FannieMae ECONOMIC AND STRATEGIC RESEARCH

ESR Economic and Housing Weekly Note **January 29, 2016**

Economics: Fed Leaves Rates Unchanged Amid Anemic Economic Growth

Data released this week confirmed suspicions that the economy performed poorly in the fourth quarter of 2015. Overall economic growth was anemic in the first estimate, as growth dipped below 1.0 percent for the seventh time during this expansion and the second time in 2015. The strong dollar and global economic slowdown were reflected in the declines in net exports and business fixed investment. Inventories remain a drag, and have not contributed to growth since Q1 2015. However, other sectors remained insulated from the global turmoil, as personal consumption continues to be the main driver of growth and residential fixed investment grew at a healthy pace for the seventh consecutive quarter. Consumers do not seem spooked by the weak fourth quarter, as two measures of their confidence remained elevated in January. The manufacturing sector, on the other hand, showed no signs of escaping its funk, as December durable goods orders posted the largest monthly drop since August of 2014 and the first annual decline since 2009. The statement following the Federal Open Market Committee meeting this week demonstrated the Fed is maintaining its wait-and-see approach amid the current economic uncertainty. The parts of the statement concerning monetary policy were unchanged from December, while the global economy and financial markets returned as sources of potential concern. The pace of future rate hikes "will depend on the economic outlook as informed by incoming data," leaving a March hike in play. The markets remain doubtful, as the fed funds futures indicated only a 16 percent probability of a March increase.

- **Gross domestic product (GDP)**, adjusted for inflation, expanded at a 0.7 percent annual rate in Q4 2015, according to the advance estimate from the Bureau of Economic Analysis (BEA). Real consumer spending continued to drive growth, rising 2.2 percent annualized and contributing 1.5 percentage points to the increase in GDP. Residential fixed investment and the government sector also contributed slightly to growth. Inventories and net exports were drags on growth for the second consecutive quarter. Business fixed investment also detracted slightly from the pace of economic expansion. For all of 2015, growth came in at 1.8 percent (Q4-over-Q4), a moderation from the 2.5 percent pace in 2014 and 2013. The chained personal consumption expenditures (PCE) index edged up 0.4 percent from a year ago, well below the Fed's target of 2.0 percent.

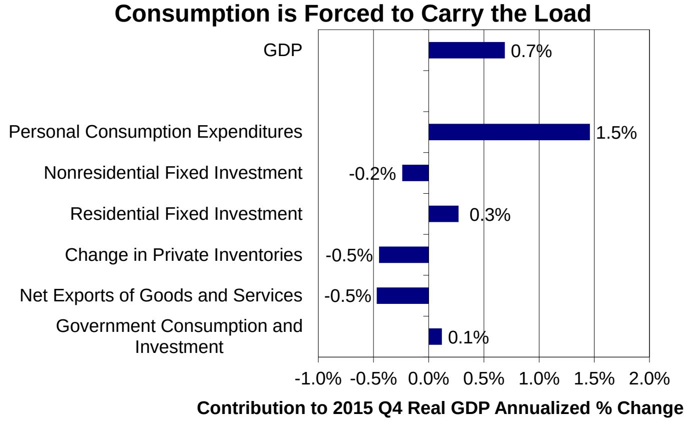
- **The University of Michigan Consumer Sentiment Index** edged down 0.6 points to 92.0 in the final January reading, driven by a drop in the current conditions component, as the expectations component was unchanged. **The Conference Board Consumer Confidence Index** rose 1.8 points to 98.1 in January. An increase in the expectations component drove the improvement, as the present situation component was unchanged from December.

- **Durable goods orders** in December dropped sharply by 5.1 percent from the preceding month, driven by a large decline in nondefense aircraft orders, according to the Census Bureau. Orders excluding transportation fell 1.2 percent, the largest decline since February. Core capital goods orders, which exclude defense and aircraft items and are a leading indicator of business equipment investment, also posted the largest drop since February, decreasing 4.3 percent in December.

- **The Employment Cost Index (ECI)**, a measure of labor compensation, rose 0.6 percent for a second consecutive quarter in Q4 2015, according to the Bureau of Labor Statistics, as the wages and salaries component increased 0.6 percent and benefits rose 0.7 percent. Over the past year, compensation increased 2.0 percent.

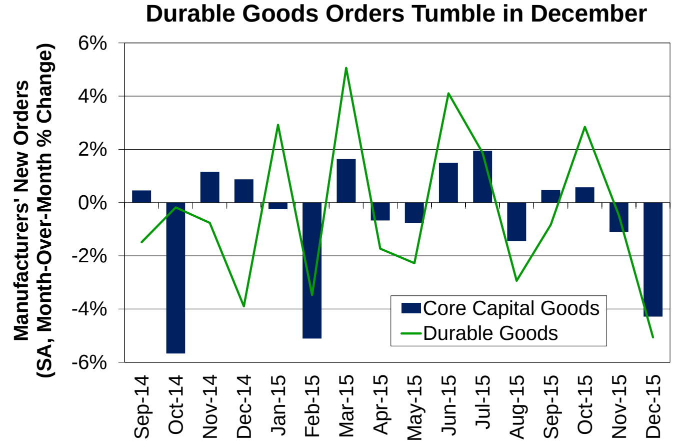
- **Initial claims for unemployment insurance** decreased by 16,000 to 278,000 in the week ending January 23, according to the Department of Labor. The four-week moving average decreased by 2,250 to 283,000.

