Economics: Consumers and Businesses Finish Strong

This week offered the first estimate of overall economic growth during the final quarter of 2017. Real GDP growth slowed six-tenths from the third quarter to 2.6 percent annualized, as trade and inventories dragged on growth. But the weakening headline masked a marked increase in domestic demand. Final sales to domestic purchasers (GDP minus trade and inventories), which is a gauge of strength in domestic demand, grew 4.3 percent annualized, the fastest pace in more than three years. Consumer spending posted the biggest increase since the second quarter of 2016, driven by outlays on durable goods, reflecting the surge in auto sales to replace hurricane-damaged vehicles. Residential investment rose the most since early 2016 and added to growth for the first time in three quarters. Nonresidential investment and government spending also contributed more to growth than in the prior quarter. Notably, business investment in equipment showed back-to-back double-digit gains, registering the strongest increase in more than three years. For all of 2017, the economy grew 2.5 percent (fourth quarter-over-fourth quarter), the best performance since 2014. Solid economic growth should continue in the first half of 2018, according to the Leading Economic Index, which ended 2017 on a strong note. Durable goods orders also posted a strong finish to 2017, with the biggest monthly rise in December since June 2017, thanks to sharp gains in aircraft and defense orders. Core capital goods orders (nondefense excluding aircraft), a forward-looking indicator of business equipment spending, fell slightly, ending a string of five consecutive increases. This suggests some softening in equipment spending growth in the current quarter. Core capital goods shipments, an input used to estimate business spending on equipment in GDP, showed a solid gain in December, posting the second consecutive quarter of double-digit annualized increases and mirroring the strength in equipment spending in the GDP report. Lastly, initial unemployment claims jumped last week but still erased less than half of the outsized decline in the prior week.

- **Gross domestic product (GDP)**, adjusted for inflation, increased 2.6 percent annualized in Q4 2017, slowing from a 3.2 percent increase in Q3 2017, according to the advance estimate from the Bureau of Economic Analysis. Real consumer spending increased 3.8 percent and contributed 2.6 percentage points to GDP growth. Real nonresidential investment rose 6.8 percent. Real residential investment rose 11.7 percent, and real government spending increased 2.9 percent. Net exports and inventory investment subtracted 1.1 percentage points and 0.7 percentage points from growth, respectively. The GDP price index rose 2.4 percent annualized, the biggest increase since Q2 2016.

- **The Conference Board Leading Economic Index (LEI)**, a gauge of the economic outlook over the next three to six months, rose 0.6 percent in December, marking the 16th consecutive monthly increase. New orders was the biggest driver, contributing nearly half of the gain in the index. Only one of the ten components, manufacturing hours worked, declined during the month.

- **Durable goods orders** rose 2.9 percent in December, according to the Census Bureau. Core capital goods orders fell 0.3 percent during the month, but the November decline was revised four-tenths higher to show a 0.2 percent gain. Core capital goods shipments increased 0.6 percent.

- **Initial claims for unemployment insurance** rose 17,000 to 233,000 in the week ending January 20, according to the Department of Labor. The four-week moving average increased 3,500 to 240,000.
Housing: 2017 Marks Best Sales Performance Since 2006

This week, home sales earned their place in the spotlight with an impressive 2017. Despite stumbling in December from expansion highs in November, new and existing home sales combined to post an increase in annual total home sales for the third consecutive year, reaching the highest level in over a decade. New home sales fell in December for the second time in three months, but the annual total increased sizably, marking the sixth consecutive rise to the highest level since 2007. The inventory of new homes for sale expanded for the sixth consecutive year, and the monthly gain in December was the largest in more than four years. Existing sales retreated in December for the first time in four months after nearing an 11-year high in November. For all of 2017, existing home sales rose only modestly but posted the third straight increase to the strongest annual pace in 11 years. Unlike the new home market, the inventory of existing homes for sale continued to contract in December. Inventory has declined year-over-year for 31 consecutive months and in December registered a double-digit annual drop for the second time in three months, sending the months’ supply (inventory-to-sales ratio) to a record low. The tight supply of existing homes continues to put upward pressure on home prices, as the FHFA Purchase-Only House Price Index posted another strong year-over-year increase in November. On the mortgage demand front, both purchase and refinance mortgage applications increased last week for the third straight week, with purchase applications reaching the highest level since April 2010. Mortgage rates jumped this week by 11 basis points to 4.15 percent, the highest level since last March, according to Freddie Mac.

- **New single-family home sales** declined 9.3 percent in December to a seasonally-adjusted annualized rate (SAAR) of 625,000 units, according to the Census Bureau. New home sales in the prior three months were revised downward 65,000 units on net. For all of 2017, new home sales rose 8.4 percent to 608,000 units. The number of new homes for sale (seasonally adjusted) rose 3.9 percent from November and 14.0 percent from a year ago. The months’ supply rose eight-tenths to 5.7 months. The median new home sales price, unadjusted for the composition of sales, rose 2.6 percent year over year.

- **Existing home sales** fell 3.6 percent in December to 5.57 million units (SAAR), according to the National Association of REALTORS®. Single-family sales fell 2.6 percent and condo/coop sales fell 11.6 percent. For all of 2017, existing home sales totaled 5.51 million, a 1.1 percent increase from 2016. The number of homes for sale, which is reported on a non-seasonally adjusted basis, fell 10.3 percent from December 2016. The months’ supply dropped to 3.2 months. The median existing home sales price rose 5.8 percent from a year ago.

- **The FHFA Purchase-Only House Price Index**, reported on a seasonally-adjusted basis, increased 0.4 percent in November. From a year ago, the index rose 6.6 percent, slowing two-tenths from the annual pace in October.

- **Mortgage applications** increased 4.5 percent for the week ending January 19, according to the Mortgage Bankers Association (MBA). Purchase applications improved 6.1 percent, as conventional and government mortgage applications increased 6.8 percent and 4.5 percent, respectively. Refinance applications edged up 0.9 percent, as a 1.4 percent gain in conventional applications outweighed a 1.1 percent drop in government applications. The MBA survey’s average 30-year fixed mortgage rate rose 3 basis points to 4.36 percent, marking a 10-month high.
Opinions, analyses, estimates, forecasts and other views of Fannie Mae's Economic and Strategic Research (ESR) Group included in these materials should not be construed as indicating Fannie Mae's business prospects or expected results, are based on a number of assumptions, and are subject to change without notice. How this information affects Fannie Mae will depend on many factors. Although the ESR group bases its opinions, analyses, estimates, forecasts and other views on information it considers reliable, it does not guarantee that the information provided in these materials is accurate, current or suitable for any particular purpose. Changes in the assumptions or the information underlying these views could produce materially different results. The analyses, opinions, estimates, forecasts and other views published by the ESR group represent the views of that group as of the date indicated and do not necessarily represent the views of Fannie Mae or its management.