

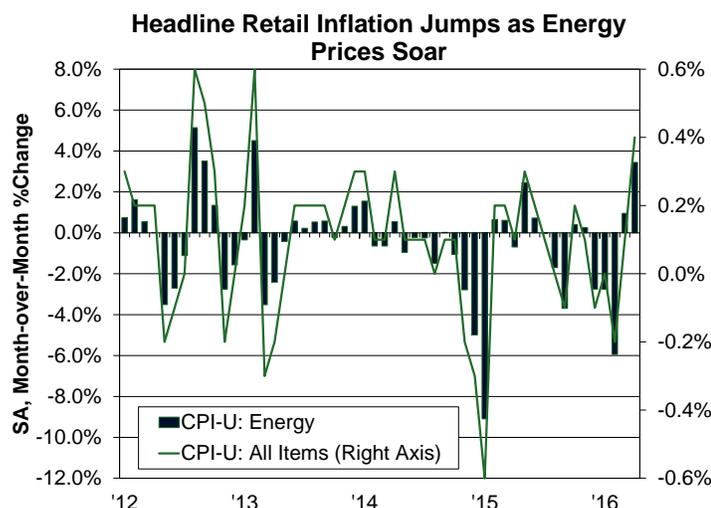


Weekly Note – May 20, 2016

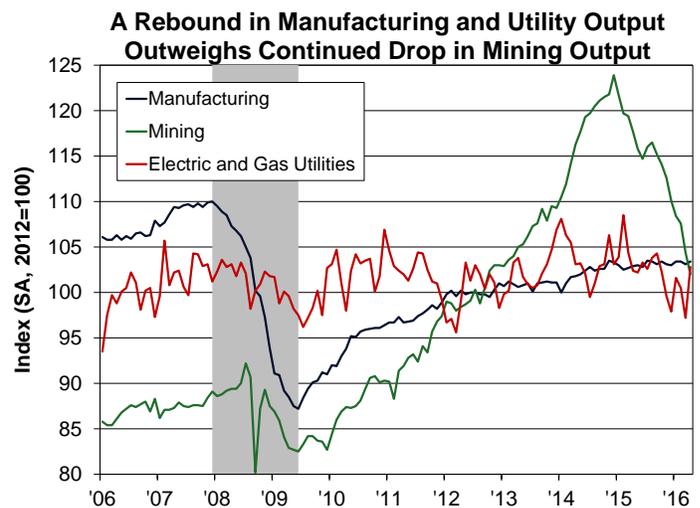
Economics: Odds for a June Rate Hike Have Risen

This week's economic reports were largely positive. Thanks to a rebound in manufacturing and utility output, industrial production rose in April for the first time in three months, even as mining output posted the largest back-to-back drops since 2008. The Conference Board's Leading Economic Index advanced in April, suggesting growth will pick up after an anemic first quarter. Headline retail inflation increased the most since February 2013, driven by the biggest gain in gasoline prices in more than three years. The market mover of the week was the minutes of the April Federal Open Market Committee (FOMC) meeting on Wednesday. The minutes indicated that "most participants" thought a rate increase in June would be appropriate if incoming economic data are "consistent with economic growth picking up in the second quarter, labor market conditions continuing to strengthen, and inflation making progress toward the Committee's 2 percent objective." The minutes increased the fed funds futures odds of a June hike from just 4 percent on Monday to 32 percent, and led to an increase in Treasury yields. The 10-year and 2-year Treasury yields each rose about 10 basis points to 1.87 percent and 0.89 percent, respectively. However, we maintain our call that the Fed will stand pat in June. We believe that uncertainty surrounding the vote on the U.K. referendum to leave the European Union, which is scheduled to occur only about a week after the June FOMC meeting — a concern also raised in the minutes — will keep the Fed from raising rates in June.

- **The Consumer Price Index (CPI)** rose 0.4 percent in April, according to the Bureau of Labor Statistics. Since reaching bottom in February, energy prices have steadily climbed, surging 3.4 percent in April, the largest gain since February 2013, as retail gasoline prices jumped 8.1 percent, the strongest increase since August 2012. Excluding food and energy, core CPI was up 0.2 percent, due entirely to solid gains in services as core goods prices fell for the second consecutive month. From a year ago, the CPI and core CPI rose 1.1 percent and 2.1 percent, respectively.
- **Industrial production**, a gauge of output in the manufacturing, utility, and mining sectors, rose 0.7 percent in April, according to the Federal Reserve Board. As demand for both electricity and gas returned to more normal levels, utility output bounced by 5.8 percent, outweighing a 2.3 percent decline in mining output, the eighth consecutive monthly drop. Manufacturing production, which accounts for about three-fourths of total industrial production, rose 0.3 percent following a 0.3 percent drop in March.
- **The Conference Board's Leading Economic Index (LEI)**, a gauge of the economic outlook over the next three to six months, increased 0.6 percent in April. The gain was broad-based, with 9 out of 10 components making positive contributions. Consumer expectations for business and economic conditions was the only negative component.
- **Initial claims for unemployment insurance** fell 16,000 to 278,000 in the week ending May 14, according to the Department of Labor. The four-week moving average increased 7,500 to 275,750, the highest level since early February. The prior week's jump in New York state claims was reversed. The press release attributed the prior week's surge to layoffs in transportation and warehousing, educational service, and accommodation and food service industries.



