Economics: Retail Sales Rebound

This week’s economic news surprised on the upside with improved retail sales and a narrower trade deficit. Headline retail sales in March posted the largest increase since September 2017 driven mainly by gas station and auto dealer sales. Sales volumes at gas stations were particularly strong due to a pickup in average retail gasoline prices, which also jumped the most since September 2017. However, gains were broad-based as core retail sales, which exclude auto, gasoline, and building material sales and are an input for the consumer goods spending component of gross domestic product (GDP), also rebounded from February’s modest decline. Core retail sales exceeded expectations during the first quarter, posing an upside risk to our April forecast of 1.0 percent annualized growth in real consumer spending. The March number also helps build momentum for the second quarter, when we expect a strong pickup in real consumer spending as worries over the government shutdown and equity market volatility fade. In other news, the nominal trade deficit narrowed to its smallest level in eight months in February as a surge in exports outweighed a slight increase in imports. However, the increase in exports was largely driven by a rebound in volatile civilian aircraft exports, which will likely weaken in coming months given Boeing’s issues with its 737 Max. The real goods trade deficit, an input into the net exports portion of GDP, narrowed for the second straight month, suggesting net exports likely added to GDP growth last quarter for the first time in three quarters. Both the retail sales and the trade reports pointed to real GDP growth of more than 2.0 percent annualized in the first quarter versus our forecast of 1.8 percent. The near-term economic outlook seemed positive as the Leading Economic Index (LEI) rose in March by the largest amount since last September, driven by declining initial unemployment claims, rising consumer expectations for business conditions, and gains in financial components. However, its recent trends showed some weakness. In the six-month period ending March 2019, the LEI increased 0.4 percent, much slower than the 2.8 percent growth posted during the previous six months. In addition, the weaknesses and strengths among the LEI have become more balanced over the past six months. Initial unemployment claims fell last week to a near 50-year low, signaling that the labor market continues to be healthy. Industrial production tempered this week’s good news, edging down in March for the second time in three months as a decline in mining output outweighed a slight improvement in utilities output. Manufacturing output was flat following two straight monthly drops. For the first quarter, headline industrial production fell for the first time since the third quarter of 2017. Capacity utilization fell for the fourth consecutive month and manufacturing capacity utilization declined to the lowest level since last May.

- **Retail sales** rose 1.6 percent in March, according to the Census Bureau. Core retail sales grew 1.0 percent. From a year ago, both headline and core retail sales were up 3.6 percent.
- **The U.S. trade deficit** narrowed by $1.8 billion to $49.4 billion in February, according to the Census Bureau. Exports rose by 1.1 percent while imports only rose by 0.2 percent. The real goods trade deficit narrowed by $1.8 billion to $81.8 billion.
- **Industrial production**, a gauge of output in the manufacturing, utility, and mining sectors, dropped 0.1 percent in March, according to the Federal Reserve Board. The manufacturing index was unchanged after declining in the prior two months, mining output fell 0.8 percent, and the utilities index rose 0.2 percent. Capacity utilization fell 0.2 percentage points to 78.8 percent, about one percentage point below its long-run average.
- **The Conference Board Leading Economic Index**, a gauge of the economic outlook over the next three to six months, grew 0.4 percent in March to 111.9 (2016 = 100). Eight of the ten indicators of the LEI rose in March, while weekly manufacturing hours and building permits were unchanged.
- **Initial claims for unemployment insurance** fell by 5,000 to 192,000 in the week ending April 13, according to the Department of Labor. The four-week moving average declined by 6,000 to 201,250.
Housing: Home Construction Appears Weak

Housing data disappointed this week as starts, permits, and mortgage demand all fell. In March, total housing starts fell for the sixth time in seven months, declining to the lowest level in almost two years. While multifamily starts were unchanged, single-family starts have fallen precipitously after spiking in January and were at the lowest level since September 2016. Downward revisions to both single-family and multifamily starts in February subtracted 20,000 units. On a quarterly basis, total home construction edged up for the first time in four quarters, boosted by the largest quarterly gain in single-family building since the end of 2017. Meanwhile, multifamily building declined for the fourth straight quarter. The near-term outlook for home building seems bleak. Multifamily permits fell for the third consecutive month in March and single-family permits, which have been trending downward since last February, declined to the lowest level since August 2017. The decline in home building is concerning for our forecast of a strong spring selling season as, even if demand increases, the dearth of supply could derail sales. Home builders’ confidence in the single-family market stagnated in April, as the National Association of Home Builders/Wells Fargo Housing Market Index edged up only one point after being flat the prior month. The index dropped steeply at the end of 2018 and has only recovered about half the declines in the first four months of 2019. The National Association of Home Builders reported that builders see solid demand but grapple with “affordability concerns stemming from a chronic shortage of construction workers and buildable lots.” Mortgage demand worsened for the second consecutive week last week, as a massive drop in refinance applications outweighed a modest improvement in purchase applications. While refinance mortgage applications spiked at the end of March when mortgage rates hit the recent low of 4.06 percent, they have since fallen off as mortgage rates are back on the rise. This week, the 30-year fixed mortgage rate rose five basis points to 4.17 percent, according to Freddie Mac. Purchase mortgage applications, on the other hand, have been making a steady comeback after hitting a two-year low in December, and last week they rose to the highest level since April 2010.

- **Housing starts** edged down 0.3 percent in March to 1.14 million annualized units, according to the Census Bureau. Single-family starts fell 0.4 percent to 785,000 while multifamily starts were flat at 354,000. Single-family and multifamily permits dropped 1.1 percent and 2.7 percent, respectively. Through the first quarter, single-family starts rose 2.5 percent but permits fell 3.1 percent, and multifamily starts fell 3.5 percent but permits rose 3.0 percent.

- **The National Association of Home Builders/Wells Fargo Housing Market Index** edged up 1 point to 63 in April. A reading above 50 indicates that more builders view the single-family market as “good” rather than “poor.” The present sales component was also up a point to 69, while the sales in the next six months component fell 1 point to 71. The traffic of prospective buyers component rose the most, increasing 3 points to 47.

- **Mortgage applications** declined 3.5 percent for the week ending April 12, according to the Mortgage Bankers Association. While purchase applications edged up 0.9 percent, refinance applications dropped 8.2 percent. Both conventional and government refinance applications fell, declining 8.1 percent and 8.7 percent, respectively. The survey’s average 30-year fixed mortgage rate increased four basis points to 4.44 percent.

Ricky Goyette and Rebecca Meeker
Economic and Strategic Research Group
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