Office of the Chief Economist

February 2013 U.S. Economic & Housing Market Outlook

Showing Some Love

While the advance report on economic growth in the fourth quarter of 2012 showed a slight decline in real Gross Domestic Product (GDP), 0.1 percent on an annualized basis, housing emerged as one of the bright spots. For the first year since 2005, residential fixed investment made positive contributions to GDP growth, adding 0.4 percent to growth in the fourth quarter and 0.3 percent for the year.

This acceleration in residential investment was reflected in the latest reading on housing starts for December 2012. Housing starts came in above consensus at an annual rate of 954,000, up 37 percent from December 2011. While the monthly numbers can be noisy, the trend is decidedly positive, with housing starts posting year-over-year gains every month since September 2011. Home sales are increasing as well, with existing sales up 9 percent and new sales up 20 percent in 2012 relative to 2011. House prices are also showing positive movement nationally. All national indexes have shown value gains over the past year; our latest projection has the Freddie Mac House Price index up 3 to 4 percent in 2013 Rents are up too, with the broad Consumer Price Index for primary residence rent up 3 percent over the past year and effective rent reported by REIS up 4 percent.

While the trend in the housing sector is encouraging, the level of housing activity is still near historic lows. This means that there is still room for substantial growth in housing and housing-related industries before we return to a more normal environment. This fact is reflected in our projections for 2013, which include large percentage increases in housing starts and home sales, and modest increases in home prices and rents. Just how much higher will construction go? We are projecting that housing starts in 2013 will increase to 950,000 units or about 22 percent higher than 2012 levels. For 2014, we are forecasting another 26 percent increase in annual starts bringing them up to about 1.2 million.

Although nationally the housing outlook has brightened, there are considerable variations in markets across the country. Many metro areas saw substantial increases in home prices and construction through 2006 and an even more severe decline during the five subsequent years. Somewhat ironically, it is many of these metro areas where current growth prospects are most positive, as they overshot the bottom leaving room for growth as these markets return to a more normal path. A key driver behind this ‘room for growth’ effect is that homebuyer affordability was the second highest in recorded history in the fourth quarter of 2012, just below the peak set in the first quarter of the year, according to latest data from the National Association of Realtors. This affordability metric incorporates the effect of low mortgage rates, low house prices, and gradually improving family income.

The charts below show the relationship of home prices, median household income, home sales and single-family construction permits for select markets. While most metro areas saw substantial run-ups in prices during the boom, well above income growth, the subsequent market correction was in many cases more severe. For instance, the Phoenix and Miami metro areas saw house prices more than double from January 2000 through the boom while average nominal incomes rose by only about 50 percent in the same period. Subsequently, house prices fell back below 2003 levels, while incomes continued rising (with a slight hiccup during the recession). This volatility had a major chilling effect on housing markets, with home sales and new construction of single-family homes in these markets falling to about one-half of their January 2000 levels during the worst of the crisis.

Home sales have been recovering modestly since 2011, while house prices have bottomed out and, in most metro areas, begun rising again. However, construction of new single-family homes remains near historically low levels. Even in metro areas that did not see much of a house price bubble, such as Chicago and Philadelphia, construction of new single-family houses is below half of January 2000 levels. The level of income in most markets suggests a continued improvement in home prices, and strong growth in sales and construction. The effect on sales should be accelerated as house price recovery allows homeowners who have been forced on the sidelines by negative equity to get back into the market.

Across the country most local housing markets have room for sustainable growth, particularly in home construction and sales. As the broader economy heals, expect to see more good news with house prices continuing their recent upward trend, and home sales and housing starts continuing to post strong growth rates. The macroeconomic recovery though 2011 helped to forestall further erosion in the depressed housing market. In return, housing is now “showing some love” by contributing to economic growth, perhaps by adding close to 0.5 percentage points to 2013 GDP growth.

