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BUILDER

Housing in a K-Shaped Economic Recovery

'At some point the two parts of the K will need to converge, whether for good or for bad,' says Meyers Research chief economist Ali Wolf.

By Ali Wolf

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Can you decouple parts of the economy from another and still have a strong recovery? That's the question the U.S. economy is facing today, and the so-called "K-shaped" recovery is sending mixed-messages depending on where you look.

A K-shaped recovery is one where parts of the economy are experiencing robust growth and strong demand while others are struggling with viability and profitability. The divergence can occur among groups of people, industry sectors, or business segments.

Currently, the economic growth in the top part of the K has been nothing short of remarkable while the bottom half continues to rebound slowly.

The top of the K includes:

- Workers with remote capabilities
- Higher-educated individuals
- Those with money in soft or hard assets
- Businesses that have benefited from the changing demand landscape
- Online retail

The bottom of the K includes:

- Those unable to work from home
- Households where child care is creating time or financial stress
- Companies and employees related to high-touch services
- Travel and tourism-related businesses

Retail sales is one example of a sector that is outperforming compared with last year. With the inability to spend our money on service-related items, sales of goods are skyrocketing. Retail sales are up 2.7% year over year as people ramp up online shopping and spend money on items for the home or new hobbies.

The housing market is another sector that is defying gravity. The latest data shows that purchase mortgage applications, which captures new and existing homes, are 27% above where they were last year. In addition, the Meyers Research New Home Pending Sales Index for July posted a 33% year-over-year increase.

Real-time data, however, shows pain persists in the bottom of the K. Here are some examples:

- OpenTable reservations are off 50% YOY, with activity in bigger cities and COVID-19 hot spots performing even worse
- Passenger traffic at U.S. airports is down 70% YOY
- Low-wage employment is 15.7% lower compared with the start of the year. In contrast, employment is off 0.5% for higher-income individuals

One can see the bifurcation even further when digging into the labor stats. The unemployment rate for someone with a bachelor's degree or higher is 6.7% (top of the K) compared with those with less than a high school diploma at 15.4% (bottom of the K). There is historically a gap between the unemployment rates for these two groups, but the spread was 2.1 percentage points this time last year compared with 8.7 today. The demographics of new-home buyers often stem from those individuals in the top of the K.

So, can a rising tide lift all boats? This depends.

For starters, some of the people and industries in the bottom of the K are at the mercy of the virus. The longer we go without a vaccine or potent anti-viral, the more permanent business closures and job losses the economy will face.

Second, while higher-income individuals are more likely to have regained employment, they are far less likely to be spending money as they did pre-COVID-19. The personal savings rate jumped to nearly 34% in April as the economy virtually came to a standstill. The phased reopenings came with increased consumer spending, but the savings rate remained stuck at 19% in June. For reference, the 60-year average is 8.8%.

For consumers, the change in spending habits has allowed them to save, which historically has been difficult. For the economy, it can cause pain as consumer spending is the key driver of growth. Important, the K-recovery is resulting in an inverse reaction with spending. Individuals who earn more money have disproportionately pulled back spending (-11.5% since January) compared with their lower-income counterparts, those that have benefited from fiscal support (-4.2%).

Housing, again, is the beneficiary of the increased level of savings. The down payment is usually the key factor holding back home sales, and four months of forced savings is enough to reach a 3.5% down payment in some markets.

Today's economy is writing the pages of future textbooks, and housing will be one of the clear winners of 2020. However, a persistent decoupling of the economy is unsustainable, and at some point the two parts of the K will need to converge, whether for good or for bad.

About the Author

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Ali Wolf is Chief Economist for Meyers Research. In her role, Ali provides data analytics, runs special research projects, and does presentations across the country on topics spanning both the housing market and wider economy. Ali has focused a lot of her career on understanding prior recessions and led the charge on 'millennials discussing millennials' in the home building space.