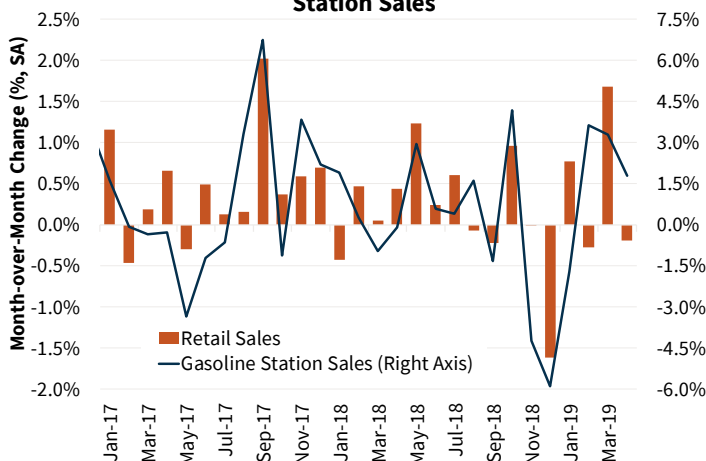


Economics: Retail Sales Fall Amid Improving Sentiment

Economic data released this week were somewhat weaker than expected as both retail sales and industrial production fell. After rising by the largest amount in over a year in March, retail sales softened in April. Weakness was widespread, with the largest declines in motor vehicle and parts sales and building material sales. Gas station sales were the bright spot of the report, rising strongly for the third straight month as retail gasoline prices hit a six-month high in April. Core retail sales, which exclude auto, gas, and building material sales and are an input for the consumer goods spending component of GDP, were unchanged. Sales at clothing and accessory stores declined for the fourth time in five months. The disappointing retail sales report poses a downside risk to our view that real consumer spending growth will pick up to 3.0 percent annualized this quarter after a sluggish first quarter. Industrial production fell for the third time in four months in April, declining to the lowest level since last July. Falling output in manufacturing and utilities outweighed a spike in mining production. The decline in utilities output was largely due to a 7.7 percent decline in gas utilities output, thanks to above-average temperatures during the month, which reduced the demand for heating. Manufacturing output has not improved in any month this year as durable goods production continues to fall while nondurable goods manufacturing has remained flat for the past three months. The Conference Board’s Leading Economic Index, which is a gauge for the near-term outlook for economic growth, rose in April for the third straight month, with the only two drags on the index involving new manufacturing orders. Small businesses were more optimistic in April, as the Optimism Index hit a four-month high, though it remains well below the expansion high reached last August. Businesses continue to be concerned about the tight labor market, as the single most important problem for small business owners was quality of labor, cited by 24 percent of respondents, just shy of last November’s expansion high. Consumers were even more upbeat as the University of Michigan’s Consumer Sentiment Index rose to a 15-year best in early May. While the current conditions component was largely flat, consumer expectations posted the largest monthly gain in seven years to reach the highest level of this expansion. Tempering the bullish sentiments, both the business and consumer surveys were taken before the recent breakdown in trade negotiations with China, and readings in the coming months will likely be more bearish as trade tensions weigh on businesses and consumers alike.

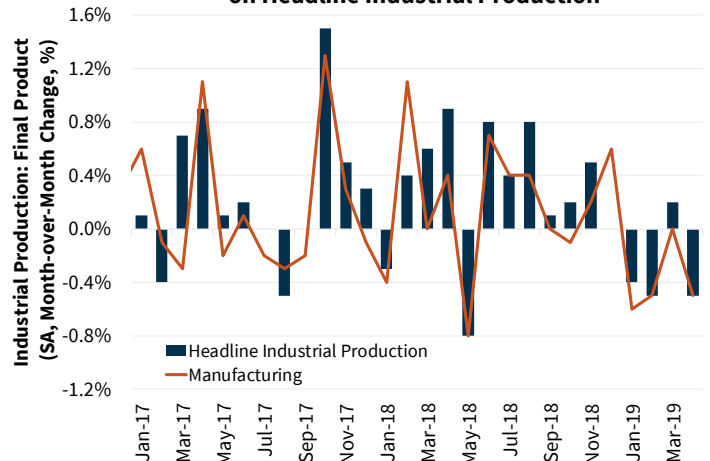
- **Retail sales** fell 0.2 percent in April, while core retail sales were unchanged, according to the Census Bureau. The March gains in headline and core retail sales were both revised upward one-tenth to 1.7 percent and 1.1 percent, respectively. Annual growth in headline sales decelerated seven-tenths to 3.1 percent and core sales slowed eight-tenths to 2.9 percent.
- **Industrial production**, a gauge of output in the manufacturing, utility, and mining sectors, declined 0.5 percent in April, according to the Federal Reserve Board. Manufacturing and utilities outputs fell 0.5 percent and 3.5 percent, respectively, while mining output jumped 1.6 percent. Capacity utilization fell six-tenths to 77.9 percent, the lowest level in over a year.
- **The Conference Board Leading Economic Index (LEI)**, a gauge of the economic outlook over the next three to six months, increased 0.2 percent in April following a 0.3 percent rise in March and a 0.2 percent improvement in February.
- **The National Federation of Independent Business (NFIB) Small Business Optimism Index** jumped 1.7 points to 103.5 in April. The net share of small businesses expecting the economy to improve edged up to 13 percent, and the net share of businesses reporting higher nominal sales this quarter over last rose to 9 percent, a six-month high.
- **The University of Michigan Consumer Sentiment Index** rose 5.2 points to 102.4 in the May preliminary reading.

