



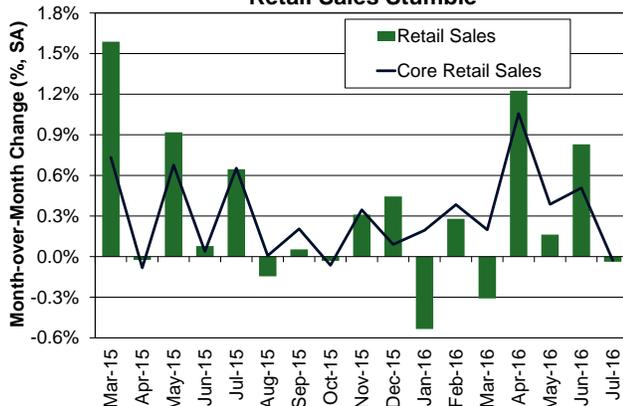
Weekly Note – August 12, 2016

Economics: Consumers Take a Breather after Solid Gains

Data released this week were largely soft. After posting strong gains in each month of the second quarter of 2016, retail sales stumbled out of the gate for the third quarter. Sales were flat in July, with broad-based weaknesses except for sales of auto and parts and at non-store retailers. Core sales, which are key to estimating consumer spending on goods, were also unchanged. Robust consumer spending drove growth in the second quarter amid declining domestic demand elsewhere, but we expect a slowdown in third quarter spending growth in our forecast. A survey of consumer sentiment showed slightly more optimistic consumers in August, ending two months of declines. Optimism among small businesses rose in July, albeit barely. Their view of the economy improved for the third consecutive month, but remains negative on net. Plans to raise wages have remained stagnant this year after falling from an 11-year high in December 2015. The share of firms with few or no qualified candidates slipped from an expansion high in June. The JOLTS showed that the rates of job openings and hiring edged up slightly in June, consistent with a strong jobs report during the month. While the labor market has shown signs of springing back to life, worker productivity has moved in the opposite direction. Nonfarm business productivity fell for the third consecutive quarter, marking the longest stretch of declines since 1979 and causing the first year-over-year drop in three years. This will remain a concern for businesses and the economy as a whole, as productivity growth is crucial for real wages and the economy's growth potential.

- **Retail sales** were flat in July, according to the Census Bureau. The gain in June was revised higher. From a year ago, sales rose 2.3 percent. Core sales, which exclude autos, gasoline, and building materials, were also unchanged during the month after rising for the past eight months. On an annual basis, core sales rose 3.3 percent.
- **The National Federation of Independent Business (NFIB) Small Business Optimism Index** edged up one-tenth to 94.6 points in July. The net share of firms expecting the economy to improve was negative 5.0 percent; the economic outlook has been negative since March 2015. On the labor front, the share of firms with open positions dropped to a four-month low of 26 percent, as plans to increase employment edged up 1.0 percentage point to 12 percent. The share of firms planning to raise wages also crept up 1.0 percentage point to 15 percent.
- **The Job Openings and Labor Turnover Survey (JOLTS)** showed that job openings increased 2.0 percent in June to 5.6 million, according to the Bureau of Labor Statistics. As a share of total employment, the job openings rate ticked up one-tenth to 3.8 percent. The hires rate also edged up one-tenth to 3.6 percent. The quits rate, a gauge of worker confidence in the labor market, remained at 2.0 percent for the third straight month.
- **Nonfarm business productivity** declined 0.5 percent annualized in Q2 2016 from the prior quarter, according to the Bureau of Labor Statistics. Compensation per hour increased 1.5 percent annualized, after declining in the first quarter. As a result, unit labor costs rose 2.0 percent, marking the sixth rise in the past seven quarters.
- **The University of Michigan Consumer Sentiment Index** edged up 0.4 points to 90.4 in the August preliminary reading. A gain in the expectations component barely outweighed a fall in the current conditions component.
- **Import prices** crept up 0.1 percent in July as the increase in nonpetroleum prices offset the first drop in energy prices in five months. **The Producer Price Index (PPI)** for final demand of goods and services fell 0.4 percent in July, ending a three-month stretch of gains. The index also fell 0.2 percent from a year ago. Core PPI was flat on a monthly basis and rose 0.4 percent on an annual basis. The Bureau of Labor Statistics produces both reports.

