Jim Tobin:

Welcome to Housing Developments. I'm Jim Tobin. And joining me this week for our edition of Housing Developments is guest host Paul Lopez. Welcome, Paul.

Paul Lopez:

Hey, Jim. How're you doing? It's always fun to be on this side of the microphone.

Jim Tobin:

Yeah, that's right. That's right. We've taken your producer hat off. So hey, look, here we are, sitting on the latter part of June, National Housing Month. It has been one of the more consequential months. I can remember it a long time. So let's walk our faithful listeners through what's been a really, like I said, eventful month for NAHB in housing, starting with the Innovative Housing Showcase. It's something you and your team spearheaded on behalf of the industry. We did it a couple few years ago with Dr. Ben Carson when he was the head of HUD. Tell us about this year's showcase and what a great success it was.

Paul Lopez:

Yeah. Actually, it was really successful. It was actually two events really. We had the Innovative Housing Showcase on the mall. We got about 18,000 people to walk through the various exhibits. We actually built seven homes on the mall that people can see, everything from the building systems folks putting it together, a two-story home that was opened up, so that people could see the innards and see what innovative products there are there, all the way to the typical tiny home on trailers that people are now used to seeing. Yeah. And then from there, we reached out to Secretary Fudge and we had an all day roundtable that was very, very cool. It started off with a couple of panels. And then the senior officers got to have a private one-on-one conversation with her.

It was supposed to last only 30 minutes. It ended up lasting close to an hour. And I think some great progress was made there. The thing that we were trying to highlight is we are housers. And regardless of who the administration is, we are trying to advocate housing on all levels and we're not trying to be adversaries. And if anything, we're trying to help them out as much as possible. And the private sector can in fact be a part of that conversation. So I think that was good. And then we invited a whole bunch of other folks to participate in a roundtable. And I think that was very eventful as well. We were able to have an off the record conversation of what we need to do to fix housing. And again, that lasted well over an hour. And I think we had some very good conversations from a variety of different folks that we normally don't speak to.

Jim Tobin:

Yeah, no. Paul, again, great job with you and your team. But once again highlighting that NAHP's leading the charge here in Washington DC with policymakers both on Capitol Hill and inside administration on how we're going to get through this affordability crisis that's facing the country right now. And we'll get in a little bit bigger detail about the larger economic implications of that. But again, that was a great week preceding, of course, the leadership meeting, the Spring Leadership Meeting here in Washington DC, which is coupled with our Legislative Conference. So a great successful week. Had, what, over 700 members here in DC?

Paul Lopez:

Well, yeah. You guys did a fantastic job of that. And by the way, in between the legislative meetings and all the stuff that was going on with the leadership board, we also had some testimony up on the Hill.

Jim Tobin:

Right, right.

Paul Lopez:

Talk about that a little bit.

Jim Tobin:

Yeah. No, that's right. We were approached the week before the board meeting, never a quiet time in NAHB, for the House Ways and Means committee was doing a hearing on women in the workforce in a post-COVID environment. And they approached us along with several other business entities to be one of the witnesses, to talk about women in the workforce, women reentering the workforce, the challenges whether with childcare or elder care coming out of COVID or the challenges inside COVID. And they asked Alicia Huey to represent not only NAHB, but also the business community and the housing community because our message was not only about getting more women in the workforce, not at all about accommodating women in their role in society and how they can stay in the workforce and manage their homes and their families, but also the importance of housing to recovering from COVID and the downturn there and how we are in this housing affordability crisis.

And we need to focus on focus on the home and the ability to provide safe, decent, affordable rental and ownership opportunities for women in particular and families. So she did a wonderful job on Capitol Hill really delivering our message. One of the biggest kicks I had out of that day was receiving a picture from one of a congressional office with members waiting to go see their member of Congress. And over their heads, they were watching Alicia testify on C-SPAN. So I've never had that happen in all the Leg Cons that I've done before. So thanks to Alicia for carrying the message forward. And more importantly, thanks for over 600 or 700 builders getting up on Capitol Hill, braving the heat and the long lines to deliver that message to their lawmakers in a really critical time for housing.

Paul Lopez:

Yeah. We really nailed it. These last two weeks have been something of a phenomenon. And again, like you said, kudos to Alicia. She knew she hit it out of the ballpark, too. The next few days, she was strutting her stuff. She knew it. She knew it. We all did. But that's okay.

Jim Tobin:

And as you know, the topic, of course, is the economy and warehousing fits in it, interest rates are rising. And that's why I think it's really important for us to bring in our guest today. Of course, our esteemed friend and colleague, Dr. Robert Dietz, our chief economist here at NAHB. Rob, welcome to Housing Development.

