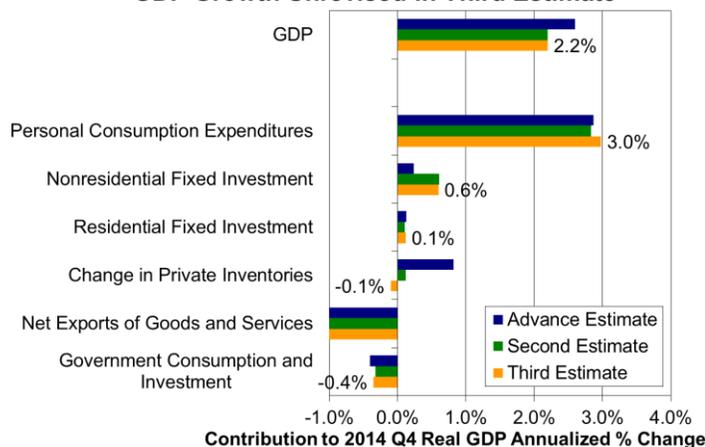


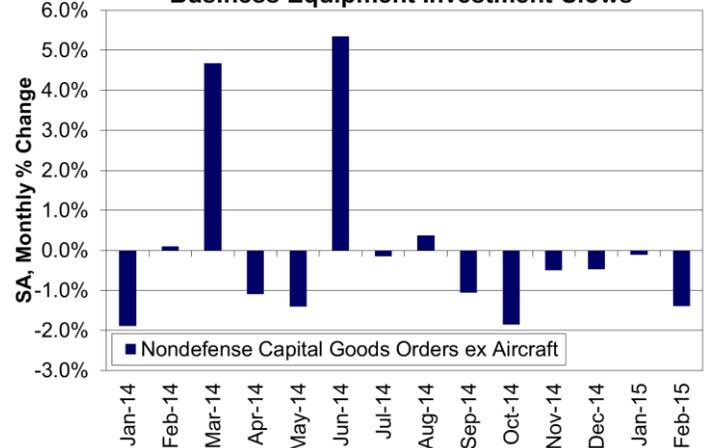
## Economics: Capital Investment Near-Term Outlook Remains Dim

Economic data released this week were mixed. Headline GDP growth in Q4 2014 was unrevised at 2.2 percent annualized, though the slight shift in composition of growth was modestly favorable to the current quarter growth outlook. Consumer spending was revised up to show the fastest quarterly growth since before the Great Recession while inventory accumulation was revised lower. Unfortunately, more timely incoming data on business capital investment posed downside risk to our March forecast of 2.0 percent growth in Q1 2015. Core capital goods orders—a leading indicator of business equipment investment—have plunged 10.3 percent annualized over the six months ending in February, painting a dim picture of business equipment investment beyond the current quarter. Consumer prices moved higher in February as oil prices stabilized during the month and were unchanged from a year ago. Core inflation continued to edge up, but remained modest at 1.7 percent on the year. On the heels of weak auto sales and retail sales data in February, March consumer sentiment continued to move lower from its expansion high in January but remained relatively elevated. We expect the consumer sector to pick up in coming months after a sluggish start to the year, supported by strengthening job and wage gains resulting from diminishing labor market slack—evidenced by continued low jobless claims.

