Box 2.1

Recent performance of the US housing market

The US housing market has been recovering since 2012 on the back of improving economic conditions and unprecedented monetary stimulus. The recovery, while gradual, has been evident on various fronts. Home prices and sales activities have both embarked on an uptrend. Housing starts have also been picking up amid declining vacancy rates (***Chart 1***).

Chart 1 : Recovery of the US housing market

(a) Home price and sales gradually recovered **(b) Housing starts picked up amid falling vacancy rates**

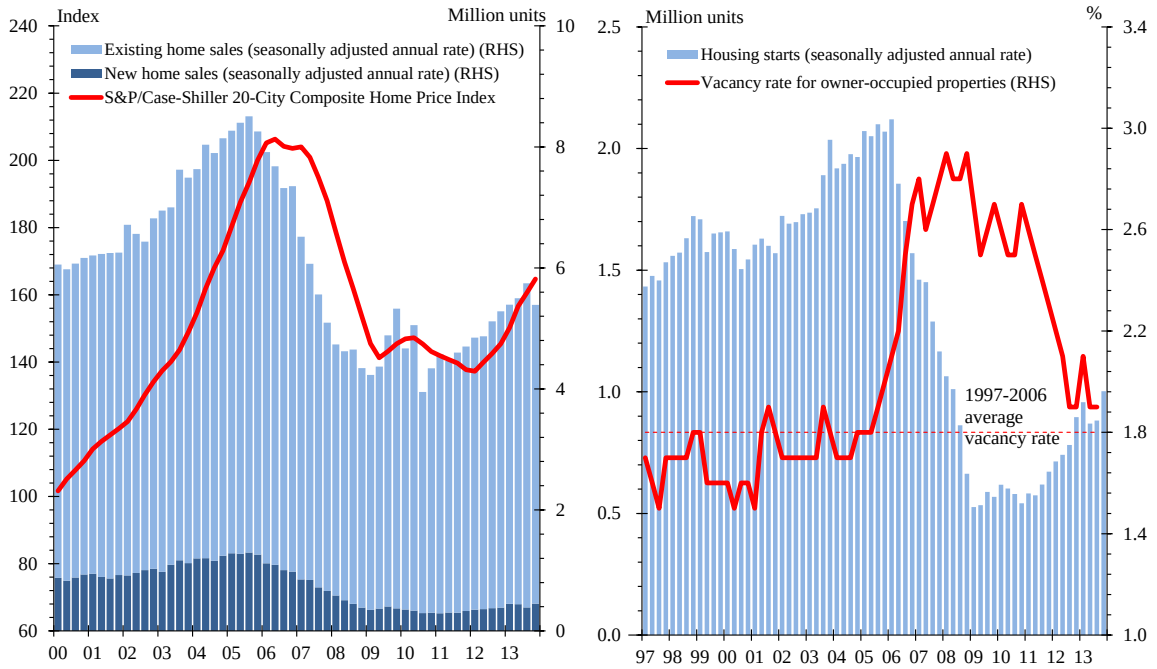
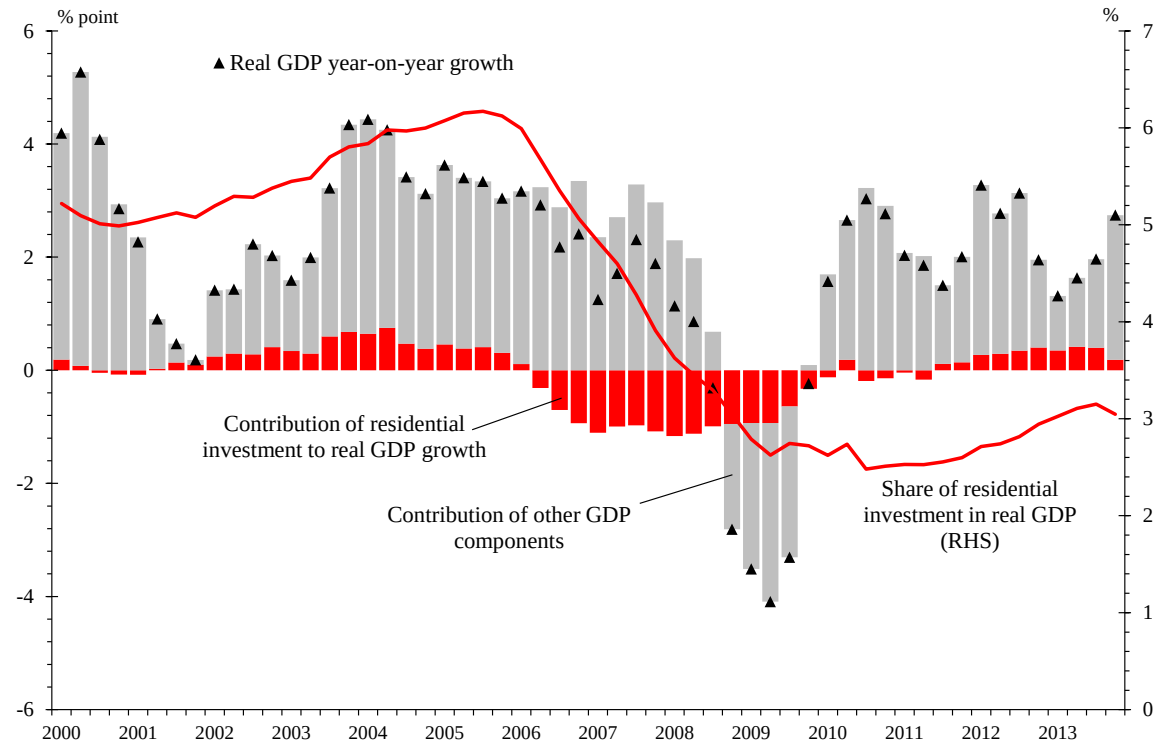


