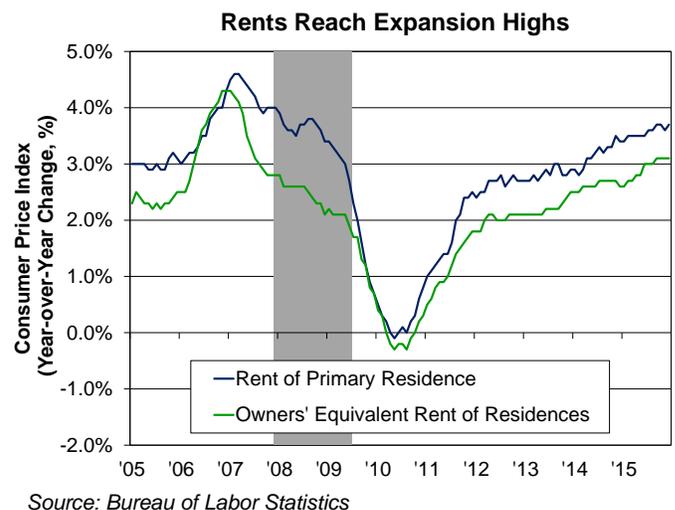
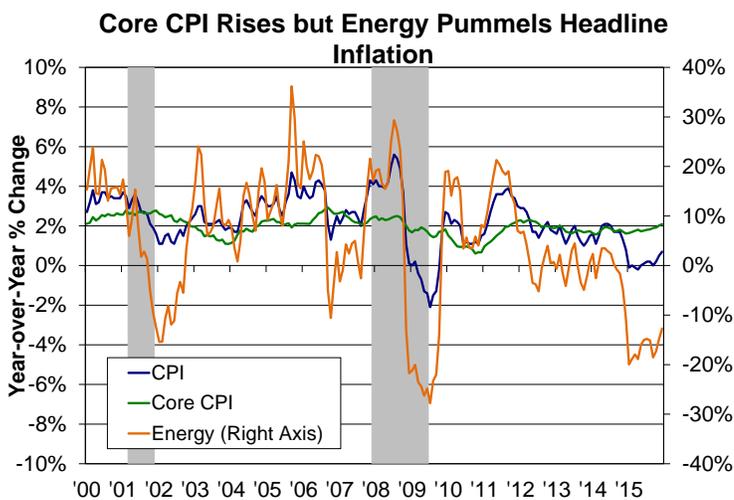


Economics: Not Quite Deflategate, But Inflation Is Still Missing in Action

Economic indicators released this week pointed to continued low inflation amidst mounting international economic and financial concerns. The appreciation of the dollar and the crash in energy prices dragged down inflation in 2015, as annual growth in the headline Consumer Price Index (CPI) was stuck below 1.0 percent all year and ended 2015 with the second smallest December-December increase in the last 50 years. Energy prices have fallen on a year-over-year basis every month for the past 16 months. The fuel oil index alone fell nearly one-third in 2015. The core CPI, a less volatile measure of inflation that excludes food and energy prices, remains a bright spot in the inflation picture, posting its largest year-over-year increase since July 2012. The increase was driven by core services, which tied an eight-year best annual growth rate for the second straight month in December. Conversely, core goods prices have been falling since early 2013. Growth in shelter costs remains elevated, tying an expansion best year-over-year change for a fourth consecutive month. Adding to the downbeat news this week, China's latest GDP release showed that growth came in at a 25-year low of 6.9 percent in 2015. The oil price rout and China's economic woes were evident in the capital markets, where the Dow Jones dropped over 500 points and the 10-Year treasury dropped below 2.0 percent intra-day on Wednesday in a flight to safety. With few signs of a pick-up in inflation and further evidence of an economic slowdown in China, the Fed faces a challenge in setting a pace for rate hikes for the balance of the year. In other economic market news, initial claims for unemployment insurance continued to edge up, but stayed just below 300,000, the threshold indicative of an improving labor market. The conference Board Leading Economic Index dropped in December for the first time in three months, suggesting near-term moderate economic growth after a lackluster growth during the final quarter of 2015.

- **The Consumer Price Index (CPI)** decreased for the first time in three months in December, dropping 0.1 percent, according to the Bureau of Labor Statistics. Headline CPI edged up just 0.7 percent from December 2014. Core CPI, which excludes food and energy prices, ticked up 0.1 percent for the month and 2.1 percent on the year. Breaking down the core index, core services rose 2.9 percent on an annual basis, while core goods declined 0.4 percent year over year. Shelter costs, which account for more than 40 percent of core CPI, grew 3.2 percent from a year ago. Rents of primary residences and owners' equivalent rents (a proxy for homeowner rents) both rose 0.2 percent in December and increased 3.7 percent and 3.1 percent for the year, respectively.
- **The Conference Board Leading Economic Index (LEI)**, a gauge of the economic outlook over the next three to six months, fell 0.2 percent in December, led by a decline in housing permits and soft manufacturing orders.
- **Initial claims for unemployment insurance** increased by 10,000 to a six-month high of 293,000 in the week ending January 16, according to the Department of Labor. The four-week moving average increased by 6,500 to 285,000, the highest level since April 2015.



