



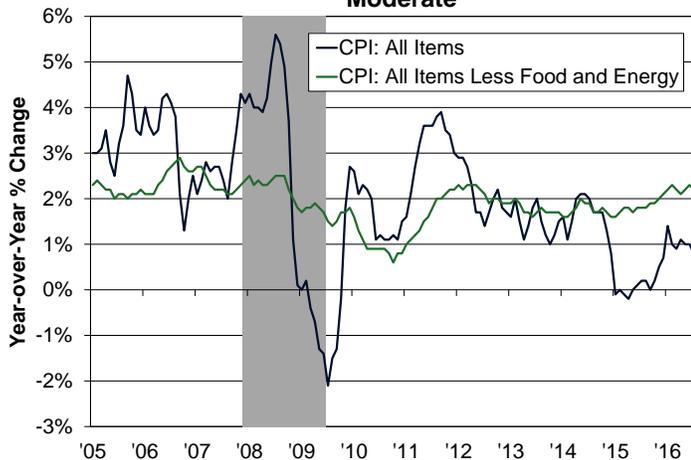
Weekly Note – August 19, 2016

### Economics: Fed Attempts to Keep 2016 Hike in Play

Economic news this week centered on the release of the [minutes](#) from the July Federal Open Market Committee (FOMC) meeting, as committee members were divided on the timing of another increase in the fed funds rate. Some believed the labor market was at or close to maximum employment, and that an increase in the rate “was or would soon be warranted.” Others judged that it was appropriate to wait for additional information to evaluate the underlying momentum in economic activity and to see whether inflation would rise to the target “on a sustained basis.” Important data released since the meeting have been mixed, thereby providing some support for each side’s view. The first estimate of Q2 2016 gross domestic product showed anemic growth, the July jobs report revealed strong hiring for a second month in a row, and July retail sales were flat. In addition, retail inflation has been dormant, as annual growth in the headline Consumer Price Index continued its recent downward trend to under 1.0 percent and the annual increase in the core index slowed. Several speeches by Fed officials this week attempted to put a rate hike on the table this year. For example, Bill Dudley, President of the New York Fed, said that “we are getting closer to the next rate hike,” as well as “September is possible.” The financial markets continued to discount that possibility, as the fed funds futures’ odds of a rate hike remain at just 20 percent for September and 45 percent for December. We maintain our belief that there will be no change in monetary policy this year. Other news this week was upbeat. Industrial production increased the most in July since November 2014, as all three components rose. Manufacturing posted the largest increase in a year to reach a new expansion high. Oil and gas well drilling had the biggest gain in over six years, marking the second consecutive increase after nine straight months of decline. Lastly, the Conference Board Leading Economic Index points to improving economic activity in the second half of this year, as the index rose in July for a second straight month.

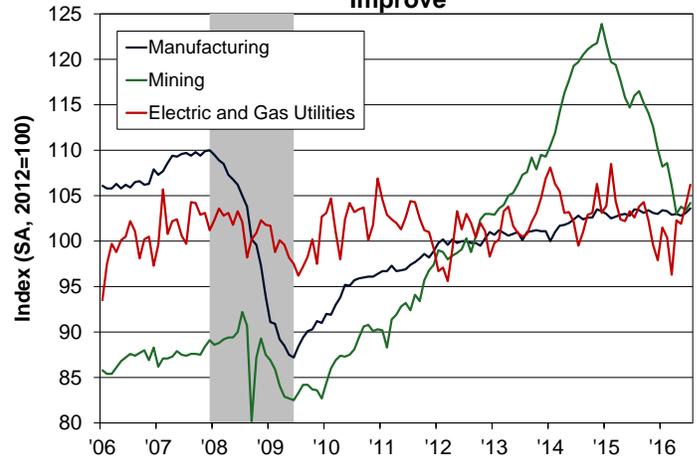
- **The Consumer Price Index (CPI)** was unchanged in July, according to the Bureau of Labor Statistics. Energy prices fell 1.6 percent from June, marking the first drop in five months. Core prices, excluding food and energy, edged up 0.1 percent, as the 0.2 percent rise in core services outweighed the 0.1 percent drop in core goods. The increase in core services was driven by medical care services, whose cost rose 0.5 percent during the month and 4.1 percent from one year ago, marking the largest annual increase since September 2012. From one year ago, the headline and core indices rose 0.8 percent and 2.2 percent, respectively.
- **Industrial production**, a gauge of output in the manufacturing, utility, and mining sectors, increased 0.7 percent in July, according to the Federal Reserve Board. Manufacturing production posted a second consecutive rise, increasing 0.5 percent. Utilities production increased 2.1 percent for a second month in a row. Mining production improved for the second time in the past three months, rising 0.7 percent. Oil and gas well drilling increased 4.9 percent.
- **The Conference Board Leading Economic Index (LEI)**, a gauge of the economic outlook over the next three to six months, increased 0.4 percent in July. Positive contributions from hours worked in manufacturing, initial jobless claims, and financial subcomponents more than offset the negative contribution from consumer expectations.
- **Initial claims for unemployment insurance** decreased by 4,000 to 262,000 in the week ending August 13, according to the Department of Labor. The four-week moving average increased by 2,500 to 265,250.

