Economics: Consumer Spending Poised to Triple in Q2

This week’s data were mixed, featuring a positive early look at consumer spending at the end of the second quarter but a softening in industrial production. After declining sharply at the end of last year, retail sales appear to have recovered. Nominal retail sales increased for the fourth consecutive month in June, helping boost second quarter sales to the best showing since the end of 2017. Core sales (excluding autos, building materials, and gasoline), which are an input used to estimate consumer spending for goods in GDP calculations, also posted a solid gain. The continued strength at the end of the quarter pushed the second quarter nominal increase to a 7.5 percent annualized rate, the fastest pace of this expansion. The report supported our view that second quarter real consumer spending growth likely more than tripled the 0.9 percent annualized pace in the first quarter, helping to drive economic growth. On a less positive note, industrial production was unchanged in June. For the second quarter, industrial output declined at a 1.2 percent annualized rate, the second consecutive quarter of declines. While manufacturing output grew in June, the gain failed to recover from the declines seen in the first four months of the year. Mining output remained a bright spot, increasing for the third straight month to reach the highest level since the inception of the series in 1921. The volatile utilities component was responsible for dragging down the headline, with declines in both electricity and natural gas usage despite above-average temperatures in June. The Conference Board Leading Economic Index, a gauge of the economic outlook over the next three to six months, declined in June for the first time since last December, suggesting growth may slow in the second half of the year. According to the press release, the yield spread made a small negative contribution to the index for the first time since late 2007. The 10-year/3-month Treasury spread, which first inverted in late May, has now passed 50 consecutive days of inversion. Finally, import prices declined in June an

- Retail sales rose 0.4 percent for the third straight month in June, according to the Census Bureau. May’s initially reported 0.5 percent gain was revised down a tenth. Sales increased in every major category except at gas stations. Notably, non-store sales continued to grow at the fastest pace in five months. Core retail sales rose 0.7 percent.

- Industrial production, a gauge of output in the manufacturing, utility, and mining sectors, was flat in June, according to the Federal Reserve Board. Manufacturing output advanced 0.4 percent, the second month of increases after falling sharply in April. Manufacturing output of both durable and nondurable goods increased 0.5 percent over the month. Mining output edged up 0.2 percent. Utility output fell sharply by 3.6 percent. Capacity utilization fell six-tenths over the quarter to 78.0 percent, the lowest level in more than a year.

- The Conference Board Leading Economic Index (LEI) declined 0.3 percent in June following a flat reading in May. The weakness was primarily driven by new orders for manufacturing, housing permits, and unemployment insurance claims.

- Import prices declined 0.9 percent in June and 2.0 percent annually. Over the month, there were large declines in the prices of imported food and beverages, industrial supplies, and petroleum products, with the latter declining 6.2 percent. Nonfuel import prices declined 0.3 percent.

Both Core and Headline Retail Sales Finish Out the Second Quarter Strong

[Graph showing retail sales and core retail sales]

Source: Census Bureau

Manufacturing Output Rises After Several Months of Declines While Headline Production Is Flat

[Graph showing industrial production]

Source: Federal Reserve
Housing: Builders Reserve Judgment as Construction Improves

Housing news came in as expected this week with starts declining, mixed permits data, and little movement in home builders’ sentiment. Total housing starts edged down for the second straight month in June as a dip in multifamily starts outweighed an improvement in single-family construction. From a year ago, single-family starts fell for the eighth time in nine months. Over the second quarter, starts were up 4.1 percent, in line with the forecast of 4.4 percent that we made in July. The increase over the quarter was driven entirely by multifamily starts, which posted the largest gain in four years. Meanwhile, single-family building continued to languish, falling for the third time in four quarters and trending down since the end of 2017. The near-term outlook for home building was bleak as total permits continued the downward spiral that started in the spring of 2018. Multifamily permits declined to the lowest level in more than three years, while single-family permits were essentially unchanged. Year to date, single-family permits declined 6.8 percent compared with the same period last year, and multifamily permits were 4.0 percent lower than during the same period the prior year. Despite this apparent weakening in building, home builder confidence in the single-family market was little changed in July as the National Association of Home Builders (NAHB)/Wells Fargo Housing Market Index held in the steady range of low- to mid-60s for the sixth straight month. While solid demand remains, the NAHB press release noted that builders continue to struggle with “labor shortages, a dearth of buildable lots, and rising construction costs.” With issues such as these exacerbating the supply-side challenges, even the recent decline in mortgage rates may not be enough to alleviate affordability concerns for some potential homebuyers still on the fence. According to Freddie Mac, the 30-year fixed mortgage rate increased 6 basis points this week to 3.81 percent. While this is the largest weekly gain since March, rates have stabilized between 3.73 and 3.84 percent for the past seven weeks. Finally, mortgage demand fell for the third straight week last week primarily due to cooling demand for refinance applications after an impressive spike in early June.

- **Housing starts** fell 0.9 percent in June to 1.25 million annualized units, according to the Census Bureau. Single-family starts rose 3.5 percent to 847,000 units, while multifamily starts declined 9.2 percent to 406,000 units. Multifamily permits posted the largest decline since February 2017, falling 16.8 percent to 407,000, while single-family permits edged up only 0.4 percent to 813,000. In the second quarter, single-family starts fell 2.5 percent and multifamily starts rose 20.3 percent.

- The **National Association of Home Builders/Wells Fargo Housing Market Index** rose one point to 65 in July. A reading above 50 indicates that more builders view the single-family market as “good” rather than “poor.” The present sales component, sales in the next six months component, and traffic of prospective buyers component all ticked up above 50 in July. Meanwhile, the largest gain in four years came in the expectations component, which posted the largest gain in four years.

- **Mortgage applications** fell 1.1 percent in the week ending with July 12, according to the Mortgage Bankers Association. A 3.8 percent decline in purchase applications outweighed a 1.5 percent gain in refinance applications. Adjustable rate mortgage applications fell 9.2 percent to the lowest level of the year.

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