



20 August 2014



SENT TO LSU AGCENTER/LOUISIANA FOREST PRODUCTS DEVELOPMENT CENTER - FOREST SECTOR / FORESTY PRODUCTS INTEREST GROUP

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To all - latest housing note. Housing not improving very quickly. Multi-family remains strong with single family taking longer to recover. Still lots of headwinds. Affordability becoming a problem, particularly with 1st time buyers. Job market improving, but still, too many jobs are part time. Most analysts have been paring down recent forecasts with many not expecting full recovery until 2016.

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# Housing comments – August , 2014

Economy – short term ( next 2-3 years):

- Housing getting better, but multi family is the driver so far – 40% of starts (SAAR) in August – rental demand is strong!!!!
- Housing's issues - slowing world economy; weak job market; sluggish income growth; tight credit environment continues
- This is not your typical housing recovery – 1<sup>st</sup> time buyers are absent while investors and cash sales are much higher percentage – this will create problems going forward.
  - (1) lost “follow-through” with delayed 1<sup>st</sup> time purchasers ( i.e., move up purchases at later date).
  - (2) also, as interest rates increase, investor and foreign buying activity will wane.

Economy – longer term ( next 4 - 8 years) – slower growth ( <3% ??) due to demographics

- that means housing starts may not return to “trend” ( 1.5 – 1.6 million) unless we get some help from favorable immigration policies – aging population spends less, buys fewer houses, consumes less, .... Similar situation in Europe

*The return of 1st time buyers is the key to any sustainable recovery in housing !!!! That depends on a stronger job recovery. Right now, prospects are not good. Student debt is serious problem for many young people so they are putting off forming households Here is good article discussing impact on housing.*

*(<http://www.td.com/document/PDF/economics/special/USStudentLoansHomeownership.pdf> )*

## Here are some good references from NAHB on Impact Of Housing on the Economy

Gives you some appreciation why housing is so important to the Economy, and why one can't move forward without the other!!!!

- (1) Impact of Homebuilding and Remodeling on the U.S. Economy  
(May 2014, Paul Emrath)
- (2) Housing's contribution to GDP ( NAHB staff)

( [http://www.nahb.org/reference\\_list.aspx?sectionID=784](http://www.nahb.org/reference_list.aspx?sectionID=784) )

# Housing, Economy, and wood products

Here is another good article on housing's impact on the economy – why the economy is having problems moving forward.

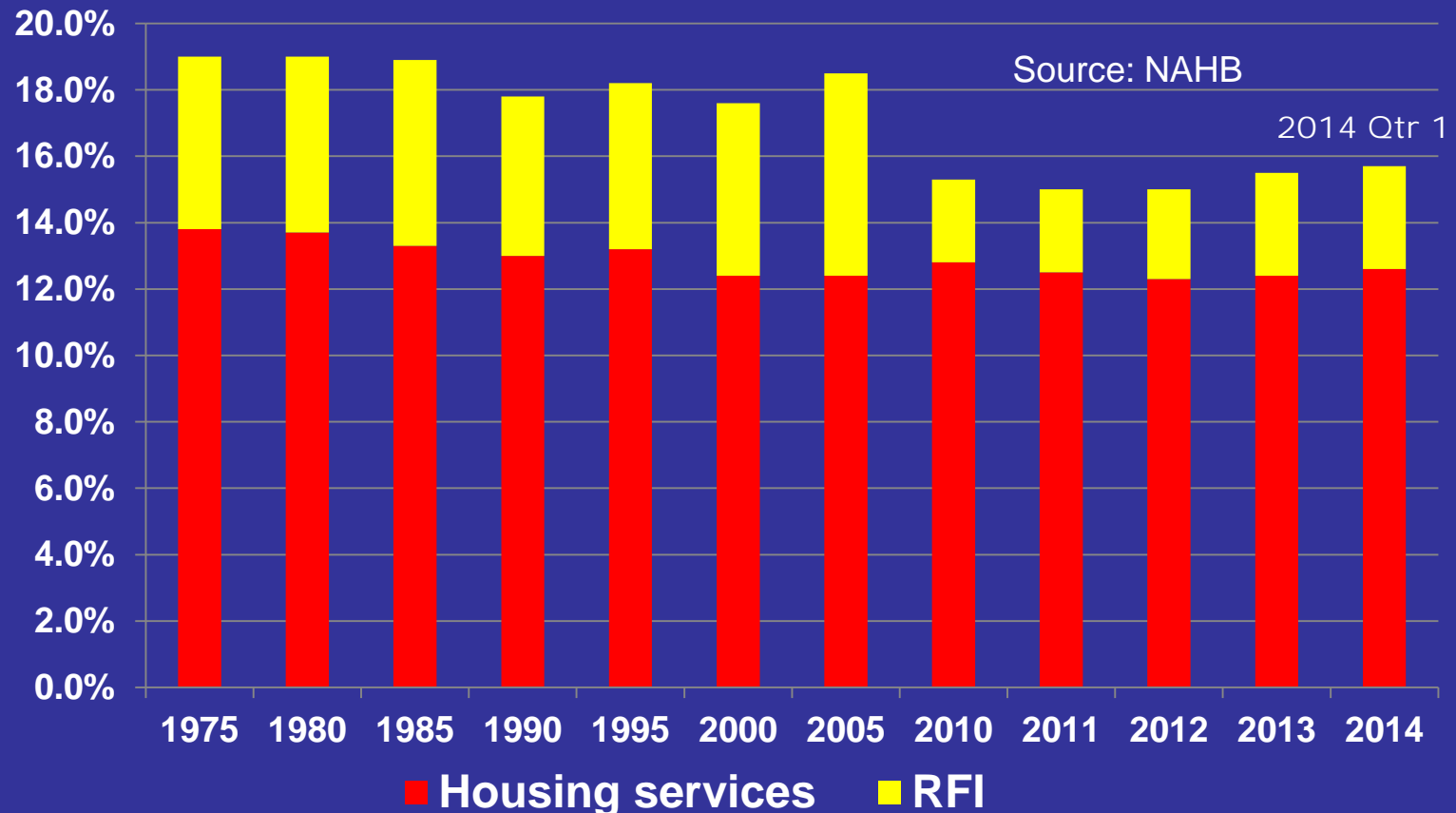
**NYT** (<http://www.nytimes.com/2014/04/27/upshot/the-housing-market-is-still-holding-back-the-economy-heres-why.html?ref=business&r=1> )

Here is the dilemma – housing contributes about 4% directly to GDP and another 12 – 15% indirectly, for a total of 16 – 19%. The key to housing's recovery is good paying jobs with benefits. That means we need a stronger economy. But, with housing and related activities contributing only 15% to GDP, that won't happen. The old “chicken and egg” dilemma. What is the solution? I've read that U.S. businesses have about 2 trillion Dollars stashed on their balance sheets ( **much of it offshore**). If they were to invest that in plant, equipment, job training, technology, R&D, Etc., that would create jobs and some momentum for the economy. What is holding them back? Uncertainty is key reason ( **and the corporate tax code**). We need ‘Washington’ to provide leadership in where the country is headed and how to get there – we need to remove some of the uncertainty. And, they need to convince businesses ( and the public) that their vision ( to fix the economy) is realistic and they have a viable strategy for achievement. A tall order and I know I have oversimplified things. But, the current mix of politicians in Washington can't agree on A unified strategy to move the country forward. Consequently, housing, the economy, and hence, the wood products industry, will continue to “underachieve”.

Housing's contribution to GDP (%) – historically, it is almost 20% of the economy when you include housing services and fixed investment, but today it is down to 15%. In reality, it is even more important when you include purchased furniture, landscaping, general maintenance, etc. key reason why the economic recovery remains muted

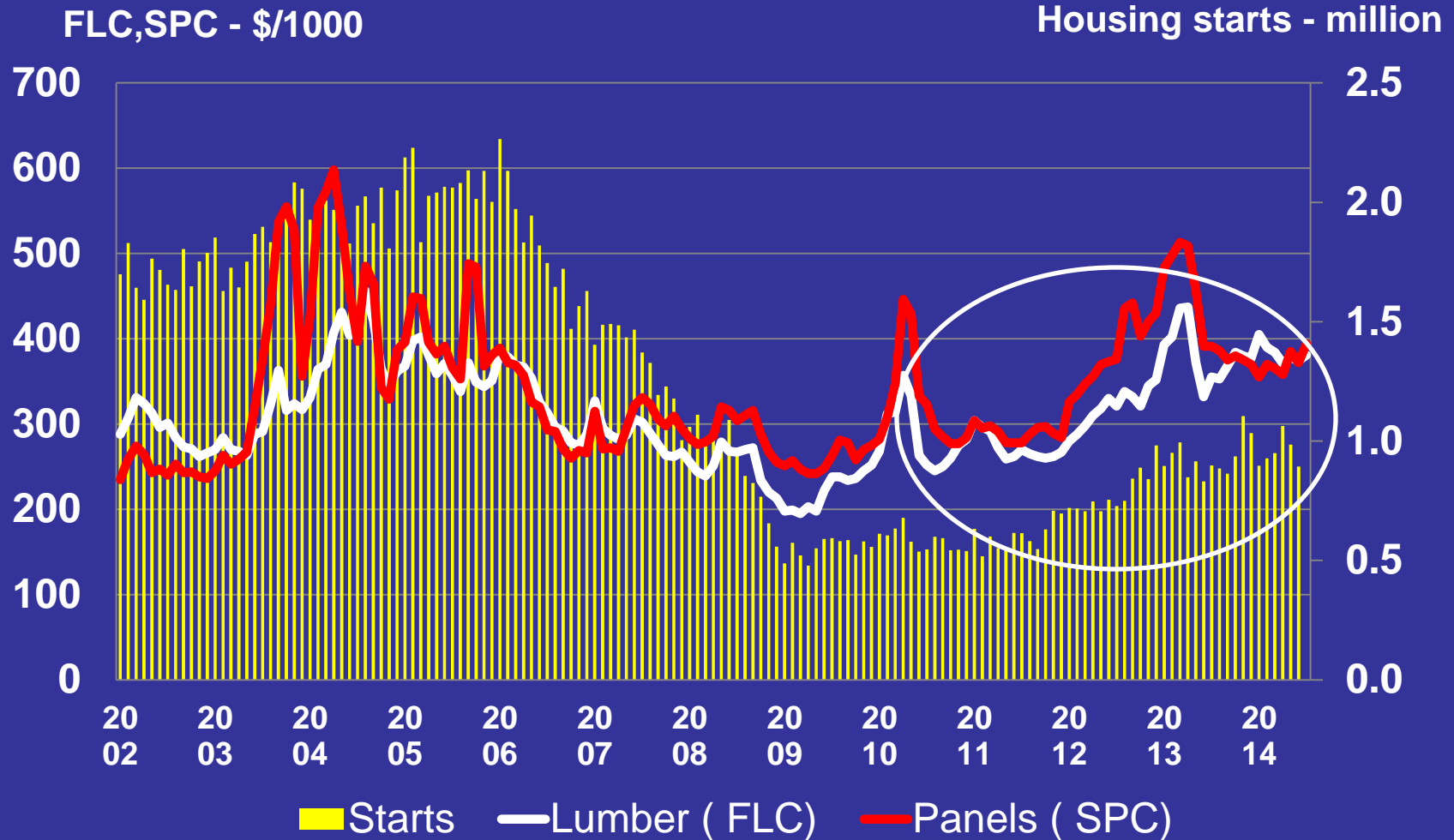
Housing services = gross rents paid by renters (include utilities) + owner's imputed rent (how much It would cost to rent owner occupied homes) + utility payments

RFI (residential investment) = construction of new SF and multifamily structures, remodeling, manufactured homes , plus broker's fees



# Housing starts and wood product prices – Economics 101

75% of structural wood products go to housing ( new construction plus remodeling)  
50% or more of hardwoods go to housing related activities.

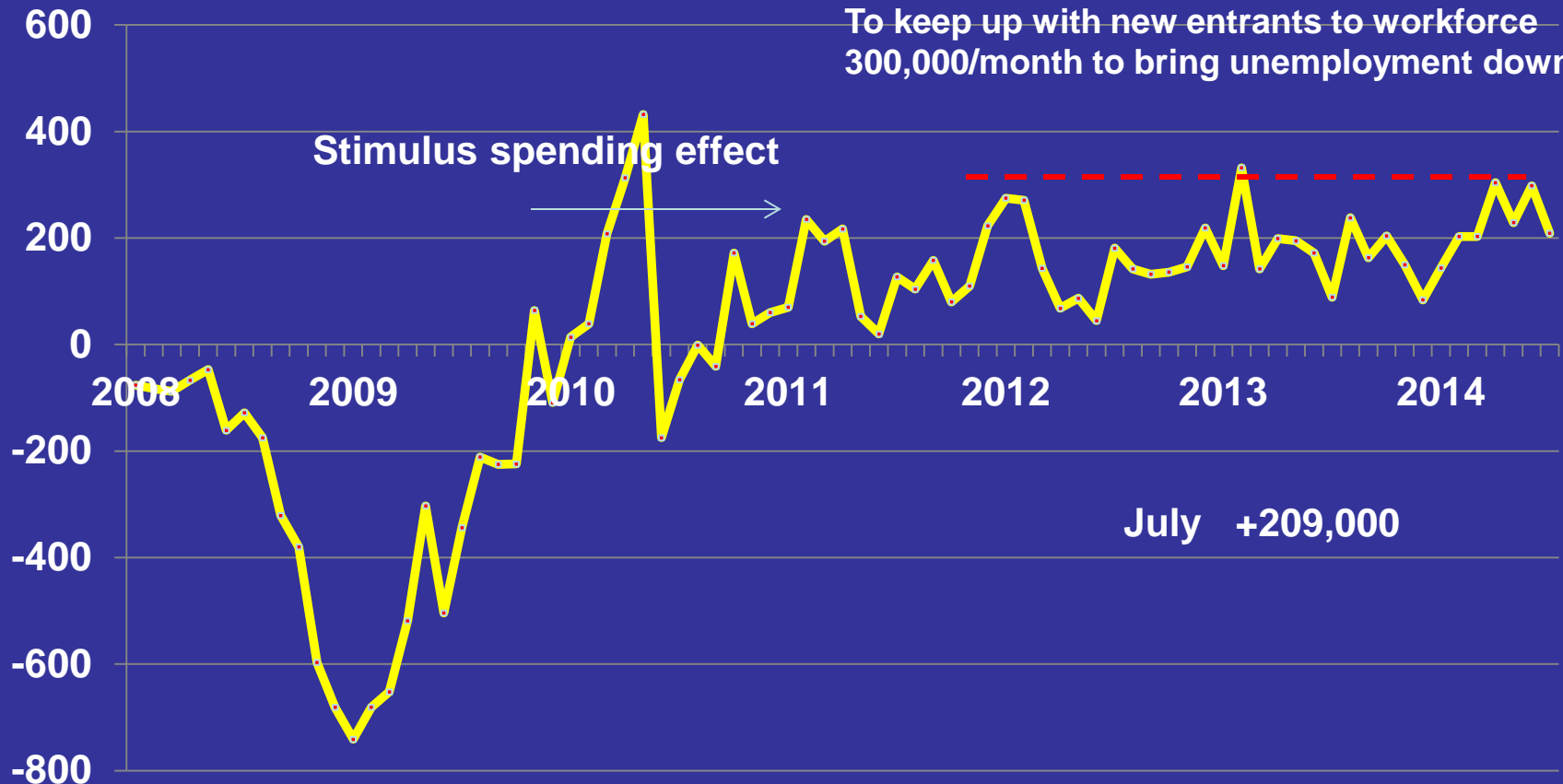


Sources: Prices – Random Lengths (<http://www.randomlengths.com/>); starts ( Bureau of Census ( <http://www.census.gov/construction/nrc/> )

