

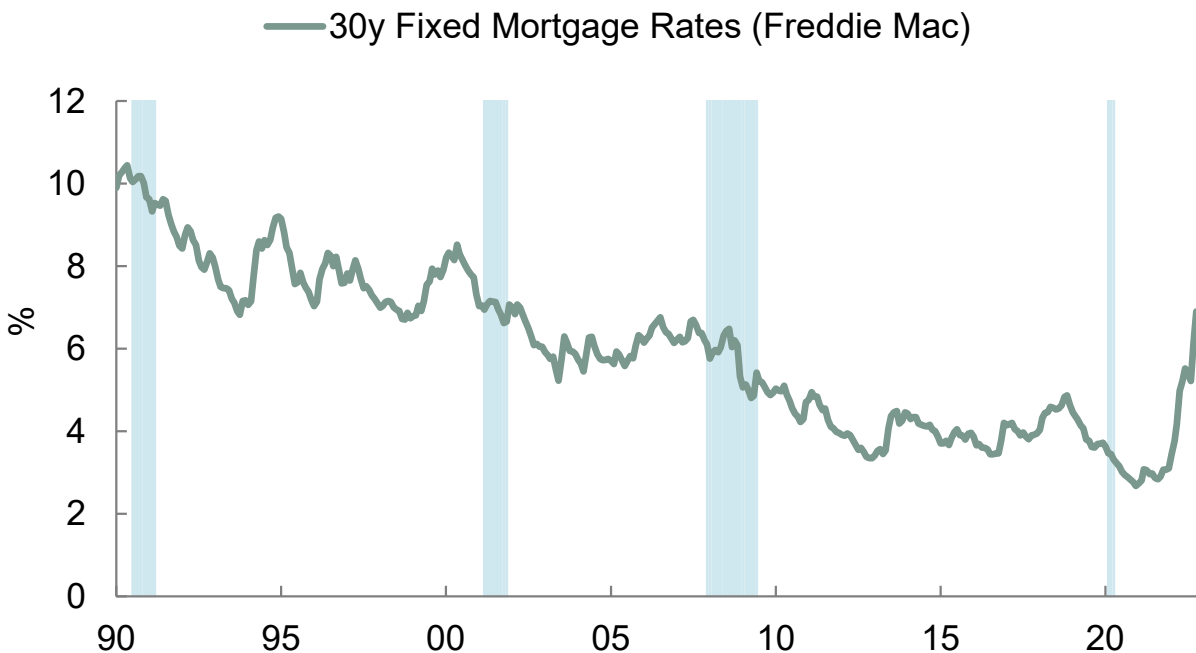
The Housing Market Is On The Precipice Of A Deep Downturn

Joe Lavorgna
Chief US Economist
SMBC Nikko, Inc.

(212) 610-1741
joseph.lavorgna@smbcnikko-si.com
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Surging Mortgage Rates

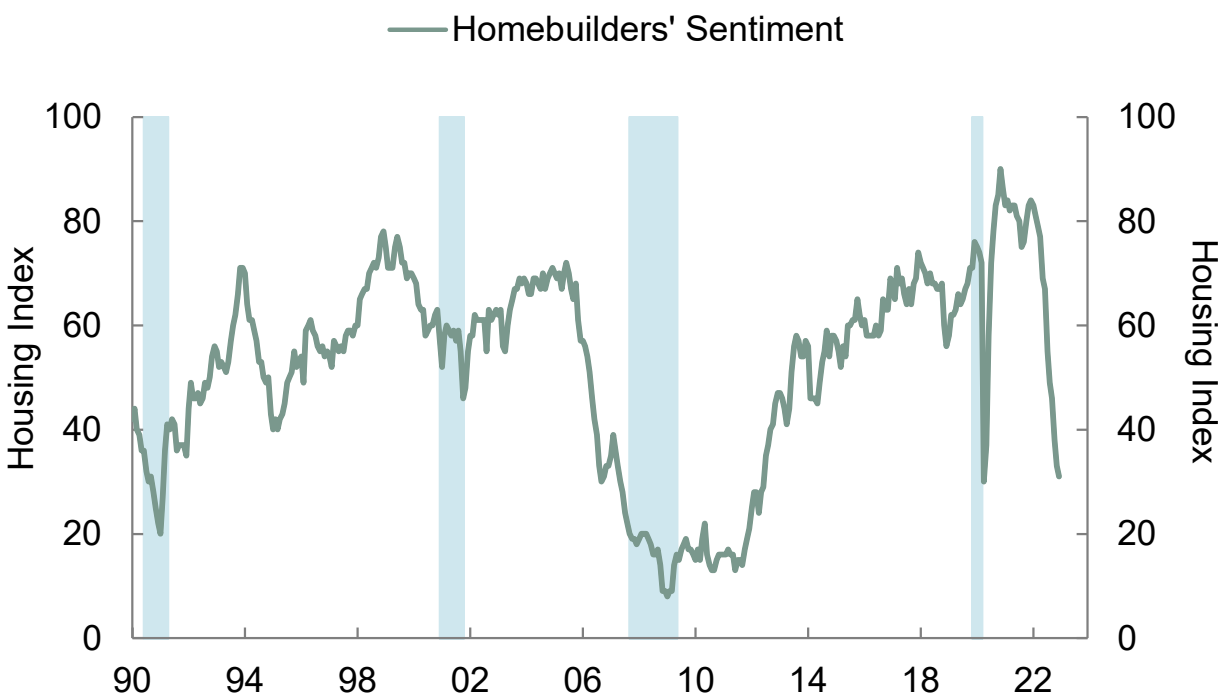
Mortgage rates have surged on the back of dramatic Fed tightening and quantitative tightening. Over the last nine months, the Fed has lifted the funds rate over 400 basis points and shrunk its balance sheet by nearly \$400 billion. This led to the biggest increase in mortgage rates since the early 1980s. While rates have fallen over the past few weeks to below 7%, they remain high. It is no wonder that home sales (new and existing) are down 27% year-to-date. Until mortgage rates fall significantly more, home sales will remain under significant downward pressure.



