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# US Macroeconomics

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## A Development Rarely Seen Outside of Recession

The first snapshot of Q2 2023 real GDP rose a better than expected 2.4%, which led many investors to increase their probability of a soft landing. However, one leading indicator of the economy continues to shrink, which is a potentially troubling sign, especially if job losses appear in the month immediately ahead.

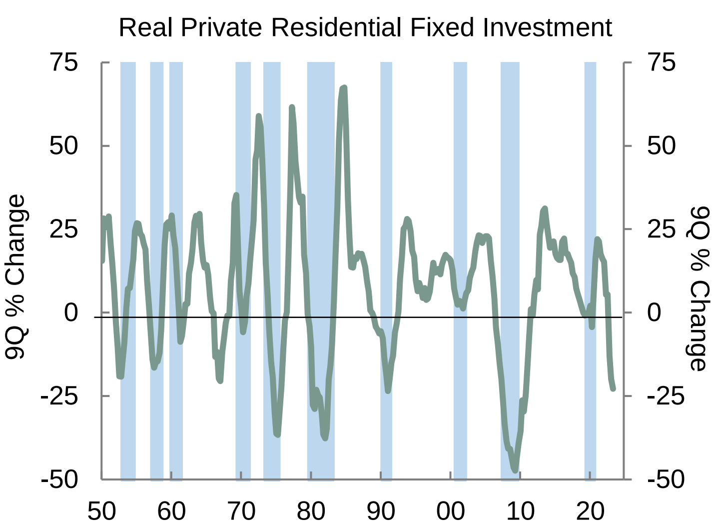
Residential investment (i.e., housing construction) fell 4.2% after a similar drop in Q1 2023. This marked the ninth consecutive quarterly decline, a development seldom, if ever, seen outside of recession, as illustrated in the left-hand side chart below.

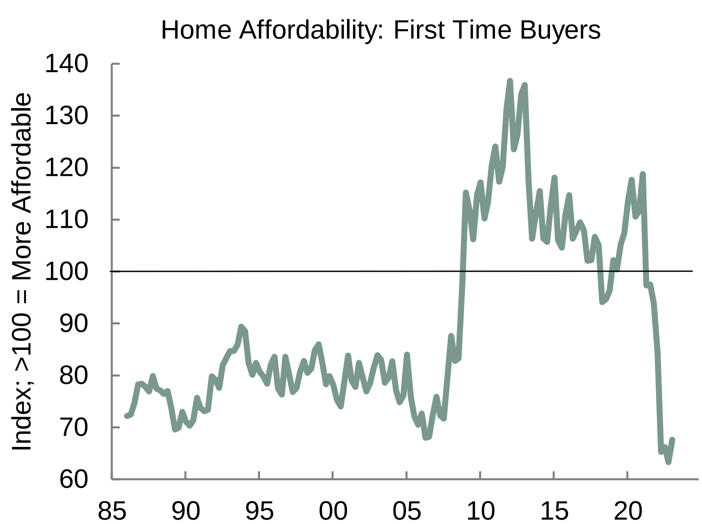
**Since its Q1 2021 cyclical peak, resident investment has fallen a cumulative 22.8%. This is the fourth largest drop on record**. The worst nine quarter stretch immediately preceded the 2008-09 downturn (-33.4%), while the other notable declines, as shown in the chart below, occurred during the 1973-75, 1981-82 and 1990-91 recessions.

With mortgage rates up near 7% and more than double where they were last year, housing affordability is near all-time lows. As we can see in the right-hand side chart below, first-time home buyers only have 68% of the requisite income to qualify for a conventional mortgage with a 20% downpayment on a median-priced existing family home.

**With affordability so low, the demand for new construction should eventually weaken**. Counterintuitively, it has been strong because many homeowners cannot afford to move because they have a low mortgage rate. This has limited transactions as seen by the collapse in pending home sales. Hence with little available supply, this has given a temporary bid to new construction. But this will not last.

Residential payrolls rose 11k in June, the third increase in a row and the fifth gain in the last six months. **When the full impact of significantly higher mortgage rates is fully felt, construction employment should falter**. And when that happens, it is likely to presage broader economic weakness given the housing market's outsized impact on GDP. For example, demand for appliances, furniture and home services should slow. Also, the construction industry tends to pay higher than average wage rates so income loss could be significant.




Sources: BEA, NAR, Bloomberg, Haver, SMBC Nikko

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