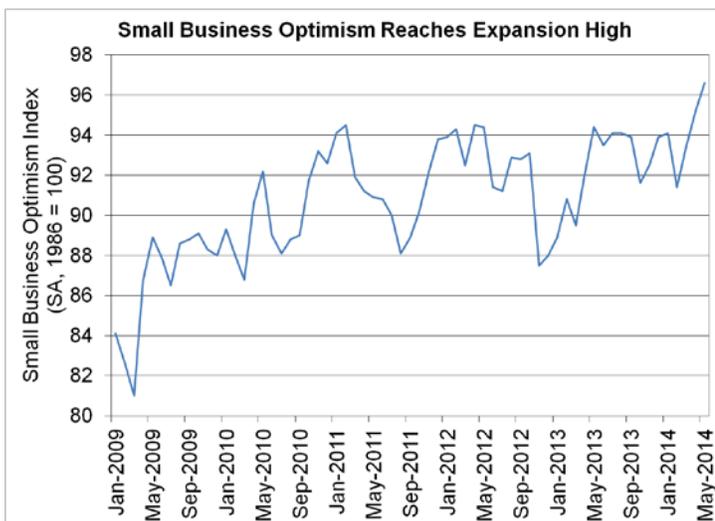


## Economics: Preparing for a Rebound

As economic activity has improved following a setback in Q1 2014, small businesses are becoming more optimistic heading into summer. The small business optimism index reached an expansion high in May amid expectations of an improving economy and increasing sales. The JOLT survey also showed that job openings rose in April to a new high in the expansion. Two reports on prices showed that inflationary pressure remained subdued in May. On a less upbeat note, May's retail sales were disappointing, and core sales—an important input to estimate GDP—present some downside risk to our forecast for real consumer spending growth of 3.3 percent annualized in the current quarter. Contrasted with business confidence, consumer sentiment edged down in June for a second consecutive month.

- **The Job Openings and Labor Turnover (JOLT) Survey** showed that the number of job openings increased from 4.2 million to 4.5 million in April, 16.5 percent above April 2013's level. Hiring and separations (including quits and layoffs) were essentially flat. However, quits as a share of total separations are steadily climbing, a signal of improving labor market conditions as workers are growing confident enough to leave their jobs to find employment elsewhere.
- **The NFIB Small Business Optimism Index** rose for the third consecutive month to 96.6 in May. Components of the index were positive as firms reported that they expect to see higher sales and increased employment. Although expectations for credit availability slid in May, the net share of firms who expect credit conditions to worsen remained near its post-recession low.
- **Retail sales** rose a modest 0.3 percent in May, driven by increases in auto and building material sales. Although May retail sales were below expectation, we believe there remains little immediate cause for concern as sales were up 4.3 percent year-over-year and April's modest growth rate of 0.1 percent was revised to 0.5 percent. However, core sales (excluding auto, gasoline, and building material sales) were flat and revisions to April and March were largely offsetting.
- **Business inventories** rose 0.6 percent in April. The gain was broad-based as manufacturing, retail, and wholesale inventories rose 0.4 percent, 0.5 percent, and 1.1 percent, respectively. The inventory-to-sales ratio was flat at 1.29.
- **The Reuters/University of Michigan Consumer Sentiment Index** fell slightly to a preliminary reading of 81.2 in June, led lower by a decrease in consumer expectations from 73.7 to 72.2. Offsetting some of the slide was the current expectations portion of the survey, which increased nearly one point to 95.4 after a 4.2 point drop in the prior month.
- **The producer price index (PPI)** decreased 0.2 percent in May after rising sharply in March and April. Prices were down for both goods and services while core goods prices, which exclude food and energy items, were unchanged. Year-over-year inflationary pressure remained moderate, with the PPI increasing 2.0 percent from May 2013.
- **Import prices** edged up 0.1 percent in May following a 0.5 percent drop in the prior month.



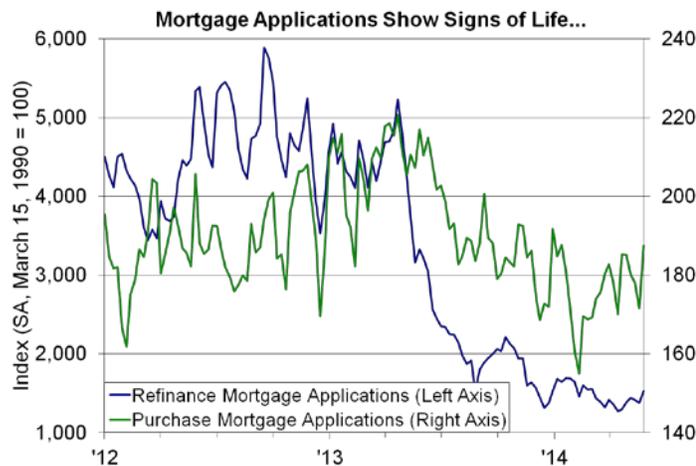
Source: National Federation of Independent Business