**Employment situation - our biggest problem - it's getting better, but the jobs recovery remains weak by past standards, and many jobs ( e.g., temporary ones)  
Don't include health care or retirement benefits – those kinds of jobs don't encourage people to buy houses**

### Net change in non farm payrolls – monthly, thousands

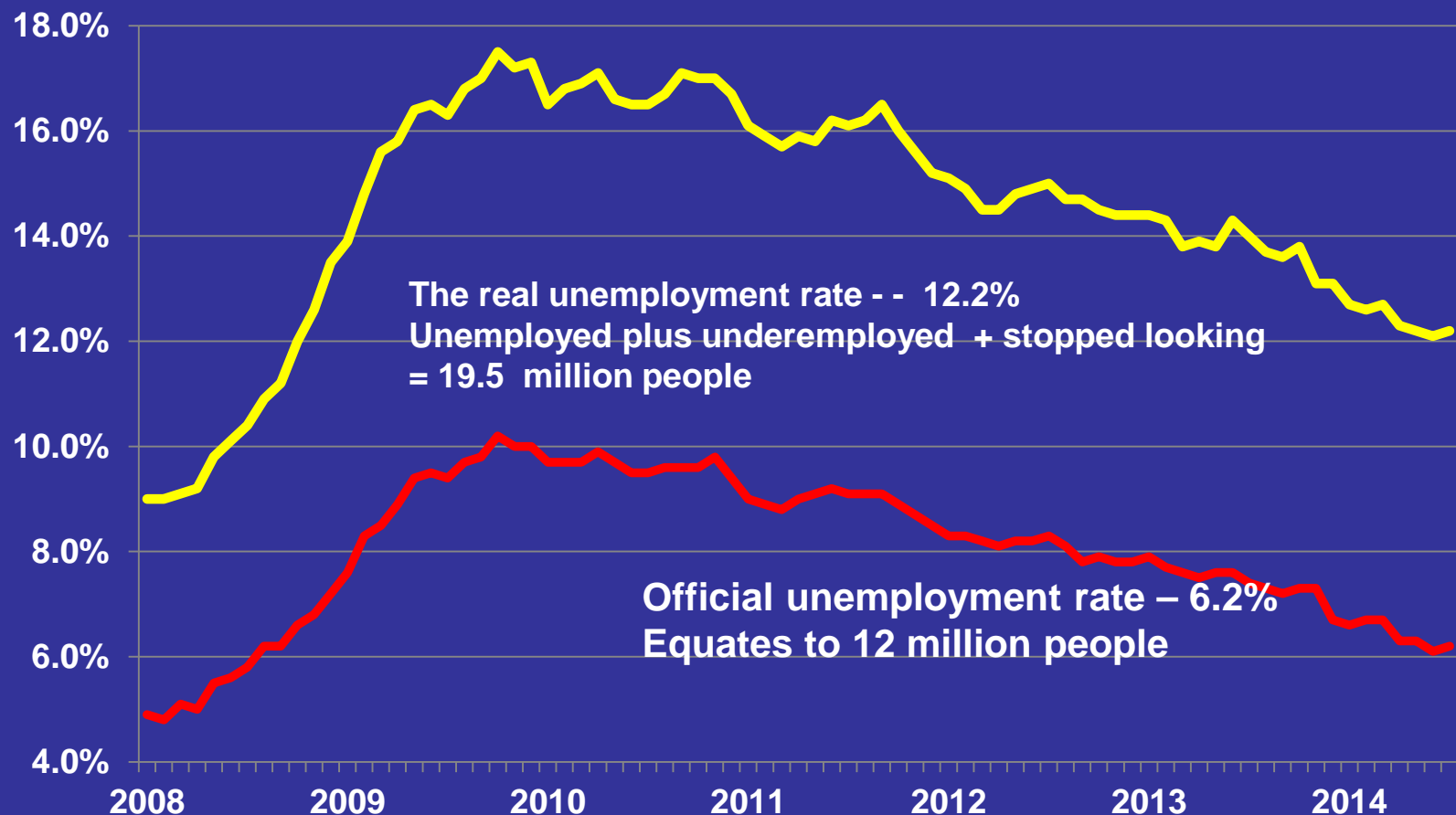
**We need 100,000 – 150,000 net new jobs/month  
To keep up with new entrants to workforce  
300,000/month to bring unemployment down**



Source: U.S. BLS ( [www.bls.gov](http://www.bls.gov) )

# Unemployment keeps coming down – but, the quality of many jobs being created is not so good!!

\*\*There are about 20 million people either unemployed, underemployed, or stopped looking – **they are not buying houses**



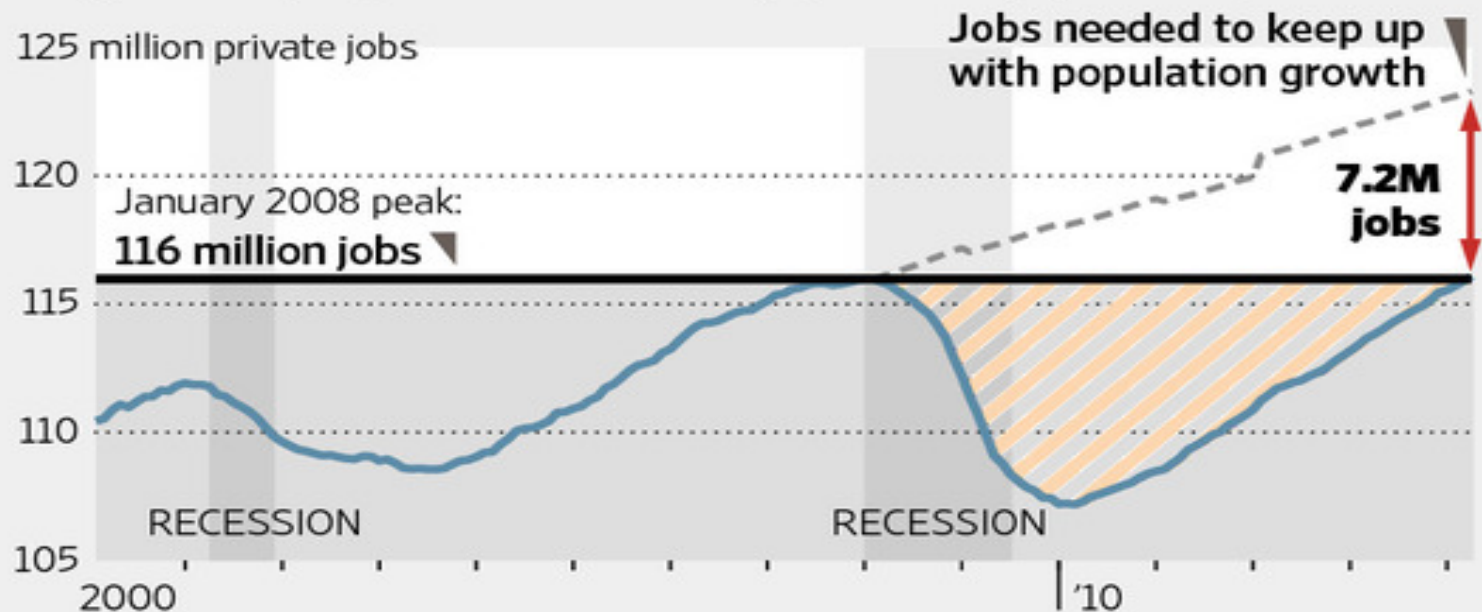


## Private sector payrolls are back to where we were in January 2008

But, we need 7.2 million more jobs just to keep pace with population growth – Key reason why job market is soft!!!! (and real wage growth is nonexistent)

### Hire Ground

Private-sector payrolls hit a high in March, but the recession derailed the potential job gains needed to keep pace with population growth.\*



\*Potential jobs measured using 2008 ratio of private-sector jobs to working-age people

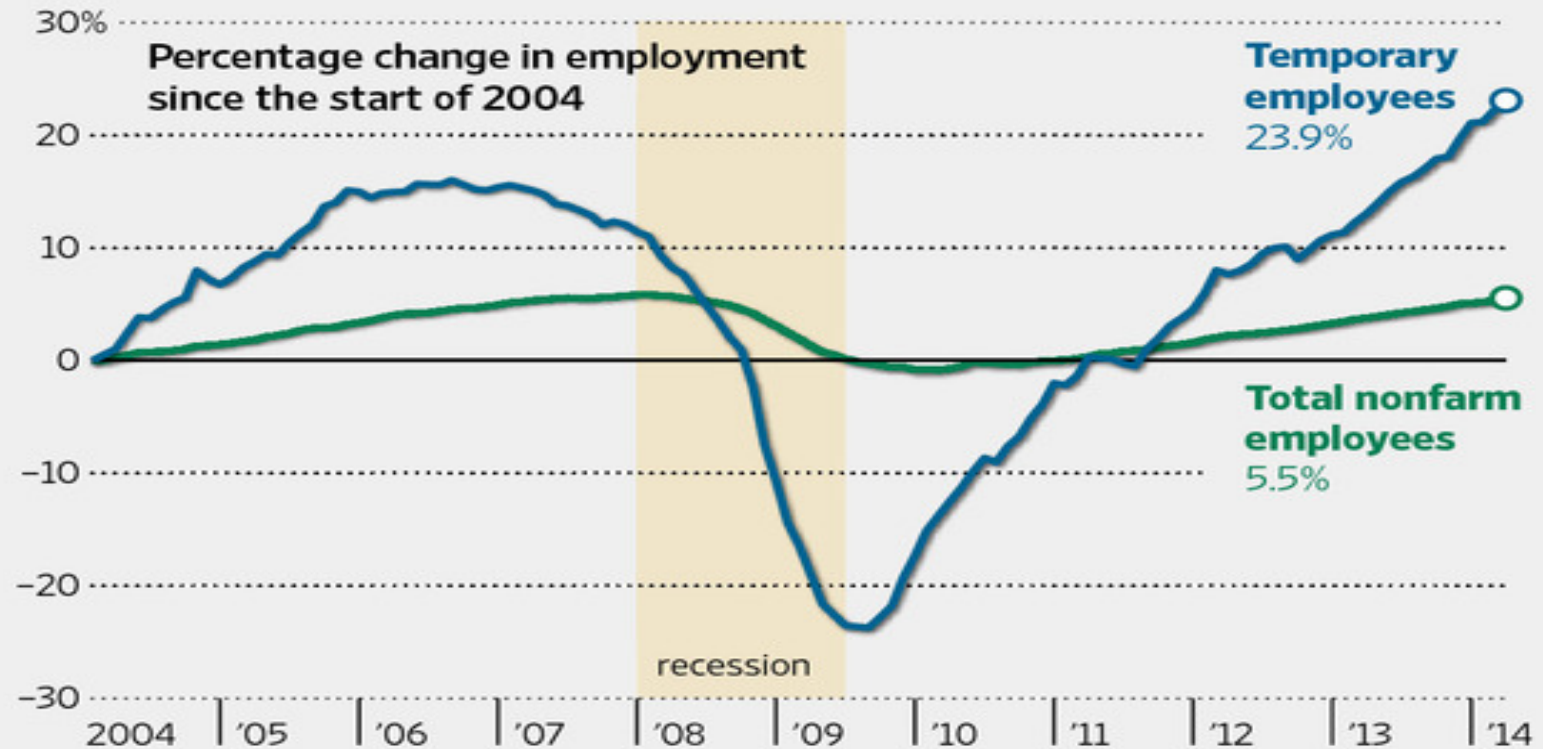
Note: Jobs data are seasonally adjusted. Source: Labor Department

The Wall Street Journal

Temporary jobs keep increasing as firms cut expenses  
( D. Paletta/WSJ) – main reason income gain is weak