After a Strong Second Quarter, Retail Sales Stumble



Source: Census Bureau

Productivity Growth Declines Quarterly and Annually for the First Time in Three Years



Source: Bureau of Labor Statistics

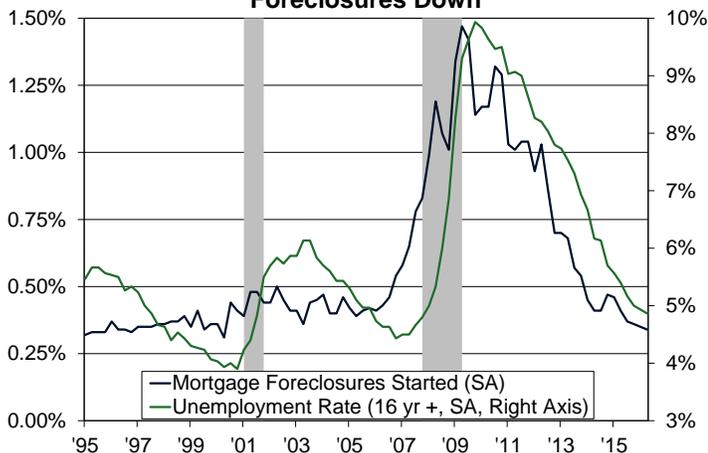


Housing: Labor Shortage Remains Key Supply Risk

This week's housing data were light and largely positive. Mortgage performance continued to improve in the second quarter, with the delinquency rate and the foreclosure started rate declining to well below their long-term averages. Notably, the foreclosure started rate fell to the lowest reading in 16 years, driven lower by improving labor market conditions. The rate peaked in 2009, when the unemployment rate also peaked, and both rates have gradually trended down since. Additional positive news was from mortgage demand, which picked up last week after a string of declines, as mortgage rates ticked down. However, Freddie Mac's survey showed that the average rate on a 30-year fixed-rate mortgage increased two basis points to 3.45 percent this week, in response to the strong July jobs report released last Friday. The JOLTS, which is released with a one-month lag to the jobs report, offered mixed news regarding construction employment in June. While the job openings rate rebounded to just shy of the expansion-best reached in March, suggesting elevated demand for workers, the hires rate plummeted to the worst showing of the expansion. The trend in the hires rate from the JOLTS is consistent with lackluster construction payroll gains in recent months from the jobs report, and supports the view that a shortage of labor, and not sluggish demand, has been the main challenge for the home building industry.

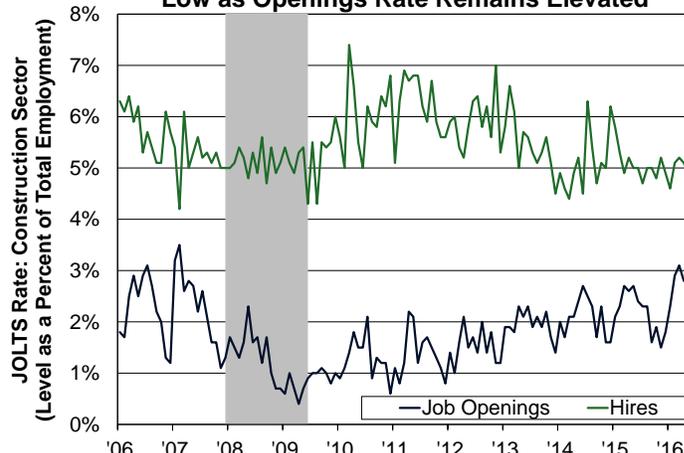
- **The Mortgage Bankers Association National Delinquency Survey** for Q2 2016 showed that the delinquency rate for mortgage loans on one-to-four-unit residential properties decreased 11 basis points from the prior quarter to 4.66 percent, marking the lowest level since Q2 2006. The percentage of loans on which foreclosure actions were started during the second quarter fell three basis points to 0.32 percent, the best showing since Q2 2000. The long-term averages for the delinquency and foreclosure started rates are 5.36 percent and 0.45 percent, respectively. The serious delinquency rate — the percentage of loans that are 90 days or more past due or in the process of foreclosure — dropped 18 basis points to 3.11 percent, its lowest reading since Q3 2007.
- **The Job Openings and Labor Turnover Survey (JOLTS)** showed that the construction job openings rate rose two-tenths to 3.0 percent in June, according to the Bureau of Labor Statistics. The hires rate plunged 0.7 percentage points to 4.2 percent. The quits rate dropped from 1.8 percent in May to 1.5 percent, the lowest reading since January.
- **Mortgage applications** rose 7.1 percent for the week ending August 5, according to the Mortgage Bankers Association. Purchase applications were up for the first time in five weeks, increasing 2.6 percent. Refinance applications rose 9.6 percent following three consecutive weekly drops, driven by the biggest jump in government applications since last October. The average rate for 30-year fixed-rate mortgages edged down two-tenths to 3.65 percent.

Improving Labor Market Has Helped Bring New Foreclosures Down



Source: Mortgage Bankers Association

Construction Hires Rate Falls to a Nine-Year Low as Openings Rate Remains Elevated



Source: The Bureau of Labor Statistics

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