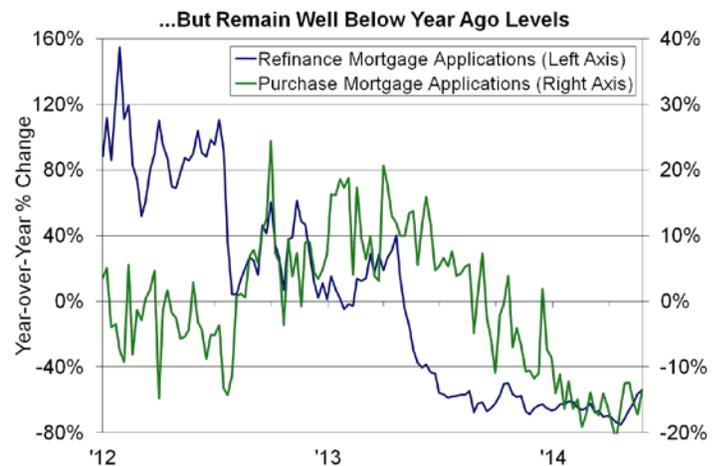
Source: Census Bureau

## Housing: Mortgage Demand Picks Up, Construction Hiring Data Mixed

Though no major housing data were in the pipeline this week, a few minor reports provide a window into current mortgage demand and the outlook for construction employment. Overall, this week's reports are broadly consistent with our expectation for a steady but unspectacular rebound in housing activity this spring and summer selling season following the nearly year-long pause in activity induced by a spike in mortgage rates in May 2013. We estimate total one-to-four family mortgage production in Q1 2014 at an anemic \$237 billion—the lowest since Q1 2000. However, data on mortgage demand show a modest (albeit choppy) upward trend in purchase applications to a four month high in the first week of June from a near two decade low reached in mid-February. Meanwhile, refinance applications have moved off of the recovery low hit at the end of April, but they remain a whopping 70% below the May 2013 peak. These data, while tepid, support our outlook for a moderate improvement in mortgage production in the current quarter.

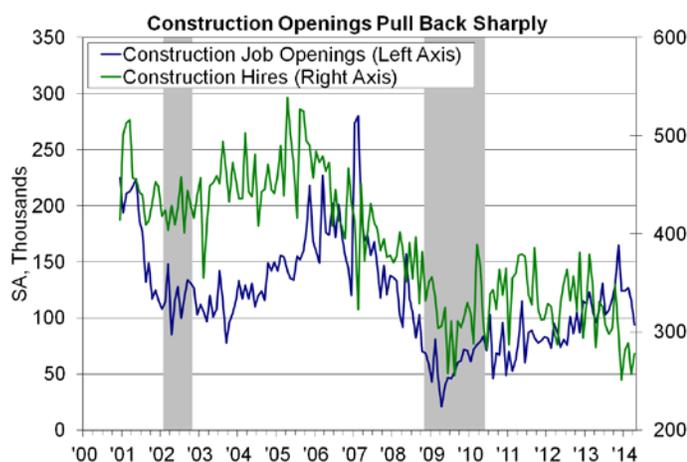


Source: Mortgage Bankers Association

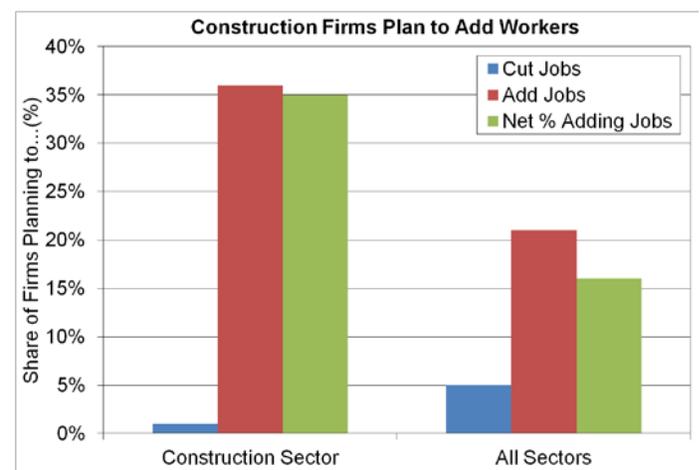


Source: Mortgage Bankers Association

Two data points on the construction employment sector were somewhat conflicting. Following a rough patch of homebuilding activity in Q1 2014, construction job openings from the JOLT Survey fell sharply again in April to below 100,000 jobs for the first time in a year, while hires bounced around near recovery lows. However, hiring may pick up later this year, signaled by the National Federation of Independent Business (NFIB) May survey showing that the construction sector had a larger share of firms reporting plans to hire than any other small business industries tracked in the survey. This is consistent with our expectation that the sluggish recovery in new home construction is due in part to limited supply of skilled labor after many of the construction workers who were laid off during the crisis (more than 2 million) sought work elsewhere or exited the labor force.

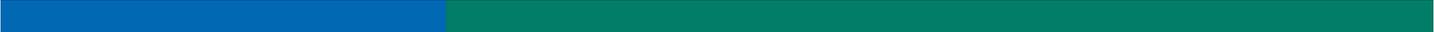


Source: Bureau of Labor Statistics



Source: National Federation of Independent Business

David Kopita and Brian Hughes-Cromwick  
Economic and Strategic Research Group  
June 13, 2014



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