## Easy Come, Easy Go

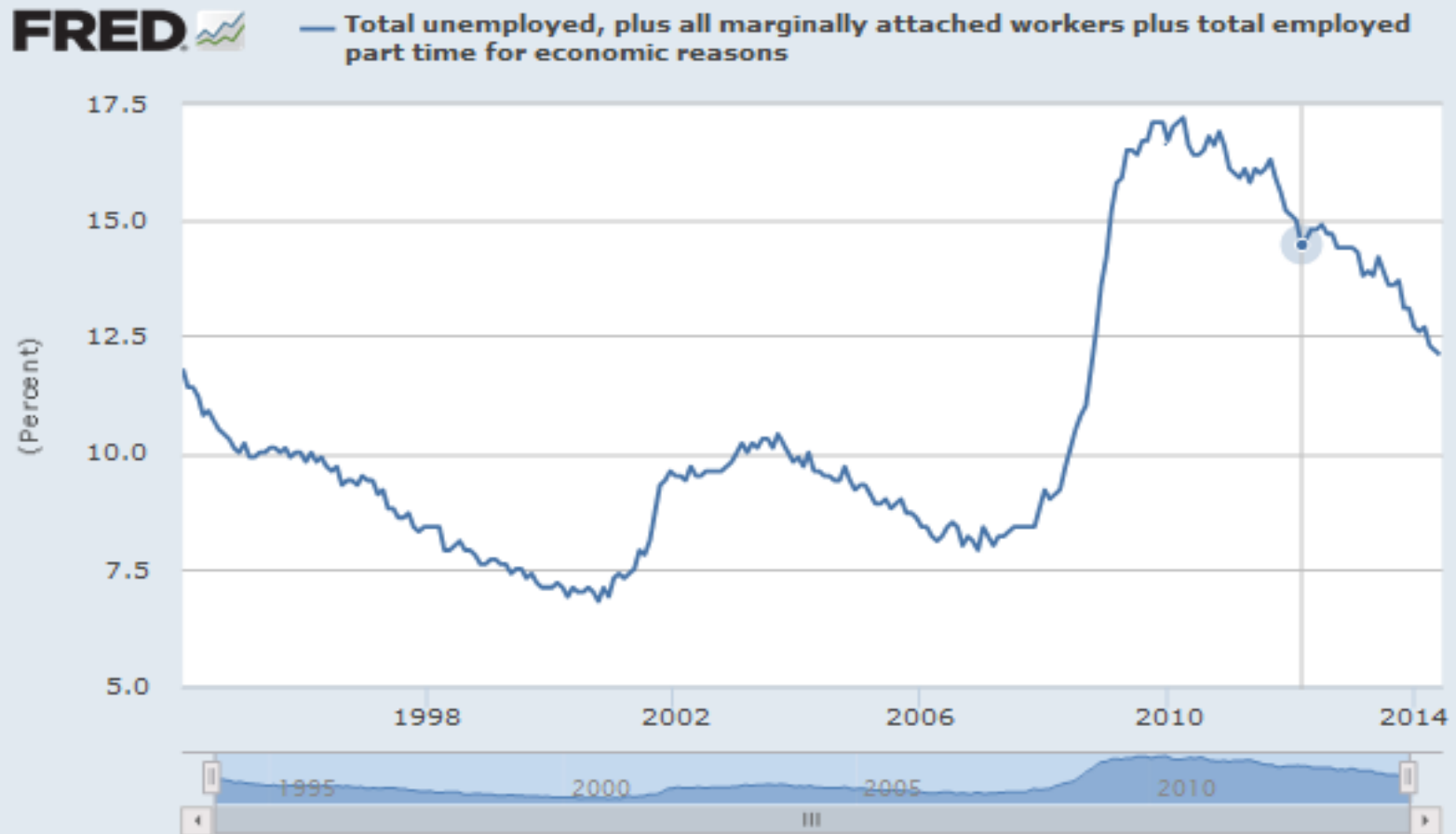
The slump in temp jobs foreshadowed the recession. The boom in such positions since 2010, economists say, could mark a lasting shift in the job market.



Source: U.S. Labor Department

The Wall Street Journal

Jobs - - Still the main problem with 12% of work force  
Either unemployed or underemployed ( about 20 million)

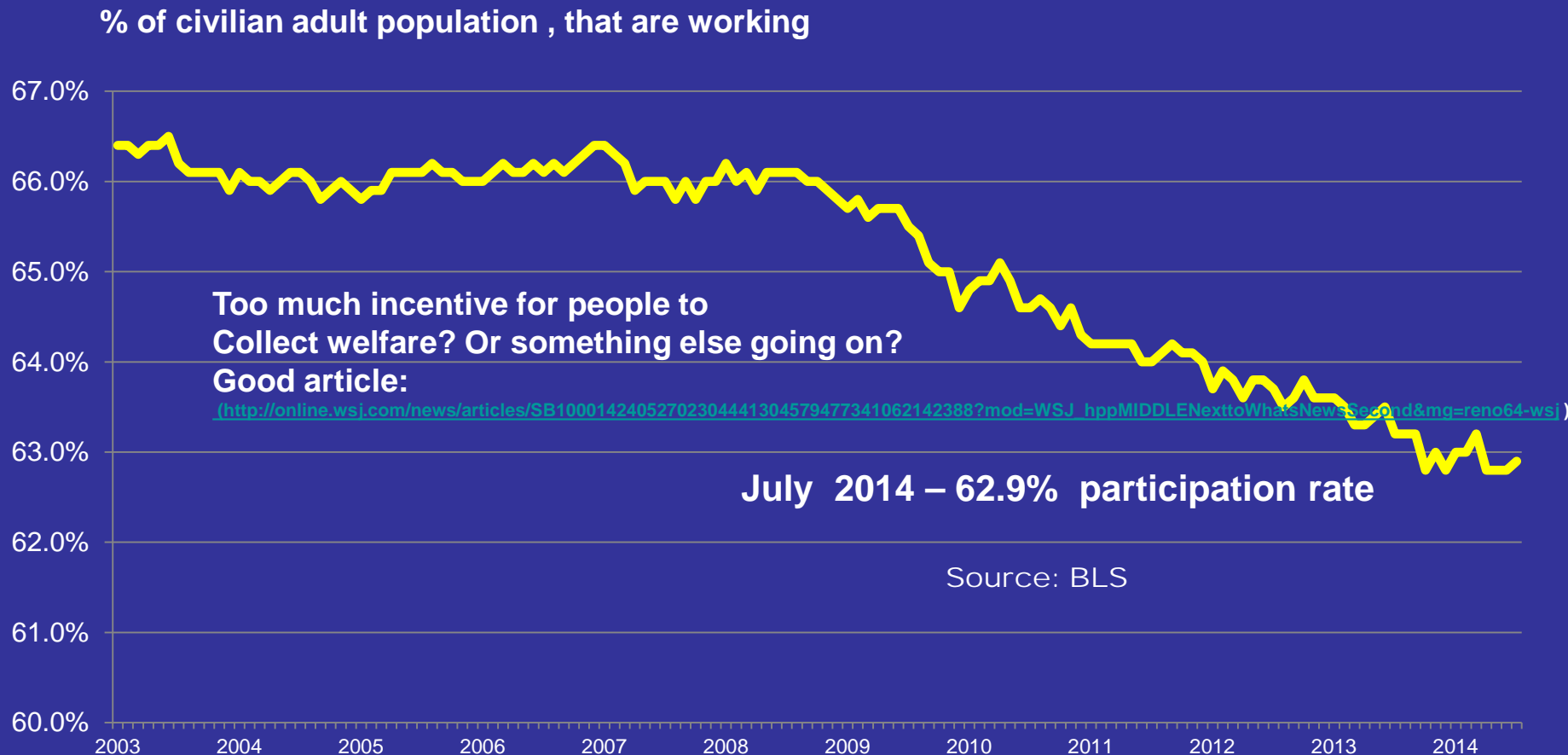


Source: U.S. Department of Labor: Bureau of Labor Statistics

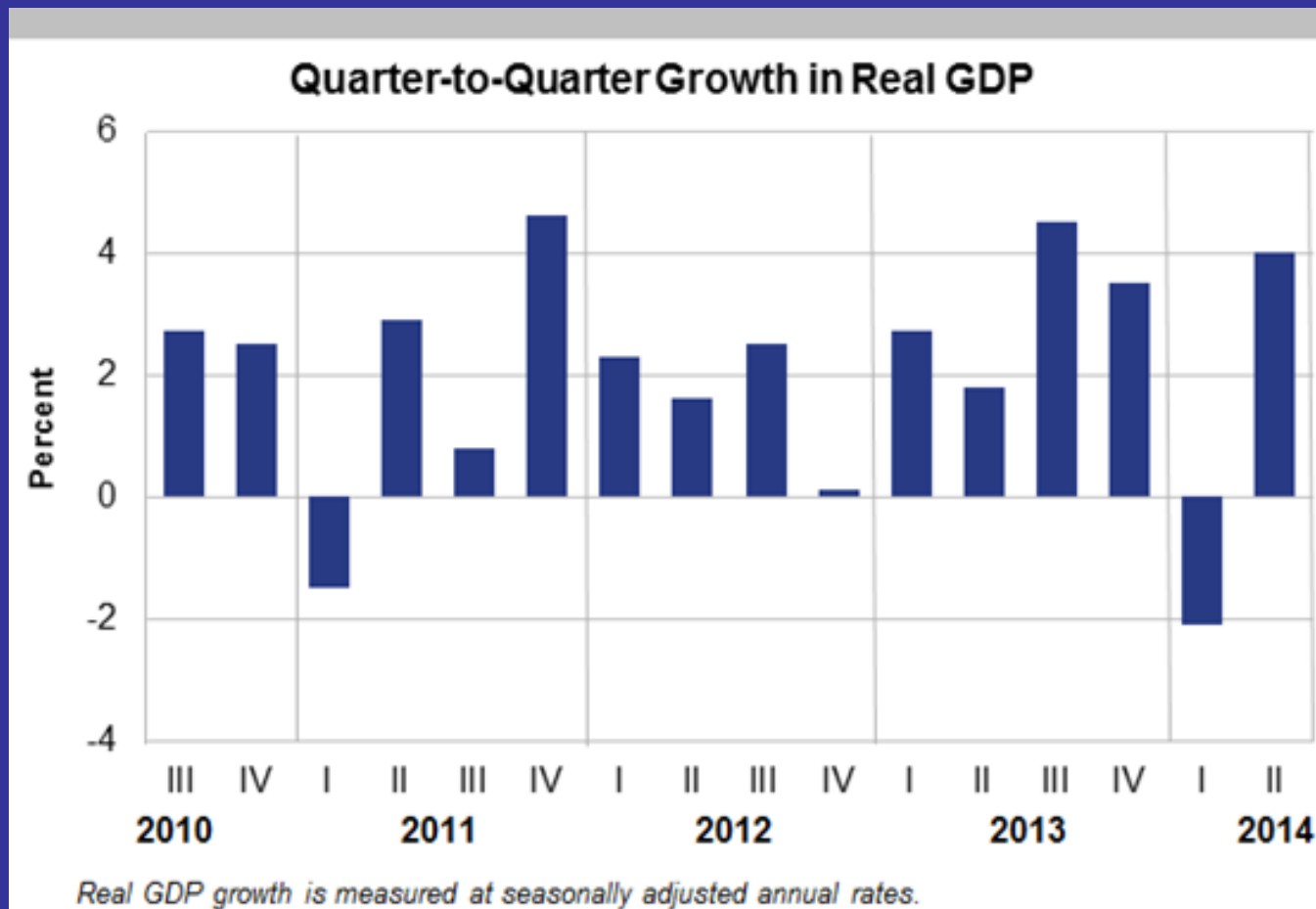
Shaded areas indicate US recessions - 2014 [research.stlouisfed.org](http://research.stlouisfed.org)

# Labor force participation rate is shrinking – this is not good!!

we will see more labor shortages in the future????



Economic growth (4.0%) – 2nd qtr 2014 – good bounce from -2.9%  
In 1<sup>st</sup> Qtr – will it continue through rest of 2014>>>>  
GDP for 2013 was 1.9% - nothing to write home about



**NAR's latest (August 2014) Economic and Housing Outlook – downward revisions from July outlook – looks like 2016 is best bet for turnaround????**

	<b>2014</b>	<b>2015</b>
<b>GDP</b>	<b>1.6%</b>	<b>2.8%</b>
<b>Housing starts(000)</b>	<b>1024</b>	<b>1302</b>
<b>Single (SF)</b>	<b>655</b>	<b>908</b>
<b>Multi (MF)</b>	<b>367</b>	<b>415</b>
<b>Resales (000)</b>	<b>4949</b>	<b>5286</b>
<b>SF Sales</b>	<b>452</b>	<b>638</b>

**My comments:**

2014 - - looks OK except MF may be a bit higher and SF lower

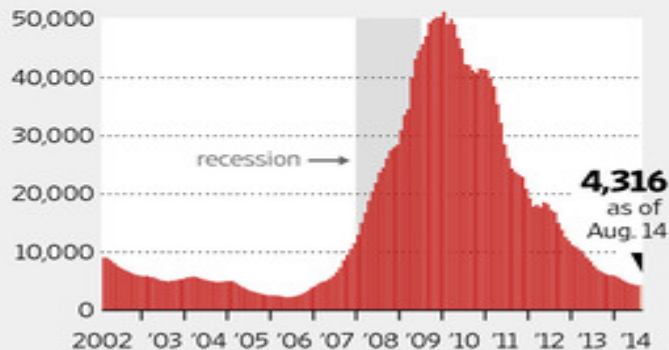
2015 - - MF may be higher at 35% ~ 460??

Many markets are slowing down – Phoenix is good example of city hurt by housing Collapse, then quick rebound **until recently** . Problem in many cities is lack of Traditional buyers with “bargain hunters” disappearing as prices increase.

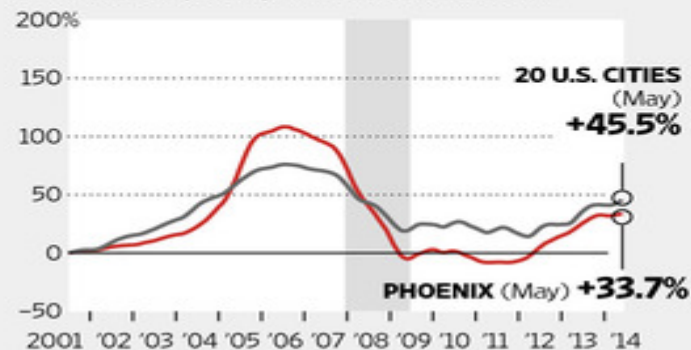
## Return to Normal

As foreclosures in Phoenix have plunged since the crash, prices have risen...

Pending foreclosures in Phoenix



Change in Case-Shiller's Phoenix home-price index and its 20-city composite since June 2001

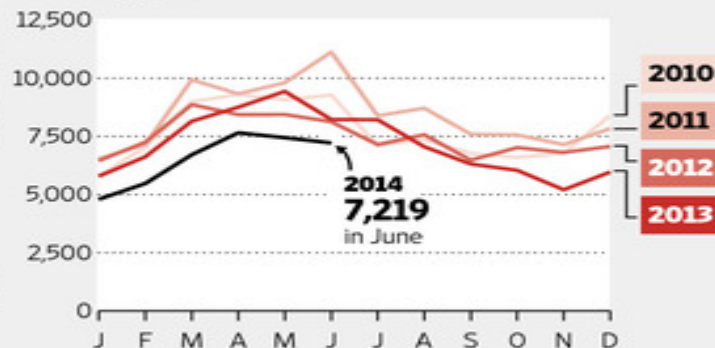


...drawing more sellers to market, though sales are lower than recent years amid questions of affordability.