Dr. Robert Dietz:

It's good to join you here at what feels like a really busy month for housing.

Paul Lopez:

Absolutely.

Jim Tobin:

Yeah. Nevermind it's National Housing month, right? But yeah, a really consequential month for housing as well.

Paul Lopez:

So we alluded to this a little bit earlier that at our Spring Leadership, a lot of it had to revolve around the fact that you've been mentioning for a while now that a recession is looming. Is it a foregone conclusion that that's the case? We are going to be, in fact, in recession?

Dr. Robert Dietz:

There's a lot of debate among forecasting economists right now on the probabilities. Our view that the NAHB forecast is that given how tight the labor market is, how elevated inflation is, and then what the Federal Reserve's intent in terms of combating inflation, that a recession at this point is all but guaranteed. Now, we're thinking it's going to be a mild recession, something that is slowing of economic activity in order to bring price growth down to fight the inflation that's been built into the system. We don't think it's going to be anything like 2008, 2009, which was a recession combined with a financial crisis. But if you look at the data right now, it's hard to avoid the conclusion that we're in a period of economic slowing. The first quarter, 2022 data was terrible. We had a 1.5% decline for GDP. Second quarter's looking a little bit better, but we're right at the edge right now. But for our forecast, we've got one built in for 2023 due to higher interest rates.

Jim Tobin:

Rob, it's been an active couple weeks. We talked about with the Fed trying to wrap their arms around monetary policy. We were over there. Talk a little bit about our interactions with the Fed and the role that you and the builders play in trying to shape what we hope will be a soft landing.

Dr. Robert Dietz:

The Federal Reserve is absolutely trying to orchestrate the soft landing of my pessimistic view notwithstanding, but they are acutely aware of the home building industry. We are highly sensitive to changes in interest rates, changes to monetary policy. They monitor things like the state of the overall economy and regulatory burdens and factors that affect economic growth. So we provide them data, survey data of how builders are doing, the monthly builder sentiment indicator. And then we have periodic meetings at the staff level and take our NAHB senior officers and other industry leaders to do a briefing with them. And in fact, Chairman Powell in his congressional testimony mentioned that they had had recently a meeting with the builders and that was in reference to our meeting. What do we do at those briefings? It's really to get them up to date on where the home building industry is.

Now, it's a truism in economics that housing is the business cycle. And what's meant by that is that given that we're sensitive to changes in interest rates, both on the demand side and the supply side, that when the Federal Reserve tightens monetary policy, which they are doing so now and they're doing so aggressively, its primary impacts show up immediately in the housing market. And we're seeing a softening of housing demand, builder sentiment has declined now for six straight months. And Powell mentioned that repeatedly during his testimony this week that they're seen as slowing the economy. Now, for what the Fed is trying to do, which is bring down inflation, that's the kind of thing that they want to see evidence of, that there's some of the overheating and things like commodities' prices, i.e., lumber, is coming down. And that could be some good news in terms of their ability to achieve that soft landing.

Paul Lopez:

So Rob, in the meeting, they talked a lot about supply, demand. They made it very clear that they can't deal with the supply side, they can only deal with the demand side. What's the Fed trying to target here? What's their overall goal when it comes to this mission?

Dr. Robert Dietz:

Yeah. Their goal actually is really quite simple. They are under a legal mandate from Congress. They're a creature of Congress to maintain maximum employment, which basically means keeping the economy healthy, and price stability, which means fighting off inflation and inflation built into the system. We can have a longer separate discussion on the reasons behind that inflation. Some of it is government spending and stimulus and the impacts from COVID. But their intent right now is to bring the inflation rate, which right now on the CPI measures above 8%, bring it back down to around 2% on the core PCE measure, which is a separate measure of inflation that the Fed uses. So in terms of policy targeting, as you mentioned, their tools are really crude. They can affect the money supply through interest rates and the size of their balance sheet and some other regulatory actions.

What they can't do is help us on some of the causes of inflation in the housing sector, which are really rooted on the supply side. It's inefficient regulatory policy. It's a lack of skilled labor, a lack of lots, capital access, particularly for private small builders. They can give voice to those challenges. And in fact, I think we've seen Chair Powell do that at the Congressional Committee Hearings this week. But there's not a lot that they can actually activate. And that's where we need Congress and the executive branch to really step up and help us achieve in a more affordable supply building materials. We could go through the full list of action items, but all of those would help us build more single-family housing, multi-family housing, get more remodeling projects done. And that in turn, that higher housing supply would help tame inflation. And that's really how we can complement what the Fed's trying to do on the demand side.

Jim Tobin:

But one quick question on labor in particular. It seems like the Fed's actions in the short-term are going to increase unemployment rate. That can't be good.

