

Home values affect much in the economy - especially the housing and consumer sectors. Periods of rising home values encourage new construction while periods of soft home prices can damp housing starts. Changes in home values play key roles in consumer spending and in consumer financial health. During the first half of this decade, sharply rising home prices boosted home equity, consequently, consumers had money to spend.

The S&P/Case-Shiller National Home Price Index, considered the gold standard, showed that prices gained 5.2% year-over-year, down from gains that averaged in the 6's during the past year. The November report also reflected a slowdown in housing. Home price appreciation began to flatten in the Spring last year but then showed more life late in the summer. But Case-Shiller indications for November aren't pointing to renewed acceleration as the 20-city adjusted index managed only a 0.3 percent gain.

Looking across 2019, we expect price hikes to settle in the 3.0%-4.0% range. This forecast may be too conservative, but several leading industry supply and demand indicators support our thesis. These include inventory levels, which are starting to tick higher. According to the National Association of Realtors, there is currently a six-month supply of existing homes for sale (the normal range is 3.5-5.5 months). We also track new home sales which, according to the U.S. Census Bureau, are running at a 675,000 per year rate, up 16.9% month over month.

Rising borrowing costs due to the Fed's rate-hike campaign are increasing the cost of buying a home, cutting into the bullish case for housing. Indeed, residential investment has declined in seven of the past eight quarters.

We note, though, that the consumer remains employed and confidence is high. Lest we forget, however, white-hot housing conditions aren't always conducive to sustainable long-term growth in the industry. Price trends in the West remind of bubble warnings in the region over the last several years. Whether this weakness begins to sap strength in other regions is a developing question for the housing sector.