Change in monthly inventory of previously owned homes listed for sale since June 2001



Monthly sales of previously owned homes in Phoenix, sorted by year



Source: Mike Orr, W.P. Carey School of Business, Arizona State University (Arizona inventory and pending foreclosures); S&P Dow Jones Indices (prices); National Association of Realtors (U.S. inventory); Arizona Regional Multiple Listing Service (sales by month) The Wall Street Journal

# Recent Housing statistics

## Background:

Markets are getting better – maybe????

Have we turned the corner? – Probably, but

The climb back will remain muted

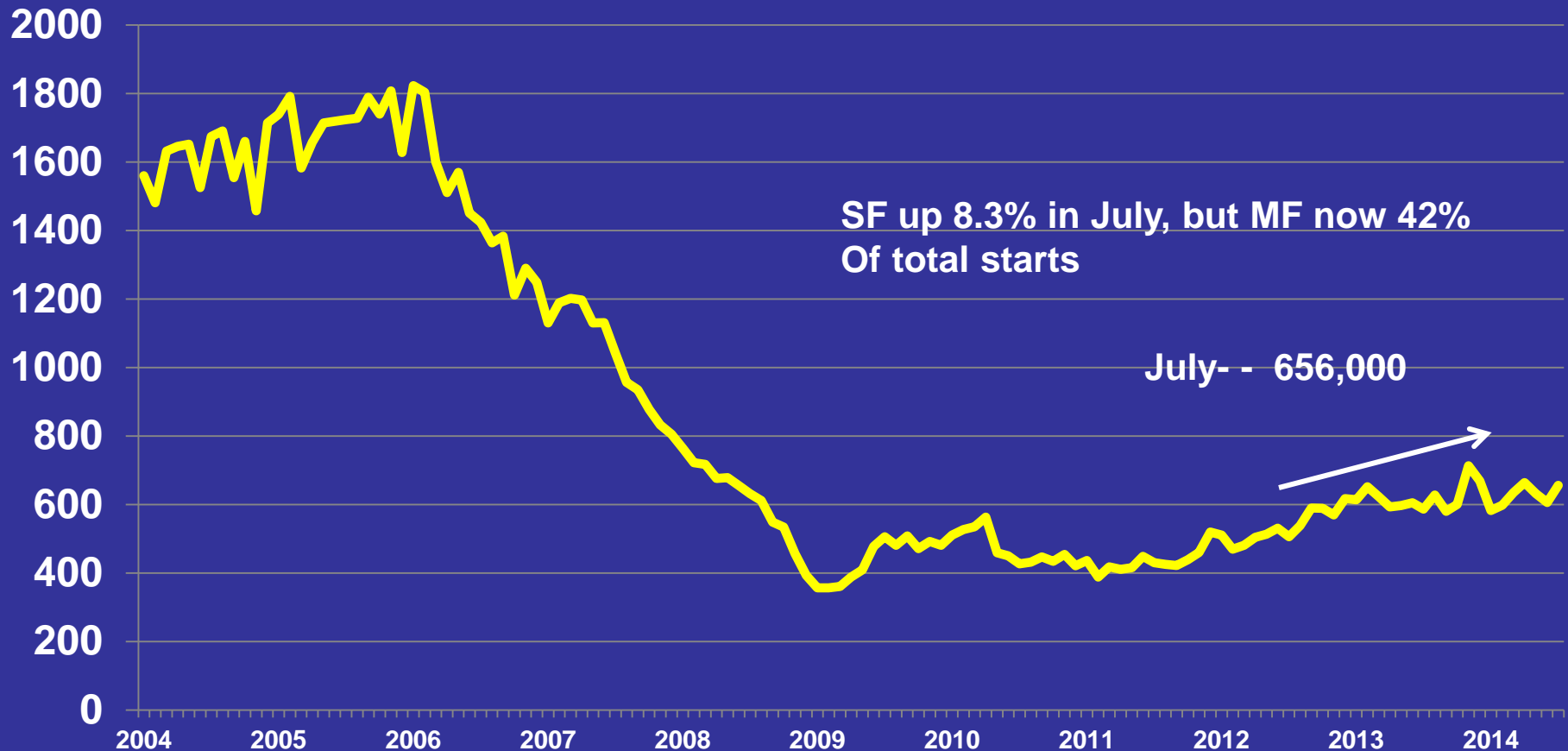
Until we see economic growth of 3% or

More for an extended period of time!!!



Starts are finally turning the corner, but growth is painfully slow – Multi family remains strong!!

### Single family starts, Thousand units, SAAR



SF up 8.3% in July, but MF now 42%  
Of total starts

July - 656,000

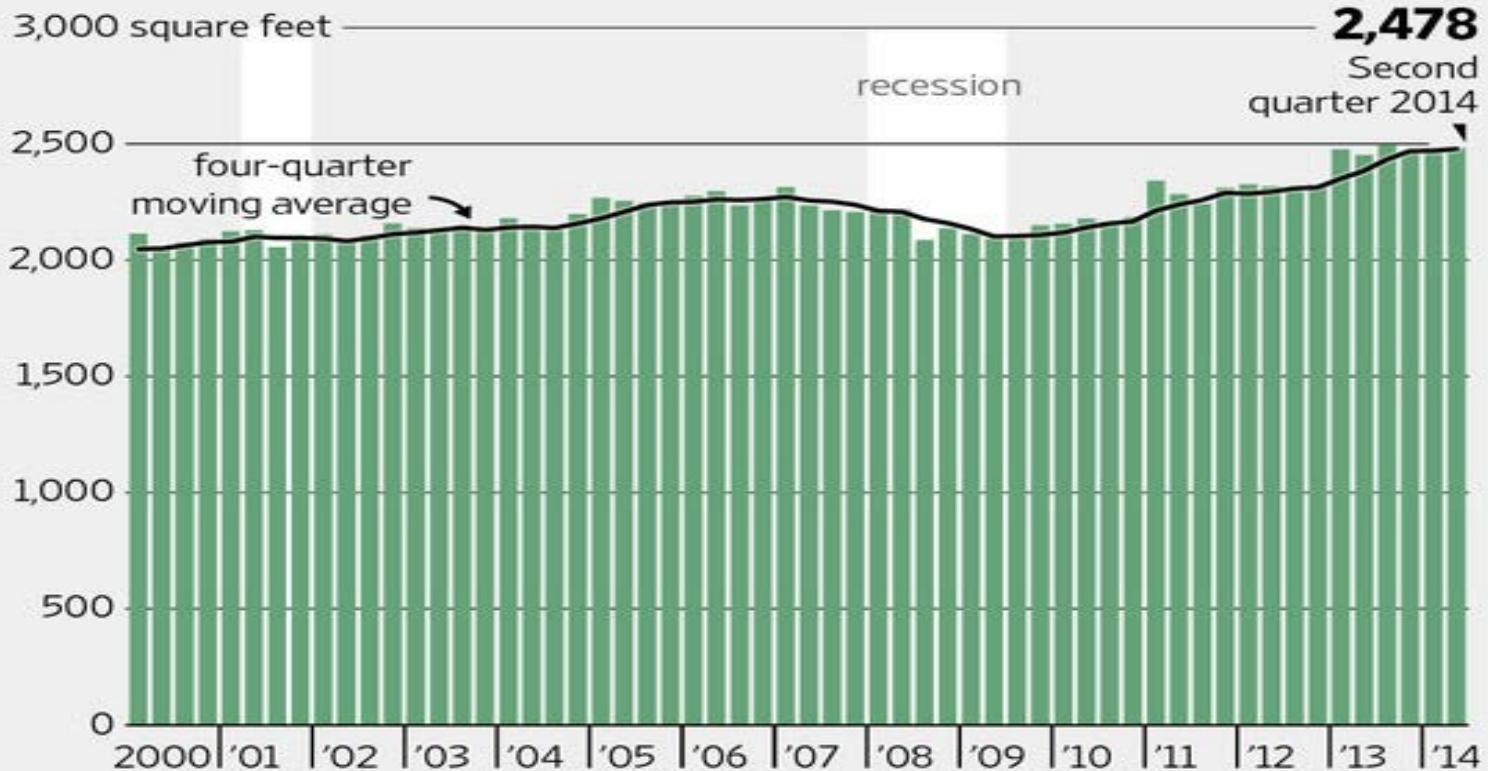
Source: Census (<http://www.census.gov/const/www/newresconstindex.html> )

Another indication that 1<sup>st</sup> time buyers are absent from this market - -  
"Dominated by better heeled , move - up buyers with capital and credit  
To buy larger homes" - Kris Hudson, WSJ

([http://online.wsj.com/news/article\\_email/u-s-home-size-levels-off-for-now-at-least-1408476927-IMyQJAxMTA0MDIwMDEyNDAYWJ](http://online.wsj.com/news/article_email/u-s-home-size-levels-off-for-now-at-least-1408476927-IMyQJAxMTA0MDIwMDEyNDAYWJ))

## Big Footprints

Median square footage of newly built U.S. single-family homes



Source: Commerce Department via Moody's Analytics

The Wall Street Journal

# Multi family continues to strengthen

## Shared Spaces

Structures with five or more units that began construction over the preceding 12-month period, not seasonally adjusted, in thousands

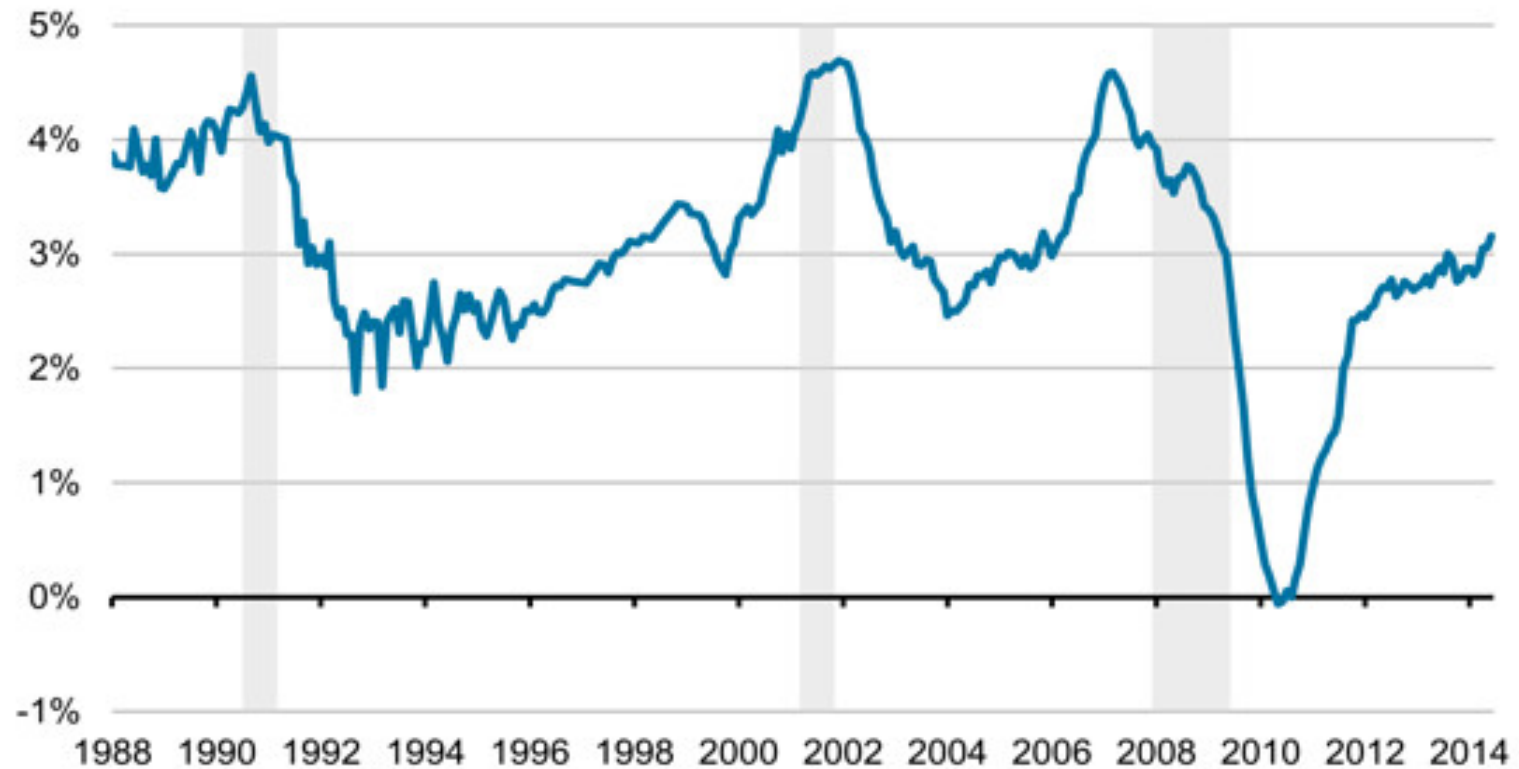


Source: Commerce Department | WSJ.com

Rental prices keep increasing as demand outstrips supply  
Rental construction strength will continue???

