



Weekly Note – January 6, 2017

Economics: Labor Market Caps a Solid Year

The headline job growth number for December in today's employment report was below market expectations but still capped a solid 2016 for the labor market. The net positive revision in the prior two months puts the three-month average change at the weakest level since June, but the gain is more than ample to hold the unemployment rate steady. Other details in the jobs report were largely positive, including the strongest annual increase in average hourly earnings in the expansion, an uptick in the labor force participation rate, and the third consecutive drop in the broadest measure of labor underutilization (U-6 unemployment rate). Furthermore, the report sealed a string of six consecutive years of annual job gains of more than two million – the best record since 1999 – and showed a visible uptrend in wage growth over the past two years. In the market reaction to the report, the yield on 10-year U.S. Treasuries rose six basis points, and the odds of a rate hike at each Fed meeting this year rose slightly, according to the fed funds futures market. Other data this week were mixed. Factory orders fell sharply in November, ending a four-month stretch of increases. However, a survey of manufacturing purchasing managers posted the second straight month of solid gains in December to reach the highest level in two years. A similar survey for the service sector remained at the highest level in over a year. The trade deficit expanded for a second consecutive month in November, due to a rise in imports and a fall in exports, suggesting that net exports likely dragged sizably on growth last quarter following a large contribution in the third quarter. Consumer spending got a boost as auto sales rose in December to the highest level since 2005 and posted the largest annual total in the 16-year history of the data series. The [minutes](#) from the December meeting of the Federal Open Market Committee underscore heightened uncertainty facing the economy this year, as the word "uncertainty" appeared 15 times throughout the minutes.

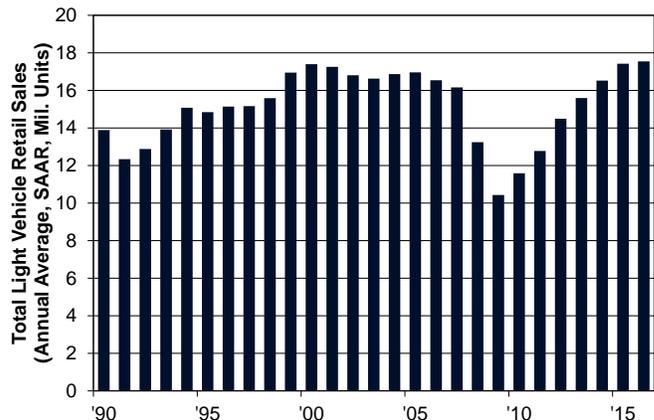
- **Nonfarm payroll employment** expanded by 156,000 in December, according to the Bureau of Labor Statistics. The three-month average change moderated from 182,000 in November to 165,000, the weakest pace since June. Job gains in the past two months were revised upward 19,000 on net. The unemployment rate ticked up one-tenth to 4.7 percent, and the participation rate rose one-tenth as well to 62.7 percent. Average hourly earnings rose 0.4 percent from November, and 2.9 percent from a year ago. The average workweek was unchanged at 34.4 hours. The broadest measure of the unemployment rate (U-6) ticked down one-tenth to 9.2 percent.
- **The Institute for Supply Management (ISM) Manufacturing Index** rose 1.5 points in December to 54.7 (any reading above 50 indicates expansion). Gains in employment, production, and new orders drove the increase. **The ISM Nonmanufacturing Index**, a gauge of service sector activity, was flat at 57.2 in December, as a spike in new orders cancelled out a fall in employment.
- **Factory orders** fell 2.4 percent in November, according to the Census Bureau. Nondurable goods, the new piece of data in the report, edged down 0.2 percent, after rising the previous three months. New orders for core capital goods (nondefense excluding aircraft) rose 0.9 percent, marking the strongest gain since August.
- **Light vehicle sales** increased 3.1 percent to an annualized pace of 18.4 million in December, according to Autodata.
- **The U.S. trade deficit** widened by \$2.9 billion in November, according to the Census Bureau, the result of a 1.1 percent rise in imports and a 0.2 percent drop in exports. The inflation-adjusted goods deficit, used in the calculation of net exports in the GDP estimate, widened by \$3.3 billion to \$63.6 billion.