Source: Freddie Mac, Haver, SMBC Nikko

Ongoing Collapse in Homebuilders' Sentiment

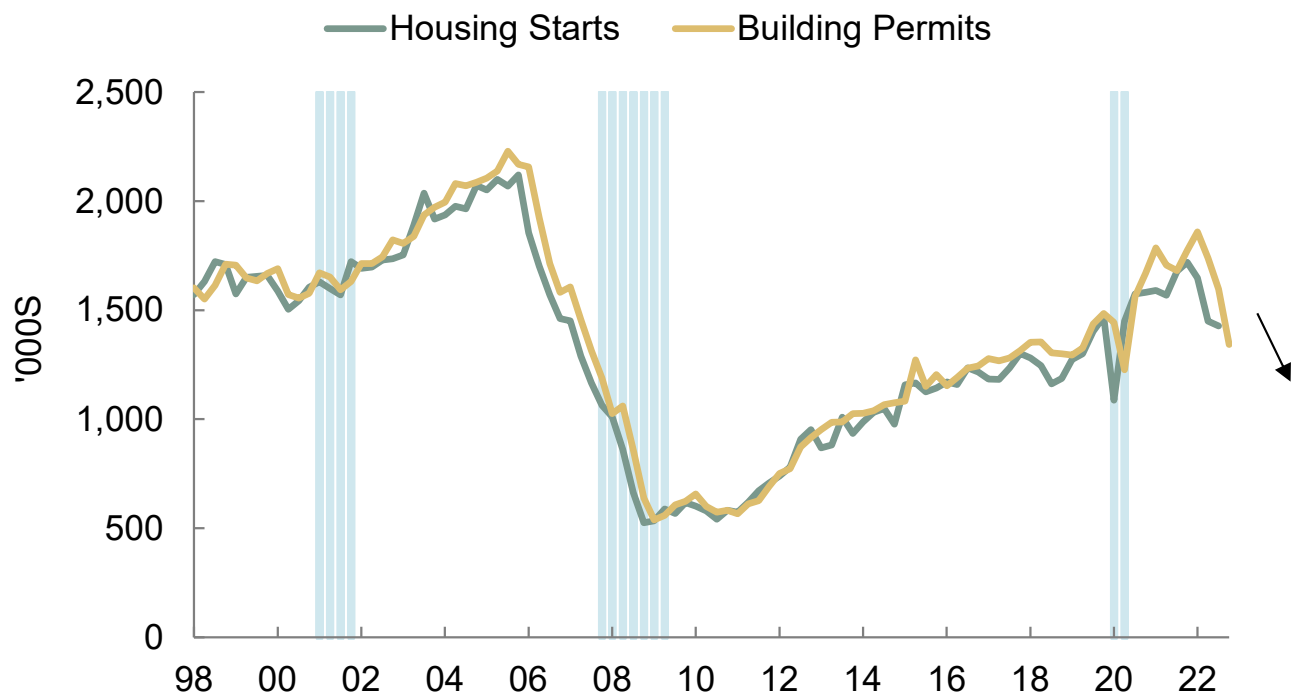
Homebuilders' sentiment fell in December to a 31 reading, just one point above its covid-related lockdown low. Over the past 12 months, sentiment is down 53 points, which is the largest annual decline in the history of the series dating back to 1985. This tells us housing starts and permits have significant further room to fall, an ominous development since they are leading economic indicators.



