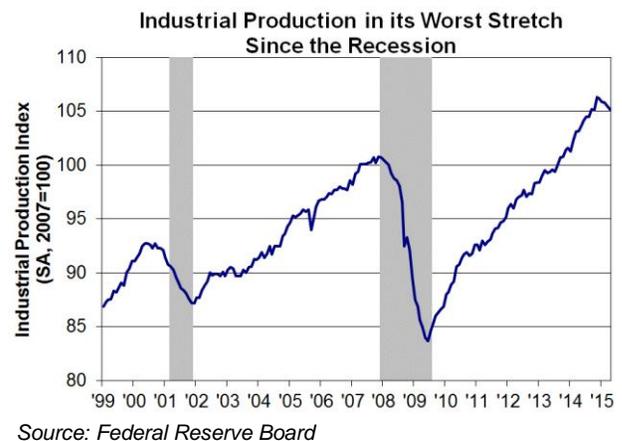
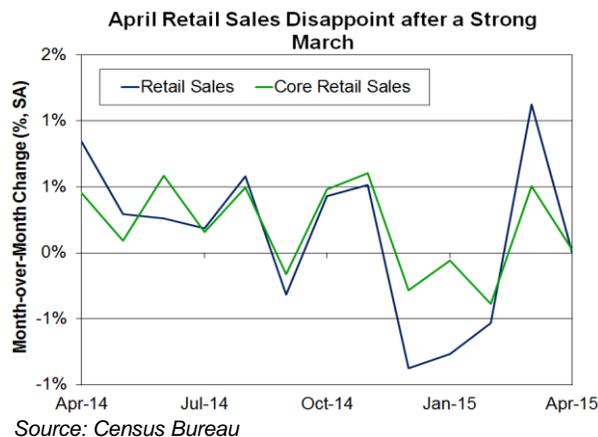


Economics: It's Spring, People – Cheer Up and Spend

Hard data to support the hopes for a spring bounce-back for the economy did not materialize in this week's economic reports. Industrial production is in the midst of its worst run since the recession, falling in April for the fifth straight month, with manufacturing production failing to improve amid declines in mining and utility output. After a strong showing in March, consumers appeared hesitant to open their wallets in April, as both overall retail sales and core sales—a direct input used to calculate consumer spending in the GDP account—were flat. Consumer sentiment also disappointed, falling sharply in May to a seven-month low as consumers fret about current and future economic conditions. Despite some setbacks on the consumer front so far in the current quarter, we believe that real consumer spending is poised to pick up sizably from the 1.9 percent annualized pace in the first quarter. Labor market conditions remain positive, with healthy levels of job openings and confidence in the job market reflected in the elevated quits rate. A survey of small businesses showed that overall confidence improved in April, with a rising share of firms reporting difficulty in filling open positions. High-frequency data point to improving conditions in May, with the trend in initial jobless claims sinking to a fresh 15-year low.

