The framework of housing crumbles

High interest rates are bringing down the rafters on the housing market, despite more Regan talk of recovery.

Home construction plunged for the second consecutive month in August, as interest rates, like the rock of Gibraltar, refused to budge.

Keeping up the talk for the party faithful, who have temporarily taken up residence in Wonderland, Treasury Secretary Donald Regan, told a Conference Board businessmen's luncheon Sept. 20, "Despite the high interest rates, the recovery is going strong." What Mr. Regan doesn't like to talk about is that home mortgage rates briefly touched 15% this summer, and are currently still above 14%. With a tightening of the issuing of Adjustable Rate Mortgages (ARMs), home buyers will find mortgage money hard to come by.

Perhaps, if Mr. Regan read housing, farming, and steel-making out of the economy, the recovery would be unaffected, but there are signs that credit lending to corporations has dried up, which means that production will soon shrivel on the vine.

Housing starts fell to 1.537 million in August, a drop of 12.8%, to the lowest level since December, 1982. Most alarming is the drop of single-family housing starts, from 984,000 in July to 904,000 in August, well below the first-half rate of 1.2 million, and the rate is likely to decline steadily. The biggest fall, 19.6%, occurred in the Southeast, where building had been most active. Many home builders had overbuilt an inventory of homes, which now can't be sold. U.S. Homes, the largest home builder in the country, began unloading 250 slow-moving housing units, accepting $27,000 for some condominiums priced at $82,000. It will attempt to liquidate a 6,000-unit, $300 million inventory by the end of the year. Not all home builders are so-overstocked, but they could find themselves liquidating homes as well.

However, the other component of the housing market, multi-family units, may be even more sharply devastated. The multi-family housing (apartment) market makes up a hefty 40% of total home construction, its highest level in years. The market depends heavily on real estate tax-shelter money. Starts of buildings of 5 or more units tumbled 19.4%, to a 517,000 rate. This could be related, as we warned in an earlier article, to the recently passed tax codes, which close some tax-shelter loopholes.

Home mortgage rates continue to stay poised at the 14% rate. Also, there has been some recent tinkering with adjustable-rate mortgages by the savings and loan industry that will tighten the mortgage credit flow. Many ARMS offer the first year of a mortgage loan at a very attractive (teaser) yield-rate, with the rate to go up in the loan's subsequent years. But often home buyers can't afford the increases that begin even during the second year. Agencies such as the Federal Home Loan Mortgage Corporation (Freddie Mac) are insisting that borrowers be qualified to pay the rate that reflects the cost of the mortgage over time, not the initial dicount rate. Freddie Mac, a large purchaser of mortgages on the secondary market, can affect this tightening of lending requirements because of its size.

Beyond the housing collapse is the frayed state of the general economy. The flow of credit into corporations in general has passed from a mighty torrent into a feeble stream. In May, the rate of bank short-term lending to businesses—90-day business loans and commercial paper—grew by 34%. But by August, this had contracted to a 15% rate, and in September, the rate seemed to be flat. What corporations are now borrowing is financing inventory stock-piling; inventories grew by 0.8% in August, a nearly 10% annualized rate.

The U.S. economy continues to live off imports of manufactured goods and the surging dollar. In July, the U.S. trade deficit was $14.1 billion. Based on projections of the first seven months of this year, exports will rise from $200.5 billion in 1983 to $215.7 billion this year, but imports will rise from $269.9 billion in 1983 to $342.2 this year. The growth of imports will send the U.S. trade deficit to $126.5 billion this year, $57 billion more than last year.

Most of the imported goods are manufactured items, feeding the enfeebled U.S. economy. Last year, the United States ran a $20 billion trade surplus with Europe, but this year, based on the flood of imported manufactured goods, Europe will run a $14 billion surplus, a $34 billion swing.

The United States is now the number-two export market for Germany and the number-three market for France.

As long as the strong dollar loots the rest of the world, Mr. Regan has fed his illusions of a "recovery." But the housing framework on which his illusions rest is fast fading from existence.