Source: NAHB, Haver, SMBC Nikko

A Large Negative Multiplier

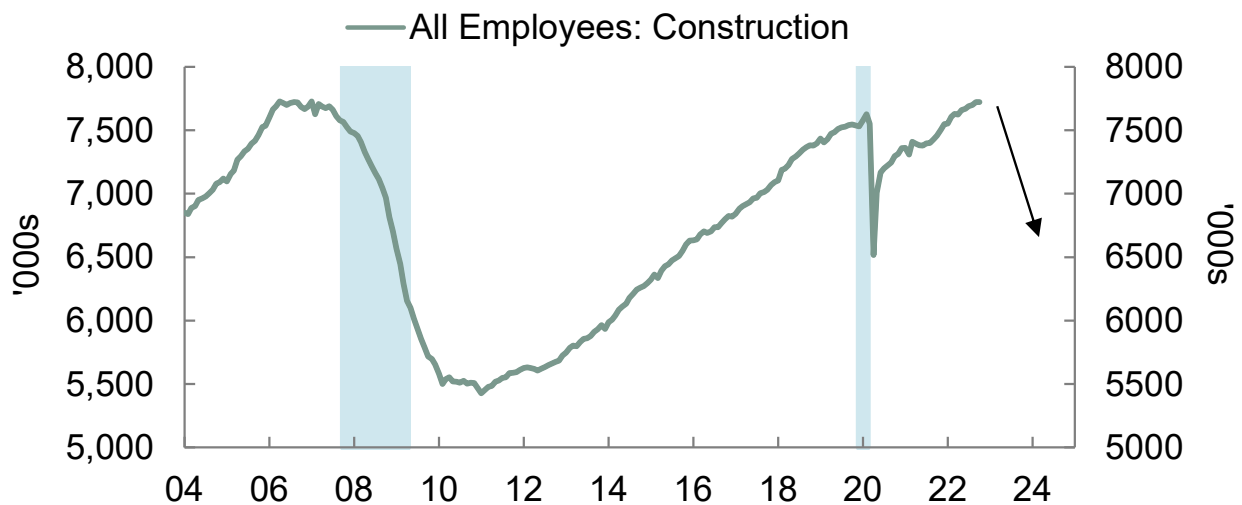
Housing starts and permits, which are leading indicators of real GDP and the stock market, are trending downward. Eventually, This suggests that construction employment should soon decline. To be sure, weaker housing activity means there will be much less spending on appliances, building materials, home electronics and furniture!



Source: Census Bureau, Haver, SMBC Nikko

Already In Recession

Residential investment within GDP has declined six straight quarters but the deterioration is worsening. The series fell a large 27% at an annualized rate last quarter. While overall construction employment has stayed elevated, a steep decline in construction jobs is forthcoming. If past is prologue, this will foreshadow a broader weakening in the jobs market by mid-2023.



Source: BEA, BLS, Haver, SMBC Nikko,

Starts and Stocks Tend to Bottom Around the Same Time

In the table below, we show the peaks and troughs trough in housing starts and the S&P 500 since 1960. In some cycles, starts bottomed before stocks (1970, 1981 and 2001) while in other cycles, starts bottomed just one month (1980 and 2009) or two months (1960 and 1975) after stocks. The only time that starts missed the mark was 1991 when they bottomed three months after equities. This sets up a troubling backdrop for the stocks if housing still has significant further downside to come. Stay tuned.

What is the Time from Housing Bottom to Stock Market Bottom?

<u>Business Cycle Troughs</u>		
Housing Starts	Dec-60	2m lag
SPX 500	Oct-60	
Housing Starts	Jan-70	5m lead
SPX 500	Jun-70	
Housing Starts	Feb-75	2m lag
SPX 500	Dec-74	
Housing Starts	May-80	1m lag
SPX 500	Apr-80	
Housing Starts	Nov-81	9m lead
SPX 500	Aug-82	
Housing Starts	Jan-91	3m lag
SPX 500	Oct-90	
Housing Starts	Oct-01	12m lead
SPX 500	Oct-02	
Housing Starts	Apr-09	1m lag
SPX 500	Mar-09	

Source: Haver, SMBC Nikko

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