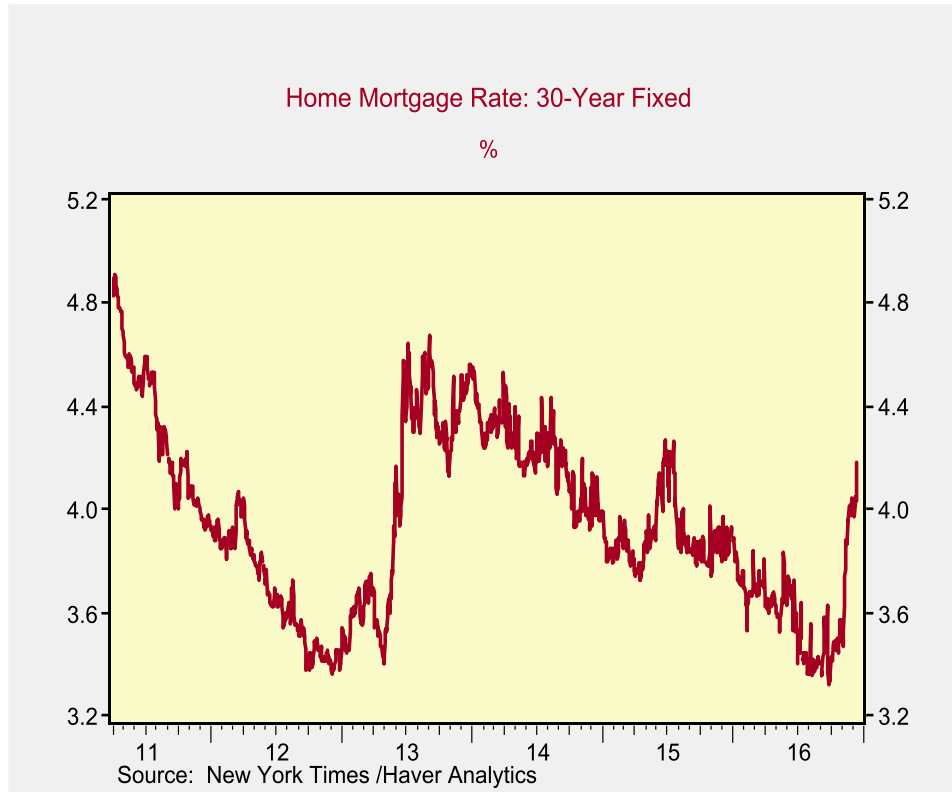
Source: Weekly data. Source: Mortgage Bankers Association and Berenberg Capital Markets

Chart 3: National Association of Home Builders Housing Market Index



Source: Monthly data. Source: National Association of Home Builders and Haver Analytics

Chart 4: 30-Year Fixed Home Mortgage Rate



Source: Daily data. Source: New York Times and Haver Analytics

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