Economics: The Least Bad Economy

A small sample of domestic economic data released this week were broadly upbeat and supportive of our economic growth outlook averaging approximately 3.0 percent annualized in the second half of this year. Following last week's solid September jobs report, the August JOLTS data showed job openings reached the highest level since January 2001 (though a retreat in hiring during the month warrants monitoring), while initial jobless claims in early October held below 300,000 for the fourth consecutive week. However, this week's most pressing economic data came from abroad as a pair of reports from Germany—the largest economy in the European Union—showed a sharp contraction in industrial production and exports in August. Evidence of further slowdown in the fragile European recovery—particularly from the core economies and not the peripheries—sparked a rally in U.S. Treasuries, pushing the 10-year yield down to 2.31 percent on Friday morning. Commodities prices sank, with the price of Brent Crude oil falling below $90 per barrel to the lowest level since June 2012 amid a sharp rally in the dollar. This suggests the year-over-year decline in import prices in September (led by a 6.6 percent annual drop in prices of petroleum imports) will likely continue at least into October. Equities also took a beating on the week with the S&P 500 sinking to a one-month low at the time of this writing. Somewhat presciently, members of the Federal Open Market Committee (FOMC) warned that "the persistent shortfall in economic growth and inflation in the euro area could lead to a further appreciation of the dollar and have adverse effects on the U.S. external sector" and that "appreciation of the dollar might also tend to slow the gradual increase in inflation towards the FOMC's 2 percent goal" in the minutes to the September 16-17 meeting released on Wednesday. Alas, considering the dismal picture in global economic activity, perhaps the sub-par economic expansion under way here in the U.S. isn't so bad after all.

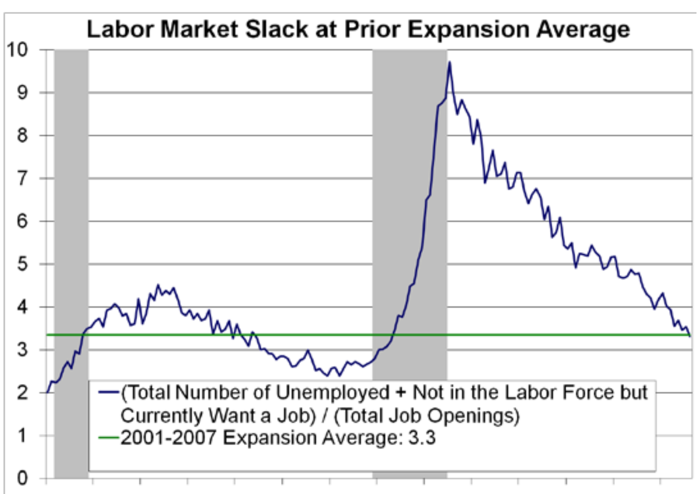
- **The Job Openings and Labor Turnover Survey (JOLTS)** showed that job openings rose 5.0 percent in August 2014 to a new recovery-best 4.84 million, while hires reversed course, declining 6.0 percent to 4.64 million, according to the Bureau of Labor Statistics. Over the past 12 months, job openings and hires are up 23.2 percent and 1.0 percent, respectively.

- **Consumer (nonmortgage) credit outstanding** increased 5.0 percent annualized in August, down from an 8.1 percent jump in July, according to the Federal Reserve Board. Revolving credit outstanding (composed primarily of credit card debt) fell for the first time since February 2014, ticking down 0.3 percent, while nonrevolving debt outstanding (composed of auto and student loans, and other financed big-ticket purchases), which has been the primary driver of debt growth in this cycle, grew 7.0 percent, down from 8.3 percent in July. Over the past year, revolving and nonrevolving consumer credit outstanding increased 3.2 percent and 8.2 percent, respectively, with the former tied for a five-year best.

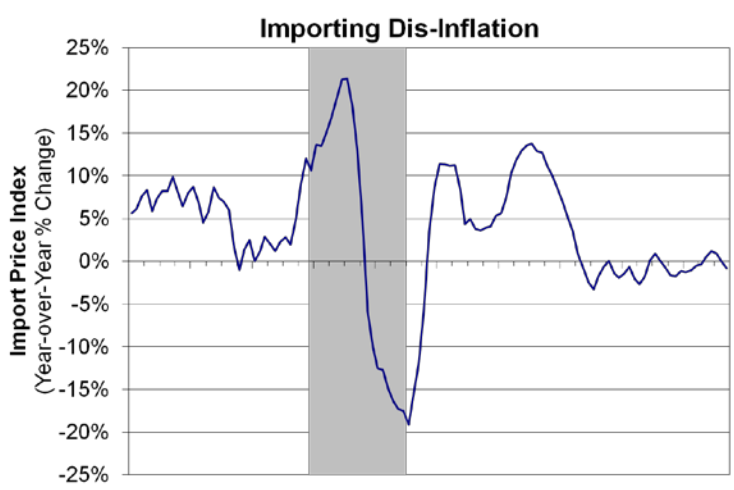
- **Initial claims for unemployment insurance** declined 1,000 to 287,000 in the week ending October 4, according to the Department of Labor. The four-week moving average sank 7,250 to 287,750—the lowest since February 2006.

- **Wholesale inventories** increased 0.7 percent in August—the fastest growth since April of this year—on the strength of both durable and nondurable goods. Year-over-year growth of 7.9 percent is little-changed over the past three months.

- **Import prices** decreased for the third consecutive month in September, driven by the decline in imported fuel prices, falling 0.5 percent on the month and 0.9 percent over the past 12 months.