## Climbing Back

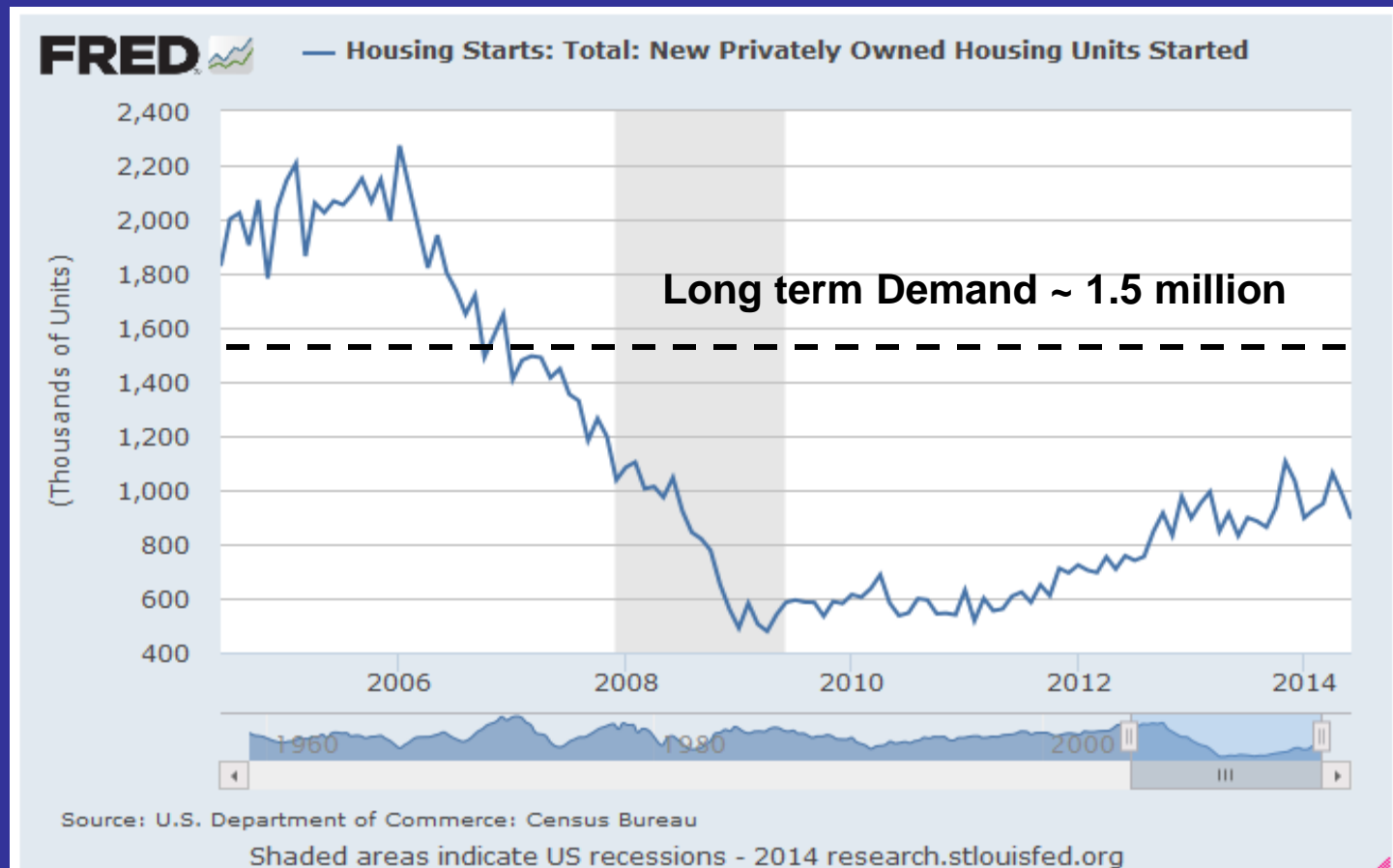
Consumer price index, rent of primary residence, change from year earlier



Source: Labor Department | WSJ.com

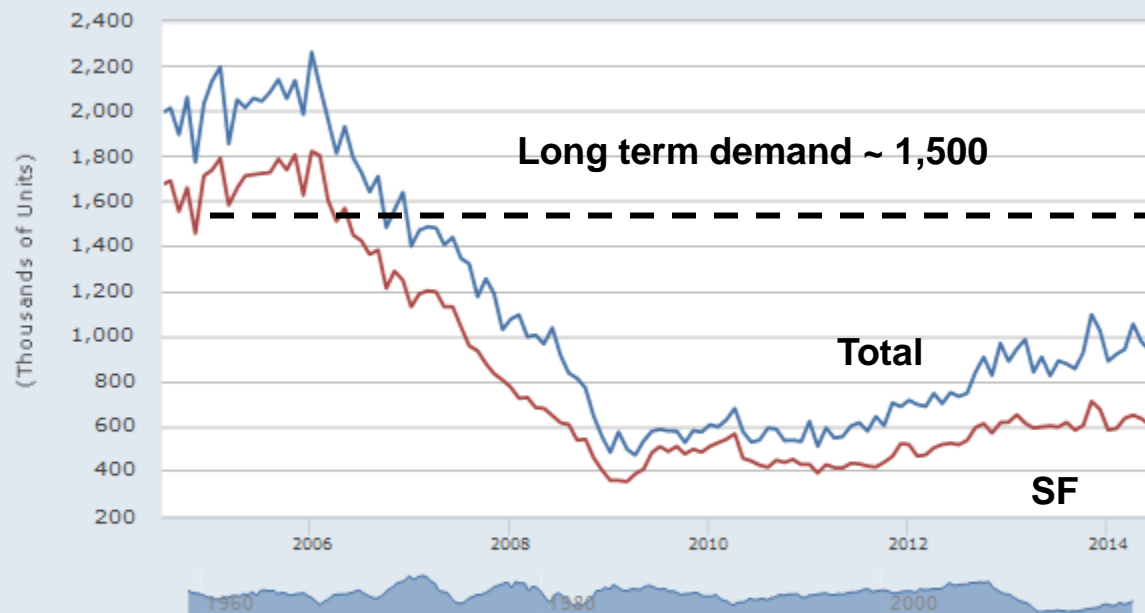
Long term shelter demand is estimated to be about 1.5 million annually  
Based on demographics (65%), replacement demand(25%), and speculative demand including 2<sup>nd</sup> homes.(10%)

(to date, the main drivers have been speculators/investors and people paying cash:  
E.g., in 1<sup>st</sup> qtr investors were 17% of existing home sales while cash sales were 43% of total purchases)



**FRED**

— Housing Starts: Total: New Privately Owned Housing Units Started  
— Privately Owned Housing Starts: 1-Unit Structures



Shaded areas indicate US recessions - 2014 research.stlouisfed.org

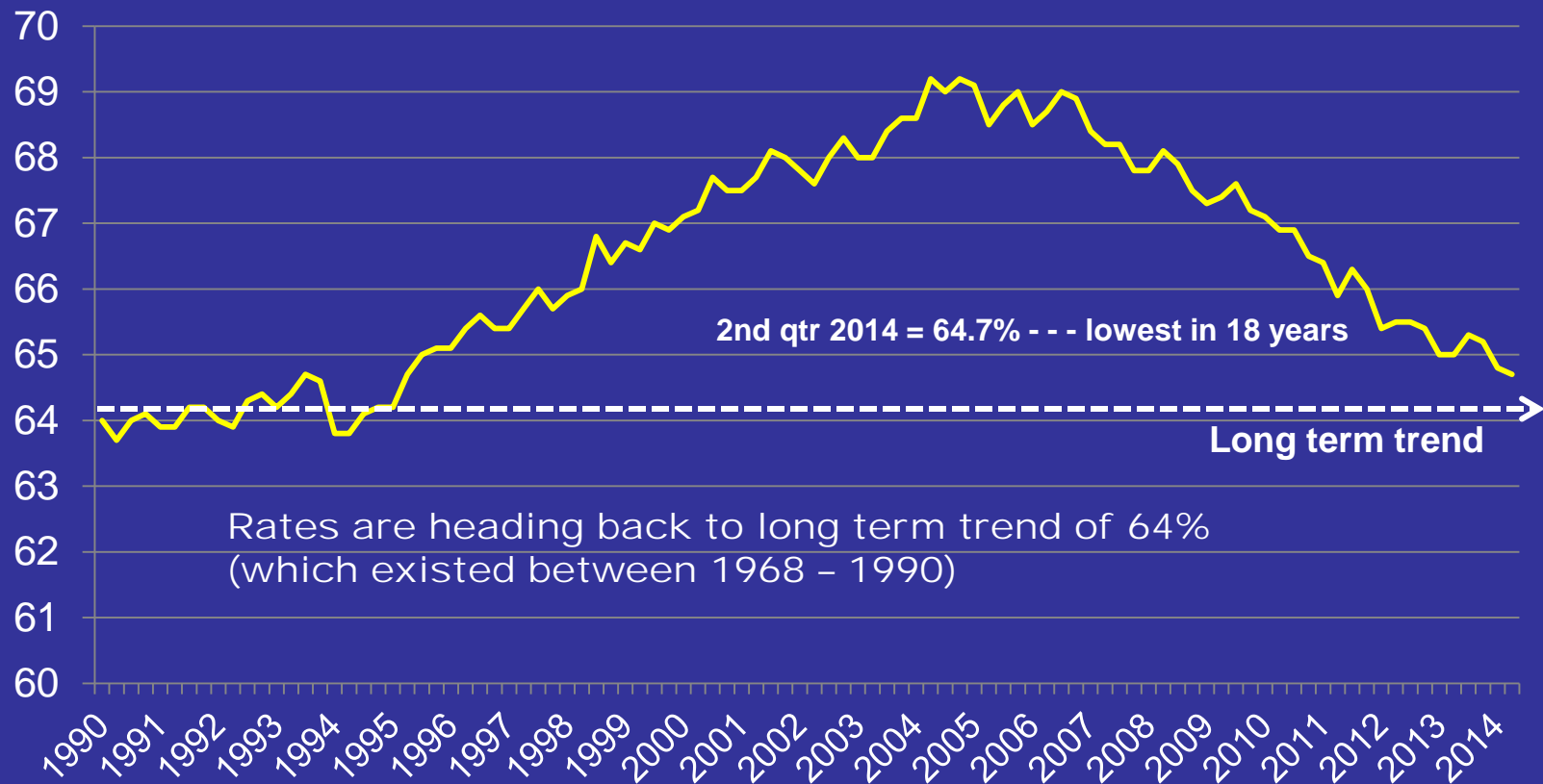
## Impact of weak household formations - -

homeownership rates have been falling for the past seven  
Years - when the economy gets back to normal,

Will people go back to single family or will we see more renting?

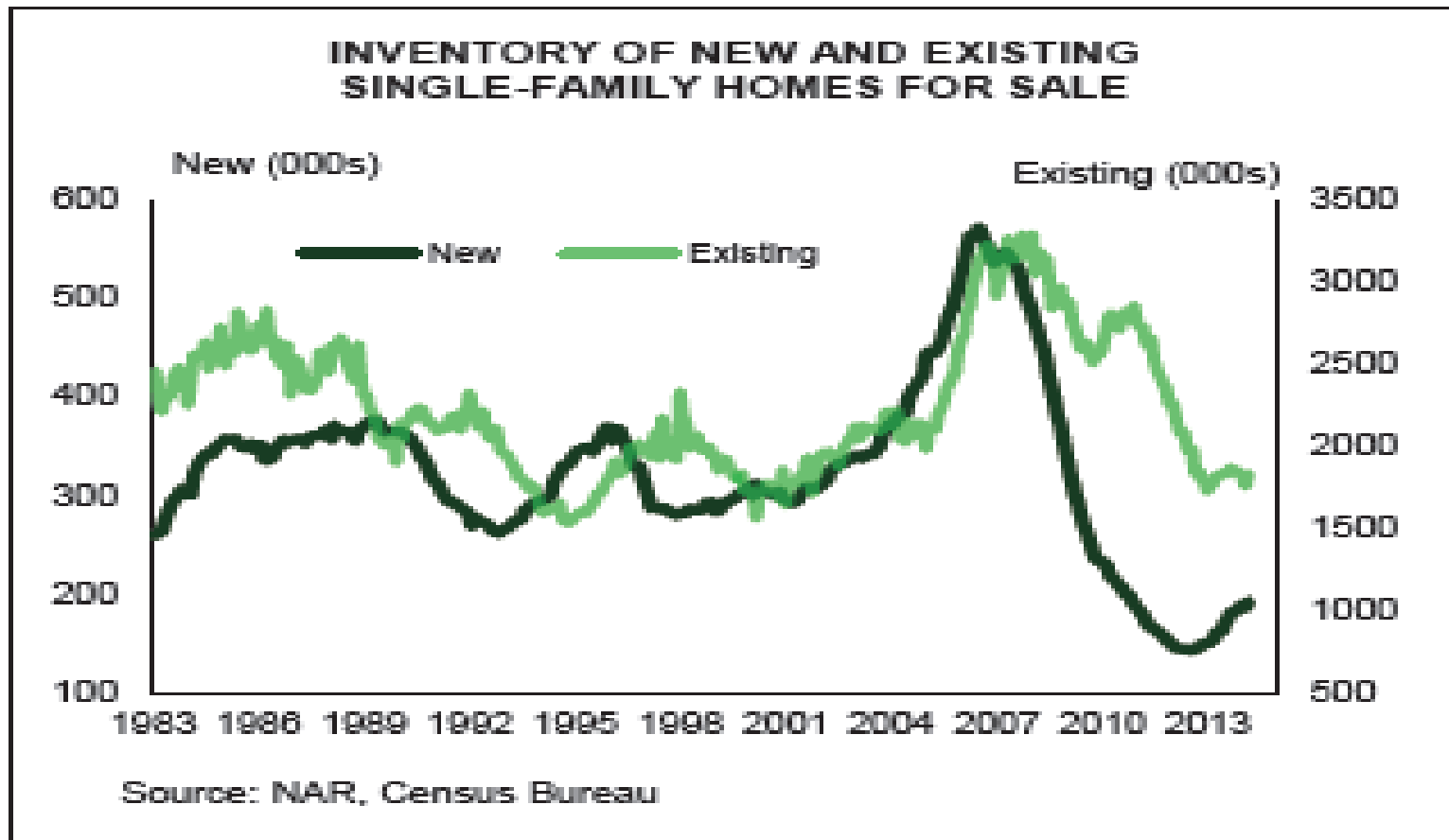
There will be impacts on wood products demand

