



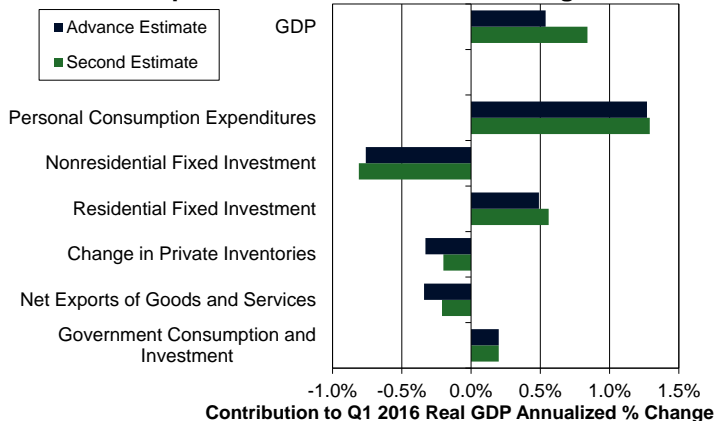
Weekly Note – May 27, 2016

Economics: Q1 Growth Revised from Anemic to Sluggish

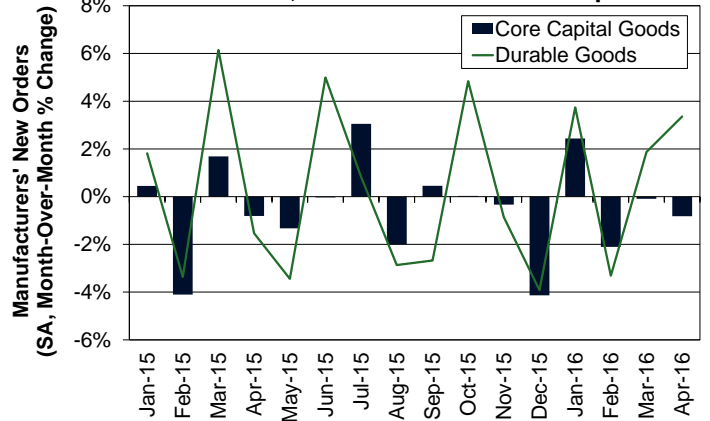
The second estimate of economic growth for the first quarter was better than initially thought, but not enough to celebrate. Even after the upward revision to the quarter, the recent trend of sluggish economic growth to start the year continued as first quarter growth has been below 1.0 percent for three straight years. Inventories and net exports proved to be smaller drags than initially estimated. The housing sector has started to flex its economic muscle in 2016, as its contribution to growth was upgraded further for the first quarter. Business fixed investment saw the only negative revision, and posted the largest decrease of the expansion. Business investment has not contributed to growth in two quarters. One of the reasons for the decline in investment is businesses are struggling to be profitable. Corporate profits declined 5.7 percent from a year ago, marking the third consecutive annual fall. The pace of decline did moderate from the double-digit drop in Q4 2015, which is a rare occurrence when not in recession. Consumers, whose spending continues to be the main driver of economic growth, have a much rosier view of their economic situation, as a survey of their sentiment rose to the highest level since last June. In addition, consumers' sentiment towards current economic conditions has not been this positive since January 2007. The outlook for manufacturing remains subdued, as April's rise in the headline durable goods orders hid underlying weakness for the sector. The volatile non-defense aircraft orders jumped by the largest amount in six months, pushing the headline number upward. In contrast, core capital goods orders, a leading indicator for business fixed investment in equipment, fell for the fifth time in the last six months. Manufacturers are still facing headwinds from the strong dollar and weak global growth, although the dollar has weakened some recently and global concerns have calmed slightly.

- **Gross domestic product (GDP)**, adjusted for inflation, grew 0.8 percent annualized in Q1 2016, according to the second estimate from the Bureau of Economic Analysis (BEA). The 0.3 percentage point upward revision was mainly due to smaller decreases in inventories and net exports than previously estimated. The contribution to growth for both were revised upwards 0.13 percentage points. Residential fixed investment and personal consumption were also upgraded slightly. The drag from non-residential fixed investment was larger than initially estimated and the contribution from government spending was unchanged. Corporate profits posted a 1.4 percent annualized quarterly rise for the first quarter, ending a two quarter stretch of decline.
- **The University of Michigan Consumer Sentiment Index** jumped 5.7 points in the final May reading to 94.7. The current conditions component posted the largest increase this year and the expectations component saw the largest jump since May 2013.
- **Durable goods orders** rose 3.4 percent in April, driven by the 64.9 percent rise in non-defense aircraft, according to the Census Bureau. Core capital goods (which exclude aircraft and defense items) shipments ended a six-month stretch of decline, edging up 0.3 percent. Core shipments in March were revised from flat to a 0.3 percent drop. Core orders fell 0.8 percent in April. The decline in March was revised upwards 0.7 percentage points to 0.1 percent.
- **Initial claims for unemployment insurance** decreased by 10,000 to 268,000 in the week ending May 21, according to the Department of Labor, marking the second consecutive fall after rising for three weeks to reach the highest level since late February 2015. The four-week moving average increased by 2,750 to 278,500, the highest level since the end of January 2016.