Frank E. Nothaft
Chief Economist

Leonard Kiefer
Deputy Chief Economist

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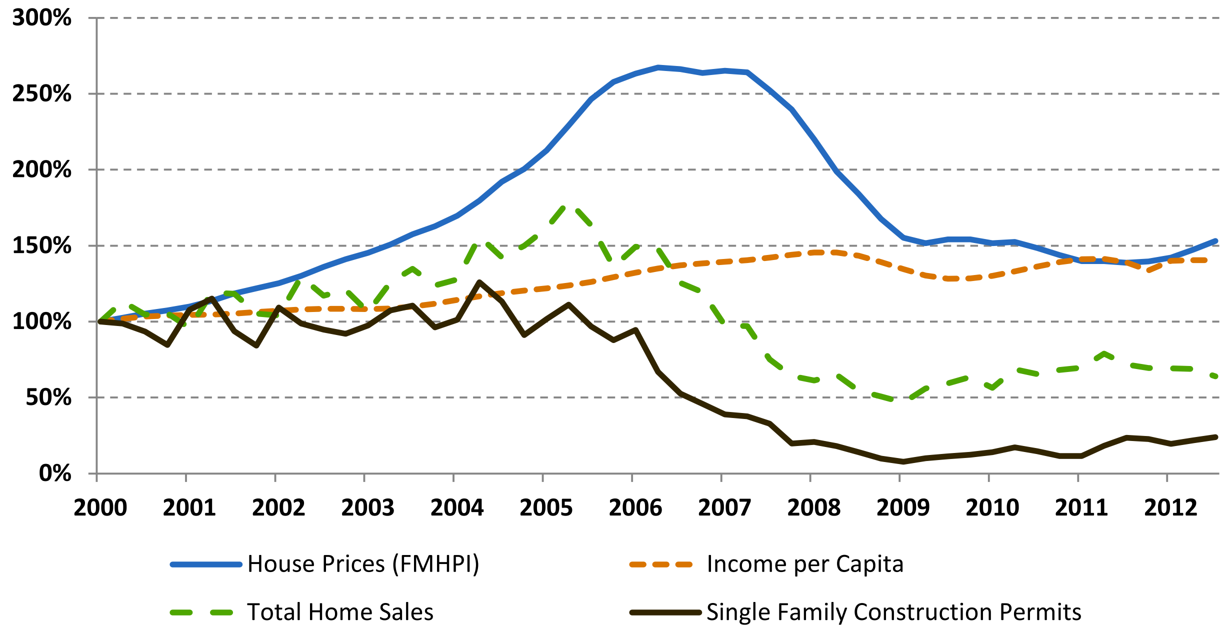
www.freddiemac.com/news/finance **chief_economist@freddiemac.com**

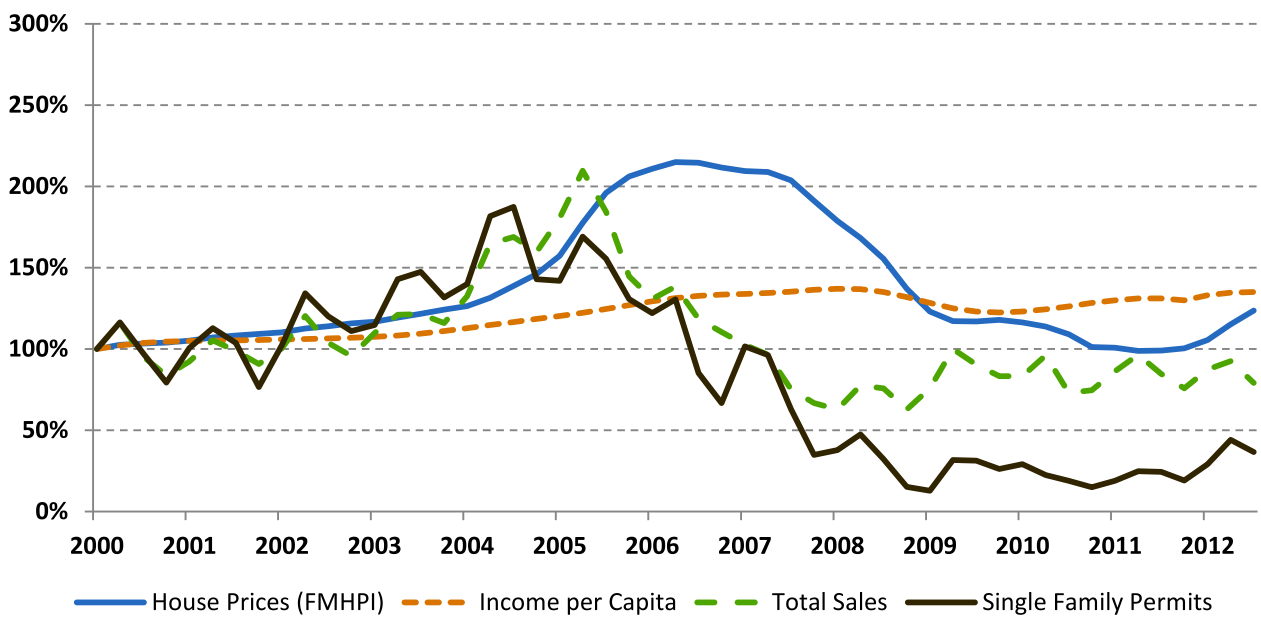
Metro areas with the largest house price declines have recently seen house price increases. New home construction remains depressed, with significant room to grow. Even in metro areas without a major housing bubble, the level of construction for single family homes is below half of the January 2000 level. New household formation and income growth will support large increases in construction and sales from their current historically low levels.