### Home Ownership(%)



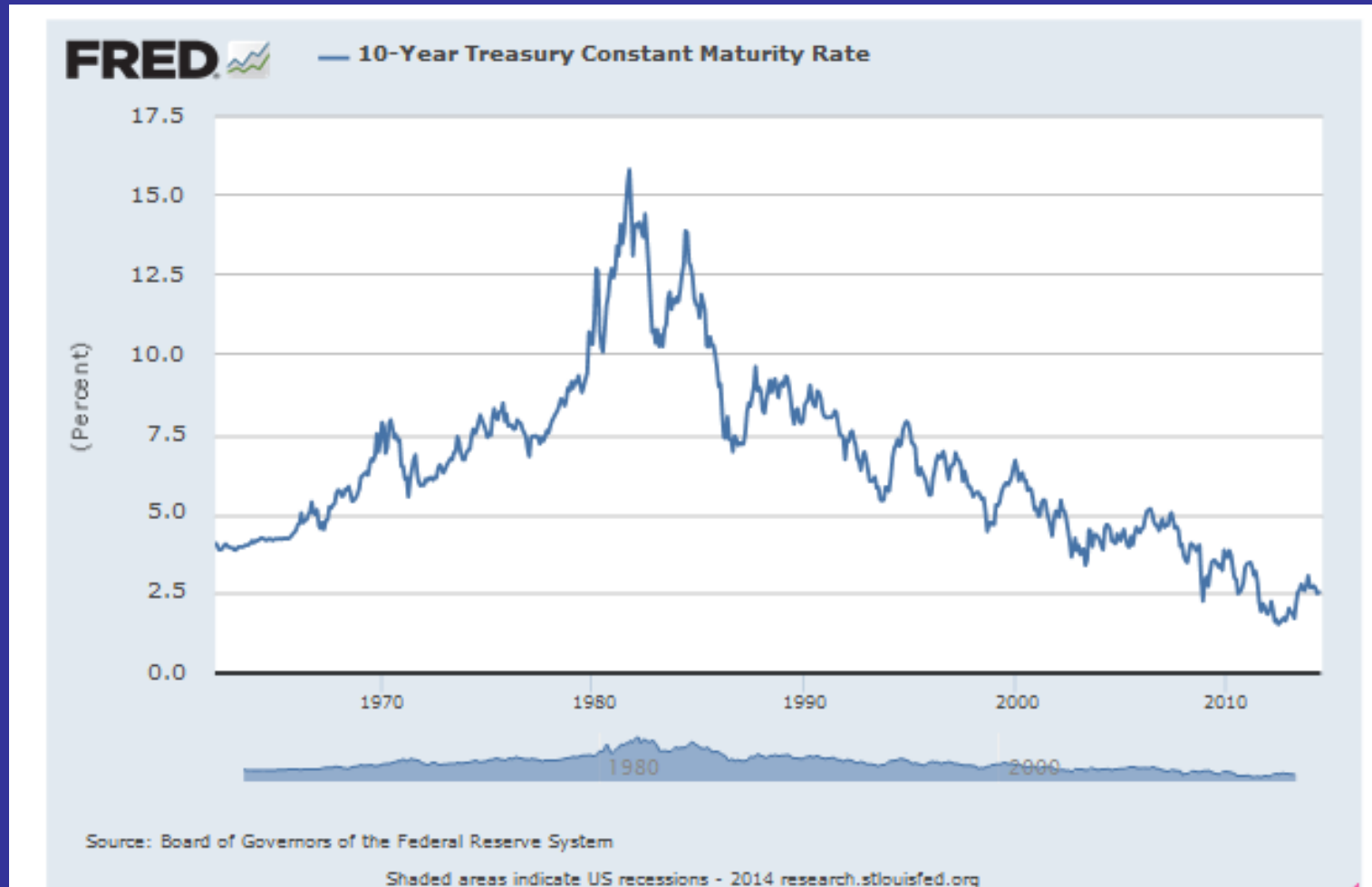
Source: Census (<https://www.census.gov/housing/hvs/data/q413ind.html>)

Low Inventories are key reason home prices are escalating so rapidly - historically, new home inventory is about 350,000 while existing home inventory is about 2,300,000. Today, existing inventory is 500,000 below trend while new homes are about 150,000 below trend

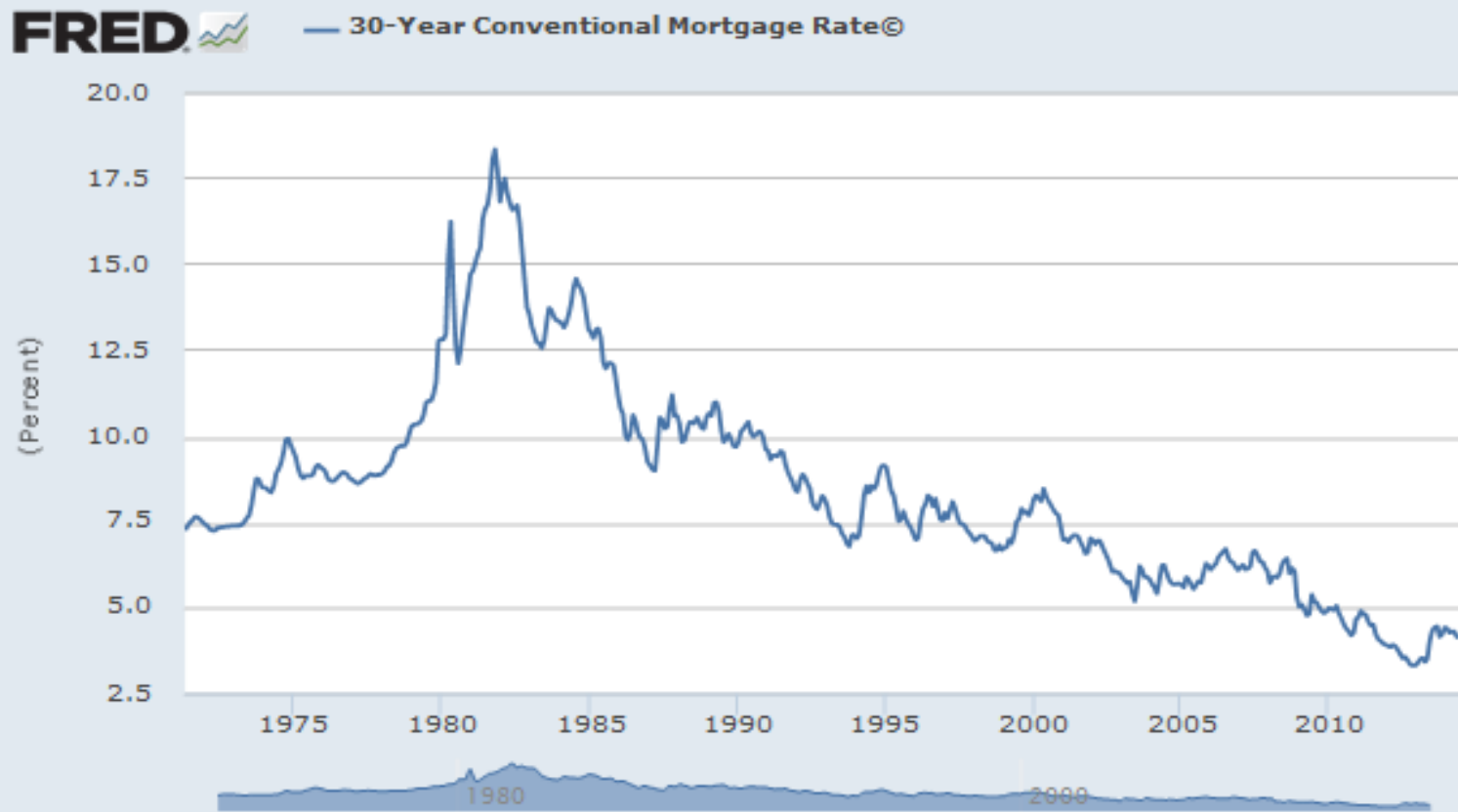




*Interest rates at all time lows – should be good for housing*



Mortgage rates have never been lower – but many people  
Are not buying a house???



Source: Board of Governors of the Federal Reserve System

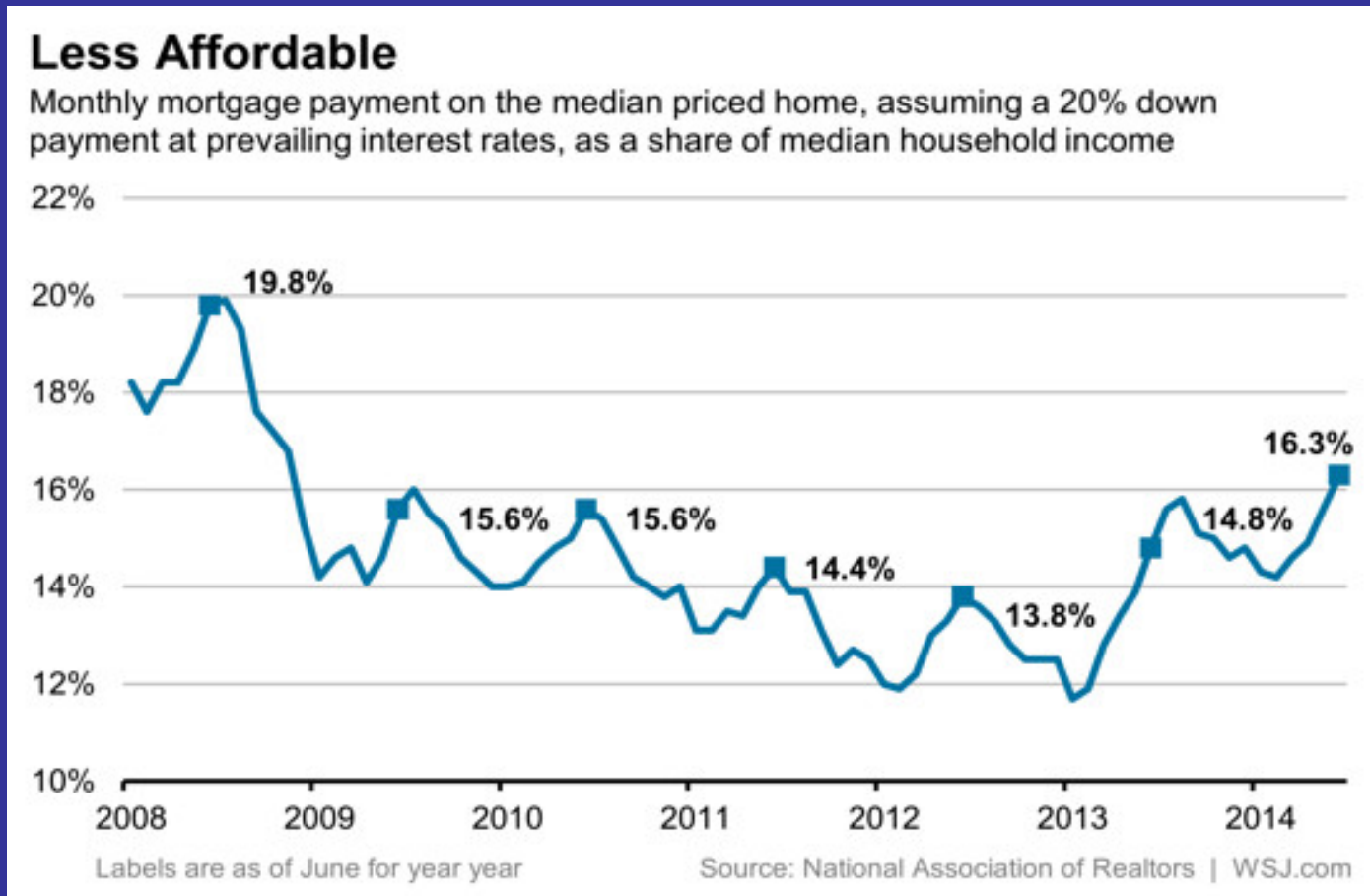
Shaded areas indicate US recessions - 2014 [research.stlouisfed.org](http://research.stlouisfed.org)

Despite low mortgage rates, people are having problems  
Buying a house because their real incomes have been shrinking  
For the past 20 years – this is a structural problem ( long term)  
And not cyclical --- no quick fixes to this problem



## Another drag on the housing recovery – decreasing affordability

(it's actually worse – many people can't afford the 20% down payment, can't Qualify for a loan with tighter credit restrictions, .... - - we need lots of better Paying jobs to get housing back on its feet )



## Real incomes are shrinking – why??

OK – we have discussed this before, but maybe it is time to Revisit the issue of education – how it impacts standard of Living, the economy, and demand for housing ( and wood products)  
PS. – a good friend pointed out that this isn't the only problem facing the Economy – agreed – I'm hoping to point out a few other structural Issues in future housing notes.

The next few slides are from a recent study by Standard and Poor's, A reputable organization in my opinion. The title of the report  
“ How Increasing Income Inequality is dampening U.S. economic growth, And Possible ways to change the tide”.

([https://www.globalcreditportal.com/ratingsdirect/renderArticle.do?articleId=1351366&SctArtId=255732&from=CM&nsf\\_code=LIME&sourceObjectId=8741033&sourceRevId=1&fee\\_ind=N&exp\\_date=20240804-19:41:13](https://www.globalcreditportal.com/ratingsdirect/renderArticle.do?articleId=1351366&SctArtId=255732&from=CM&nsf_code=LIME&sourceObjectId=8741033&sourceRevId=1&fee_ind=N&exp_date=20240804-19:41:13))

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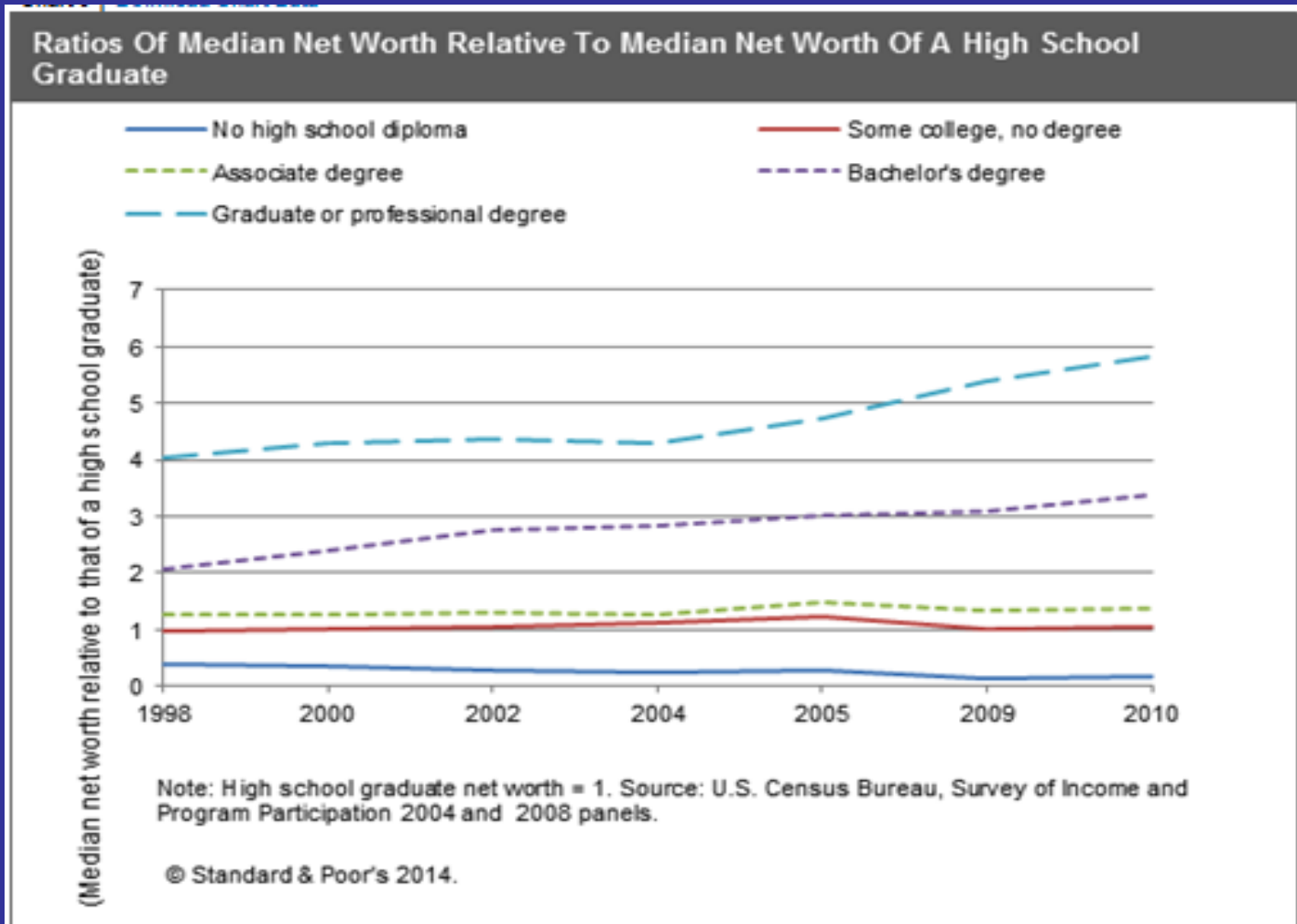
Real household incomes today at 1995 levels  
i.e., we're going backwards!!!!!!!!!!



