

THE ECONOMIC OUTLOOK GROUP



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ECONOMIC TALKING POINTS

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Housing Starts and Jobless Claims: The Economic Hangover Begins

Welcome to the White House, Mr. President. Here are your first reports on the economy. Confidence among homebuilders has just fallen to its lowest level ever. Another report showed new home construction dropped to the fewest on record. And, oh yes, last week the number of Americans who applied for unemployment benefits for the first time jumped to its highest in 26 years. Coffee, sir?

OK, perhaps that's not quite the way President Obama received the latest news on the economy, but the point is the economic cycle operates independently of the political cycle. The historic transition in Washington and the huge celebration afterwards managed --- for a few moments at least --- to transport us away from our massive financial woes. What occurred in Washington was a spectacle for the ages and everyone in the nation wanted to share in the experience. But the formal party is over and the young, new Administration woke up to a pounding economic hangover. It's a hangover that will likely last for some time since no one yet knows how to deal with it.

Conditions in the housing industry --- the sector that brought on this whole crisis --- have just gotten worse. The National Association of Home Builders reported that confidence among their members dropped this month to its worst level ever. The Housing Market Index fell to 8 in January. It was 9 in December, and 19 a year ago. It stood at 24 in July 2007, just before the subprime crises erupted. (By the way, to put that 8 figure in perspective, 50 is considered the point where half the home builders are upbeat and the other half pessimistic.)

What's disturbing is here is that homebuilders are truly on the front lines of a critical industry. The U.S. economy cannot emerge from recession unless home prices and sales stabilize and builders begin to break new ground. Simply put, without a recovery in housing, this economy goes nowhere.

As if to underscore the point, the government today released December's housing starts and regrettably there was nothing to suggest the worst is over. Housing starts fell by another 15.5% last month to 550,000 unit annual rate, its slowest pace ever. It was 45% below its year ago pace, and down more than 75% from the 2.26 million peak reached January 2006. While new home construction did increase in the Northeast (12.7%) during December, it absolutely plummeted in the South (-22.2%) and the West (-24.5%), with a smaller decline in the West (-2.2%).

Plans for future home construction can be derived from permits filed with municipalities, but here too the numbers were dismal. Total building permits plummeted 10.7% last month, to a 549,000 unit rate, and that too was the fewest ever recorded.

These are all awful numbers, but builders really have no choice. It's not as if homes are unaffordable. Mortgage rates are below 5% in some communities and home prices have fallen sharply throughout the country. Indeed, home affordability as measured by the National Association of Realtors is now at its highest in more than five years. The primary problems homebuilders face is the lack of mortgage finance for those who want to buy a new home, the difficulty prospective buyers have in even selling their current homes, the growing stock of houses on the market for sale, and the worsening job market which has scared people away from making large purchases.

The job outlook got even grimmer today after the government said that 589,000 Americans filed for unemployment benefits for the first time last week. That's a 62,000 increase from the previous week and the most since November 1982. The same week a year ago, the number of new claims filed came to 324,000.

The total number of Americans now collecting unemployment benefits rose to 4.607 million, compared with 2.68 million a year ago. Said another way, the number of people out of work and relying on unemployment insurance now exceeds the combined population of Vermont, New Hampshire, Delaware, Rhode Island, and South Dakota.

Is there anything ---anything at all ---in these stats that might be a portent of better times?

Perhaps, but it's a stretch. First, there are two subset statistics in the home builder survey that are (possibly) worth mentioning. The traffic into showrooms and new home models has picked up in January. This index rose to 8 in January from a record low 7 in November and December. Nothing dramatic here except to say that this was the first rise in traffic seen since September. Another subset is based on builder expectations of what conditions will be like in six months from now and it, too, increased by a tick, to 17 this

month, from a record low 16 in December. This was also the first increase since September.

Maybe these two data points are not worth the ink we just spent on them. But they have been fairly good leading indicators in the past. At the very least, they just might prevent the economic hangover many feel in the White House from turning into a full-blown migraine.

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