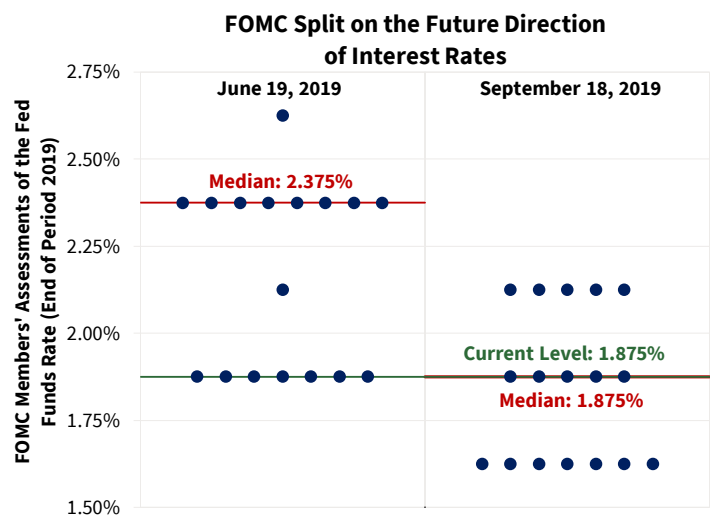


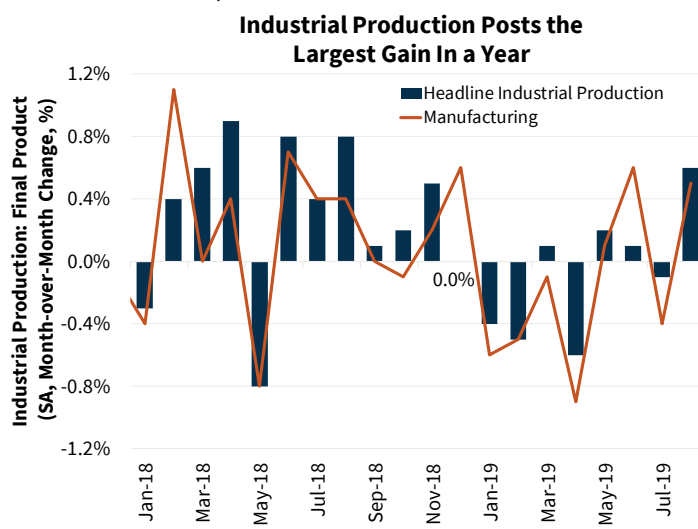
# Economics: Fed Cuts Rates Amid Dissent and Contention

The September meeting of the Federal Open Market Committee (FOMC) took center stage this week as the Fed lowered the federal funds rate 25 basis points to a range of 1.75 percent to 2.00 percent. The FOMC also directed cuts in the interest paid on excess reserves (IOER) and overnight reverse repurchase agreements amid tumult in the repurchase (repo) market, which saw rates jump as high as 10 percent this week due to reserve scarcity. The spike forced the central bank to conduct temporary operations for the first time in a decade, injecting liquidity into the market. However, Chairman Powell stated that these issues “have no implications for the economy or the stance of monetary policy.” The post-meeting statement was little changed from July, continuing to reference a favorable baseline outlook battered by significant downside risks such as “global developments...as well as muted inflation pressures.” While the latest economic projections showed no changes to the inflation paths, 2019 real GDP growth was revised upward one-tenth to 2.2 percent, implying strong growth expectations for the remainder of the year. In the post-meeting press conference, Powell characterized the cut as “insurance against ongoing risks” and to “help keep the U.S. economy strong” despite pressures from geopolitical risks (Brexit), slowing global growth, and ever-volatile trade tensions. Despite these dovish tones, Powell refused to say that the Fed is on an easing path with more accommodation to come, stating multiple times that policy decisions are “data dependent” and will be assessed on a meeting-by-meeting basis. The dot plot, which shows the median forecast of the federal funds rate, showed a large decline from the June projection, a result of the two intervening rate cuts. For 2019 the median rate is now 1.875 percent, implying no more rate cuts this year, though there appears to be a growing division among participants about the best path forward, with seven members seeing an additional rate cut this year and five members seeing appropriate policy being a rate hike before year-end. Contention about the appropriate policy path was evident in the three dissents to the FOMC’s decision to cut rates out of a total of ten voting members. Despite the growing rifts among the committee, the FOMC decision and subsequent actions were consistent with our forecast of one further cut to the fed funds rate this year, in December, as further insurance against downside risks before pausing in 2020. An example of the data on which the Fed’s policy decisions will be based came when industrial production posted the largest monthly gain in a year in August, rising to the highest level since the beginning of 2019. Encouragingly, all three components of the index improved with manufacturing output hitting a five-month high, mining output rising to just shy of the all-time high seen in June, and utility output edging up after a disappointing summer. Additionally, capacity utilization rose for the first time since last November, though it remains well below year-ago levels.

- **Industrial production**, a gauge of output in the manufacturing, utility, and mining sectors, climbed 0.6 percent in August, according to the Federal Reserve Board. All components increased with manufacturing rising 0.5 percent, utilities growing 0.6 percent, and mining increasing 1.4 percent. Capacity utilization rose 0.4 percentage points to 77.9 percent.
- **The Conference Board Leading Economic Index (LEI)**, a gauge of the economic outlook over the next three to six months, was unchanged in August, following a 0.4 percent increase in July and no change in June. In the six-month period ending August 2019, the LEI increased 0.5 percent, about the same rate of growth over the previous six months. Strength in housing permits and credit conditions offset weakness from the manufacturing sector and the interest rate spread.
- **Initial claims for unemployment insurance** rose by 2,000 to 208,000 in the week ending with September 14, according to the Department of Labor. The four-week moving average edged down 750 to 212,250.