Housing: Existing Home Sales Surge Amid Limited New Home Construction

This week's housing data revealed that 2015 was the best year for housing since before the recession hit, with existing home sales and housing starts posting the strongest levels since 2006 and 2007, respectively. Existing home sales ended the year with a bang, registering the largest month-over-month increase ever recorded in December. The spike in sales was mainly due to a correction after the implementation of new disclosure regulations (TILA-RESPA Integrated Disclosure) delayed closings from November to December. The combination of strong sales and another drop in the number of homes available for sale pushed the months' supply down to a tie for the second lowest level ever recorded. While the supply of existing homes struggles to keep pace with demand, potential homebuyers are not getting relief from the new home market either, as home construction fell in December, despite warmer temperatures that allowed building to continue later in the year than usual. There is a risk that building could slow further in the near term as more seasonal weather has arrived. Homebuilders remain confident, as a survey of their view of the market remained elevated in January. Yet, some doubts might be creeping in, as their expectations for the next six months have worsened for three straight months. In addition, the value of homebuilder stocks dropped significantly in the first three weeks of the year. Mortgage applications have recovered almost completely from the post rate hike slump, as mortgage rates fell for third week in a row. The 30-year fixed mortgage rate dropped 11 basis points to 3.81 percent, according to Freddie Mac's survey.

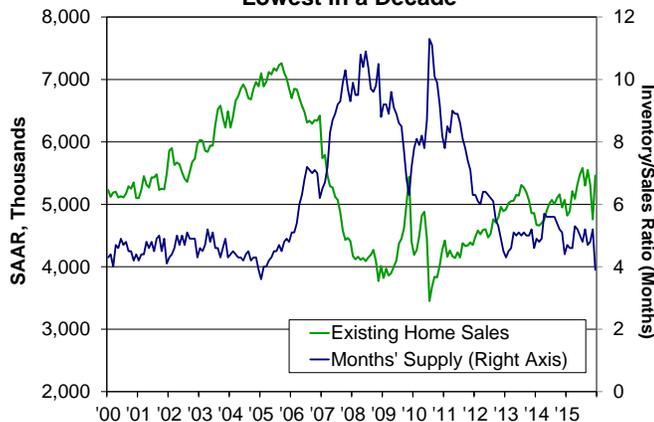
➤ **Housing starts** fell 2.5 percent in December to 1.15 million units annualized, according to the Census Bureau. Single-family starts decreased 3.3 percent to 768,000, while multifamily starts dropped 1.0 percent to 381,000. Total housing starts totaled 1.11 million in 2015, a 10.8 percent increase over 2014 and the highest level since 2007. Single-family housing starts totaled 715,000 in 2015, rising 10.4 percent from the previous year. Multifamily starts posted the best year since 1989 with 396,000 units started, an 11.4 percent improvement from 2014. New residential building permits dropped 3.9 percent in December, as an 11.4 percent decline in multifamily permits outweighed a 1.8 percent rise in single-family permits.

➤ **Existing home sales** spiked 14.7 percent to 5.46 million units annualized in December, according to the National Association of REALTORS®. For all of 2015, sales totaled 5.26 million, up 6.5 percent from 2014. The number of homes available for sale, which is not seasonally adjusted, fell for the fourth consecutive month, dropping 12.3 percent during the month and 3.8 percent from December 2014, to the lowest level since January 2013. As a consequence of a robust sales pace and a steep decline in inventories, the months' supply, or inventory/sales ratio, dropped sharply by 1.2 months to 3.9 months, the lowest level in 11 years. According to the National Association of REALTORS®, the median existing home price, unadjusted for sales composition, increased 7.6 percent from the same period a year ago.

➤ **The National Association of Home Builders/Wells Fargo Housing Market Index** was unchanged in January at 60. A reading above 50 indicates more builders view the single-family market as "good" rather than "poor". Declines in sales expectations and builder assessments of prospective buyer traffic nullified a slight rise in the current sales component.

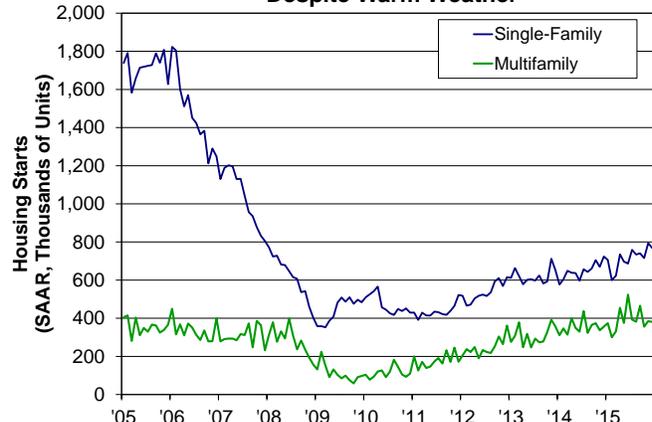
➤ **Mortgage applications** improved for the second consecutive week, rising 9.0 percent in the week ending January 15, according to the Mortgage Bankers Association. Refinancing applications drove the rise, increasing 18.7 percent after a 23.7 percent jump in the prior week, helped by the survey's 30-year fixed-rate mortgage reaching 4.06 percent after declining six basis points in each of the last two weeks. Purchase applications slipped 1.6 percent during the week.

Existing Home Months' Supply Dips to the Lowest in a Decade



Source: National Association of Realtors

Housing Starts Disappoint in December Despite Warm Weather



Source: Census Bureau



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