Economics: The Elephant in the Room

With most of the short week occupied by generally upbeat economic data, Friday's disappointing jobs report was a mild surprise. Job growth slipped to an eight-month worst, and broke a six-month streak of monthly gains of at least 200,000. A slip in the labor force participation rate was also a letdown. In fact, the number of unemployed persons dropping from the labor force has outpaced those finding work for nearly all of the current economic recovery. However, we are hesitant to let one sub-par jobs report derail our expectation for a relatively strong second half, especially when other incoming data such as purchasing manager employment indices and initial jobless claims are at odds with the report. Furthermore, a surge in vehicle sales in August and continuing measured improvement in the trade deficit were positive for current quarter GDP growth, supporting our view of approximately 3.0 percent growth in the second half of the year.

- **Nonfarm payroll employment** rose 142,000 in August while downward revisions to the prior two months totaling 28,000 jobs pushed the average monthly gain over the last three months down to 207,000 from 245,000. Average hourly earnings ticked up 0.2 percent from July 2014 and 2.1 percent from August 2013. Average hours worked remained flat. The separate household survey showed a 0.1 percentage point drop in the unemployment rate to 6.1 percent, while the labor force participation rate edged down one tick to 62.8 percent.

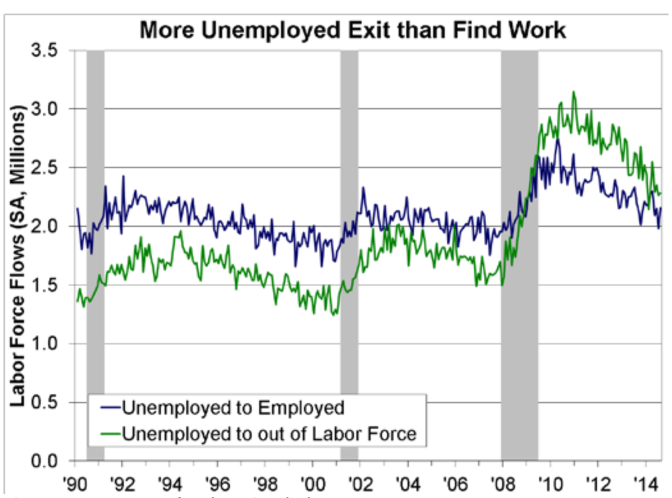
- **The Institute for Supply Management (ISM) Manufacturing Index** increased 1.9 points in August to a nearly four-year high reading of 59.0 (any reading above 50 indicates expansion in the sector), boosted by surging growth in production and the forward-looking new orders components. The employment index ticked down one-tenth from a three-year high, but remained in healthy expansion territory at 58.1. **The ISM Nonmanufacturing Index**, which measures the service sector, rose 0.9 points in August to a nine-year high of 59.6. The business activity component exhibited similar strength, while new orders edged down from a more than eight-year high. The employment index increased 1.1 points to an eight-year best.

- **Factory orders** soared 10.5 percent in July following a 1.5 percent gain in June. Nondurable goods orders, the new data in the report, declined 0.9 percent in July. The previously reported 22.6 percent surge in durable goods orders, boosted by a 317.3 percent jump in civilian aircraft and parts orders due to a sharp increase in Boeing contracts during the month, was unrevised. Nondefense capital goods excluding aircraft—a leading indicator of business investment in equipment in the calculation of GDP—was revised lower to show a 0.7 percent decline.

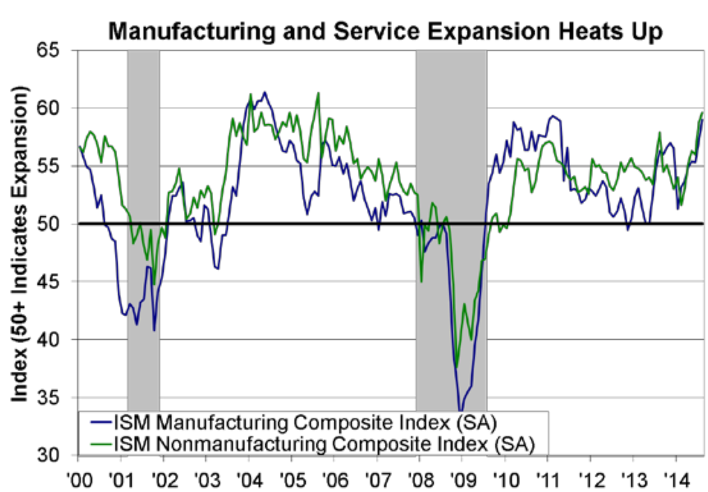
- **Light vehicle sales** jumped 6.4 percent in August to a seasonally adjusted annual rate of 17.5 million—the strongest pace since January 2006. Over the past 12 months, unit vehicle sales are up 10.0 percent.

- **The U.S. trade deficit** narrowed $264 million in July to $40.5 billion as a gain in exports of goods and services outpaced a gain in imports of foreign goods and services. The real goods deficit, used to estimate the trade sector in the calculation of GDP, narrowed for the third consecutive month to the smallest gap recorded this year.

