



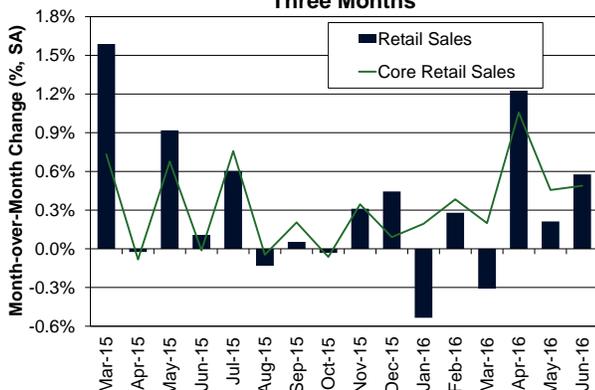
Weekly Note – July 15, 2016

Economics: Steady as She Goes

The week's data suggest the economy keeps plugging along amid global uncertainty. Consumer spending is set to drive economic growth yet again in Q2 2016, as retail sales showed solid gains every month during the quarter. Combined with strong April and May consumer spending, the strength in June core retail sales, a gauge for goods spending, points to more than 4.0 percent annualized growth in real consumer spending in Q2. An index of consumer sentiment declined in early July, as the expectations component worsened to a near two-year low. The drop perhaps reflected the adverse impacts of Brexit on the financial markets, which have largely been reversed. In contrast, a survey of small businesses showed improving confidence in June for the third consecutive month, in part due to a less negative assessment of the outlook for the domestic economy. Details showed that plans to increase employment and worker compensation both fell slightly, even as the share of firms with unfilled positions crept back up to tie an expansion best. Results from the JOLTS showed the level of job openings fell in May for the first time this year amidst the fourth decline in hiring in the past five months. Industrial production rose in June for the second time in three months. Manufacturing, which accounts for about three-fourths of total industrial production, increased for the first time since January, driven by a rebound in motor vehicle production. Oil and gas well drilling increased for the first time since August 2015. Notably, on the inflation front, annual core retail prices ticked up in June to tie an expansion high, boosted by shelter costs, which rose to an expansion high.

- **Retail sales** increased 0.6 percent in June, according to the Census Bureau. The gain in May was revised lower. From one year ago, sales rose 3.1 percent. Core sales, excluding autos, gasoline, and building materials, edged up 0.5 percent, marking the seventh consecutive rise. On an annual basis, core sales rose 4.8 percent.
- **The Job Openings and Labor Turnover Survey (JOLTS)** showed that job openings dropped 5.9 percent in May to 5.5 million from an all-time high in the previous month, according to the Bureau of Labor Statistics (BLS). As a share of total employment, the job openings rate declined two-tenths to 3.7 percent. The hires rate remained unchanged at 3.5 percent. The quits rate was flat as well at 2.2 percent.
- **The Consumer Price Index (CPI)** rose 0.2 percent in June, according to the Bureau of Labor Statistics. Energy prices increased for a fourth consecutive month, gaining 1.3 percent. Excluding food and energy, core CPI increased 0.2 percent. From one year ago, the CPI and core CPI are up 1.0 percent and 2.3 percent, respectively. **Import prices** edged up 0.2 percent in June, driven by energy prices. **The Producer Price Index (PPI)** for final demand of goods and services increased 0.5 percent in June, and rose 0.3 percent from one year ago. Core PPI was flat from May and increased 0.5 percent from June 2015. (The BLS produces all three reports.)
- **Industrial production**, a gauge of output in the manufacturing, utility, and mining sectors, improved 0.6 percent in June, according to the Federal Reserve Board. Manufacturing production rose 0.4 percent. Mining output increased slightly for a second straight month, edging up 0.2 percent. Utilities production rose 2.4 percent.
- **The National Federation of Independent Business (NFIB) Small Business Index** rose 0.7 points to 94.5 in June. The net share of firms expecting the economy to improve reached negative 9.0 percent, up from negative 13 percent in May. The share of firms with few or no qualified candidates remained at 48 percent, a tie for the highest level of the expansion.
- **The University of Michigan Consumer Sentiment Index** dropped 4.0 points to 89.5 in the July preliminary reading. Both the current economic conditions and the expectations components declined.