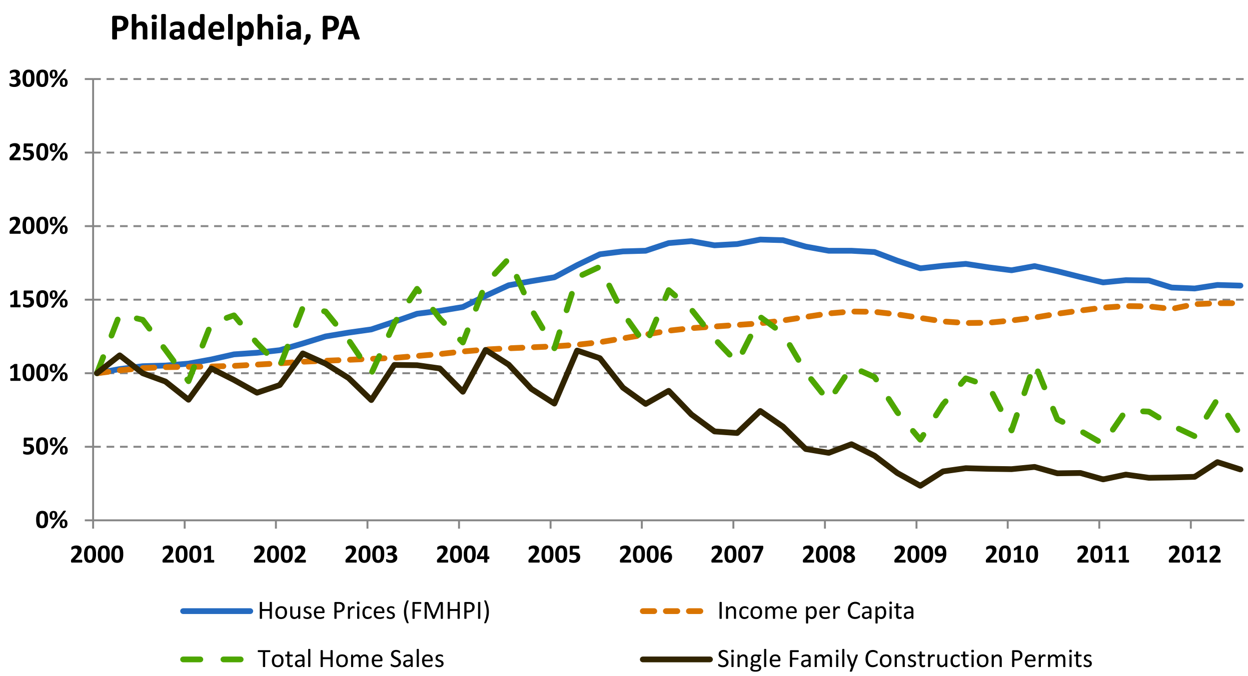
Source: Freddie Mac, BEA, Moody's Analytics, CoreLogic, Census. House Prices, Income, Home Sales, and Construction Permits 2000-2012. All values are expressed relative to their 2000 Q1 values

