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ECONOMIC TALKING POINTS

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Focus on the Right Data Point – Home Inventories

While existing home sales slipped another 5.3% in January, we continue to be encouraged by the ongoing decline in inventories for all types of housing. The mere fact that the supply of unsold homes keeps shrinking even as sales fall suggests that once demand picks up, we could see prices stabilize fairly quickly.

How close are we to that point? Given the decline in inventories, historic low mortgage rates, the implementation next month of President Obama's $275 billion housing plan, and the pent-up demand for homes, we expect to see the housing market strengthen before the end of this year. Our projection is for sales of new and existing homes to bottom out this summer.

(Some have argued that the deterioration in the job market has been so substantial, it will delay an upturn in home sales until 2010 or later. We disagree. There is no doubt that labor market conditions are awful and that it will temper any rebound in real estate. But housing typically leads the economy out of recession and history has shown it does so even in the face of rising unemployment. That pattern is expected to continue this cycle as well.)

We want to highlight just how much inventory numbers have fallen.

• The aggregate supply of unsold existing homes on the market dropped in January to 3.6 million. It's the sixth consecutive monthly drop and now stands substantially below its peak of 4.57 million of last July. Indeed, inventory levels are now edging close to where it stood in 2006, when sales reached record levels.

• Now let's break down these numbers by type of home:
The inventory of existing "single family houses" has fallen to 3.11 million last month, significantly off its high of 3.9 million reached in June '08. It, too, is a hair's length of the 2.92 million seen in the record sales year of 2006.

• The supply of existing condos and co-ops on the market has also been shrinking since summer. Inventory for these units fell to 490,000 in January, down sharply from the glut of 775,000 seen in July '08. In fact, inventory levels are now ***below*** that of 2006.

There's one last statistic that relates to home sales. The Mortgage Bankers Association's reported that applications for mortgages declined 15.1% in the previous week. Most of the decline was the result of fewer financings, which decreased 19.1%. Applications for actual purchases slipped 2.6%, but it followed a 9.1% jump the week before. It's our expectation that prospective home buyers, who have been sitting on the sidelines for the last two years, will take advantage of the President's plan once more details come out next month. Mortgage rates have already plummeted since December after the Federal Reserve announced it would buy mortgage backed securities from Fannie Mae, Freddie Mac and Ginnie Mae. The average rate on a 30-year fixed loan stands at 5.07%, near its record low of 4.89% in mid- January.

Tomorrow we'll get new home sales data and believe it will match the inventory trends seen with existing home sales.