Source: Bureau of Labor Statistics



Source: Federal Reserve Board

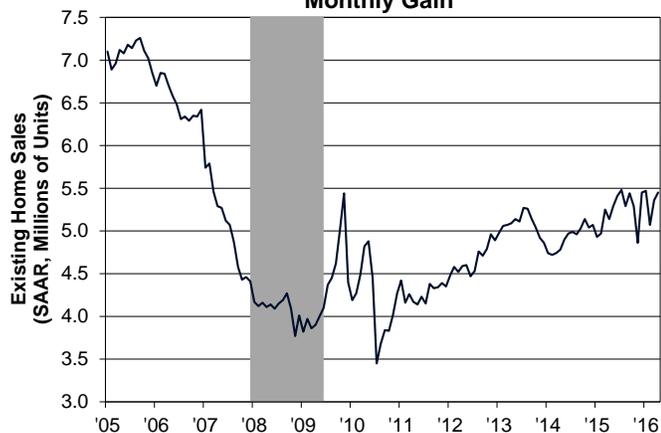


Housing: Heading into Spring, Housing Finds Some Mojo

Data released this week showed signs of the housing market building momentum entering the spring and summer selling season. After recent volatility, existing home sales posted a second consecutive monthly gain in April to reach a level just 0.5 percent below the expansion best reached last July. Year-to-date sales also improved from a year ago. However, the low inventory of existing homes remained the nagging concern for the market. The number of homes for sale fell year over year for the eleventh consecutive month, dampening the prospects of a breakout in sales this summer. While existing homes struggle to be a source of much-needed supply, there was good news from the new homes market. Both single-family and multifamily starts rose in April, suggesting home construction might have a spring in its step. In addition, permits for both sectors increased during the month. While single-family permits have trended sideways, they remain at a level near the expansion best. Multifamily permits ended their recent free fall, giving hope to a sector that had shown signs of teetering. Homebuilders still have a wait-and-see attitude, as a survey of their confidence was unchanged in May for the fourth consecutive month, though sales expectations over the next six months rose for the second straight month to reach the highest level this year. Demand for mortgages faltered again last week as purchase applications fell sharply to the lowest level since mid-February. The average 30-year fixed mortgage rate edged up one basis point from the nearly three-year low rate in the prior week to 3.58 percent, according to the survey by Freddie Mac.

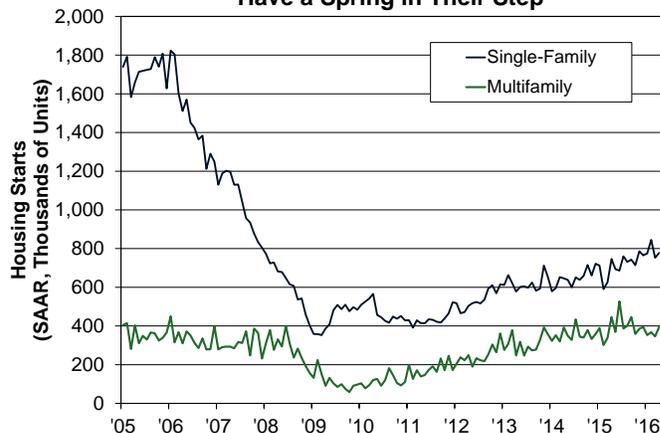
- **Housing starts** rose 6.6 percent in April to 1.17 million annualized units, according to the Census Bureau. Single-family building increased 3.3 percent to 778,000 units, while multifamily starts jumped 13.9 percent to 394,000 units, the highest level this year. Through the first four months of the year, single-family starts are 16.7 percent higher than the same period a year ago, while multifamily starts are 1.8 percent lower. New residential permits increased 3.6 percent to 1.12 million annualized units in April, ending four months of decline. Both single-family and multifamily permits improved, by 1.5 percent and 8.0 percent, respectively.
- **Existing home sales** increased 1.7 percent in April to 5.45 million annualized units, according to the National Association of REALTORS®. On a year-to-date basis, sales are up 5.5 percent from a year ago. The number of homes for sale (not seasonally adjusted) fell 3.6 percent from April 2015. The months' supply (inventory-to-sales ratio) rose to 4.7 months, compared with 5.2 months last April. The median sales price, which is not adjusted for the composition of sales, rose 6.3 percent from a year ago.
- **The National Association of Home Builders/Wells Fargo Housing Market Index** remained unchanged at 58 in May. A reading above 50 indicates more builders view the single-family market as "good" rather than "poor." The present sales and traffic of prospective buyers components were unchanged from April, while the future sales component rose for the second straight month.
- **Mortgage applications** declined for the third time in the past four weeks, falling 1.6 percent for the week ending May 13, according to the Mortgage Bankers Association. Purchase applications drove the decline, dropping 5.8 percent to mark the fourth fall in the past five weeks. Refinance applications, on the other hand, posted the second consecutive week of modest gains, rising 1.4 percent. The average 30-year fixed mortgage rate was flat at 3.82 percent.

Volatile Existing Home Sales Post a Second Monthly Gain



Source: National Association of REALTORS®

Single-family and Multifamily Housing Starts Have a Spring in Their Step



Source: Census Bureau

Frank Shaw and Orawin T. Velz
Economic and Strategic Research Group
May 20, 2016



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.