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COSTAR ECONOMY

Consumers power forward into the holiday season

Incomes grow and a key measure of inflation accelerates



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CoStar Analytics

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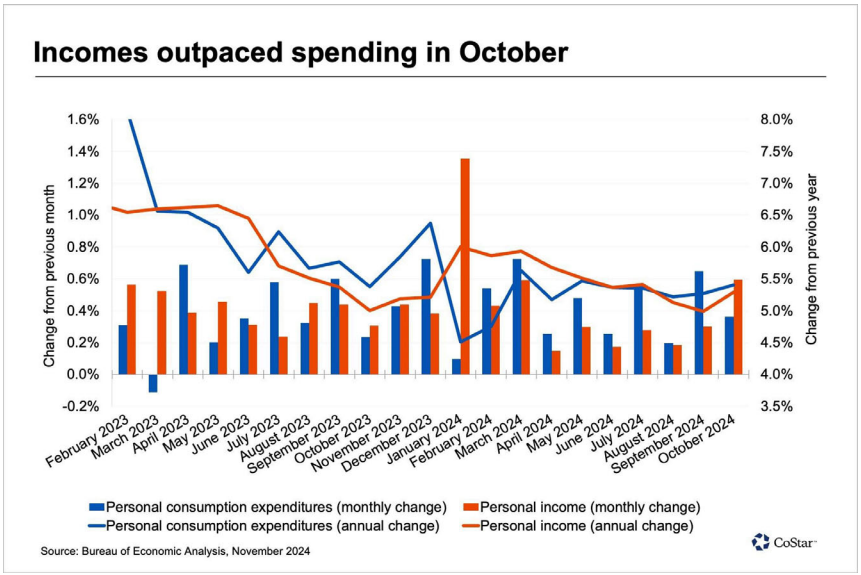
New data released by the Bureau of Economic Analysis before the Thanksgiving holiday showed that higher-than-expected income growth and lower energy prices bolstered consumer spending power just as the holiday season began.

But a measure of underlying inflation accelerated, likely reinforcing the Federal Reserve's possible preference for more gradual interest rate reductions.

Personal income grew by 0.6% in October, while consumer spending rose by only 0.4%. However, revisions to previously released data based on the release of administrative wage data from the year's second quarter showed that income growth did not outpace spending growth as strongly as initially reported.

According to the revised data, October was the first month since January that income grew faster than expenditures. On an annual basis, spending was up 5.4% while incomes have risen 5.3%, marking the third-consecutive month during which annual expenditure growth outpaced yearly income growth.

Adjusted for inflation, expenditures are up 3% annually, while income rose 2.9%.

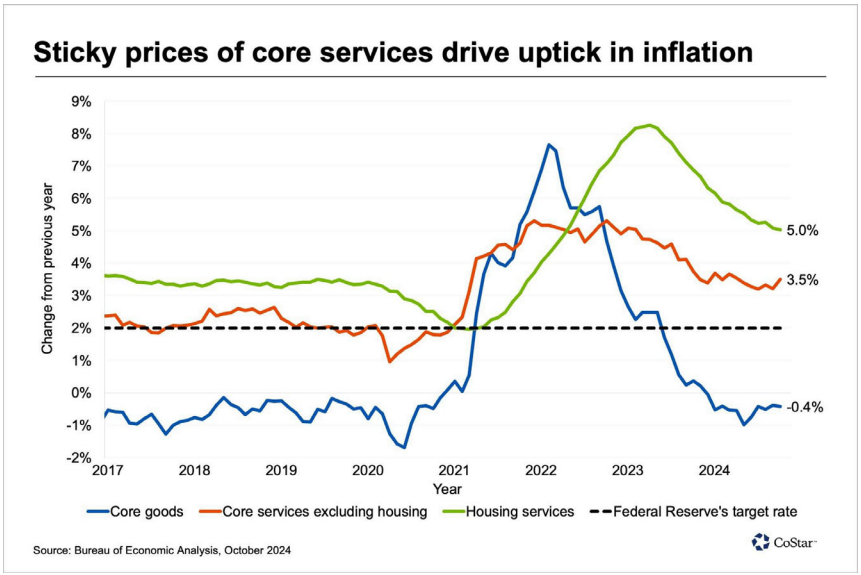


While spending on some goods, such as clothing and vehicles, ticked up in October, the largest growth in spending has come from the services sector.

On an annual basis, nearly every service category has seen spending grow faster than the inflation rate, especially among those geared toward higher-income consumers. For example, spending on financial services and insurance rose more than 10% annually, while spending on transportation services, including airline tickets, rose 6.1%. Healthcare services spending also rose 8.2% over the course of the year, while recreation services spending rose 6.1%

The headline personal consumption expenditures price index, the Federal Reserve's preferred annual inflation measure, ticked higher to 2.3% in October from 2.1% in September. That remains on par with August's reading as longer-term progress toward the Fed's 2% target continues. However, core inflation, which excludes the more volatile food and energy price categories, rose to 2.8%, its highest level in six months, a worrisome development.

The price of physical goods, which fell for the 10th consecutive month in October, offset some of the increase in the price of services. However, prices of core services excluding housing rose to 3.5%, its highest level since April 2024.