Annual Wage Gains Climb to an Expansion Best



Source: Bureau of Labor Statistics

2016 Marks Best Year Ever for Auto Sales



Source: Autodata

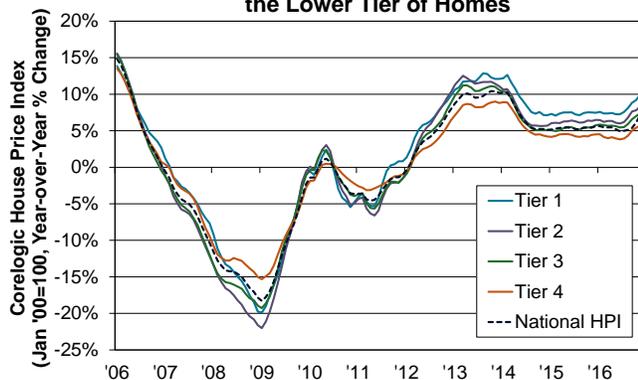


Housing: Construction Spending Turns a Corner

This week's reports included further evidence of a turnaround in residential investment, strengthening home price appreciation, and a pullback in mortgage demand. Private residential construction spending improved for the second consecutive month in November. Spending on new single-family construction posted the first back-to-back monthly gains in a year; however, single-family spending fell on an annual basis for the fourth straight month, marking the longest streak of year-over-year declines since mid-2011. Multifamily construction spending, on the other hand, declined from a month ago for the first time in four months but continued to post annual gains. Overall, the report supports our forecast for a rebound in residential investment in the fourth quarter, reversing the recent trend that showed two consecutive quarters of decline for the first time since early 2014. Another piece of positive news this week was the annual rise in the CoreLogic National Home Price Index of more than 7.0 percent in November, marking the largest annual gain since May 2014. However, the pace of appreciation varied substantially by region and price tier. Although the national index is still 4.1 percent below the April 2006 peak, the indices for 27 states have fully recovered. Also, the lowest-price tier of homes continued to appreciate faster than the rest of the market and is the only tier to see prices exceed the pre-crisis peak. Stiff competition for starter homes appears to have put extra upward pressure on prices at the lower end of the market. Lastly, mortgage rates took a breather this week after rising nearly 80 basis points in the eight weeks since the election, according to Freddie Mac's survey. The average rate on 30-year fixed-rate mortgages fell 12 basis points to 4.20 percent after climbing to the highest level since late April 2014 last week. The dramatic rise in rates has significantly curtailed refinance demand, leading to a fifth consecutive monthly drop in December and the biggest decrease since June 2013. Purchase demand fared better, as some potential home buyers rushed to apply for mortgages before rates rise further. Despite two straight weekly drops to close out the year, purchase applications for all of December rose for the second straight month.

- **Private residential construction spending** increased 1.0 percent in November, according to the Census Bureau. Spending on new construction grew 0.8 percent, as the 1.8 percent rise in single-family spending outweighed the 2.7 percent drop in multifamily spending. Home improvement spending increased 1.5 percent. From a year ago, new single-family construction spending declined 0.7 percent, while multifamily spending improved 10.5 percent.
- **The CoreLogic National Home Price Index**, a repeat sales measure, rose 1.1 percent in November (not seasonally adjusted). From a year ago, prices increased 7.1 percent, accelerating from the 6.1 percent annual gain in October. Home prices have increased year over year every month since February 2012. In addition to the overall index, CoreLogic reports four home price tiers calculated relative to the median national home price. The low-price tier (75 percent or less of the median) rose 9.9 percent from a year ago, compared with 8.3 percent for the low-to-middle tier (between 75 and 100 percent of the median) and 7.4 percent for the middle-to-moderate tier (between 100 and 125 percent of the median). The highest-price tier (greater than 125 percent of the median) rose 5.7 percent.
- **Mortgage applications** edged up 0.1 percent for the week ending December 30, following a 12.1 percent drop the prior week, according to the Mortgage Bankers Association. The 1.7 percent rise in refinancing applications barely outweighed the 1.4 percent decline in purchase applications. The average 30-year fixed mortgage rate fell six basis points to 4.39 percent, ending a nine-week streak of rate increases.

Home Price Growth Accelerates, Especially for the Lower Tier of Homes



Note: Tier 1: 0-75% of median, Tier 2: 75%-100% of median, Tier 3: 100%-125% of median, Tier 4: 125%+ of median

Source: CoreLogic

Mortgage Rates Pull Back After the Fastest Run Up Since the Taper Tantrum



Source: Freddie Mac

Frank Shaw
Economic and Strategic Research Group



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