GDP Growth Anemic in Q4 as Personal Consumption is Forced to Carry the Load



Source: Bureau of Economic Analysis

Durable Goods Orders Tumble in December



Source: Census Bureau

Housing: Stellar December Home Sales Cap the Best Year for the Expansion

This week's housing news was largely upbeat. New home sales, which measure contract signings on new homes, posted the biggest monthly jump in December since August 2014 and the best 2015 annual performance since 2007. Pending home sales, which also record contract signings but for existing homes, were essentially flat in November, but their stabilization following the downtrend between May and November could be considered a good thing. Despite volatile month-to-month movements toward the end of 2015 due to the implementation of new disclosure regulations (TILA-RESPA Integrated Disclosure), existing home sales (reported last week) had the best year since 2006. Together, 2015 total (new and existing) home sales performed the best since 2007. While December pending home sales suggest lukewarm existing home sales at the start of 2016, recent trends from weekly purchase mortgage applications have been much more encouraging, with average readings for December rising 7.0 percent on top of nearly a 5.0 percent gain in November. Mortgage rates remain supportive, as the Freddie Mac survey's fixed mortgage rate fell this week for the fourth consecutive week to 3.79 percent. The two reports on house prices showed continued strong annual appreciation through November, thanks to lean inventories and a declining share of distressed sales. On a downbeat note, the Q4 2015 Housing Vacancy Survey showed the homeownership rate declined from a year ago, sending the 2015 average to the lowest annual reading since 1967. Data on household formation from the survey also disappointed. Following a year-over-year increase of at least 1.45 million households for four consecutive quarters, household growth moderated significantly to less than 500,000, weighed down by the smallest gain in renter households since 2008. However, we are reluctant to draw conclusions regarding household formation trends from just one quarter of this survey, which can produce volatile estimates of household growth.

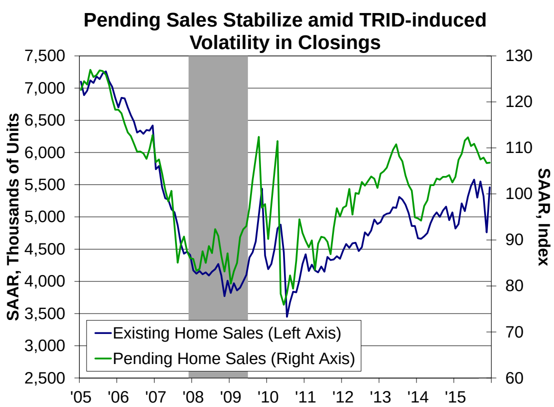
➢ **New single-family home sales** jumped 10.8 percent to 544,000 units annualized in December, with upward revisions totaling 28,000 in the prior three months, according to the Census Bureau. The months' supply dropped to 5.2 months, the lowest since August. The median sale price, which does not control for changes in the mix of sales, fell 4.3 percent from a year ago, marking the third consecutive month of year-over-year declines.

➢ **The National Association of REALTORS® (NAR) pending home sales index** edged up 0.1 percent in December. Pending sales (contract signings) typically lead existing home sales (closings) by one to two months. Sales rose only in the Northeast, which NAR attributed to unseasonably warm weather, and thus a payback in January is likely.

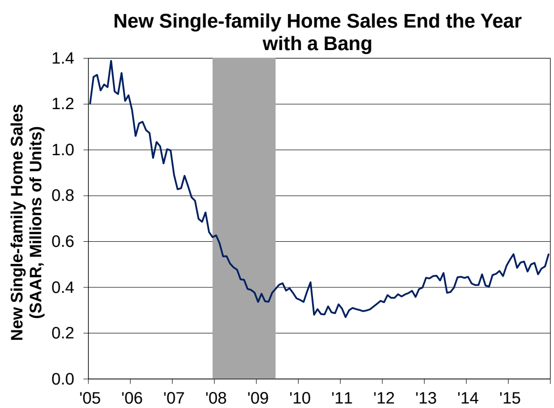
➢ **The Census Bureau Housing Vacancy Survey** for Q4 2015 (not seasonally adjusted) showed that the homeownership rate was 63.8 percent, 0.2 percentage points below the level in Q4 2014. The homeowner and rental vacancy rates were 1.9 percent and 7.0 percent, respectively, both unchanged from a year ago. The number of households rose 462,000 from a year ago, as renter households increased 300,000 and homeowner households rose 162,000.

➢ **The FHFA purchase-only house price index**, which is reported on a seasonally adjusted basis, rose 0.5 percent in November. From a year ago, the index rose 5.9 percent, moderating from 6.1 percent in the prior two months. **The S&P/Case-Schiller national home price index** (not seasonally adjusted) increased 0.1 percent from October and 5.3 percent from November 2014, the strongest year-over-year gain since July 2014.

➢ **Mortgage applications** rose 8.8 percent in the week ending January 22, according to the Mortgage Bankers Association. Purchase applications rose 4.6 percent, following a 1.6 percent decline in the prior week. Refinance applications jumped 11.3 percent, marking the third consecutive week of double-digit increases as the average rate on 30-year fixed-rate mortgages dropped for three straight weeks to 4.02 percent, its lowest level since the end of October.



Source: The National Association of REALTORS®



Source: Census Bureau

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