

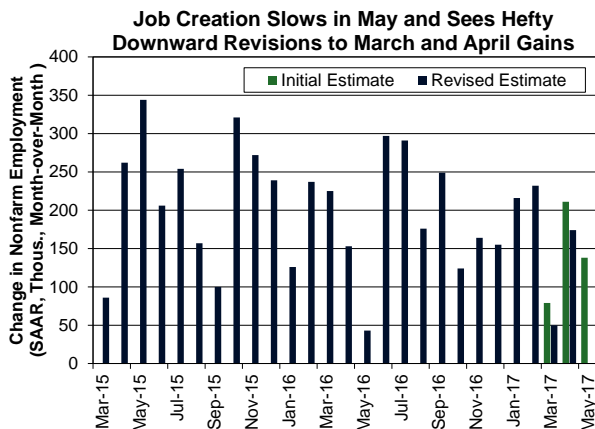


Weekly Note – June 2, 2017

Economics: Labor Market Shows Signs of Slowing

This week's economic news featured a May jobs report showing that the labor market has lost some momentum. The headline payroll gain surprised to the downside and came on top of sizable downward revisions to the prior two months. Notably, the three-month moving average gain has steadily declined from 201,000 in February to 121,000 in May. Results from the household survey also provided little encouragement. The drop in the unemployment rate to the lowest level in 16 years was caused by a large decrease in the labor force that outpaced a decline in household employment, and the labor force participation rate fell to the lowest level this year. The report begins to raise questions about the recent hawkish tone of Fed officials, who have hinted at potentially more rate hikes and a start of the process of balance-sheet shrinking this year. We believe that the jobs report does not meet the high bar required for the Fed to stand pat on the fed funds rate at its June 13-14 meeting. Other news this week featured another rise in consumer spending in April, on the heels of an upward revision that pushed March's gain to the strongest in six months. Inflation pressures have eased over the past two months, as annual growth in the Fed's favored measure of inflation, the Personal Consumption Expenditures deflator, slowed in April to the weakest pace this year. The trade deficit widened in April as imports rose and exports fell. The manufacturing sector recorded its ninth consecutive month of expansion in May, according to a survey of purchasing managers. Consumer confidence fell further in May from a 16-year high reached in March, marking the largest back-to-back declines since late 2015. Finally, auto sales decreased in May, reversing most of April's gain.

- **Nonfarm payroll employment** expanded by 138,000 in May, according to the Bureau of Labor Statistics. The three-month average gain slowed to 121,000 from 152,000 in April. Job gains in the prior two months were revised downward by 66,000 on net. The unemployment rate fell one-tenth to 4.3 percent, and the labor force participation rate fell two-tenths to 62.7 percent. The broadest measure of the unemployment rate, the U-6 rate, fell two-tenths to 8.4 percent. The average workweek was unchanged at 34.4 hours. Average hourly earnings rose 0.2 percent from April and 2.5 percent from a year ago.
- **Personal income**, adjusted for inflation, increased 0.2 percent in April, according to the Bureau of Economic Analysis. Real personal consumption expenditures (PCE) also improved 0.2 percent, following a 0.5 percent increase the prior month. The personal saving rate was unchanged at 5.3 percent for the third consecutive month. Both the PCE and core (excluding food and energy) PCE deflators rose 0.2 percent from March. From a year ago, the PCE deflator increased 1.7 percent while the core PCE rose 1.5 percent, the weakest gain since December 2015.
- **The U.S. trade deficit** widened by \$2.3 billion to \$47.6 billion in April, according to the Census Bureau. Imports rose 0.8 percent and exports fell 0.3 percent. The inflation-adjusted goods deficit, used in the calculation of net exports in the gross domestic product estimate, widened by \$2.9 billion to \$63.5 billion.
- **Nonfarm business productivity** fell 0.6 percent in Q1 2017, unchanged from the initial estimate, according to the Bureau of Labor Statistics. Compensation increased 2.4 percent, and unit labor costs rose 3.0 percent.
- **The Institute for Supply Management (ISM) Manufacturing Index** edged up 0.1 points to 54.9 in May (any reading above 50 indicates expansion).
- **The Conference Board Consumer Confidence Index** fell 1.5 points to 117.9 in May, as a second consecutive drop in the expectations component outweighed a slight gain in the current conditions component.
- **Light vehicle sales** fell 1.3 percent to a 16.7 million annualized rate in May, according to Autodata.



