This Homebuilder Index Is Still Well Below Its All-Time High

1. Investors are likely aware that most major U.S. equity indices have been setting numerous record highs over the past year. There are, however, niches of the market that have lagged the broader stock indices.

2. Today's post shows that while valuation levels of homebuilder stocks are up sharply from their bear market lows in 2009, valuations still reflect a notable discount to their peak, set in July 2005 (see chart).

3. Bloomberg's 2018 and 2019 estimated year-end price-to-earnings (P/E) ratios on the S&P Homebuilding Select Industry Index are 14.70 and 13.35, respectively, as of 12/7/17. Both are well below the index's three-year average P/E of 17.26.

4. For comparative purposes, the 2018 and 2019 estimated year-end P/E ratios on the S&P 500 Index are 17.93 and 16.29, respectively, as of 12/7/17. Its three-year average P/E was 19.76.

5. Year-to-date through 12/6/17, the S&P Homebuilding Select Industry Index posted a total return of 28.02%, compared to a gain of 19.67% for the S&P 500 Index, according to Bloomberg.

6. Even though the bottom in homebuilding investment was reached in March 2009, the rebound did not pick up steam until the latter part of 2011, according to Bloomberg.

7. In October 2017, housing starts stood at a seasonally adjusted annual rate of 1.290 million, compared to a pace of just 610,000 in October 2011, according to the U.S. Census Bureau. Based on population growth and “scrappage,” housing starts should eventually rise to about 1.5 million units per year, according to Brian Wesbury, Chief Economist at First Trust Advisors L.P.

8. One of the potential headwinds for home sales moving forward could stem from the passage of tax reform legislation. While not finalized, the Republican Party's proposed tax plan includes caps on mortgage interest and local property tax deductions, which could possibly impact sales of higher end homes if passed into law. Congress could hold a vote on tax reform by year-end.

Source: Bloomberg. Weekly data points from 12/5/03 to 12/1/17. Past performance is no guarantee of future results.

View from the Observation Deck

This chart is for illustrative purposes only and not indicative of any actual investment. The illustration excludes the effects of taxes and brokerage commissions or other expenses incurred when investing. Investors cannot invest directly in an index. The S&P Homebuilding Select Industry Index provides investors with an equity benchmark for U.S. traded Homebuilding-related securities. The S&P 500 is a capitalization-weighted index comprised of 500 stocks (currently 505) used to measure large-cap U.S. stock market performance.

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