



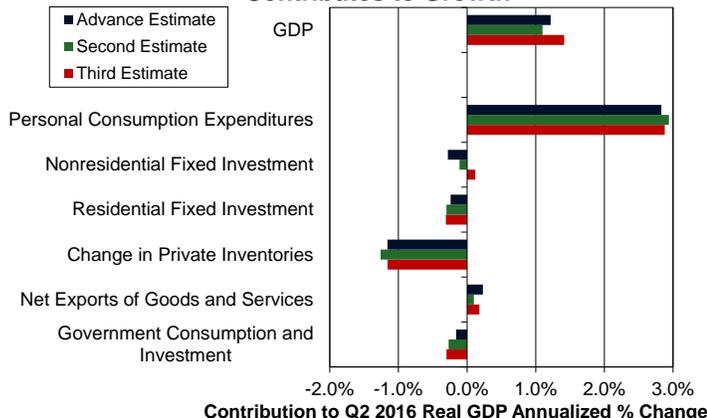
Weekly Note – September 30, 2016

Economics: Growth Looks for a Spark

Data this week showed the sluggish economy still needs a shot in the arm after a disappointing first half of the year. In the final estimate, second quarter real GDP was revised upward slightly to bring first half growth to 1.1 percent, still uninspiring. The key revision came from business fixed investment, as both business investment in structures and in equipment were revised higher to show smaller declines. Growth in intellectual property investment outweighed the declines in the other two components, leading overall business fixed investment to contribute slightly to growth in the final estimate, whereas it subtracted from growth in the first two estimates. Looking ahead to the third quarter, consumers found the going tougher in August, pulling back on spending for the first time since March amid slowing income growth from a seven-month high. However, two gauges of consumer confidence showed more optimistic consumers in September, albeit to varying degrees. The Conference Board consumer index painted a particularly rosy picture, climbing to a nine-year high. The University of Michigan sentiment index, on the other hand, increased modestly for the first time in four months, but remained well below the expansion high reached in early 2015. On the inflation front, the Fed's preferred measure, the PCE deflator, showed a slight increase, with annual growth still remaining a full percentage point below the Fed's 2.0 percent target. The annual growth in the core index ticked up during the month after staying at 1.6 percent for five consecutive months. The other key news this week came from the manufacturing sector. Headline durable goods orders were unchanged in August, but details were mixed. Core capital goods shipments, a proxy for business investment in equipment, fell for the fourth straight month, suggesting that business equipment spending will likely decline this quarter for the third consecutive quarter. However, core capital goods orders, a forward-looking indicator, rose for the third consecutive month, providing hope for a turnaround in business capital investment in the fourth quarter.

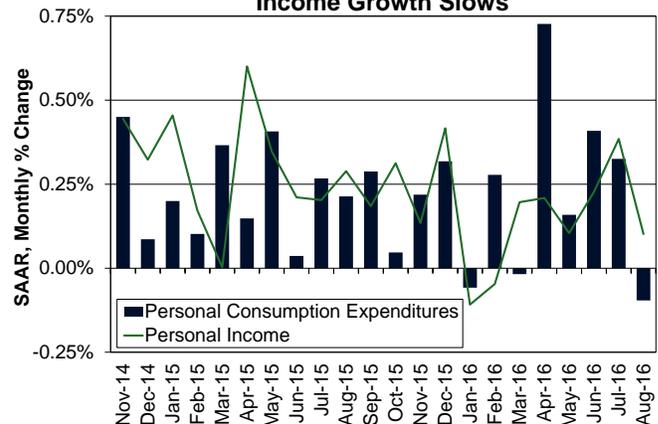
- **Gross domestic product (GDP) growth**, adjusted for inflation, was revised three-tenths higher to 1.4 percent annualized in Q2 2016, according to the third estimate from the Bureau of Economic Analysis (BEA). Nonresidential fixed investment was revised from a slight drag on growth to a slight contributor. Of the other two components that added to growth, consumer spending was revised downward, and net exports was revised upward. The drags from residential fixed investment and government spending were greater than previously reported, while the drag from inventories was less than in the second estimate.
- **Personal income**, adjusted for inflation, rose 0.1 in August, according to the BEA. Real personal consumption expenditures (PCE) slipped 0.1 percent. The personal saving rate ticked up one-tenth to 5.7 percent. The PCE deflator rose 0.1 percent during the month and 1.0 percent from a year ago. Excluding food and energy, the core deflator rose 0.2 percent from July, and 1.7 percent from August 2015.
- **The Conference Board Consumer Confidence Index** rose 2.3 points to 104.1 in September. Both the present situation and the expectations components rose. **The University of Michigan Consumer Sentiment Index** improved 1.4 points to 91.2 in the final September reading, as the rise in expectations outweighed the fall in current conditions.
- **Durable goods orders** were flat in August, according to the Census Bureau. Core capital goods orders (nondefense capital goods ex-aircraft) rose 0.6 percent, but core shipments fell 0.4 percent.
- **Initial claims for unemployment insurance** increased by 3,000 to 254,000 in the week ending September 24, according to the Department of Labor. The four-week moving average decreased by 2,250 to 256,000.