Smaller Drags from Inventories and Net Exports Push Economic Growth Higher



Nondefense Aircraft Orders Lift Durable Goods, While Core Orders Slump



Source: Bureau of Economic Analysis

Source: Census Bureau

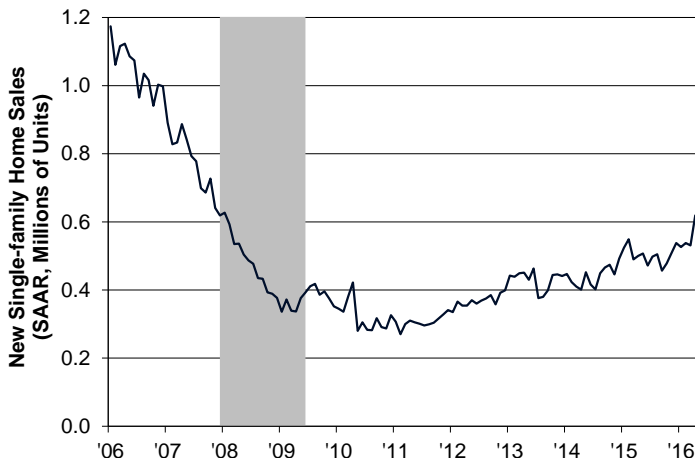


Housing: Good Spring and Likely a Better Summer

This week's housing data were upbeat. New home sales, which record contract signings of new homes, posted the biggest jump in April since January 1992 and reached the strongest pace since January 2008. New home sales data are often volatile and subject to large revisions. However, if this positive development persists, it will bode well for single-family building activity and home builders' confidence, which held steady in May for the fourth consecutive month. The existing home sales market also received bullish news, as pending home sales (or contract signings on existing homes) rose for the third consecutive month in April, jumping to the highest level in more than a decade. Another forward-looking indicator for home sales — purchase mortgage applications — reinforces the recent trend in pending home sales, as average monthly applications rose 4.0 percent in April for the second consecutive month. Home price appreciation strengthened, with the FHFA purchase-only house price index rising sizably in March and posting the biggest annual gain since last October. A blemish this week is the six-basis-point rise in the average 30-year fixed mortgage rate to 3.64 percent, according to Freddie Mac.

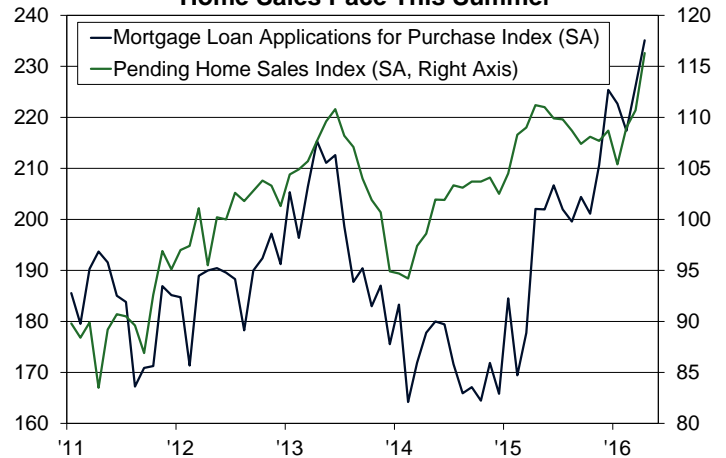
- **New single-family home sales** surged 16.6 percent in April to 619,000 annualized units, according to the Census Bureau. Sales soared 52.8 percent in the Northeast and also posted double-digit gains in the South and the West. The Midwest saw a drop for the third time over the last four months. Sales in the prior three months were revised higher by 44,000 units. Year-to-date sales through April were 10.1 percent higher than sales over the same period in 2015. The inventory of new homes for sale (seasonally adjusted) was little changed during the month, and thus the strong sales pace pushed the months' supply down to 4.7 months, the lowest reading since February 2015. The median price, which does not control for changes in the mix of sales, was up 9.7 percent from a year ago, sending the level to a new record high. The share of home sales priced under \$150,000 fell to 2.0 percent, the lowest share since record keeping began in 2004.
- **The FHFA purchase-only house price index**, reported on a seasonally adjusted basis, rose 0.7 percent in March. On a year-over-year basis, home prices rose 6.1 percent.
- **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 5.1 percent in April. Pending sales increased strongly in the West and the South, rose moderately in the Northeast, and dropped modestly in the Midwest.
- **Mortgage applications** increased 2.3 percent for the week ending May 20, according to the Mortgage Bankers Association. Purchase applications rose 4.8 percent, largely reversing the decline in the prior week. Refinance applications edged up 0.4 percent, marking the third consecutive increase. The average contract interest rate for 30-year fixed-rate mortgages increased three basis points to 3.85 percent.

New Home Sales Jump to Expansion High



Source: Census Bureau

Leading Indicators Suggest Strong Existing Home Sales Pace This Summer



Source: The National Association of REALTORS®, Mortgage Bankers Association

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