



The Northern Trust Company
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Daily Economic Comment
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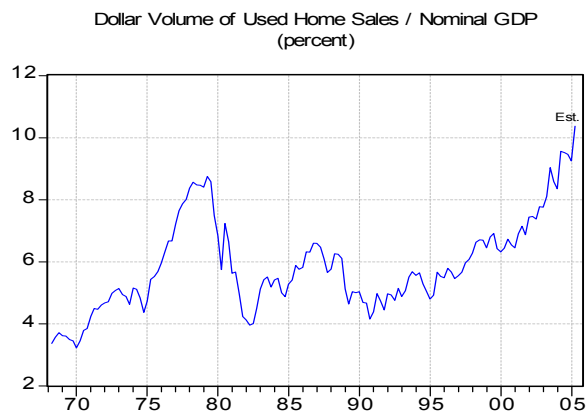
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Housing Frenzy

Not only did existing single-family home sales hit a record annualized *unit* sales rate of 6.28 million in April, but the median sales price of used single-family homes hit a record high of \$203,800. Thus, in April, the *dollar* volume of existing single-family home sales was approximately \$1.28 *trillion* – obviously also a record high. (I say approximately because I am using the median home price rather than the average price, which the NAR does not provide.) The chart immediately below shows the dollar volume of existing single-family home sales as a percent of nominal GDP. For the second quarter of 2005, I have assumed that nominal GDP will have grown at an annual rate of 6% vs. the first quarter and I have assumed that the quarterly annualized dollar volume of used home sales will equal the April annualized dollar volume. Based on these assumptions, the dollar volume of existing single-family home sales hit a record high 10.36% of nominal GDP in this quarter. In yesterday's daily commentary, Asha noted that 43% of the increase in private nonfarm payrolls in this current expansion was related to the housing industry. Of course, the principal direct contribution to GDP from existing home sales comes from commissions paid to real estate brokers, mortgage brokers and Wall Street securities houses which "securitize" mortgages. New home sales would include these commissions plus the actual value added of new construction. Nevertheless, at 10.36% of nominal GDP, the dollar volume of trading in existing homes is nothing to sneeze at. And if this housing frenzy were to slow down, it likely would have a major ripple effect on the economy as a whole.



One last item of note on the chart. A prior housing frenzy occurred in the late 1970s. This was a time when many baby boomers were buying their first residence. I wonder if the current housing frenzy also is not being driven by baby boomers. Are they now buying second homes for vacations and/or seasonal retirement residences? Are they buying multiple properties in a "roll-the-dice" act of desperation to rebuild their retirement nest eggs that got cracked when the NASDAQ bubble burst? Just a thought.

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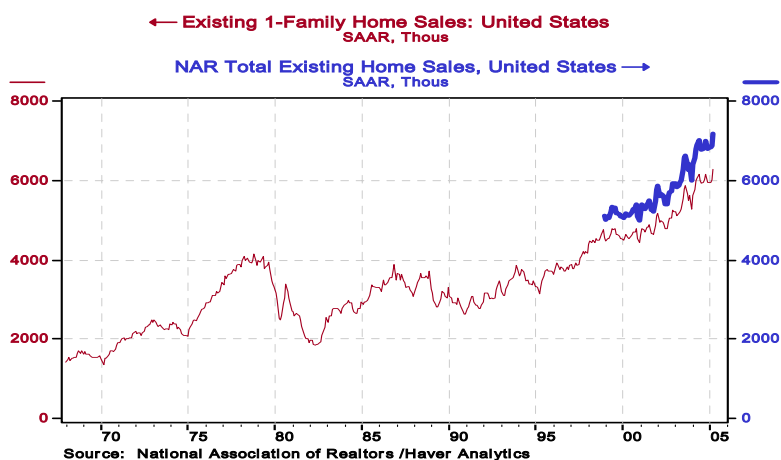
Minutes of May 3 FOMC Meeting – Uncertainty Looms Large

The Fed is on track to change the federal funds to 3.25% at the close of the June 30 FOMC meeting. There was nothing in the minutes of May 3 FOMC to change our forecast. These are the highlights from the details of minutes.