- **Gross domestic product (GDP)**, adjusted for inflation, increased at a 2.2 percent annual rate in Q4 2014, according to the Bureau of Economic Analysis' third estimate, unchanged from the prior estimate but down from the robust 5.0 percent growth in Q3. Consumer spending remained the engine of growth, contributing 3.0 percentage points to GDP, up from 2.8 percentage points in the prior estimate and the best showing since Q1 2006. This upward revision was mostly offset by a downgrade to inventory investment during the quarter, from a modest boost to growth to a modest drag. For all of 2014, GDP grew 2.4 percent, down from 3.1 percent in 2013.
- **The Reuters/University of Michigan Consumer Sentiment Index** dipped 2.4 points from February in the final March reading to a four-month low of 93, but was up from the preliminary March figure of 91.2. Both the current conditions and consumer expectations components deteriorated.
- **The Consumer Price Index (CPI)** increased 0.2 percent in February after three consecutive monthly declines, according to the Bureau of Labor Statistics. Prices were flat from a year ago, up from the 0.1 percent annual decline reported in January. The core CPI, which excludes the volatile food and energy components, edged up 0.2 percent in February for a second consecutive month, and 1.7 percent from a year ago.
- **Durable goods orders** declined 1.4 percent in February, according to the Census Bureau. A 0.5 percent decline in motor vehicle and parts orders (the second consecutive drop), a pullback in aircraft orders (notably a 33.1 percent plunge in defense aircraft orders to the lowest level in nearly a decade), and a 1.8 percent decline in machinery orders (the fifth decline in six months) all weighed on the headline. Core capital goods shipments, which exclude defense and aircraft items and are an input to estimate business equipment investment in GDP, rose just 0.2 percent after a 0.4 percent drop in the prior month, suggesting modest growth in business equipment investment in the current quarter. Core capital goods orders sank for a sixth consecutive month, dropping 1.4 percent in February and rising just 2.1 percent over the past 12 months.
- **Initial claims for unemployment insurance** fell 9,000 to 282,000 in the week ending March 21, according to the Bureau of Labor Statistics. The four-week moving average declined to below 300,000 for the first time in four weeks.

**GDP Growth Unrevised in Third Estimate**


Source: Bureau of Economic Analysis

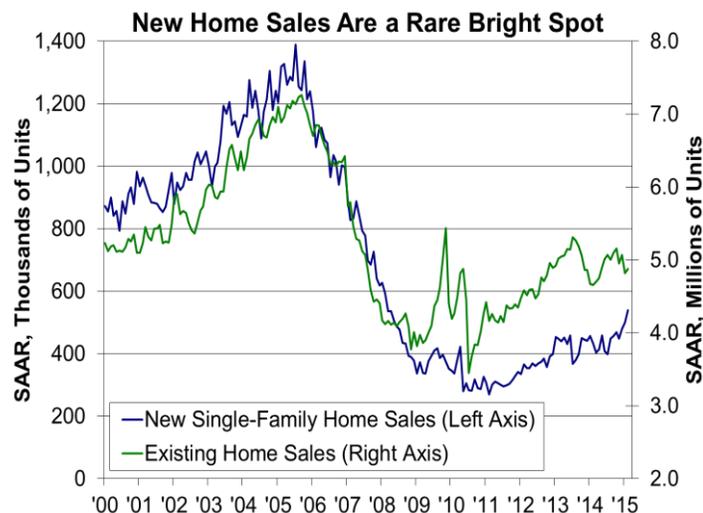
**Business Equipment Investment Slows**


Source: Census Bureau

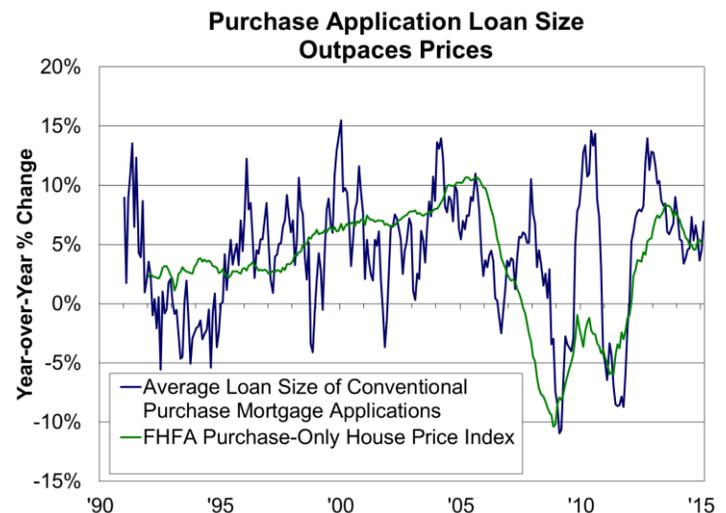
## Housing: A Ray of Sunshine through the Clouds