In Final Estimate, Business Investment Contributes to Growth



Source: Bureau of Economic Analysis

Consumers Hold Back on Spending as Income Growth Slows



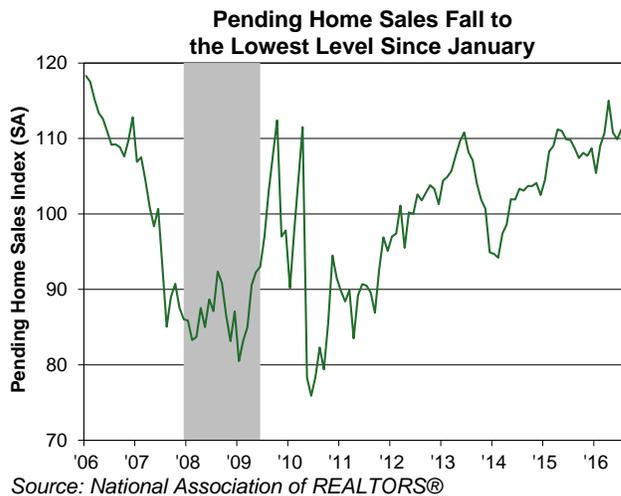
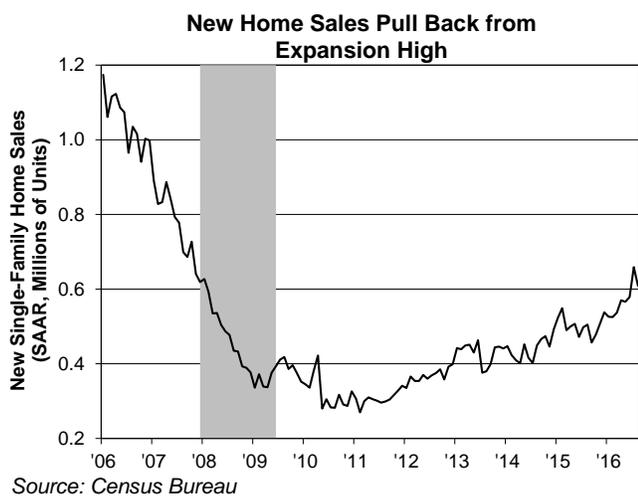
Source: Bureau of Economic Analysis



Housing: Low Inventory Takes the Wind Out of Sales

Data released this week showed that the historically low inventory of existing homes continues to weigh on sales. Pending home sales, which reflect contract signings of existing homes, fell in August for the third time in the past four months to reach the lowest level since January. Extremely lean inventory of existing homes helped boost home price gains further in July, with the Case-Shiller National Home Price Index posting at least 5.0 percent annual growth for the ninth straight month. The primary concern in the home sales market is not a lack of demand, but that potential home buyers could become so discouraged by tight inventory and strong home price gains that they give up their search. For the new home market, sales fell back in August, as expected, following the largest month-over-month jump in over 23 years, which sent the sales pace to a new expansion high and pushed the for-sale inventory down to the lowest level this year. The near-term outlook for inventory remains gloomy, as single-family housing starts have trended down since reaching an expansion best in February. Unlike the existing home market, inventory is less of an issue in restraining new home sales because sales are recorded at contract signings, which can occur even when houses are not started or are still under construction. On a positive note, demand for purchase mortgages rebounded last week following a sharp drop in the prior week. Purchase applications have risen in four of the past five weeks, an encouraging sign after average purchase applications in August fell for the second consecutive month. In contrast, refinancing demand has lost momentum, falling last week for the second consecutive week despite declining mortgage rates. This week's Freddie Mac survey showed that the average 30-year fixed mortgage rate dropped six basis points to 3.42 percent, marking the lowest level since the first week of July.

- **The National Association of REALTORS® Pending Home Sales Index**, which records contract signings of existing homes and typically leads closings by one to two months, declined 2.4 percent in August. Contract signings fell in every region except the Northeast.
- **New single-family home sales** fell 7.6 percent to a seasonally adjusted annualized rate of 609,000 units in August, according to the Census Bureau. Through the first eight months of the year, new home sales are 13.6 percent higher than the same period a year ago. Sharp drops in sales in the Northeast and South and a slight fall in the Midwest outweighed a gain in the West. New homes for sale improved 1.7 percent during the month, partially recovering last month's drop, which was the second largest monthly decline of the expansion. A drop in sales and a rise in inventory pushed the months' supply (inventory-to-sales ratio) four-tenths higher to 4.6 months. The median sales price, which is not adjusted for the mix of sales, fell 5.4 percent from one year ago, marking the largest drop since January 2012.
- **The S&P/Case-Shiller National Home Price Index** (not seasonally adjusted) in the three months ending in July rose 5.1 percent from a year ago, improving slightly from the 5.0 percent pace in June.
- **Mortgage applications** slipped 0.7 percent for the week ending September 23, according to the Mortgage Bankers Association. Purchase applications edged up 0.8 percent as a rise in conventional applications outweighed a slight decline in government applications. Refinancing applications, on the other hand, declined 1.6 percent with a second straight drop in conventional applications more than offsetting a rise in government applications. The average 30-year fixed mortgage rate declined four basis points to 3.66 percent, marking the lowest level in six weeks.



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