ESR Economic and Housing Weekly Note ***April 3, 2015***

Economics: Hiring Picture Now Consistent with Weakening Economic Growth

This week features many pieces of disappointing news. The biggest downside surprise was an increase in nonfarm payrolls of only 126,000 in March, the slowest job creation since the end of 2013. However, not all was downbeat as initial jobless claims during the last week of March fell to near an expansion low. Consumer spending pulled back in February, and even with the first rise in four months in March auto sales, real consumer spending growth likely came in about 0.5 percentage points below our expectations of 2.7 percent annualized in the March forecast. Income continued to grow faster than spending, pushing the saving rate up further to the highest reading in more than two years. Altogether, improving income trends and household balance sheets, a higher saving rate, and a rebound in consumer confidence should help boost consumer spending in the second quarter. Meanwhile, weak global demand, the run-up in the U.S. dollar, declining drilling activity related to the oil price declines, and the West Coast port shutdown have taken a toll on the factory sector. This is evident in the sixth consecutive decline in core capital goods orders in February and the fifth consecutive drop in the ISM manufacturing index in March, which matches the longest losing streak since 2008. These factors also had mixed impacts on the trade deficit. It's difficult at this point to assess how much of the recent weakness in manufacturing, exports, and imports stemmed from the port disruptions and how much was a result of softening underlying domestic and global demand and the strength in the dollar. Overall, data are pointing to economic growth of just about 1.0 percent in the first quarter.

- **Nonfarm payroll employment** rose 126,000 in March, according to the Bureau of Labor Statistics. The downward revision of 69,000 in the prior two months sent the average monthly gain in Q1 2015 to 197,000, a one-year low. The unemployment rate held at 5.5 percent as a drop in the labor force offset weak household employment gain. While average hourly earnings picked up 0.3 percent, the year-over year rise of 2.1 percent showed no signs of a break-out from its trend over the past two years.

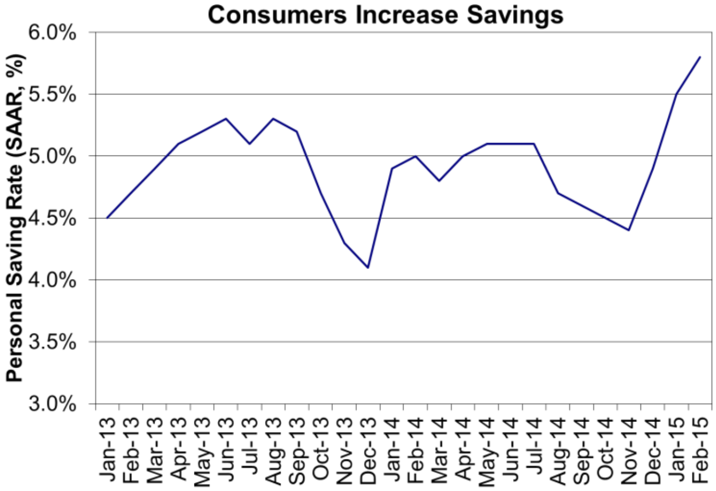
- **Personal income**, adjusted for inflation, edged up 0.2 percent in February following a 0.9 percent jump in the prior month, according to the Bureau of Economic Analysis. Meanwhile, real personal consumption expenditures (PCE) ticked down 0.1 percent. While real goods spending fell 0.4 percent, presaged by an earlier report of soft retail sales, real services spending disappointed, rising just 0.1 percent against expectations of a large gain in utility spending amid very cold temperature. The PCE deflator, the Fed's favorite inflation gauge, was up 0.2 percent from January and 0.3 percent from a year ago. Excluding food and energy, core prices edged up 0.1 percent in February, rising 1.4 percent year over year.

- **The Conference Board Consumer Confidence Index** rebounded to 101.3 in March from 98.8 in February but remained below the eight-year high reading reached in January. The rebound in the headline index was solely a result of the gain in the expectations component; the present situation component fell slightly further.

- **The Institute for Supply Management (ISM) Manufacturing Index** fell 1.4 points to 51.5 in March (any reading above 50 indicates expansion in the sector). The details were weaker across the board. Notably, new export orders remain in contractionary territory for the third consecutive month.

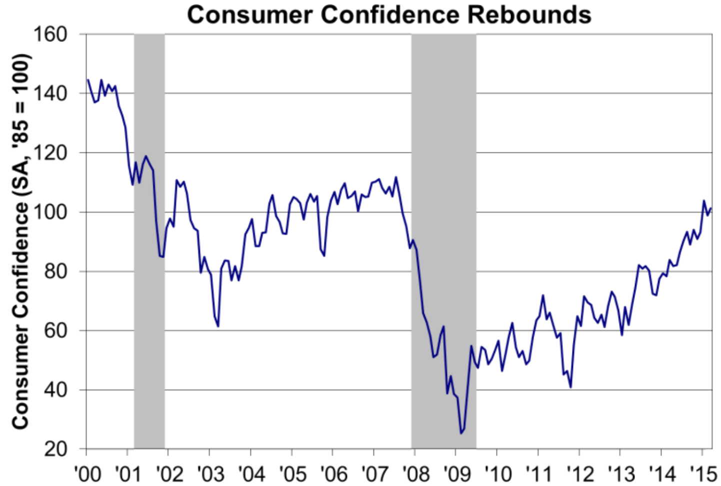
- **The U.S. trade deficit** narrowed by $7.2 billion to a six-year low of $35.4 billion in February, according to the Census Bureau, as both exports and imports plunged.