Retail Sales Decline Despite Strong Gasoline Station Sales



Source: Census Bureau

Manufacturing Output Declines Continue to Drag on Headline Industrial Production



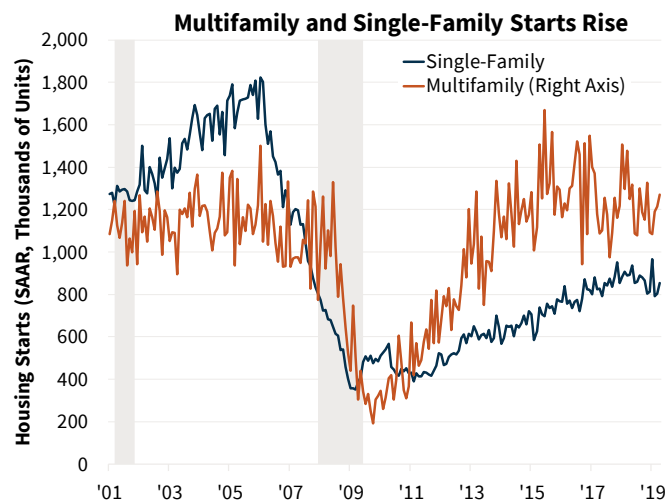
Source: Federal Reserve



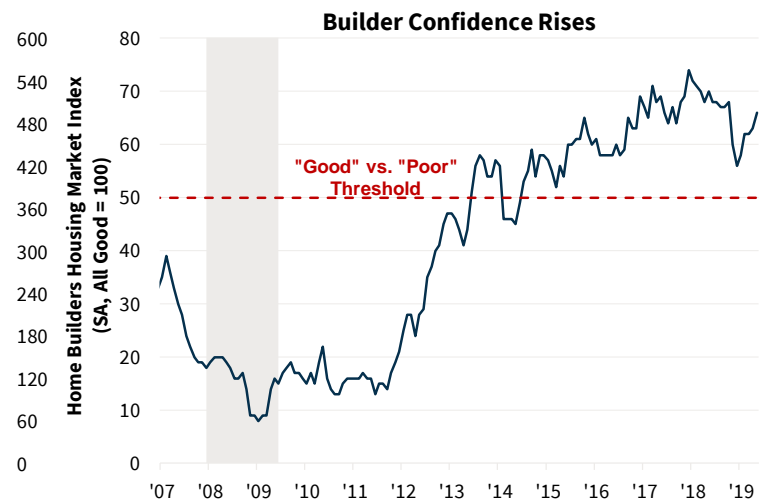
Housing: Housing Starts Jump, Mortgage Rates Fall

Housing news this week was largely positive as housing starts improved and homebuilder sentiment rose. Total housing starts rose in April for the second straight month, driven by increases in both single-family and multifamily starts, although on an annual basis, starts fell for the seventh straight month. The increase in single-family starts was particularly strong in the Midwest, where they rose by the largest amount in nearly a year. In contrast, single-family permits fell for the fifth straight month, posting the largest decline since last August. Over the prior two months before April, single-family permits outpaced starts, suggesting the comparative weakness in April permits likely reflected homebuilders starting construction on a pipeline of already-permitted projects. In contrast, multifamily permits increased to the highest annualized level in over a year. Turning to survey data, an index of homebuilder sentiment rose in May to its highest level since last October, with all subcomponents of the index rising. The current sales expectation component rose for the fifth consecutive month. The continued pullback in mortgage rates is likely contributing to increased buyer demand. This week, the 30-year fixed mortgage rate fell 3 basis points to 4.07 percent, the third straight week of declines, and is down 54 basis points from a year ago and 87 basis points from last November's peak, according to Freddie Mac. Finally, mortgage applications fell last week, with both purchase and refinance applications dipping slightly; however, even with the decline, purchase applications remain at a similar level to the April average. Looking at the week's data as a whole, the slow pace of single-family permits likely dampens the short-run potential for a strong pickup in single-family construction, though the increase in starts combined with improved homebuilder sentiment and declining mortgage rates reinforces our view of a solid spring homebuying season.

- **Housing starts** rose 5.7 percent to 1.24 million units in April, according to the Census Bureau. Single-family starts increased 6.2 percent to 854,000 units, driven by strong gains in the Northeast and Midwest of approximately 30 percent and 38 percent, respectively. Multifamily starts rose 4.7 percent to 381,000. However, from a year ago, total housing starts were down 2.9 percent. Permits grew 0.6 percent over the month, driven entirely by multifamily permits jumping 8.9 percent. Single-family permits, in contrast, fell 4.2 percent.
- **The National Association of Home Builders/Wells Fargo Housing Market Index** rose 3 points to 66 in May, indicating improvement in homebuilder confidence. A number above 50 indicates that builders view conditions as being good. The current sales conditions index rose 3 points to 72, the index measuring expectations over the next six months ticked up by 1 point to 72, and the index measuring buyer traffic rose by 2 points to 49. Three of the four regional indices rose, with only the Midwest remaining unchanged. The index for the Northeast jumped 10 points to 65, the highest level since October 2005
- **Mortgage applications** fell 0.6 percent for the week ending May 10, according to the Mortgage Bankers Association. Refinance applications and purchase applications both dropped, falling 0.5 percent and 0.6 percent, respectively.



Source: Census Bureau



Source: National Association of Home Builders

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