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Homebuilder Confidence Continues to Grow This Year

The NAHB HMI index's February reading is the highest since September.

The housing market may be turning a corner even as builders continue to contend with high construction costs and building material supply chain logjams, according to a new report from the National Association of Home Builders (NAHB).

Its HMI index, produced with Wells Fargo, measures builder confidence in newly built single-family homes in February rose seven points to 42. It marks the second consecutive month of improvement and represents the strongest reading since September.

The rise matches the cautious optimism noted by a large number of builders at the recent International Builders' Show in Las Vegas, who reported a better start to the year than expected last fall, NAHB Chairman Alicia Huey, a custom home builder and developer from Birmingham, Ala., said in prepared remarks.

The report noted that the construction of entry-level homes is the most challenging part of the home-building market.

Erica Bell, Marketing Manager with mid-Atlantic-based Miller & Smith, tells GlobeSt.com that she sees that sales are picking up.

“We still aren't back to 2022 numbers, but we see an upbeat in traffic and interest at all of our communities,” Bell said.

New-Home Construction Might Be Stabilizing

Crystal Sunbury, real estate senior analyst with RSM US, tells GlobeSt.com that January building permits increased slightly in January to 1.339M annualized units from 1.330M the prior month. Housing starts declined 5.3% to 1.309M from 1.382M in December.

“Builders have pulled back in construction because of low demand,” Sunbury said. “However, the slight decrease in permits coupled with rising builder confidence, which rose to 42 in February, as builders have reported stronger than expected January sales, indicate there may be stabilization in new home construction.”

She said that buyers are ready to get back into the market; however, volatile mortgage rates (which had dropped in January, encouraging sales activity) will continue to pose challenges for builders, given home buyers' high sensitivity to mortgage rates."

The average 30-year fixed rate mortgage rate peaked at 7.08% in October, according to Freddie Mac. Rates declined lately, but again recently rose to approximately 6.7% this week.

"Recently reported earnings indicate builder margins while falling back to pre-pandemic levels, remain strong (generally 22% to 25% range for larger builders), with some builders reporting higher and closer to the pandemic period (average of 28%)," according to Sunbury.

"Builders have employed various strategies, with some being more flexible with pricing to encourage sales activity and others pulling back more significantly on construction.

"As we enter the spring market, we are likely to see more builders providing incentives to encourage sales activity, particularly if rates remain high."

"Hopefully" A Positive Indicator
Michael J. Romer, Managing Partner, Romer Debbas, tells GlobeSt.com, "This is certainly positive news and hopefully an indicator that a major upward shift is coming.

"The recent slight increase in builder confidence can best be attributed to cautious optimism after an uptick in buyer demand. However, to put things in perspective, builder confidence per the Housing Market Index was 81 only one year ago, it currently sits at 42 but it's trending in the right direction.

"Across the country, builders are starting to reduce prices which is certainly helping the cause. But concern regarding mortgage rates and affordability has many buyers priced out or sitting on the sidelines. For far too long, the housing market has felt the brunt of the government's battle against inflation."

Northeast and Central Florida See a Surge
Noah Breakstone, CEO of BTI Partners, tells GlobeSt.com that it is difficult to predict the short-term direction of the housing market. However, he has observed a recent surge in inquiries from regional and national homebuilders seeking to expand their land pipelines in Northeast and Central Florida.

"Typically, homebuilders do not hold large tracts of land for future development as it is perceived as a liability by Wall Street," Breakstone said.

"Therefore, when the market turns favorable, they actively seek ready-to-build land to quickly resume building operations. Developing land for vertical construction purposes can take anywhere from two to four years, which is too long to capitalize on a changing market unless the land is already available.

"A decade ago, our primary objective was to develop the large tracts of land we had purchased across Florida. As we secured the entitlements and completed the infrastructure work, we were dealing with homebuilders who were experiencing a shortage of ready-to-build sites and were interested in purchasing entitled and improved land tracts. The demand for these sites has grown significantly and our business model shifted to meet this need."

Might Be the Right Time to Jump Back In
Paul Rahimian, CEO and Founder of Parkview Financial, tells GlobeSt.com that the market is still in flux, with monthly changes as to what can be expected next.

"With recent increases in employment numbers and inflation not really subsiding fast enough, there is more uncertainty in the market today than there was a few weeks ago.

"However, home builders are suddenly confident, with lower mortgage rates (still higher than last year, but lower than recent highs) and the possibility of lower construction costs on the horizon (they are not here yet but are anticipated later this year).

"There is a lack of supply of homes and the builders think this might be the right time to jump back in. They could switch gears if mortgage rates go up significantly in the next few quarters."

Sales Improve with Price Drops
Mathew A. Wyman, Partner & Chairperson, Cox Castle, tells GlobeSt.com that most builders are seeing improved sales but that is because they dropped pricing to offset some of the interest rate increases.

"So, deals cut before the builders found the clearing price may still need to be repriced to reflect these lower exit values not contemplated in the builder's original underwriting," Wyman said.

"I am cautiously optimistic that now that we are in a market reset phase similar to 2018, and now that the builders have found the market clearing price, they can look to transact on land acquisitions.

"However, there is still a lot of uncertainty around where the economy and the capital markets and interest rates are going generally and, for the private builder, availability of construction financing. So, I would not expect to see any big acquisition activity in the very near future."

A Focus Along I-35 in Texas
Shannon Livingston, president of RREAF Communities, a division of RREAF Holdings focused on acquiring, developing, and delivering highly amenitized, large-scale master-planned communities, tells GlobeSt.com that the HMI is an index of builders' current perception of single-family homes.

"This market tends to be volatile and heavily dependent on geography, so sales can be dramatically different in different locations around the country," Livingston said.

"While the increase in interest rate negatively impacts the ability of buyers to purchase such homes – this negativity is offset by the increased demand, in certain markets, for affordable housing and desired locations.

"These locations are usually areas where jobs are available, taxes are low, and the perceived quality of life is high or growing."

He said that RREAF has focused its communities' efforts on locations along I-35 in Texas for example, where the increase in net positive migration of workers and young professionals driven to the area by growth in job opportunities in new plants such as Tesla and Samsung, fuels the demand for single-family homes.

“The market eventually reaches an equilibrium of supply and demand, but the HMI increase is indicative of the positive offset of demand, over the now slightly stabilized, yet elevated, interest rate,” according to Livingston.

Home Price Collapse ‘Never Came’

John Hunt, chief analyst, MarketNsight, tells GlobeSt.com that pending sales bottomed in November 2022 as rates hit 7% highs.

“As mortgage rates have moderated, we have seen pending sales show solid gains since then. Builders are more positive in January and February of this year because home buyers started coming back to the market in November of 2022.

“The collapse in home prices that many headlines predicted never came, and the sticker shock of rates rising at the fastest clip ever has begun to wear off. Rates are still at historical lows as is inventory, and people still need a place to live.”

Accidental Landlords Emerge

Dana Dunford, CEO at Hemlane, tells GlobeSt.com that record low supply has been the biggest story in real estate for the past five years “but we’re seeing a new trend away from flipping homes and back to fundamentals; 83% of rental owners stated they purchase for cash flow.

The combination of a strong rental market and homeowners locked into record low interest rates means that they’re holding onto their prior properties and converting them to cash-flowing rentals, according to the most recent Hemlane State of Property Management report, she said.

This trend is gaining momentum and 70% of rental owners are planning to buy purchase more single-family rentals in the next three years, according to Hemlane.

https://www.globest.com/2023/02/17/homebuilder-confidence-continues-to-grow-this-year/