- (1) Inflation is still a major concern. Members viewed the inflation outlook to be “skewed somewhat to the upside,” but held that inflation expectations are contained. This view strengthens expectations of the next tightening in June. Energy prices appeared to play a big part of the discussion.
- (2) Although the most likely outcome in the FOMC’s opinion is one “stable prices” and “sustainable growth,” the downside risks to growth were believed to be more evident. Some members of the FOMC considered the soft economic numbers prior to the May 3 meeting as a “transitory” event. Despite this optimism, the outlook for 2005 and 2006 was “marked down somewhat.” These descriptions are inconsistent and the FOMC appears to be undecided about the growth path of the economy.
- (3) There was mention of “hot” segments in the housing market and of “speculative excesses” in some areas
- (4) The “measured pace” phrase in the forward looking policy statement was again an issue of considerable importance. But, they retained it despite the controversy about its meaning and implications.
- (5) “Uncertainty in the current economic environment” was noted as the reason for “greater uncertainty about the range of possible policy outcomes.” In other words, monetary policy in the near term depends on the nature of incoming data.

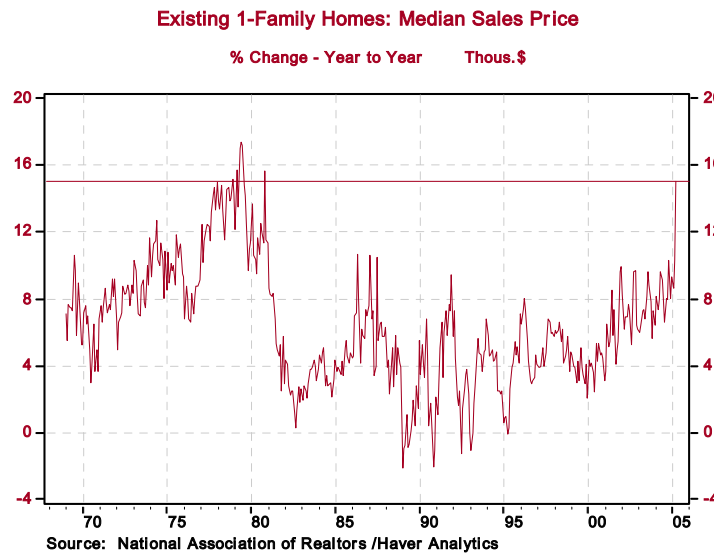
Existing Home Sales Post New Record

Sales of all existing homes (single-family, townhouses, condos) rose 4.5% to an annual rate of 7.18 million units in April. Sales of single-family homes also advanced 4.5% to an annual rate of 6.280 million. These are record high readings for sales of existing homes (see chart). On a regional basis, sales of existing homes rose 4.3% in the Northeast, 5.8% in the Midwest, 7.0% in the South, and held steady in the West.

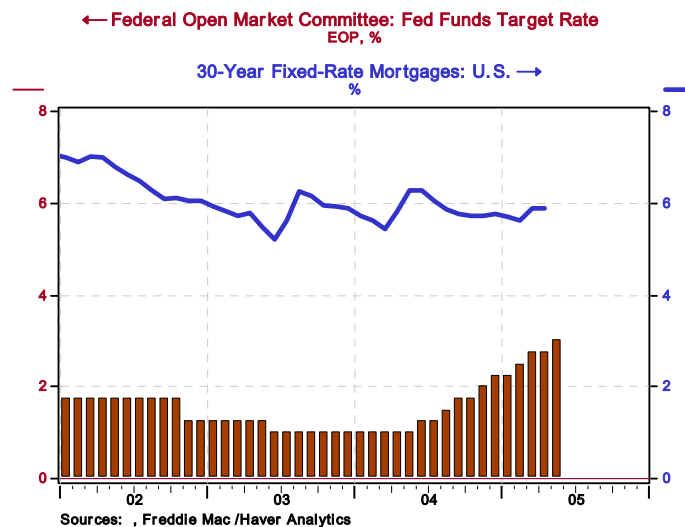


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There was a significant jump in prices of existing homes, with the median existing-home price for all housing types up 15.1% in April from year ago. The median price of an existing single-family home was \$203,800 in April, up 15.1% from a year earlier. Price gains of this magnitude were last seen in the 1979-80 period (see chart).



The inventory of unsold existing homes rose to a 4.2-month supply at the current sales pace in April, up from a 4.0-month reading in March. Favorable mortgage rates are supporting the robust pace of home sales. The Fed has raised the federal funds rate from 1.00% to 3.00% in the period June 2004 to May 2004. In this same time span, the 30-year fixed-rate mortgage has declined from 6.29% in June 2004 to 5.89% in April 2005. The 30-year fixed-rate mortgage was quoted at 5.71% during the week ended May 20.



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