Retail Sales Have Been Strong Over the Past Three Months



Source: Census Bureau

Core Retail Prices Tick up as Shelter Costs Climb to an Expansion High



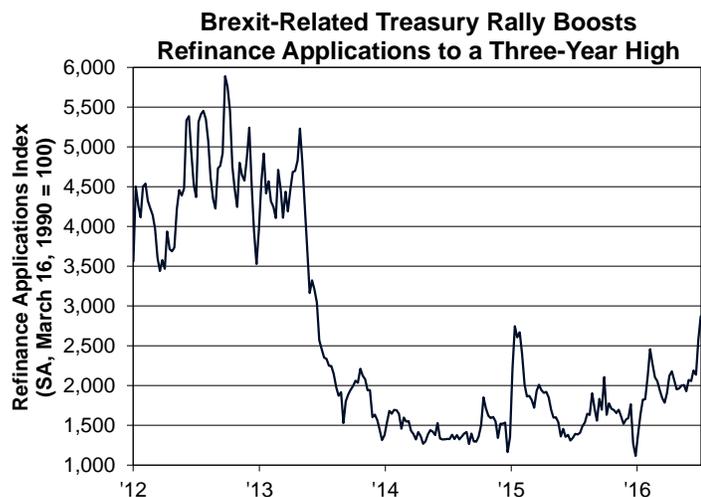
Source: Bureau of Labor Statistics



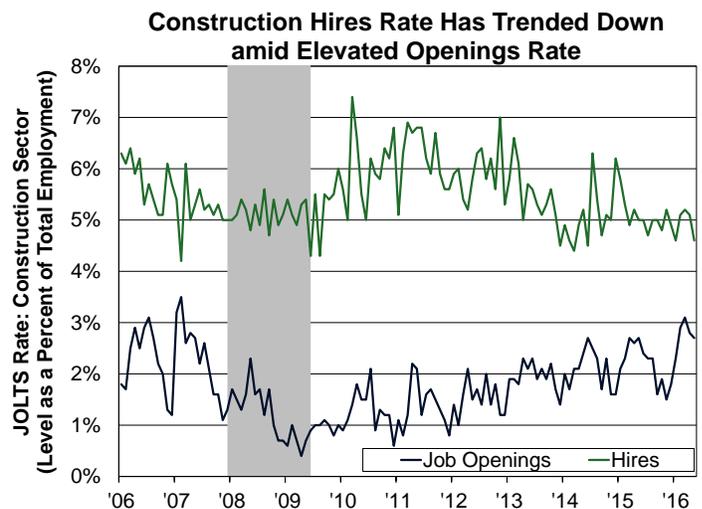
Housing: Brexit Continues to Boost Refinance Activity

A light week for housing data offered good news on refinance activity. The Brexit-induced rate decline helped spur refinance applications for the second consecutive week, sending them to the highest level since June 2013 as mortgage rates fell to the lowest reading since May 2013. However, reaction from purchase applications has been relatively muted, supporting our view that the renewed decline in mortgage rates will not materially improve the outlook for home sales this year. The other report released this week provided added insight on this spring's construction jobs slump through the rearview mirror. The May JOLTS report, which is released with a one-month lag to the jobs report, showed deteriorating hiring trends in construction employment in recent months, similar to the development seen in the June jobs report released last week. However, worsening hiring trends occurred amid elevated job openings, which helps support the view that a shortage of labor remains a significant challenge for home builders. Combined with weakening single-family construction spending and permits activity in May, sluggish hiring of construction workers adds downside risks for building activity. Without relief from new construction, single-family housing inventory will likely remain tight, boosting home prices and constraining affordability. Rates should remain supportive for the mortgage market for some time, even with volatile Treasury yields, as the mortgage spread adjusts. Freddie Mac's survey showed that mortgage rates remained low this week even after a jump in the 10-year Treasury yield, in contrast to the prior two weeks when mortgage rates declined only about half as much as the drop in the 10-year yield. The average 30-year mortgage rate edged up one basis point to 3.42 percent.

- **Mortgage applications** rose 7.2 percent for the week ending July 8, according to the Mortgage Bankers Association. The results included an adjustment for the Fourth of July holiday. The 11.2 percent jump in refinance applications, which followed a 20.8 surge in the prior week, was solely responsible for the overall increase, as purchase applications were flat during the week. Conventional refinance applications rose 12.0 percent, and the government segment increased 8.0 percent. Refinance activity within the government segment has been uneven in recent weeks. FHA applications rose last week for the first time in three weeks, surging nearly 30 percent, while VA applications dropped modestly after double-digit jumps in the prior two weeks. The average 30-year fixed mortgage rate fell 6 basis points to 3.60 percent.
- **The Job Openings and Labor Turnover Survey (JOLTS) showed construction job openings** fell 2.6 percent in May, according to the Bureau of Labor Statistics. The drop in job openings followed a 10.2 percent decline in April from the expansion high in March. The job openings rate (openings as a percent of employment) edged down to 2.7 percent, but remained near the cycle's high of 3.1 percent reached in March. Meanwhile, the hires rate fell 0.5 percentage points to 4.6 percent, the lowest reading since January and well below the expansion high of 7.4 percent recorded in March 2010. The layoffs and discharges rate dropped 0.7 percentage points to 2.6 percent, while the quits rate was unchanged at 1.8 percent.



Source: Mortgage Bankers Association



Source: Bureau of Labor Statistics

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