Economics: Domestic Strength, Foreign Fright

Our outlook for above-trend second-half growth remains intact as economic data released this week were broadly consistent with strengthening economic momentum. Growth for Q2 2014 was revised up to 4.6 percent annualized—the fastest rate of economic expansion since Q4 2011. Upward revisions were broad-based, though a 0.4 percentage point upgrade in the contribution of consumer spending on healthcare services to GDP growth, matching the total upward revision to headline growth, was notable. Despite the expected decline in headline durable goods orders in August following the surge in civilian aircraft orders in July, the details were positive for second-half business fixed investment in equipment following the 11.2 percent annualized jump in Q2. Consumer sentiment improved during the past month to the most optimistic reading since last summer amid jobless claims holding below 300,000—a threshold indicating healthy labor market conditions. Global risks remain, however, as tensions with Russia and in the Middle East have escalated, and concerns over slowing growth in China combined to pull stocks lower and support a rally in U.S. Treasuries. The 10-year yield sank to 2.53 percent on Friday morning, down from a two-month high reached last Thursday of 2.63 percent.

➢ The Reuters/University of Michigan Consumer Sentiment Index increased 2.1 points in September to 84.6 from the final August reading, though it was unrevised from the preliminary September figure. A rebound in the consumer expectations component outweighed a small decline in the current conditions component, and pushed the headline index to a 14-month high.

➢ Gross domestic product (GDP), adjusted for inflation, increased at a 4.6 percent annualized rate in Q2 2014 according to the Bureau of Economic Analysis’ third estimate, a 0.4 percentage point upgrade from the second estimate of 4.2 percent and a strong rebound from the 2.1 percent decline in Q1 2014. All six major categories of growth were revised up modestly, with the largest being upgrades to nonresidential fixed investment and net exports. Consumer spending remained the primary driver of growth during the quarter, contributing 1.8 percentage points. Real final sales to private domestic purchasers, a measure of the underlying growth trend that includes personal consumption spending and business fixed investment, increased at a 6.0 percent annual rate during the quarter, the fastest pace since Q1 2012.

➢ Durable goods orders sank 18.2 percent in August following the 22.5 percent July surge driven by a jump in civilian aircraft orders. Orders for motor vehicles and parts also declined, falling 6.4 percent after July’s 10.0 percent gain, though orders for nondefense capital goods excluding aircraft—a leading indicator of business investment in equipment in the calculation of GDP—increased 0.6 percent in August and 25.2 percent annualized over the past three months.

➢ Initial claims for unemployment insurance increased 12,000 to 293,000 in the week ending September 20, according to the Department of Labor. The four-week moving average reached the lowest level in a month at 298,500.

Source: Bureau of Economic Analysis

Source: Census Bureau
Housing: New Home Sales Surprise on the Upside

Data on home sales for August 2014 surprised as the largest monthly percentage gain in new single-family home sales in more than 20 years, bucking roughly two years of flat-lining, was countered by the first decline in existing home sales in five months. Existing sales, which comprise the large majority of total home sales, suffered a minor setback despite recent strength in pending home sales. However, a silver lining to the report is the ongoing decline in the cash share of existing home sales this year, corroborating other data sources such as CoreLogic. We expect this trend, if combined with stronger job and income growth, will provide opportunity for first-time and trade-up buyers (the organic housing demand that has been limited for much of the current cycle) to fill the void. Unfortunately, the decline in cash sales has yet to be offset with a substantial pickup in purchase mortgage demand, underscoring our modest outlook for near-term home sales activity. Meanwhile, the FHFA purchase-only home price index provided further evidence of strong but moderating home price appreciation. Though home price growth was broad-based, with all nine census divisions showing year-over-year price appreciation, the slowdown in gains also was widespread as all nine regions showed lower annual price growth in July 2014 than in July 2013.

- **Existing home sales** declined 1.8 percent in August to a seasonally adjusted annual rate of 5.05 million units according to the National Association of REALTORS®. Year-to-date through August 2014, sales were 5.6 percent below the total from the same period last year. The number of homes available for sale declined for the first time this year, falling 1.7 percent in August to 2.31 million units, though inventory is up 4.5 percent over the past 12 months. The months’ supply (or inventory/sales ratio) was unchanged at 5.5 for the fourth consecutive month. The median sales price, which can be biased by the mix of sales, increased 4.8 percent from a year ago. The distressed sales share (REO and short sales) was 8.0 percent during the month, down from 12.0 percent a year ago, while all cash sales accounted for 23.0 percent of August transactions, down from 29.0 percent in July and the lowest since December 2009. The first-time homebuyer share was unchanged in August at 29.0 percent and has held below 30.0 percent for 16 of the last 17 months.

- **New single-family home sales** jumped 18.0 percent in August to a seasonally adjusted annual rate of 504,000 units—a new recovery best according to the Census Bureau. Year-to-date through August 2014, sales were up 2.7 percent compared to the 2013 total over the same period. New homes available for sale increased 1.0 percent during the month—the 13th gain in 14 months—to a four-year high of 203,000 units. The months’ supply (or inventory/sales ratio) declined sharply, falling to a 14-month low of 4.8. The median sales price, which is unadjusted for the changing mix of sales, increased 8.0 percent from a year ago.

- **Mortgage applications** declined in the week ending September 19, falling 4.1 percent as refinance applications sank 7.0 percent amid the highest contract interest rate for 30-year fixed-rate mortgages (4.39 percent) in four months, according to the Mortgage Bankers Association (MBA). Purchase mortgage applications fell just 0.3 percent, holding near a three-month best but remaining well below the 2014 highs reached earlier in the year.

- **The FHFA purchase-only home price index** (reported by FHFA on a seasonally adjusted basis) increased 0.1 percent in July 2014 and 4.5 percent from a year ago. This marked the 8th and 30th consecutive gains in monthly and annual price appreciation, respectively, though the latter has slowed since peaking at 8.6 percent a year ago. Since bottoming out in May 2011, the index has increased a cumulative 17.9 percent, though it remains 6.4 percent below the April 2007 peak.

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