Source: St. Louis FED ( <http://research.stlouisfed.org/fred2/series/MEHOINUSA672N> )

# Education pays - a no brainer!!

(study by Standard and Poor's – a reputable organization)



Source: Standard and Poors

([https://www.globalcreditportal.com/ratingsdirect/renderArticle.do?articleId=1351366&SctArtId=255732&from=CM&nsi\\_code=LIME&sourceObjectId=8741033&sourceRevId=1&fee\\_ind=N&exp\\_date=20240804-19:41:13](https://www.globalcreditportal.com/ratingsdirect/renderArticle.do?articleId=1351366&SctArtId=255732&from=CM&nsi_code=LIME&sourceObjectId=8741033&sourceRevId=1&fee_ind=N&exp_date=20240804-19:41:13))

# If education pays, why is U.S. slipping behind????

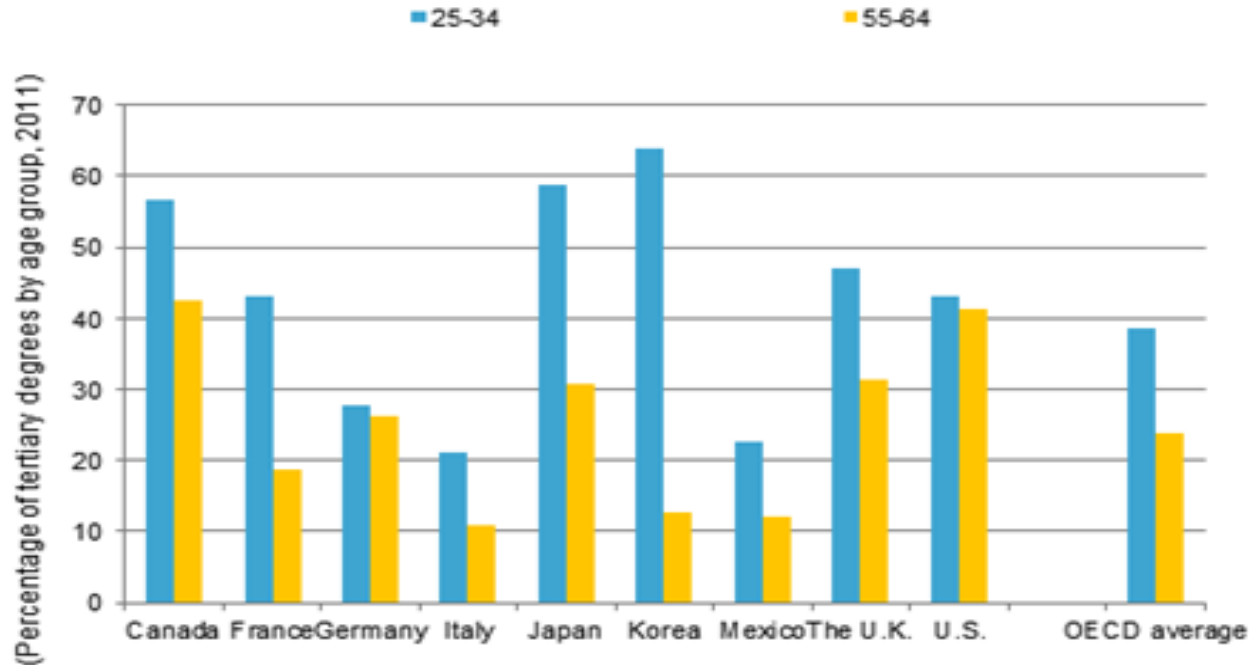
Chart shows percentage of college degrees by age group - -

Note the difference between young and old . e.g., in most

Countries, young people are better educated, but in U.S. , there is little difference

I don't know about you, but I would feel a lot better if the next generation was better Educated than their parents.

## U.S. Education Is Slipping Behind

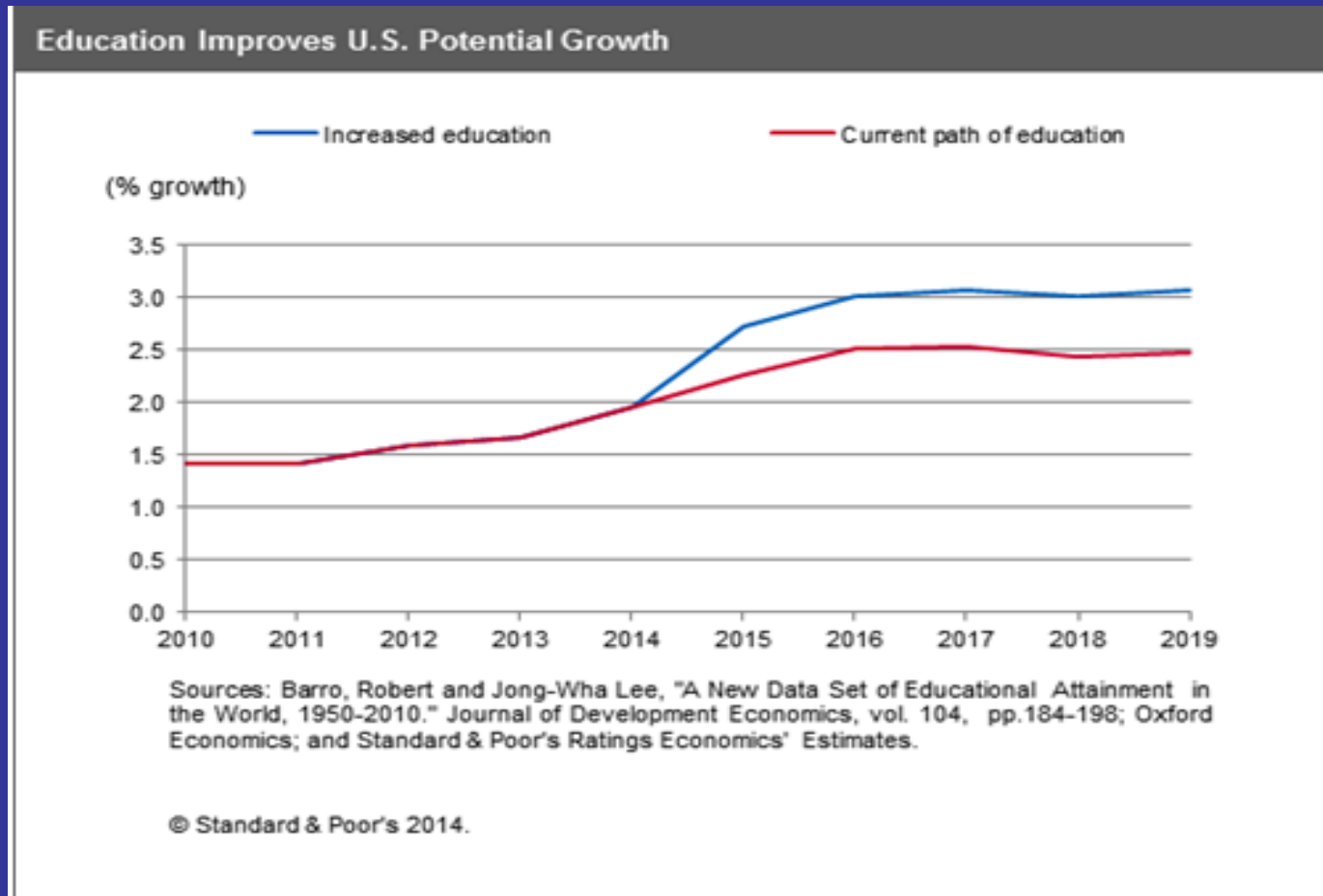


Source: The Organisation for Economic Co-operation and Development (OECD), "Education At A Glance 2013."

© Standard & Poor's 2014.



# Education can improve our economy – again, why are we Falling behind????



PS. A colleague suggested that better education alone won't  
Fix the economy – I agree – we have additional structural problems

# What's the problem and How do we solve it??

(you have seen this movie before, but let's take another look)

We consume too much and don't invest enough in our future - - -  
Most of our competitors consume 60% or less of their economy – yet,  
We consume 70% or more. We need to consume less and invest more  
In education, infrastructure, R&D, ....

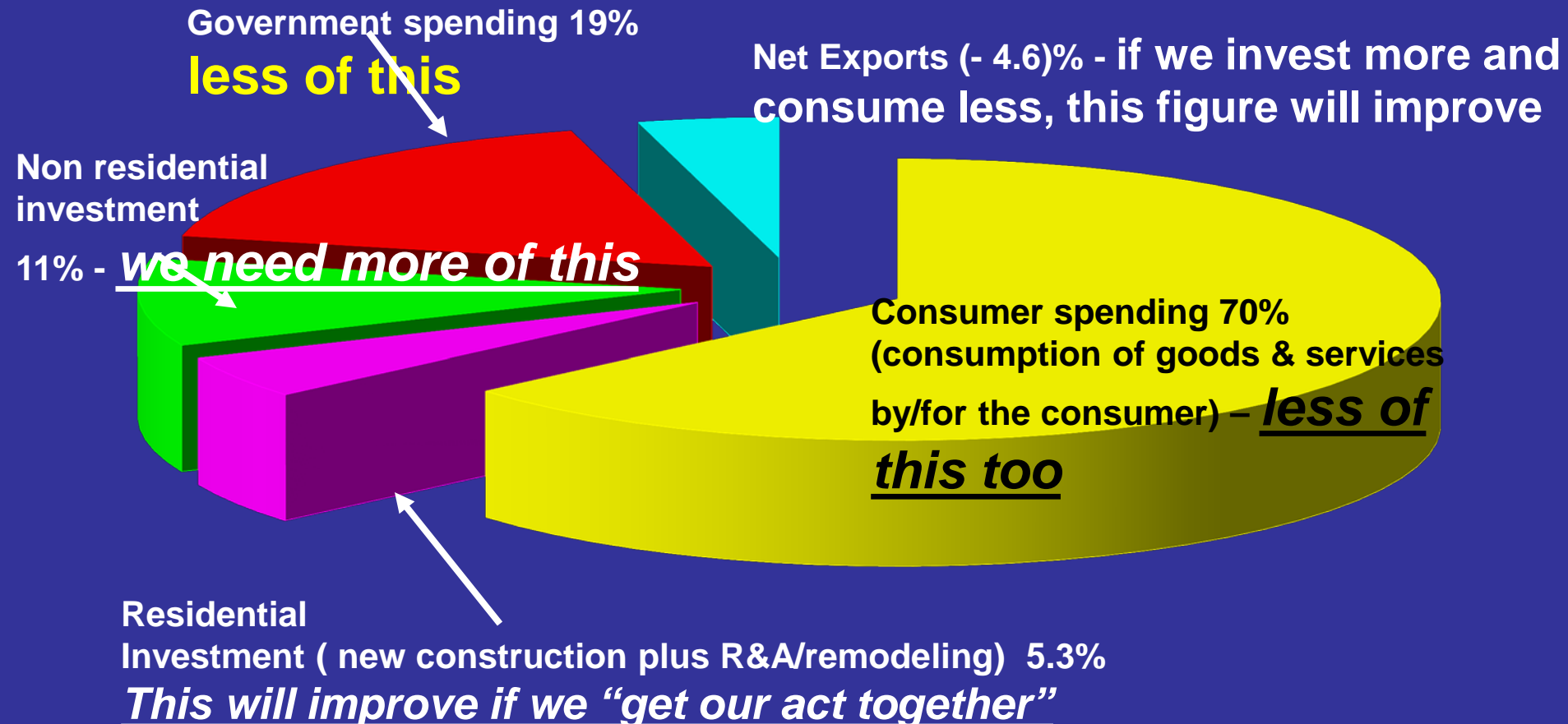
This is a legitimate strategy for improving our economy, and promoting  
More demand for housing, and wood products.

I know this is an oversimplification – but, one strategy  
Is we need to change the tax laws to favor investment and discourage  
consumption ( at least until we regain our global competitiveness). And,  
The government needs to be involved. By  
the way, this is what we did following WWII – after the war was over, the  
GI Bill encouraged soldiers to get an education, and other laws were enacted to  
Encourage America to invest in its future ( e.g., Eisenhower knew the importance  
Of investing in a world class interstate highway system).