Source: Bureau of Labor Statistics



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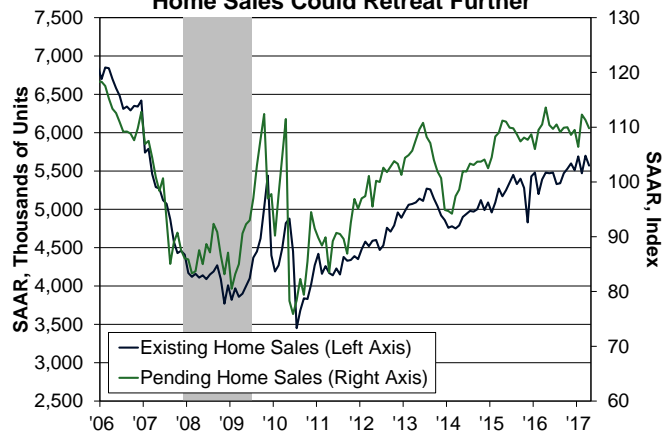


Housing: Losing Steam after a Solid First Quarter

This week's news is in line with other recent data on housing starts and home sales from the beginning of the second quarter. Pending home sales fell in April for the second consecutive month, posting the first year-over-year drop since December 2016 and the largest annual decline since June 2014. The report suggests that existing home sales, which pulled back in April from the expansion high in March, will likely weaken further in the near term. Recent data on pending home sales are at odds with another leading indicator of home sales—purchase mortgage applications—which increased during March and April. However, more timely weekly applications data were bearish, showing that purchase mortgage demand fell during the last week of May for the third consecutive week despite declining mortgage rates. Mortgage rates fell further during the first week of June, according to Freddie Mac, with the average rate for 30-year fixed-rate mortgages ticking down one basis point to 3.94 percent. Supply is extremely lean in the existing home market, with the number of homes for sale posting year-over-year declines for nearly two years. Tight inventory has been a headwind for home sales, but it continues to be a tailwind for home prices. The Case-Shiller National House Price Index posted the largest annual gain in March since June 2014. The index, which had already surpassed its pre-recession high in December, has recorded steadily strengthening annual increases since June. Lastly, spending on new construction rose in April, as spending on new single-family structures outweighed the first drop in the multifamily segment in four months. However, the increase in new construction spending was the smallest monthly gain this year. Overall, this week's reports support our forecast that growth in real residential investment, which includes construction spending and broker commissions on home sales, will moderate significantly this quarter after jumping 13.7 percent annualized during the first quarter.

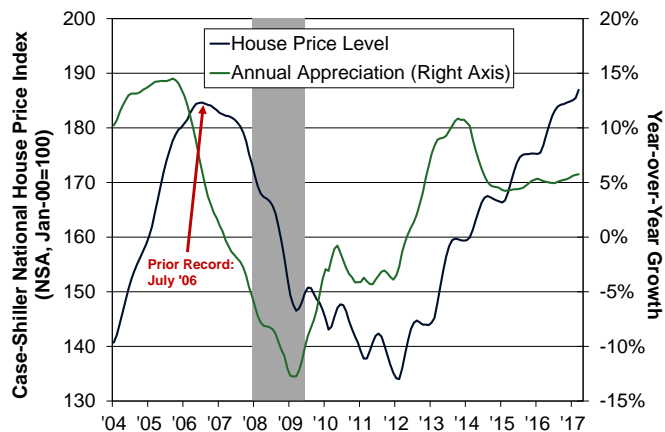
- **Private residential construction spending** edged down 0.7 percent in April, according to the Census Bureau. The weakness came entirely from the volatile home improvement component, as spending on new construction rose 0.6 percent, the smallest increase since December. New single-family construction spending, which has risen every month since October, increased 0.8 percent, while spending on new multifamily construction ticked down 0.2 percent. Spending on home improvement declined 2.9 percent. From a year ago, new single-family and multifamily construction spending rose 7.9 percent and 10.2 percent, respectively.
- **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, fell 1.3 percent in April. Pending sales fell in every region except the West. The index fell 3.3 percent from last April, with every region experiencing annual declines.
- **The S&P/Case-Shiller National Home Price Index** (not seasonally adjusted) rose 0.8 percent in March. From a year ago, the index increased 5.8 percent.
- **Mortgage applications** dropped 3.4 percent for the week ending May 26 as mortgage rates held steady, according to the Mortgage Bankers Association. Purchase applications fell for the third straight week, declining 1.4 percent. Refinance applications fell 5.6 percent following a 10.5 percent jump in the prior week. The average rate for 30-year fixed-rate mortgages was unchanged at 4.17 percent, which was the lowest level since November. For all of May, purchase applications edged up 0.7 percent, marking the third consecutive monthly gain. Meanwhile, refinance applications increased 2.4 percent in May following a 3.2 percent drop in the prior month.

Pending Sales Fall Again, Suggesting Existing Home Sales Could Retreat Further



Source: The National Association of REALTORS®

Annual Home Price Gain Strengthens



Source: Standard and Poor's

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