Home sales picked up in February, calming fears that the sharp contraction in February building activity and continued eroding of builder sentiment in March (notably flagging buyer traffic) reported last week were a precursor to a winter sales slump. New home sales reached a seven-year high last month, bringing the months' supply down to a 20-month low. If those gains stick through typically large revisions, we can expect builders to respond in the spring—in line with our forecast for strengthening single-family homebuilding this year. Existing home sales, which make up the vast majority of home sales, moved modestly higher, but remain well below activity witnessed in the second half of 2014. Details by sales price highlighted weakness in sales in lower-priced segments. Homes sold for less than \$250,000, which accounted for 62 percent of total resales in February, were up less than 3.0 percent from a year ago, in stark contrast to double-digit year-over-year sales gains in higher-priced segments. Tight inventory in the lower end of the market has likely contributed to sluggish sales, and continued tight inventory could suppress first-time homebuyer activity, which is crucial to a healthy housing market in the face of reduced investor activity. A survey from the National Association of REALTORS® showed that first-time buyers accounted for 29 percent of sales in February, little changed from a year ago. Meanwhile, mortgage demand improved amid declining mortgage rates, and the Freddie Mac contract interest rate for 30-year fixed-rate mortgages dropped an additional 9 basis points this week to a six-week low 3.69 percent. These rates are expected to continue to support elevated, albeit moderating, refinance activity in the near term and benefit potential buyers as the spring selling season gets under way. Consistent with the trend of improving sales at the upper end of the market, the average loan balance for conventional purchase applications surpassed \$330,000 in late February, holding thereabouts through mid-March while its annual gain is outpacing the 5.1 percent annual appreciation reported by the FHFA purchase-only home price index.

- **New single-family home sales** jumped 7.8 percent in February to 539,000 annualized units, according to the Census Bureau. Year-to-date sales through February were up 19.1 percent from the same period in 2014. The number of homes available for sale (reported on a seasonally adjusted basis) edged down 1.4 percent, pushing the months' supply, or inventory/sales ratio, down four-tenths to 4.7. The median sales price was up 2.6 percent from last February.
- **Existing home sales** increased 1.2 percent in February to 4.88 million annualized units, according to the National Association of REALTORS®. Through February, year-to-date sales are up 2.1 percent from a year ago. The number of homes available for sale, which is not seasonally adjusted, edged up 1.6 percent to 1.89 million units in February, but was down 0.5 percent from February 2014. The months' supply was unchanged at 4.6, down from 4.9 in February 2014. From a year ago, the median sales price for existing homes, which is not adjusted for the composition of sales, increased 7.5 percent in February. The cash sales share and the distressed sales share (which includes REO and short sales) were both little changed on the month, but down from a year ago.
- **The FHFA purchase-only house price index**, reported by FHFA on a seasonally adjusted basis, increased 0.3 percent in January from December 2014. Over the past 12 months, prices are up 5.1 percent, down from the 5.4 percent year-over-year appreciation reported for December. All nine Census Divisions registered annual appreciation in January.
- **Mortgage applications** increased for the first time in three weeks, rising 9.5 percent in the week ending March 20, according to the Mortgage Bankers Association. Both purchase and refinance applications rose during the week, increasing 4.9 percent and 12.3 percent, respectively. The contract interest rate for 30-year fixed-rate mortgages reported in the survey declined 9 basis points to a six-week low of 3.90 percent.



Source: Census Bureau, National Association of REALTORS®



Source: Mortgage Bankers Association, Federal Housing Finance Agency



---

Brian Hughes-Cromwick  
Economic and Strategic Research Group  
March 27, 2015

*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.*