Chart 2 : Contribution of residential investment to real GDP



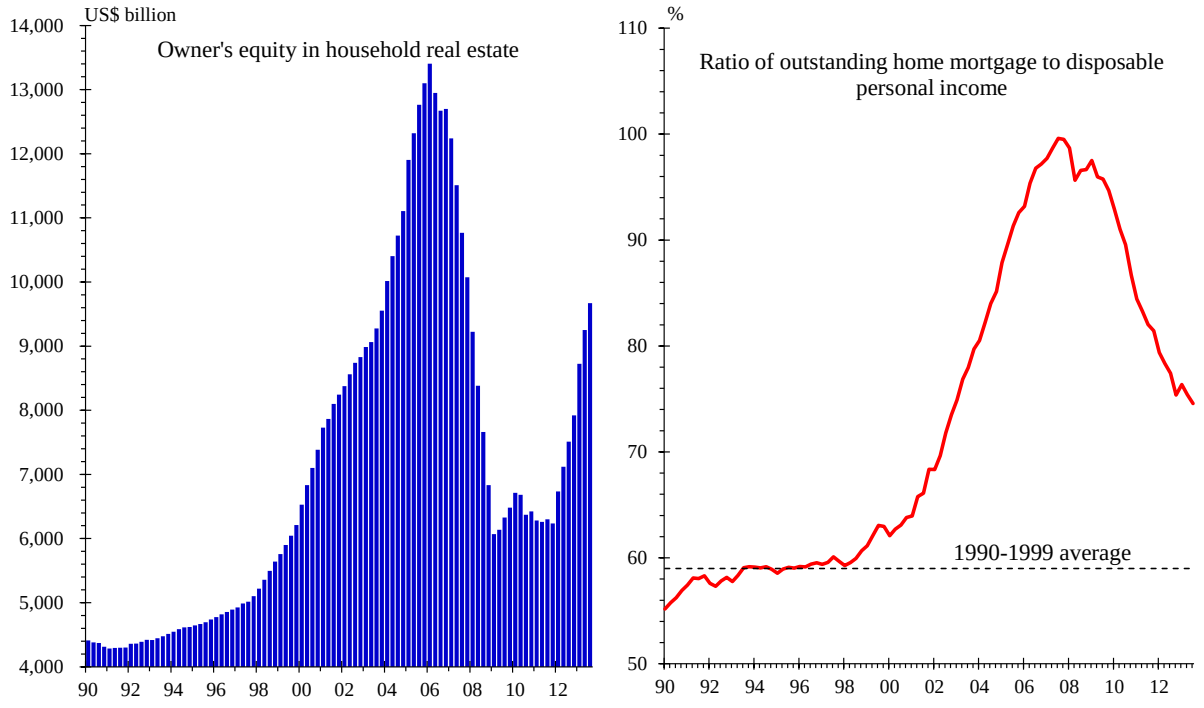
Box 2.1 (Cont'd)

The housing market recovery has contributed to the faster US economic growth in the second half of 2013, both directly and indirectly. The visible pick-up in housing starts since 2012 was directly reflected in the residential investment component of GDP. Its contribution to real GDP growth picked up from 0.01% point in 2011 to 0.32% point in 2012 and 0.33% point in 2013 (***Chart 2***). Correspondingly, the share of residential investment in real GDP rose from a low of 2.5% in the third quarter of 2010 to 3.0% in the fourth quarter of 2013. This compared with the average of 4.4% in the 1990s, before the housing boom in the 2000s.

The housing market recovery should have also helped drive the economy indirectly through wealth effects on consumption. According to the Federal Reserve, owners' equity in household real estate increased notably by 55% from US$6.2 trillion in the fourth quarter of 2011 to US$9.7 trillion in the third quarter of 2013 (***Chart 3***). However, it is unclear whether the household deleveraging process is completed. The ratio of outstanding home mortgages to disposable personal income went down from a high of 100% in the third quarter of 2007 to 75% in the third quarter of 2013. Despite the decline, the ratio remained higher than the average of 59% in the 1990s, when the housing market was in a more normal state (***Chart 3***). Should the deleveraging process continue in 2014, it may still constrain the growth of private consumption, keeping the US economic growth from moving to higher gear.

Chart 3 : Recovering housing wealth amid deleveraging

(a) Housing wealth recovered **(b) Housing debt remained relatively high**



Also, whether the US housing market recovery could withstand the unwinding of the monetary stimulus is another concern. The Fed's monetary policy direction has proved to be a deciding factor. The indication by the Fed in mid-2013 on the prospect of asset purchase tapering was soon followed by increases in mortgage rates and slowdown in home sales. Now that the Fed has begun reducing the asset purchases, the dynamics between the monetary policy, housing market and overall economic conditions warrant close watch. Given the tapering, it remains to be seen if the US housing market would continue to gather momentum by riding on improving economic fundamentals and in turn contribute to further economic growth.