Consumers Increase Savings



Source: Bureau of Economic Analysis

Consumer Confidence Rebounds



Source: Conference Board

Housing: A First Look at the Spring Selling Season

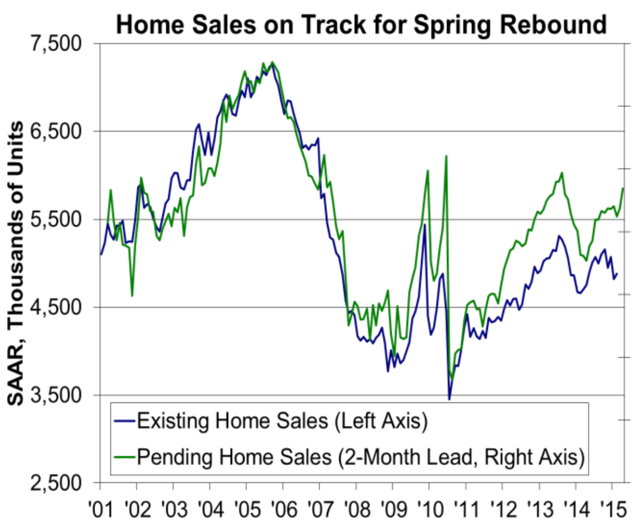
This week's housing data were upbeat, particularly for the home sales outlook this spring. Pending home sales, a leading indicator of existing home sales, jumped in February to the highest level since the summer of 2013, before the "taper tantrum" led to a surge in mortgage rates that restrained home sales. Following a pullback in February, purchase mortgage applications, another leading indicator of home sales, rebounded sharply in the second half of March, approaching the highs witnessed in January. We expect this to transition into a pickup in sales activity this spring. Stronger income growth and continued low mortgage rates are expected to help boost home sales through the summer. The contract interest rate for 30-year fixed-rate mortgages ticked up just one basis point to 3.70 percent this week, according to Freddie Mac. Not all was rosy, however, as February featured the largest monthly drop in private single-family residential construction spending since 2010, with bad weather explaining only part of the weakness. However, we expect this pullback to be transitory. The acceleration in February new home sales reported last week, if sustained, should prompt builders to respond with more housing starts in coming months.

- **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, rose 3.1 percent in February to the highest reading since June 2013. The index is up 12.0 percent from February 2014, with growth in the Midwest and West regions leading the way.

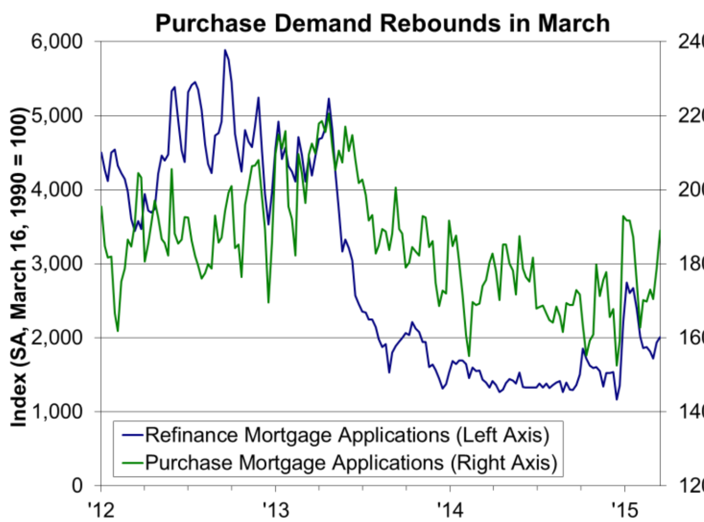
- **Private residential construction spending** declined 0.2 percent in February, weighed down by a 1.4 percent drop in spending on private single-family construction, according to the Census Bureau. Private multifamily construction spending increased 4.1 percent during the month. From a year ago, single-family construction spending is up 10.5 percent, compared to a 31.0 percent jump in multifamily spending.

- **The S&P/Case-Shiller composite 20-city home price index** (not seasonally adjusted) was flat in the three months ending in January following a 0.1 percent monthly increase in the prior period. Prices are up 4.6 percent from a year ago—the fastest annual appreciation since September, but down from a peak of 13.8 percent recorded in November 2013. All 20 cities registered year-over-year appreciation in January, ranging from 1.3 percent in Washington, D.C. to 8.4 percent in Denver.

- **Mortgage applications** increased for a second straight week, rising 4.6 percent in the week ending March 27, according to the Mortgage Bankers Association. Both purchase and refinance applications rose during the week, increasing 5.7 percent and 3.9 percent, respectively. The contract interest rate for 30-year fixed-rate mortgages reported in the survey ticked down one basis point to a seven-week low of 3.89 percent.



Source: National Association of REALTORS®



Source: Mortgage Bankers Association

Brian Hughes-Cromwick and Orawin T. Velz
Economic and Strategic Research Group
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