Headline and Core Inflation Measures  
Moderate



Source: Bureau of Labor Statistics

All Three Components of Industrial Production  
Improve



Source: Federal Reserve Board

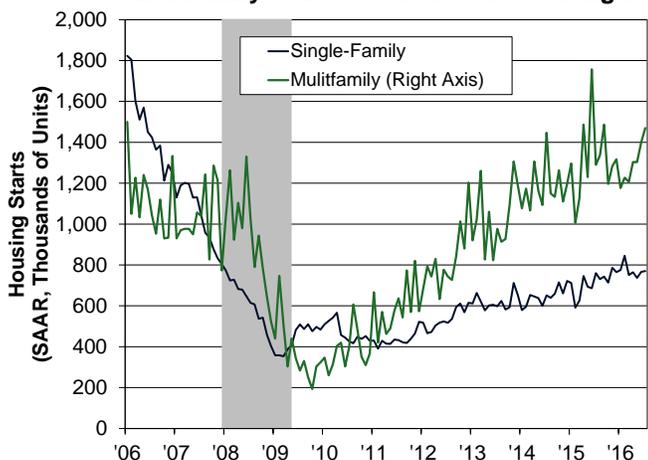


## Housing: Multifamily Boosts Housing Starts

This week's news was somewhat positive. Housing starts rose in July for the second consecutive month, but remained just shy of the expansion high. However, the gain came largely from the multifamily segment. Single-family starts were little changed, and permits — a forward-looking indicator — fell to the lowest level since last September. Another weak quarter of single-family construction will be a serious cause for concern after residential investment fell in the second quarter for the first time in more than two years. Labor and lot shortages may help explain the weakness in activity, but the effect of the past declines in oil prices appears to be weighing down permit activity in some oil-producing regions, such as the Houston/Woodlands/Sugar Land MSA. The area accounts for about one-third of Texas' single-family permits, which were little changed in the first quarter from one year ago. Builders' confidence, as measured by the Housing Market Index, improved in August as new home sales rose in July for the third time in four months to an expansion high. So far this year, the Housing Market Index has moved within a narrow range of between 58 and 61. While the index remains at elevated levels, it is still below the recovery best reached last October, despite continued improvement in the new home sales trend since then. On a weak note, both purchase and refinance mortgage demand pulled back last week for the fourth time in five weeks. Historically low mortgage rates have not helped spur purchase mortgage demand in recent months. Purchase applications have trended down since early June, when they reached the highest level since last October's spike induced by the implementation of the TILA-RESPA Integrated Disclosure Rule (TRID). They are currently at the lowest level since February. By contrast, refinance applications have remained elevated despite their recent declines. Freddie Mac's survey showed that the 30-year fixed mortgage rate fell two basis points this week to 3.43 percent.

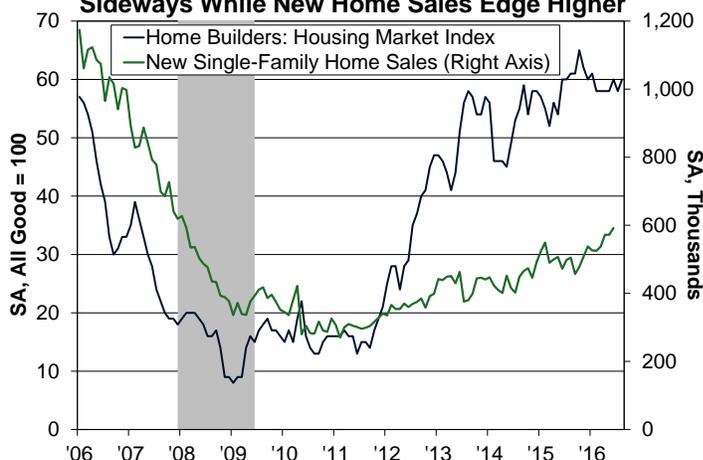
- **Housing starts** increased 2.1 percent in July, according to the Census Bureau. Multifamily starts drove the gain, rising 5.0 percent to 441,000 seasonally adjusted annualized units, the strongest pace since last September. This marks the second consecutive increase and the third gain over the last four months. Single-family starts ticked up 0.5 percent to 770,000 units, but remained well below the expansion high reached last February. Year-to-date, single-family starts are 10.6 percent more than the same period one year ago, compared with a 0.6 percent drop in multifamily starts. The double-digit gain in single-family starts reflects a small base, while the relatively flat multifamily starts suggest a mature stage of the multifamily expansion, which exhibited a faster recovery that has lifted activity above its pre-recession levels. Single-family permits dropped 3.7 percent to 711,000 units while multifamily permits advanced for the fourth consecutive month, increasing 6.3 percent to 441,000 units.
- **The National Association of Home Builders / Wells Fargo Housing Market Index** rose two points in August to 60. (A reading of more than 50 indicates more builders view the market as good rather than poor). The present and future sales components posted gains, while the prospective buyers traffic component fell.
- **Mortgage applications** fell 4.0 percent for the week ending August 12, according to the Mortgage Bankers Association. Purchase applications declined 3.9 percent while refinance applications dropped 4.2 percent. The average contract interest rate for the 30-year fixed-rate mortgage edged down one basis point to 3.64 percent.

**Multifamily Starts Show Renewed Strength**



Source: Census Bureau

**Home Builders Sentiment Has Moved Sideways While New Home Sales Edge Higher**



Source: Census Bureau and the National Association of Home Builders

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Economic and Strategic Research Group  
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