- **Initial claims for unemployment insurance** increased 4,000 to 302,000 in the week ending August 30 according to the Department of Labor. Jobless claims averaged 300,000 in August, a slight uptick from the 298,000 July average.



Source: Bureau of Labor Statistics



Source: Institute for Supply Management

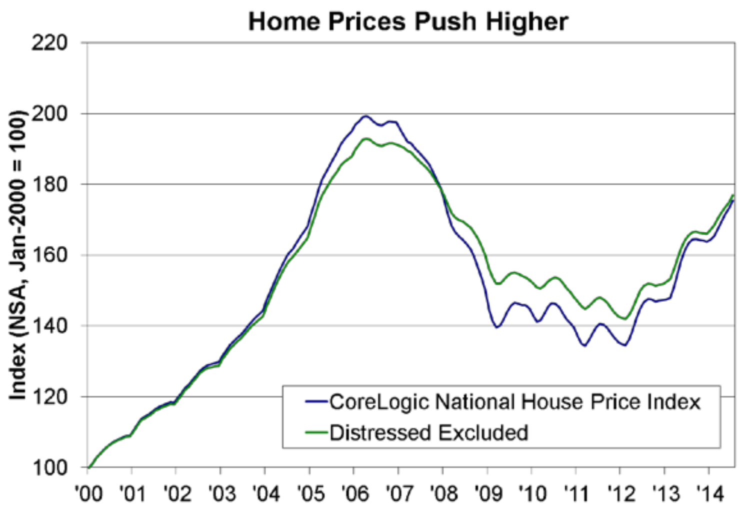
Housing: Residential Investment Poised for a Solid Gain

Limited housing data released this week suggest that residential investment was off to a good start for the third quarter. Construction spending rebounded strongly in July, with broad-based gains across private residential, private nonresidential and public segments. Within the private residential category, the year-over-year gains in single-family and multifamily construction spending continued to diverge, mirroring the trend in housing starts. Furthermore, the pickup in July existing home sales and pending home sales suggests increased brokers' commissions from the prior quarter. Home prices bucked the familiar trend of slowing monthly and annual appreciation in July, as both accelerated during the month, though growth remained below recent peaks. Some aspects of the mortgage market remains bearish, however. Purchase mortgage activity continued to disappoint in the final week of August, reversing most of the modest gain in the prior week, while the third consecutive weekly increase in refinance applications put refi activity at the strongest level since early June. Retail mortgage rates held firm this week at 4.10 percent for the third consecutive week according to Freddie Mac.

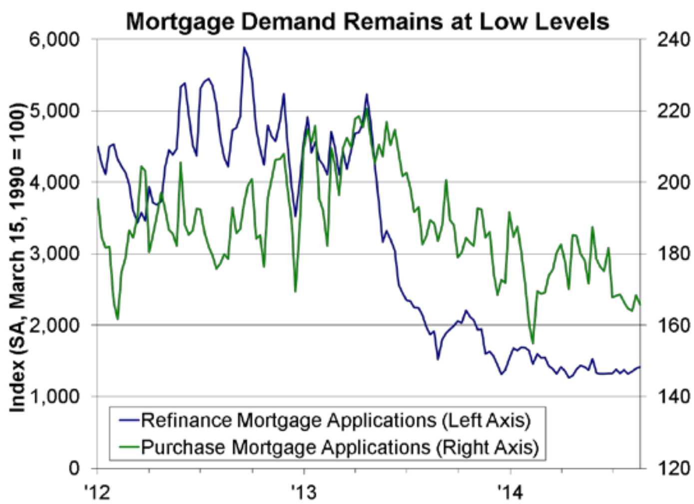
Construction spending increased 1.8 percent in July from an upwardly revised June figure according to the Census Bureau. This marks the third increase in four months, driving spending to a seasonally adjusted annual rate of $981.3 billion—the highest total since December 2008. Private residential construction spending increased for the first time in three months, rising 0.7 percent in July as the single-family, multifamily, and improvements categories all improved. However, year-over-year growth in private single-family construction spending moderated to a 30-month low of 9.4 percent, compared to 41.0 percent annual growth in the private multifamily sector.

➢ **The CoreLogic national home price index**, a repeat sales measure, increased 1.2 percent in July on a non-seasonally adjusted basis, up from 0.9 percent in June. Year-over-year price appreciation increased to 7.4 percent in July from 7.3 percent in June, but remains well below the recent peak of 11.9 percent reached last October.

➢ **Mortgage applications** were flat in the week ending August 29, rising just 0.2 percent according to the Mortgage Bankers Association. A 1.4 percent increase in refinance applications amid a three basis point decline in the contract interest rate for 30-year fixed rate mortgages to 4.25 percent was largely offset by a 1.5 percent decline in purchase mortgage applications—the fourth decline in five weeks.



Source: CoreLogic



Source: Mortgage Bankers Association

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