Source: Federal Reserve



Source: Federal Reserve

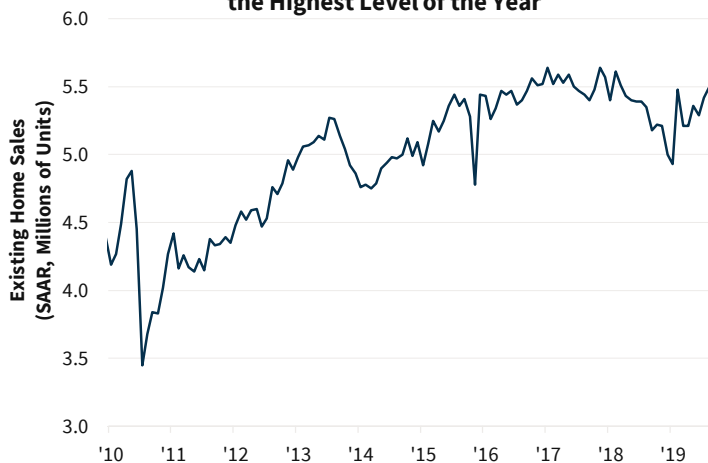


# Housing: Residential Investment Ready for a Rebound

The increase in existing home sales and housing starts in August both point to a stronger than expected rebound in residential fixed investment in the third quarter. Existing home sales rose in August, defying consensus expectations, and increased on an annual basis for the second straight month after more than a year of annual declines. The average pace of existing home sales in July and August exceed our current Q3 forecast, indicating that we may have to revise the quarterly pace of sales modestly upward even though weak purchase mortgage applications in August and increasingly tight inventories of homes available for sale suggest a pullback of sales in September. Housing starts jumped in August to an expansion high, ending three straight months of decline, as multifamily construction rebounded from steep drops in the prior two months and single-family construction rose for the third straight month. Moreover, an index of homebuilder sentiment rose in September to the highest level of the year as builders became increasingly optimistic regarding current sales. The strong pace of starts and the increase in total permits to the highest level since May 2007 may lead us to revise upward our housing starts outlook for the remainder of the year in light of renewed building vigor and builder confidence. The average rate on 30-year, fixed-rate mortgages rose 17 basis points this week to 3.73 percent, according to Freddie Mac, the highest since the beginning of August, but still more than a full percentage point below the latest peak in November 2018. Purchase applications rose last week for the third consecutive week, providing support for sales in Q4 following an expected pullback in September, as low mortgage rates encourage homebuyers back into the market. Finally, household net worth rose in the second quarter, according to the Federal Reserve, driven by gains in stocks and real estate wealth. However, homeowner's equity in real estate as a percent of household real estate value fell in the second quarter for the first time since Q1 2012.

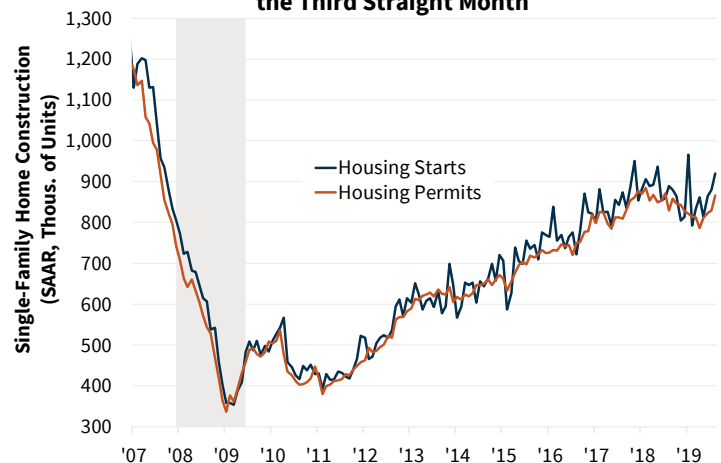
- **Existing home sales** rose 1.3 percent in August to a seasonally adjusted annualized rate (SAAR) of 5.49 million, according to the National Association of REALTORS®. From a year ago, existing sales rose 2.6 percent. Sales rose in every region except the West. The median existing home price increased 4.7 percent from a year ago to \$278,200. The months' supply fell one-tenth to 4.1 months, while total existing homes available for sale fell 2.6 percent from a year ago to 1.86 million.
- **Housing starts** jumped 12.3 percent to 1.36 million (SAAR) in August, according to the Census Bureau. Single-family starts rose 4.4 percent to 919,000 units, and multifamily starts soared 32.8 percent to 445,000 units. Total permits rose 7.7 percent to 1.42 million, as single-family and multifamily permits rose 4.5 percent and 13.3 percent, respectively.
- **The National Association of Home Builders/Wells Fargo Housing Market Index** rose one point to 68 in September. A reading above 50 indicates that more builders view the single-family market as "good" rather than "poor."
- **U.S. household and nonprofit organization net worth**—the value of assets minus liabilities—rose \$1.8 trillion to \$113.5 trillion in the second quarter, according to the Federal Reserve. **Owners' equity in real estate** rose \$40.6 billion to \$18.7 trillion while **owners' equity in real estate as a percentage of household real estate value** fell one-tenth to 64.2 percent. **Single-family mortgage debt outstanding** increased \$79.4 billion to \$11.0 trillion.
- **Mortgage applications** edged down 0.1 percent in the week ending September 13, according to the Mortgage Bankers Association. Refinance applications fell 4.3 percent, while purchase applications increased 6.4 percent.

**Existing Home Sales Increase to the Highest Level of the Year**



Source: National Association of REALTORS®

**Single-Family Starts Rise for the Third Straight Month**



Source: Census Bureau

Ricky Goyette and Rebecca Meeker  
Economic and Strategic Research Group  
September 20, 2019



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