Dr. Robert Dietz:

Right. On the demand side, that's absolutely not good. And that's why our members get concerned when we start talking about recessions. The expectation is even if we achieve a soft landing, so that's the Federal Reserve bringing inflation down, but we don't fall into an official recession, there's still going to be some uptick in unemployment because of higher interest rates. And that's what economists call a growth recession. If you're more in my line, in terms of our forecast that we're going to have a hard landing, which is a mild recession, unemployment goes up as well. And that is going to reduce demand for apartments and entry-level homes and the like. But it is a economic necessary type process to bring inflation rates down.

Paul Lopez:

So Rob, and we're going to put some of your slides in the show notes, so people can download. But I guess my question is first of all, how far will rates go up? And what can our members do to insulate themselves from that impact? Because I think it's obviously going to play a big psychological role with home buyers, right?

Dr. Robert Dietz:

Yeah, absolutely. I think in terms of where the Fed is intending to go with the Fed funds rate, which is the short-term target rate that they control, the overnight lending rate, right now, it's at 1.75%. Just a few weeks ago, it was at 1%. So it is moving up quickly. That 75 basis point increase was the largest rate increase they had done in a single meeting and more than three decades. And we think they're likely to push that rate up to 3.5% to 4%, their official target on their economic projections of 3.8%. All right. What does that mean then for the housing market? Well, a lot of the expected impacts of higher short-term rates are already baked into the cake in terms of long-term interest rates.

So at the start of the year, the 30-year fixed rate mortgage was at 3.1%. Recently, according to Freddie Mac's weekly survey, it got up to around 5.8%. And in our forecast, we do have it going up above 6%. Now, the debate gets more contentious of who do we see at 7% rate. I even had builders come up to me this week and say, "I'm thinking an 8% average 30-year fixed rate." I think maybe the economy would fall into a recession before that happens. But something between 6% and 7% is likely to be the peak rate of this tightening cycle. And then at least according to our forecast, the economy would soften, weaken, fall into a recession. And when we fall into a recession, rates then come back down.

Now, your question in terms of what our members can do to insulate themselves is a good one. I think most builders have been through a cycle or three in terms of thinking about downturns. You need to think about the kind of market that you're participating in, that you play in. If you're in a high cost, highly regulated market and your business strategy's to build entry-level homes, in other words, those first time buyers who are most sensitive to changes in interest rates, that's a tough place to be and you're going to want to be as cautious as you can. Don't overbid on the land, make sure you're building right to the demand that you can see in front of you. If you're in a high population growth market that's a little bit lower cost, lower regulatory costs, like markets in the South, a downturn or higher interest rates is likely to affect you less.

And in fact, if your buyers tend to be move-up buyers who are putting down large down payments, they're spending out of wealth, rather than having to buy a home with a large mortgage, they're going to be even less sensitive to changes in interest rates. So you're going to be in a more favorable position. So it really depends on the kind of homes you're building, the type of buyer that you're facing, and then the local economic conditions as the economy softens. But I think what we need to do at NAHB in terms of thinking about helping the members is, again, finding those policies that will help on the supply side, reducing the costs of developing land and building homes, so that as the costs of buying a home where the mortgage goes up on demand side, we can offset it somewhat on the supply side.

Jim Tobin:

Right. Yeah. That makes sense, Rob. Well, thanks for joining us today. Obviously, the work you've been doing, not only in the media warning of this over the last several months, of course, the work that Paul has done to give those opportunities, we are in the thick of it now. And of course, your continued advocacy on behalf of members with the very people who are making these decisions serve the members well and will continue to be a canary in the coal mine, so to speak, but more importantly, to try to help our members get through the next whatever it is, hard landing, soft landing, but to prepare for their businesses to accelerate once we get past this soft spot.

Dr. Robert Dietz:

Absolutely. And we got a lot of work ahead of us. So wish I had better news. But housing is in the news right now, and so we're engaged. Thanks, guys.

Jim Tobin:

Thanks, Rob.

Paul Lopez:

I appreciate it. Thanks, Rob. All right. So once again, great conversation with Rob as always. For those listening, just a reminder that his slide deck is available on nahb.org under podcasts. So you can check those out if you'd like. But I definitely think that it's worth it for you all to do so because I think he has some great information as always there. Jim, thank you so much for having me. It's always fun to play host.

Jim Tobin:

Yeah. Thanks for being with us. Next time, we'll have the normal crew headed by our CEO Jerry Howard with us. But until next time. Paul, thanks for joining us. This is Housing Developments. I'm Jim Tobin.

Paul Lopez:

And I'm Paul Lopez.

Jim Tobin:

Talk to you soon. Thanks, everybody.

Paul Lopez:

Thank you.