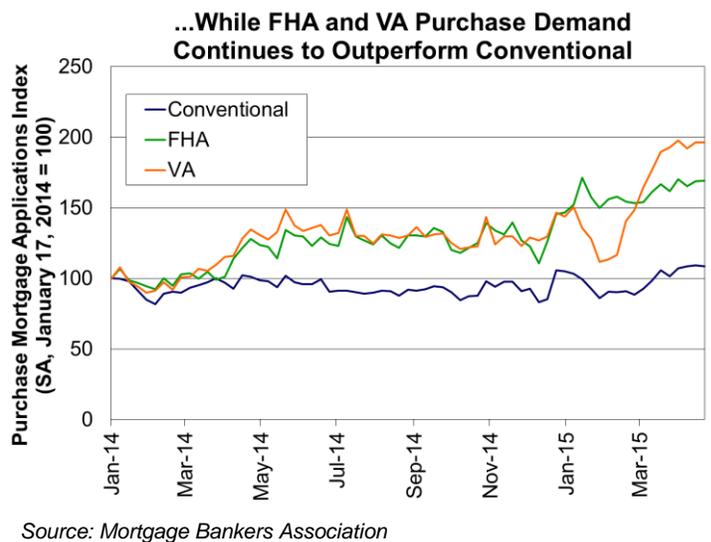
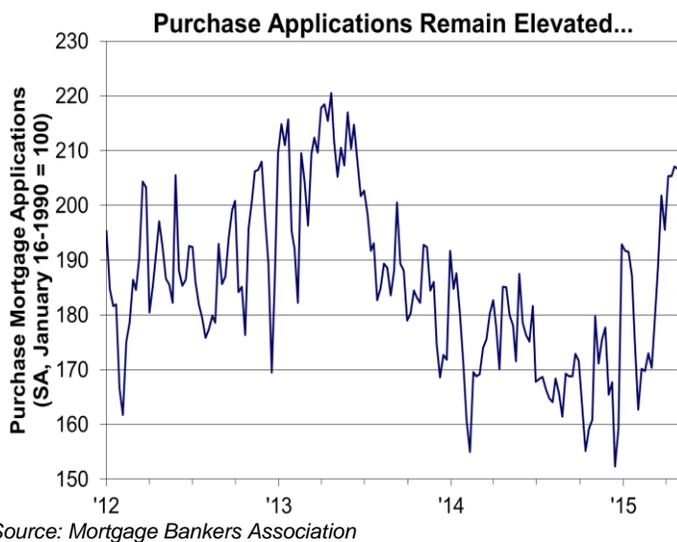
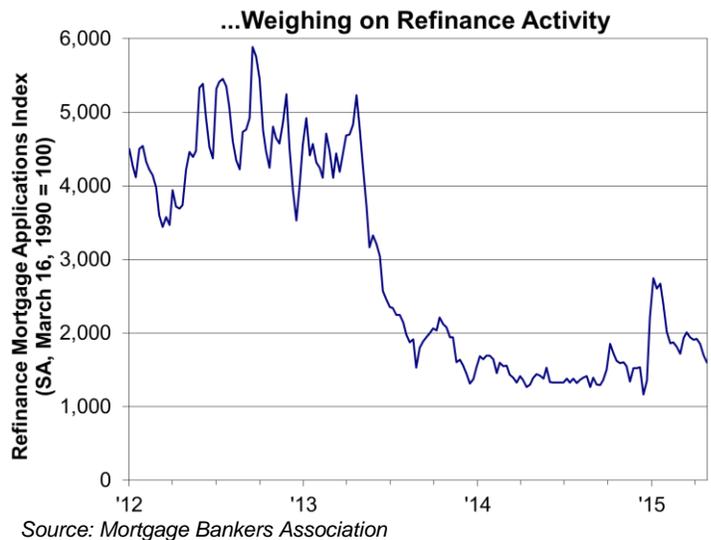
- **Retail sales** were flat in April following a 1.1 percent pop in March, according to the Census Bureau, as gains in nonstore retailers (i.e., internet sales, restaurant and bar sales) offset broad-based declines elsewhere. After recovering the past two months, gasoline station sales resumed their declining trend, falling 0.7 percent. Core sales (excluding food services, auto, building supplies, and gasoline station sales) were flat following an upward revision in the prior month.
- **Industrial production**, a gauge of output in manufacturing, utility, and mining sectors, dropped 0.3 percent in April according to the Federal Reserve Board. Manufacturing output was unchanged, as a rebound in motor vehicle production offset declines in consumer goods and business equipment production. Utility output fell 1.3 percent, while mining output declined for the fourth consecutive month, falling 0.8 percent, driven by another double-digit drop in oil and gas drilling.
- **The Reuters/University of Michigan Consumer Sentiment Index** tumbled 7.3 points to 88.6 in early May, the largest drop in two years. Both the present conditions and expectations components fell sharply.
- **The National Federation of Independent Business (NFIB) Small Business Optimism Index** rose 1.7 points to 96.9 in April, with eight of the 10 subcomponents of the index improving. In particular, the share of firms reporting higher earnings posted the biggest improvement in three years.
- **The Job Opening and Labor Turnover Survey (JOLTS)** from the Bureau of Labor Statistics showed that the March job openings rate ticked down 0.1 percentage point to 3.4 percent. The hiring rate remained unchanged at 3.6 percent, while the quits rate, an indicator of labor market confidence, rose to 2.0 percent—its expansion high.
- **Import prices** remained weak, decreasing 0.3 percent in April, according to the Bureau of Labor Statistics. Petroleum prices rose 1.0 percent. Non-petroleum prices, on the other hand, have not increased in over a year, and fell 0.4 percent. **The Producer Price Index (PPI)** for final demand fell 0.4 percent in April and 1.3 percent from a year ago, according to the Bureau of Labor Statistics. Core prices (excluding food and energy items) fell 0.1 percent from March, but rose 0.3 percent from a year ago.
- **Initial claims for unemployment insurance** decreased by 1,000 to 264,000 in the week ending May 9, according to the Department of Labor. The four-week moving average decreased for the third consecutive week, falling 7,750 to 271,750.



Housing: Refinance Demand Slips as Rates Rise, Purchase Demand Elevated

A quiet week of housing data shined light on falling consumer demand for refinances as mortgage rates approached their high for 2015. Mortgage applications for refinance fell for the fifth time in six weeks to the lowest level this year. Increasing mortgage rates appear to be choking off the refi resurgence of 2015; the 30-year fixed mortgage rate increased five basis points this week to 3.85 percent, the highest since mid-March, according to Freddie Mac. Meanwhile, though demand for purchase mortgage applications edged down last week for the first time in four weeks, activity remains near the highest level since June 2013, prior to the spike in mortgage rates associated with the “Taper Tantrum,” which weighed on housing demand. Continued strength in the FHA and VA segments has helped boost purchase activity, supporting our outlook for an improved spring/summer selling season this year compared to a disappointing 2014. The government sector has shown stellar performance over the past year—while the conventional purchase index remains only modestly higher than its level at the beginning of 2014, the VA purchase index has nearly doubled over that same span. However, potential interest rate volatility associated with the anticipation of monetary policy normalization remains a key downside risk to this rosy spring resurgence in home purchase activity.

➤ **Mortgage Applications** declined for a third consecutive week, falling 3.5 percent in the week ending May 8, according to the Mortgage Bankers Association. A 5.9 percent drop in refinance applications—the third consecutive decline—drove the headline decline. Purchase applications edged down just 0.2 percent from the highest level since June 2013. According to the survey, the 30-year fixed mortgage rate increased seven basis points to 4.0 percent, just one basis point below the high for the year reached in early March.





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