Miami, FL



Phoenix, AZ

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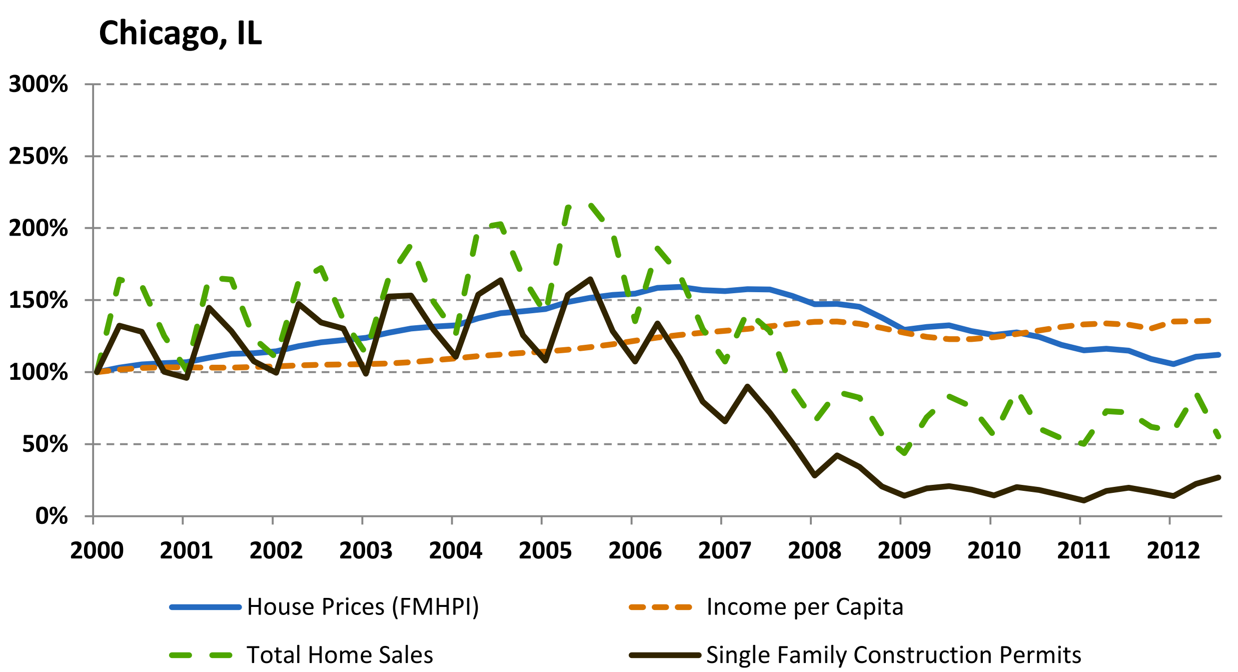
House Prices (FMHPI)
Income per Capita
Total Home Sales
Single Family Construction Permits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Revised 2/13/2013

Indicator	2012 Q3	2012 Q4	2013 Q1	2013 Q2	2013 Q3	2013 Q4	2014 Q1	2014 Q2	2014 Q3	2014 Q4	Annual Totals 2009	2010	2011	2012	2013	2014
Real GDP (%)	3.1	-0.1	1.8	2.3	2.8	3.0	3.3	3.5	3.6	3.5	-0.1	2.4	2.0	1.5	2.5	3.5
Consumer Prices (%) a.	2.3	2.1	1.5	2.0	2.0	2.0	2.0	2.0	2.0	2.0	1.5	1.2	3.3	1.9	1.9	2.0
Unemployment Rate (%) b.	8.0	7.8	7.8	7.7	7.6	7.5	7.3	7.2	6.9	6.8	9.3	9.6	8.9	8.1	7.7	7.1
30-Year Fixed Mtg. Rate (%) b.	3.6	3.4	3.5	3.7	3.8	4.0	4.1	4.3	4.5	4.6	5.0	4.7	4.5	3.7	3.8	4.4
1-Year Treas. Indexed ARM Rate (%) b.	2.7	2.6	2.6	2.6	2.6	2.7	3.8	2.8	2.9	3.0	4.7	3.8	3.0	2.7	2.6	3.1
10-Year Const. Mat. Treas. Rate (%) b.	1.6	1.7	2.0	2.1	2.3	2.4	2.6	2.7	2.9	3.1	3.3	3.2	2.8	1.8	2.2	2.8
1-Year Const. Mat. Treas. Rate (%) b.	0.2	0.2	0.2	0.2	0.2	0.3	0.4	0.4	0.5	0.6	0.5	0.3	0.2	0.2	0.2	0.5

