Economics: Economic Growth Remains Solid Amid Fixed Investment Weakness

This week’s news featured the first glance at third quarter real gross domestic product (GDP), which grew at a solid rate of 3.5 percent. Personal consumption expenditures (PCE) were strong, contributing 2.7 percentage points to GDP growth, its largest contribution since the fourth quarter of 2014 as the tax cuts passed at the end of last year continue to provide support to households. Although consumer sentiment dipped in October, it has been higher thus far in 2018 than in any prior year since 2000. Government spending contributed slightly more to GDP growth in the third quarter as state and local government spending and investment growth accelerated. Meanwhile, inventory build-up added a robust 2.1 percentage points to overall growth, reversing the drawdown that subtracted 1.2 percentage points from growth over the second quarter. However, the swing from a negative to a positive contribution was largely offset by a reverse move in net exports, which subtracted 1.8 percentage points from GDP growth in the third quarter after adding 1.2 percentage points in the second, as the surge in exports ahead of the tariffs in the second quarter turned into a sharp pullback in the third quarter and the U.S. dollar continued to strengthen. Fixed investment fell for the first time since the fourth quarter of 2015. Residential investment declined and has now fallen in each of the first three quarters of 2018. At the same time, a decrease in structures spending and a deceleration in the growth of intellectual property products and equipment spending contributed to a slowdown in nonresidential investment. The durable goods orders report showed that core capital goods orders, a forward-looking indicator, fell for the second consecutive month. Meanwhile, the PCE deflator slowed over the quarter to a 1.6 percent annual rate after growing at or above 2.0 percent for three consecutive quarters. Excluding food and energy prices, core PCE inflation also slowed to 1.6 percent. However, over the past year the PCE deflator rose by 2.2 percent and the core PCE deflator rose to 2.0 percent. Amid manageable inflation, additional information reaffirming a strong labor market, initial claims for unemployment insurance remain near their cycle low, despite an uptick over the past week that likely reflected the impact of Hurricane Michael.

- **Gross domestic product**, adjusted for inflation, rose by 3.5 percent annualized in Q3 2018, decelerating from an increase of 4.2 percent in the prior quarter, according to the advance estimate from the Bureau of Economic Analysis. Real consumption spending rose by 4.0 percent and government spending rose by 3.3 percent. Fixed investment fell by 0.3 percent, nonresidential fixed investment grew by 0.8 percent while residential fixed investment fell by 4.0 percent.

- **Durable goods orders** rose 0.8 percent in September, according to the Census Bureau. Orders for defense aircraft and parts soared 119.1 percent, while nondefense orders excluding aircraft fell 0.1 percent. Shipments of nondefense capital goods excluding aircraft were flat in September.

- **The University of Michigan Consumer Sentiment Index** fell 1.5 points to 98.6 in the October final reading as the current conditions component fell 2.1 points to 113.1 and the expectations component declined 1.2 points to 89.3.

- **Initial claims for unemployment insurance** increased by 5,000 to 215,000 in the week ending October 20, according to the Department of Labor. The four-week moving average was unchanged at 211,750.
Housing: Fewer Sales and More Homes For Sale Push Up Months’ Supply of New Homes

This week’s slate of releases provided an update on conditions in the for-sale market. According to Freddie Mac, mortgage rates remain elevated relative to their level at the beginning of the year. The 30-year, fixed-rate averaged 4.83 percent in October, compared with 4.03 percent in January of this year. However, rates have stabilized in recent weeks. Pending home sales, a measure of contract signings for existing homes, rose modestly in September, partially reversing two consecutive monthly declines. In the face of higher mortgage rates over the year, pending home sales have remained relatively steady near their level from one year ago. In contrast, sales of new homes, which represent signed contracts for the purchase of new homes, declined for the fourth consecutive month and are now only 3.6 percent higher year to date than the same period a year ago, versus August’s 6.2 percent. Amid fewer new home sales, the number of new homes for sale continued to rise, reaching 327,000 in September, a level last seen in early 2009. Consequently, the months’ supply, which measures the number of months it would take to exhaust the inventory of homes at the current sales pace, rose to 7.1 months, a level last exceeded in early 2011. Readings above 6.0 months typically indicate a lack of inventory shortage. Meanwhile, the Federal Housing Finance Agency (FHFA) reported that year-over-year house price appreciation slowed for the second consecutive month, but at 6.1 percent growth has exceeded 6.0 percent for 19 consecutive months. After declining for two consecutive weeks, mortgage demand rebounded as both purchase and refinance applications rose moderately last week.

- **New single-family home sales** fell by 5.5 percent to a 553,000 seasonally-adjusted annual rate (SAAR) in September, according to the Census Bureau. Sales over the past three months were revised lower by 49,000 units. The number of homes for sale rose 2.8 percent to 327,000. Months’ supply increased to 7.1 in September, the fourth consecutive month at or above 6.0 months.

- **The National Association of REALTORS® Pending Home Sales Index**, which records contract signings of existing homes and typically leads closings by one to two months, rose by 0.5 percent to 104.6 in September. In August the Index fell by 1.9 percent following a 0.8 percent decline in July.

- The FHFA Purchase-Only House Price Index, reported on a seasonally-adjusted basis, rose by 0.3 percent in August. From a year ago, the index rose by 6.1 percent. Year-over-year ending in July, the Index rose by 6.6 percent following a 6.8 percent over the 12 months ending in June.

- **Mortgage applications** rose 4.9 percent for the week ending October 19, according to the Mortgage Bankers Association. Mortgage applications for refinance climbed 9.7 percent, while mortgage applications for purchase rose by 2.0 percent. Conventional mortgage applications for purchase increased 2.9 percent, while government mortgage applications for purchase fell 0.7 percent.

![Amid Rising Rates, Pending Home Sales Hold Steady But New Home Sales Fall](image)

![Months’ Supply Rises As Sales Fall and Inventory Climbs](image)

Source: Census Bureau, NAR, Freddie Mac

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