Source: Bureau of Labor Statistics



Source: Department of Labor

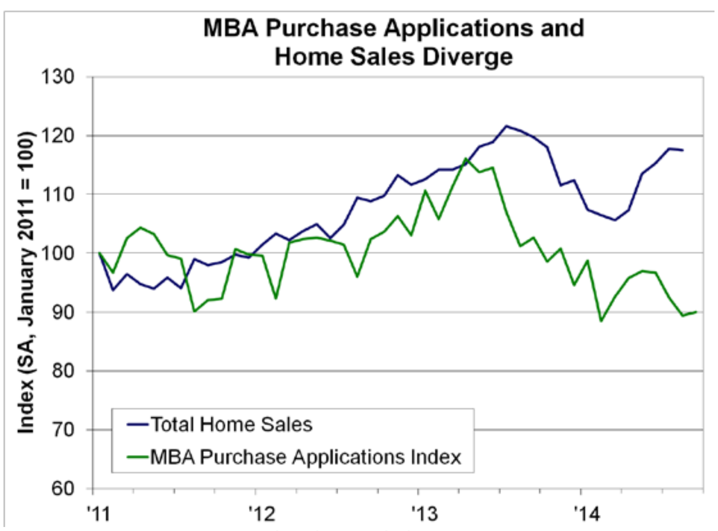
Housing: Reevaluating the MBA Mortgage Application Index

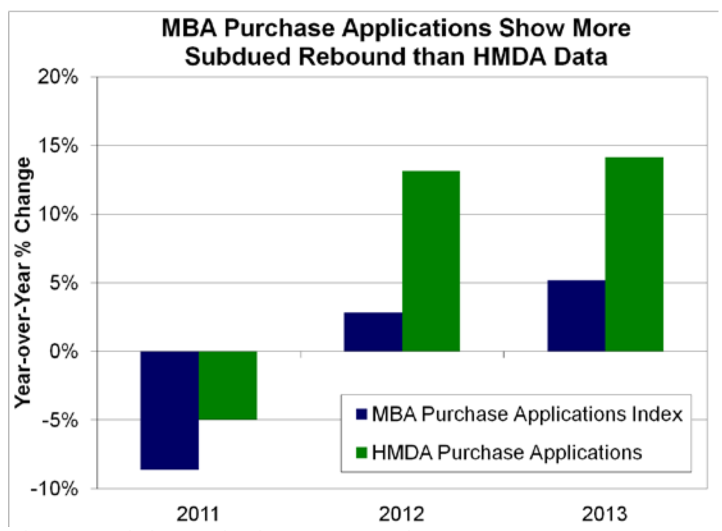
Sparse housing data released this week painted a familiar picture: healthy but steadily moderating annual home price appreciation (nationally and regionally) and sluggish mortgage applications in the face of low mortgage rates (which fell to a one-month low of 4.12 percent this week according to Freddie Mac). Previously in this space we have lamented lackluster mortgage demand as reported by the Mortgage Bankers Association (MBA) while noting a loss of predictive power of purchase mortgage applications on home sales, largely due to the elevated share of homes purchased with cash in the current housing recovery. However, even as cash sales as a share of total home sales have slowly trended lower after peaking in early 2011 (according to data from CoreLogic), the divergence between total home sales and purchase mortgage applications has persisted and even worsened over the past two years. Of note, during the trough of housing activity in early 2014 (following the sharp rise in mortgage rates in mid-2013 and an unseasonably harsh winter), the MBA purchase mortgage applications index declined more than 10.0 percent below the January 2011 level, compared to a 5.0 percent increase in total home sales over the same period. While there may likely be a timing issue between the two series, as the pull-through rate from applications to originations varies over time, we believe it is unlikely to explain this divergence amid a moderating cash sales share.

Last month's release of the 2013 Federal Reserve Home Mortgage Disclosure Act (HMDA) data—generally viewed as the most reliable annual benchmark of mortgage activity—includes data on mortgage applications, allowing a comparison of the purchase applications trends between the two sources. While MBA and HMDA purchase applications showed the same direction in year-over-year changes over the past several years, the MBA data showed a more pronounced drop and less pronounced gains. One plausible explanation for the difference in the magnitude of the year-over-year changes could be that shifts in the mortgage industry may have skewed the representativeness of the MBA survey. In recent years, the share of mortgage originations from the top 10 largest banks has been declining. Recognizing this trend, the MBA increased the sample size of its survey substantially since 2011, but many small lenders still may not participate. In addition, the changing structure of the market as mortgage activity shifts away from traditional banks to less regulated mortgage banks also could pose an issue for the MBA survey, which focuses on the retail channel rather the broker/wholesale channel. We continue to view the MBA purchase mortgage applications as a useful leading indicator of home sales but exercise caution in projecting their trend to our near-term home sales outlook.

➢ **The CoreLogic national home price index**, a repeat sales measure, increased 0.3 percent in August on a non-seasonally adjusted basis, down from a 0.8 percent gain in July. Year-over-year, prices were up 6.5 percent in August, down from 6.8 percent in July and a recent peak of 11.9 percent in October 2013. Though moderating, home price gains remained broad-based, as no state recorded a year-over-year decline August.

➢ **Mortgage applications** rose 3.8 percent in the week ending October 3, according to the MBA. Purchase applications rose 2.4 percent to a three-month best, while refinance applications increased 5.0 percent amid a three-basis-point decline in the contract interest rate for 30-year fixed-rate mortgages to 4.30 percent—a four-week low.





Source: Census Bureau, National Association of REALTORS®, Mortgage Bankers Association, Federal Reserve Board

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