Indicator	2012 Q3	2012 Q4	2013 Q1	2013 Q2	2013 Q3	2013 Q4	2014 Q1	2014 Q2	2014 Q3	2014 Q4	Annual Totals 2009	2010	2011	2012	2013	2014
Housing Starts c.	0.77	0.90	0.90	0.93	0.97	1.00	1.10	1.15	1.25	1.30	0.55	0.59	0.61	0.78	0.95	1.20
Total Home Sales d.	5.03	5.27	5.30	5.40	5.50	5.60	5.70	5.80	5.80	5.90	4.72	4.51	4.57	5.02	5.45	5.80
FMHPI House Price Appreciation (%) e.	1.3	0.4	0.5	3.0	0.4	-0.9	0.5	1.0	1.0	0.5	-2.3	-5.5	-3.9	7.3	3.0	3.0
S&P/Case-Shiller® Home Price Index (%) f.	2.2	0.2	0.0	3.5	1.0	-1.5	0.5	1.0	1.0	0.5	-2.5	-3.8	-3.7	7.9	3.0	3.0
1-4 Family Mortgage Originations g.																
Conventional	$454	$428	$377	$385	$318	$280	$240	$335	$235	$190	$1,549	$1,300	$1,208	$1,627	$1,360	$1,000
FHA & VA	$96	$102	$83	$95	$92	$70	$50	$80	$65	$55	$451	$377	$292	$373	$340	$250
Total	$550	$530	$460	$480	$410	$350	$290	$415	$300	$245	$2,000	$1,677	$1,500	$2,000	$1,700	$1,250
ARM Share (%) h.	8	7	10	11	12	13	14	15	15	16	3	5	11	10	12	15
Refinancing Share - Applications (%) i.	82	83	75	70	65	50	50	45	45	40	70	76	75	81	65	45
Refinancing Share - Originations (%) j.	76	76	75	70	65	50	50	45	45	40	68	67	64	75	65	45
Residential Mortgage Debt (%) k.	-2.8	-2.0	-1.0	0.0	0.0	1.0	1.0	2.0	3.0	4.0	-1.6	-4.1	-2.3	-2.5	0.0	2.5

Note: Quarterly and annual forecasts (or estimates) are shown in shaded areas; totals may not add due to rounding; quarterly data expressed as annual rates.
Annual forecast data are averages of quarterly values; annual historical data are reported as Q4 over Q4.

a. Calculations based on quarterly average of monthly index levels; index levels based on the seasonally-adjusted, all-urban consumer price index.
b. Quarterly average of monthly unemployment rates (seasonally-adjusted); Quarterly average of monthly interest rates.
c. Millions of housing units; quarterly averages of monthly, seasonally-adjusted levels (reported at an annual rate).

d. Millions of housing units; total sales are the sum of new and existing single-family homes;quarterly averages of monthly, seasonally-adjusted levels (reported at an annual rate).
e. Quarterly growth rate of Freddie Mac's House Price Index (FMHPI); not seasonally-adjusted; Dec.to-Dec. for yearly data.
f. National composite index (quarterly growth rate); not seasonally-adjusted; Q4-to-Q4 for yearly data.

g. Billions of dollars (not seasonally-adjusted).
h. Federal Housing Finance Agency (FHFA); quarterly averages of monthly shares of number of loans of conventional, home-purchase mortgage closings (not seasonally-adjusted).
i. Primary Mortgage Market Survey®; quarterly averages of monthly shares of all single-family mortgage applications (not seasonally-adjusted).

j. Home Mortgage Disclosure Act for all single-family mortgages (not seasonally-adjusted); Annual share is dollar-weighted average of quarterly shares.
k. Federal Reserve Board; growth rate of residential mortgage debt, the sum of single-family and multifamily mortgages(not seasonally-adjusted, annual rate).

Prepared by Office of the Chief Economist and reflects views as of 2/13/2013 (MAS); Send comments and questions to chief_economist@freddiemac.com.