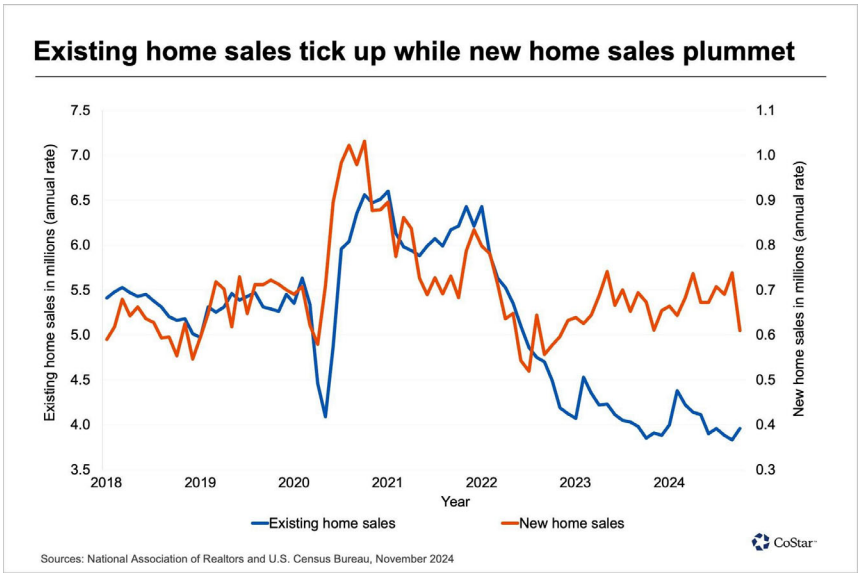


Ultimately, housing costs have proven to be the stickiest contributor to inflation. Though waves of new supply have brought multifamily rents down over the past year, the costs of for-sale housing continue to rise, albeit at a slower rate.

According to the S&P/Case-Shiller and the Federal Housing Finance Agency price indices, existing home prices were up 4% in September over the prior year. This was a relief from the double-digit annual price increases seen during the pandemic and even slower price appreciation than the five-year pre-pandemic average.

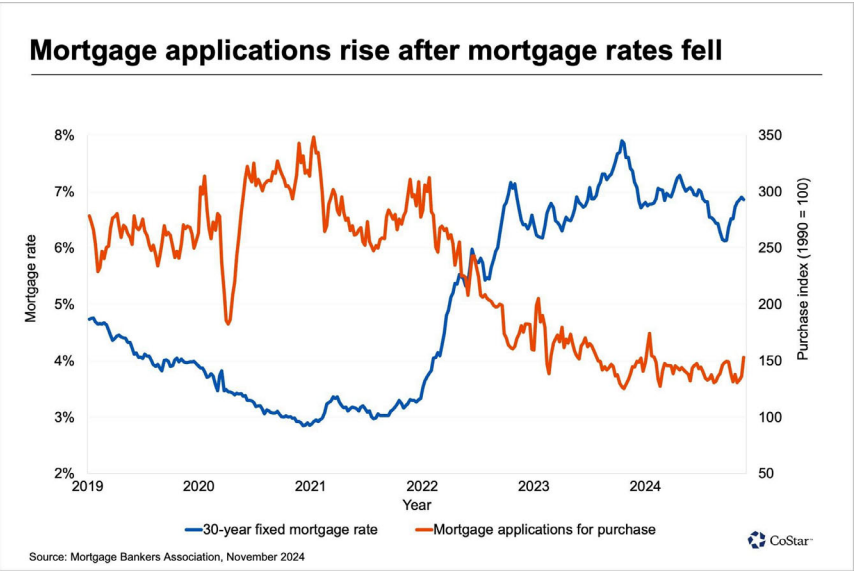
The housing market has yet to fully recover from pandemic-era disruptions. Sales of newly built homes plummeted by 17.3% in October, largely due to Hurricane Helene's impacts on Southeastern states, but the existing home market, which accounts for about 85% of for-sale housing, showed some signs of thawing.

A seasonally adjusted annual rate of 3.96 million existing homes sold in October was a 3.4% monthly increase and a 2.9% increase from October 2023.



October's performance represented the first year-over-year increase since July 2021. However, total sales remain well below the pre-pandemic average of 5.37 million as in-place mortgage rates for homeowners remain substantially lower than current market rates. The October increase likely reflected the impact of lower mortgage interest rates in September when many October sales went under contract. Weekly applications for new for-purchase mortgages surged to over 149,000 in mid-September, when mortgage rates reached 6.14%, down from highs above 7% earlier in the year.

Since then, mortgage rates have risen as 10-year Treasury yields remain stubbornly high. However, a slight pullback in interest rates to 6.86% from 6.9% led to a surge in new mortgage applications. Over 152,000 for-purchase mortgage applications were filed the week ending Nov. 22, the highest rate since the beginning of the year.



While it's too early to tell if the pre-Thanksgiving uptick in mortgage applications will prove sustainable, pending home sales, which reflect contract signings, increased 2% in October, according to the National Association of Realtors.

That uptick will likely flow into the existing home sales data for November and December. However, the index of 77.4 reflects that contract signings were more than 20% below levels reached in 2001, showing just how stagnant the current housing market remains.

What we're watching ...

Post-election analysis is focused on the potential policy agenda of the incoming administration.

President-elect Donald Trump has announced his intentions to extend (and expand) provisions of the 2017 Tax Cuts and Jobs Act past their expiry at the end of next year, lower the corporate income tax rate and ease regulatory burdens for American businesses. This combination is likely to boost economic growth in the near term, while his proposals to increase tariffs on some imports and impose tighter immigration restrictions may, depending on their extent, lean in the opposite direction in subsequent years.

This balance has yet to play out, as are their impacts on inflation and how the Federal Reserve navigates the new environment.

CoStar Economy is produced this week by Christine Cooper, CoStar's managing director and chief U.S. economist, and Chuck McShane, senior director of market analytics.