**Bottom line – if we don't invest in our future, we won't have one!!!!!!!!!!**

## U.S. Economy 2000 – 2010

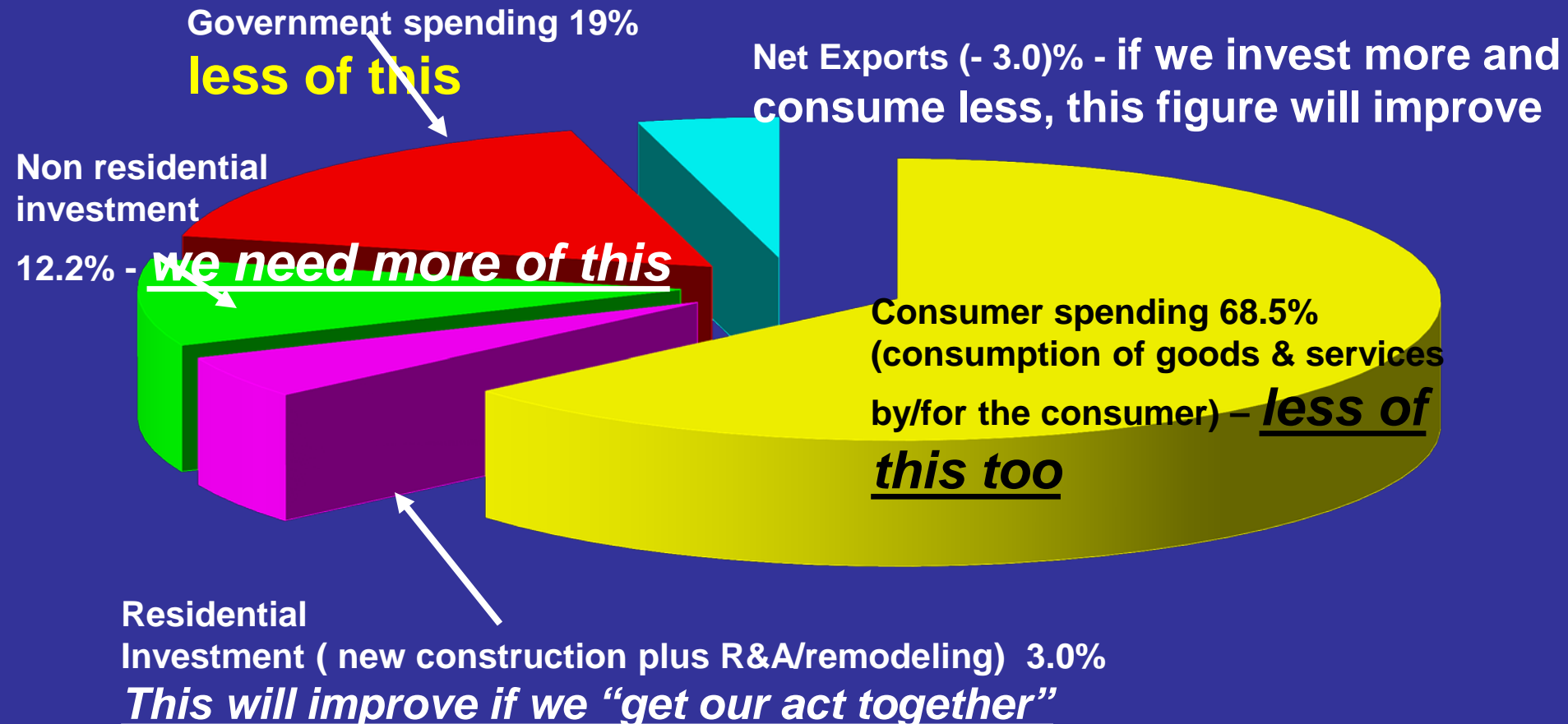
this type of economy not sustainable – insufficient investment in infrastructure, R&D, education makes us less competitive and this leads to reduced standard of living and less housing demand



Source: BEA ( <http://bea.gov/national/nipaweb> )

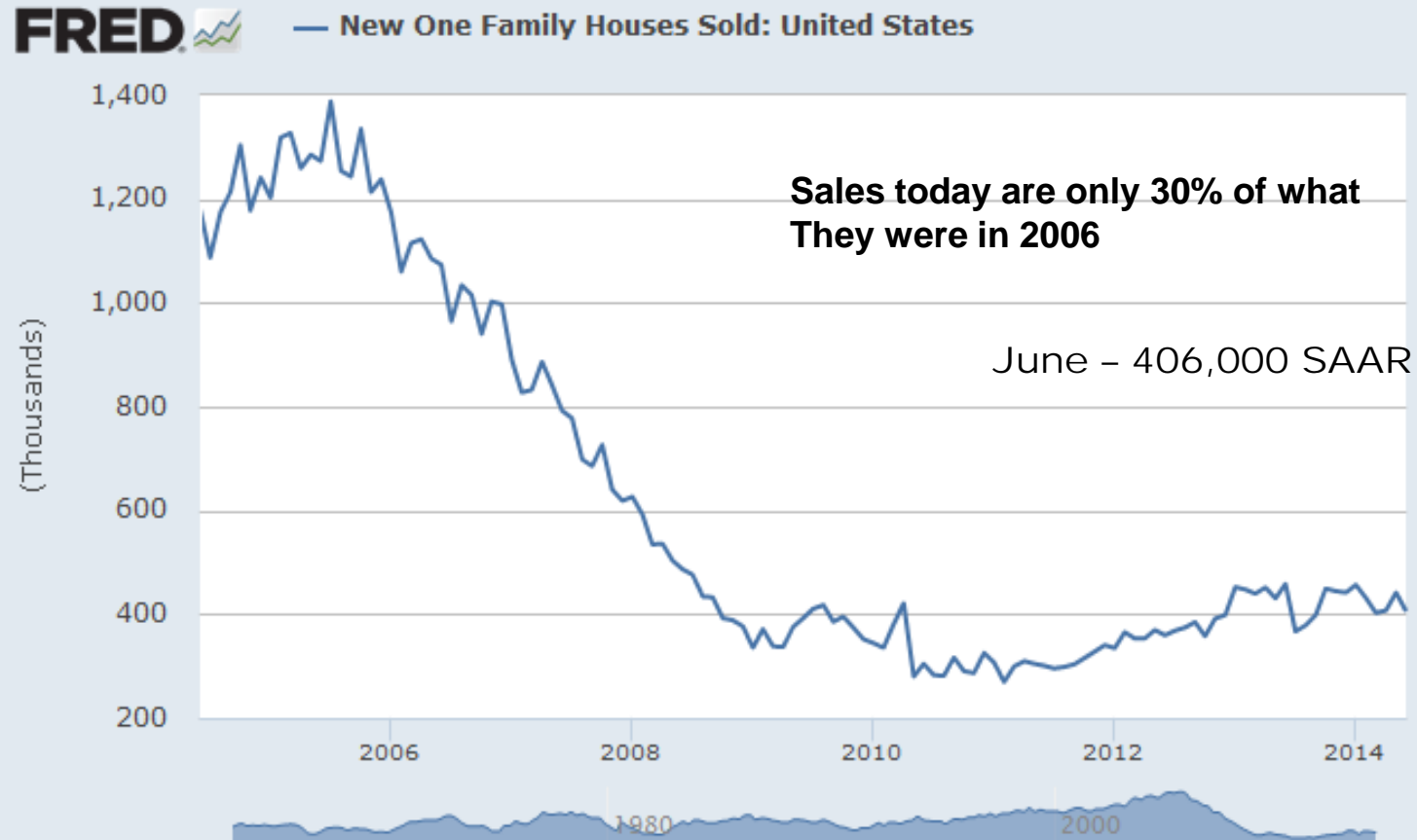
# U.S. Economy 2013 - - GDP as % of Economy = 68.5%

China consumes <40%; Russia < 50%; Europe <60%



Source: BEA ( <http://bea.gov/national/nipaweb> )

This is key statistic to watch – new single family sales drive wood product demand more than any other housing number



Source: U.S. Department of Commerce: Census Bureau

Shaded areas indicate US recessions - 2014 research.stlouisfed.org

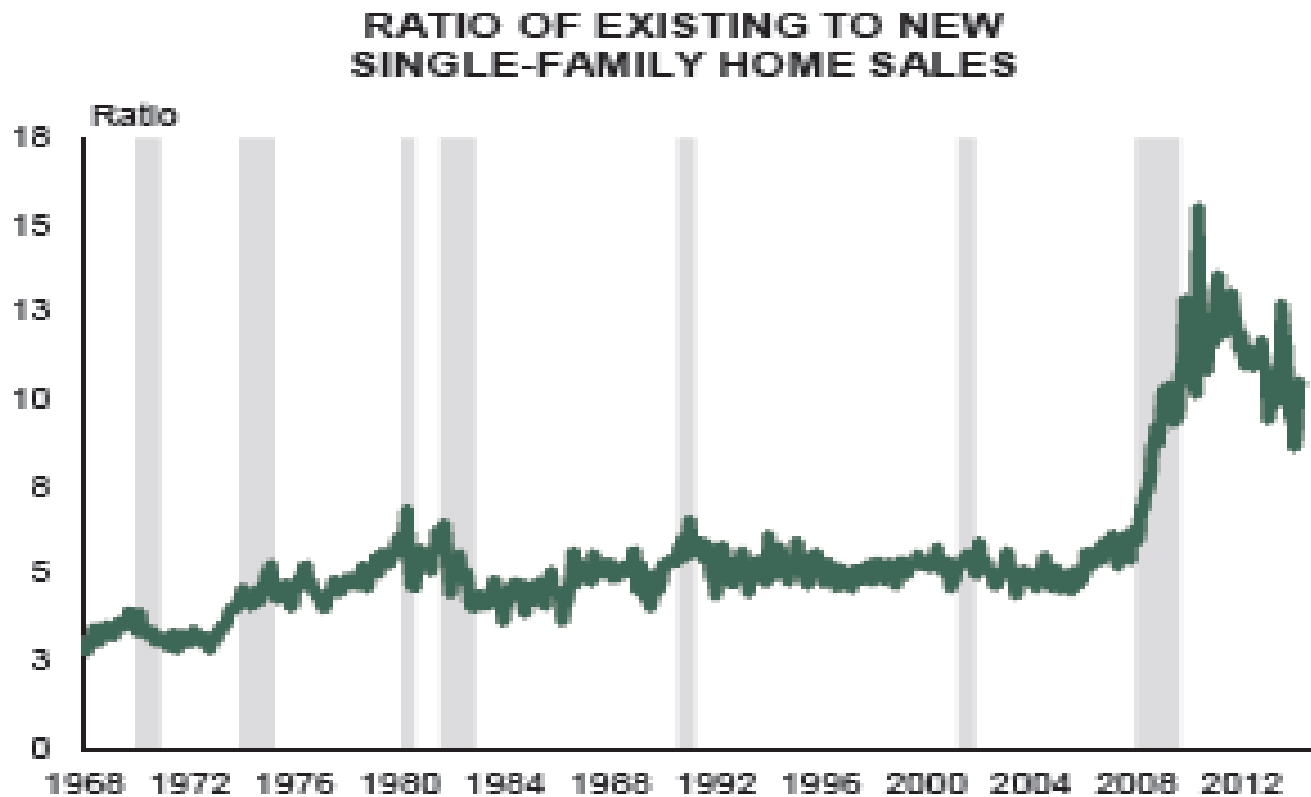
## Resale market – more than 30% are cash sales, including foreign buyers – not sustainable

Single family (incl condos), Monthly, Thousand units, SAAR



Source: NAR (<http://www.realtor.org/research> )

Problem for wood products industry – traditionally, new homes  
Account for about 20% of the housing market, but today,  
They represent only 10%. Another reason why housing starts are still weak  
And lumber/panel sales are low!!!! Resales are still being driven by cash sales,  
Foreigners, and investors purchasing foreclosed properties – not your typical market!!!!



Source: National Association of Realtors, Census Bureau

Some conclusions – housing continues to improve albeit slowly  
Most forecasters now suggesting that 2016 will be “breakout year”??

Short term:

- (1) Economy will muddle along until 2016 - i.e., **2015 still below trend**
- (2) This is still not a healthy housing market - 1<sup>st</sup> time buyers are absent and household formations are off 50% from trend – furthermore, many of sales are cash, many foreign buyers, etc. I.e., **NOT SUSTAINABLE**
- (3) The key to a recovery in housing is the return of 1<sup>st</sup> time buyers, traditionally about 40- 45% of the market. Current market skewed to cash buyers and investors. 1<sup>st</sup> time buyers are mostly young people, but they can't find jobs.
- (4) Political discourse will continue to slow a truly strong economic and housing recovery.



## Longer term:

- (1) Housing demand will hinge partly on the footprint of the Federal government – will they continue to promote housing to the degree they have in the past? Yes, the economy is important, but the politicians know how to “grease the wheels”
- (2) Labor participation rate keeps falling – this suggests that there will be future labor shortages. Furthermore, tax revenue will be impacted as more people collect from growing number of government programs while fewer people pay taxes. Look for changes in tax code; consumption tax??; social security; Medicare/Medicaid; ....
- (3) How will USA deal with aging demographics; crumbling infrastructure; out of control public debt; and, generally, decreasing global competitiveness!!!! My thought – revamp the tax system to Discourage consumption (bring it in line with other countries); and invest more in our future!!! Otherwise, we will continue to “underperform”, and housing and wood products will suffer. This will take a long term commitment from the country, politicians, voters, ..... The U.S. consumption rate ( % of GDP) is about 70% while our competitors , it is 60% or lower. Invest for the future – sounds simple, but requires some thinking that prevailed in this country following WWII.
- (4) LEADERSIP IS important – politicians need to work on long term solutions – And, more Americans need to get involved in the voting process – non presidential turnout is less than 40%. If you don't vote, don't complain about the outcome or resulting poor or lack of legislation.

Here is good article summarizing the current economy –  
In Random Lengths, Comment section, cover page/Through a knothole section –  
“U.S. Economic malaise is Structural, not Cyclical”. July 11, 2014, Vol 70, Issue 28  
(<http://www.randomlengths.com/Product/Detail/RandomLengths/> )

I couldn't agree more with the writer – I take 30 – 35 Powerpoint slides to say  
Similar things. Have to admire someone who can boil down tons of data, analyses, etc.,  
To an excellent ( and pretty accurate) 250 word treatise on the U.S. economy. I guess  
Is why he (she?) is editor for prestigious market report, and I'm a retired economist.

I apologize to my readers – the link above won't get you the report, but will get you in  
contact with Random Lengths. Contact lumber buddies too – they all subscribe to RL.