Fannie Mae

Economic and Strategic Research

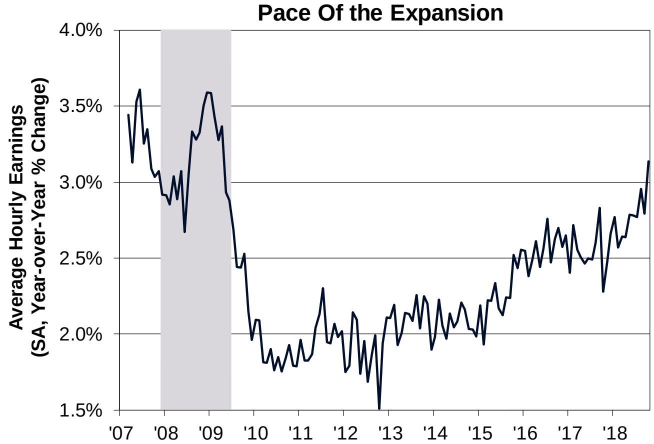
Weekly Note – November 2, 2018

Economics: Strong Job Growth and Wage Gains

In a busy week, the labor market took center stage with an impressive October jobs report, though a portion of the payroll gains likely reflected a recovery from severe weather in September. Leisure and hospitality, a weather-sensitive industry added 42,000 jobs, its strongest monthly growth since last October's recovery from Hurricanes Harvey and Irma. The unemployment rate remained at the lowest level since 1969. Annual growth in average hourly earnings accelerated to an expansion high, a welcome sign for workers, and is unlikely to stoke faster inflation given steady growth in productivity. The report supports our call that the Fed will raise the fed funds rate in December. The annual increase in the Fed's preferred measure of inflation, the personal consumption expenditures (PCE) deflator, decelerated for the second straight month in September, although both the annual gains in the headline and core deflators remained at the Fed's 2.0 percent target. Annually, third quarter productivity growth was unchanged from the second quarter, remaining within the 1.0 percent to 1.4 percent range seen since the end of 2016, while unit labor costs growth moderated to the slowest pace in almost two years. A measure of manufacturing activity indicated the slowest pace of expansion in six months in October. Notably, the new export orders component was the weakest in nearly two years. The trade deficit widened in September and we expect trade to continue to drag on growth this quarter. Auto sales rose in October to the highest level of the year as replacement demand from the hurricanes continued. Finally, consumer confidence rose for the fourth consecutive month in October, increasing to a fresh 18-year high as both the present and expectations components gained ground.

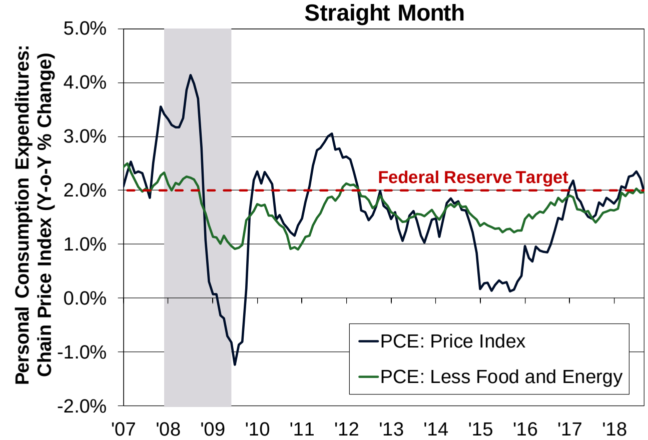
- **Nonfarm payroll employment** expanded by 250,000 in October, according to the Bureau of Labor Statistics. On net, there were no revisions to the prior two months. The unemployment rate was flat at 3.7 percent, while the labor force participation rate rose two-tenths to 62.9 percent. The U6 rate fell one-tenth to 7.4 percent. The average workweek rose a tick to 34.5 hours. Average hourly earnings rose 0.2 percent from September and 3.1 percent from a year ago.
- **Personal income**, adjusted for inflation, edged up 0.1 percent in September, according to the Bureau of Economic Analysis. Real PCE rose 0.3 percent from August and 3.0 percent from a year ago. The saving rate fell two-tenths to 6.2 percent. The PCE deflator rose 0.1 percent, while the core deflator increased 0.2 percent during the month.
- **Nonfarm business productivity** rose 2.2 percent annualized in Q3 2018, according to the Bureau of Labor Statistics. Annually, productivity and compensation grew 1.3 percent and 2.8 percent, respectively, resulting in a 1.5 percent increase in unit labor cost.
- **The U.S. trade deficit** widened by $710 million in September to $54.0 billion, according to the Census Bureau. Exports and imports both rose 1.5 percent. The real goods trade deficit rose $765 million to $87.0 billion.
- **The Conference Board Consumer Confidence Index** improved 2.6 points to 137.9 in October. The present situation component rose for the fifth time in six months. The expectations component increased for the third consecutive month, reaching the highest level in 18 years.
- **Factory orders** rose 0.7 percent in September, while factory shipments rose 0.9 percent, according to the Census Bureau. Nondurable goods orders increased 0.6 percent to the highest level in four years.
- **The ISM Manufacturing Index** fell 2.1 points to 57.7 in October (any reading above 50 indicates expansion). The decrease was driven by every component except supplier deliveries.
- **The Employment Cost Index (ECI)**, a measure of labor compensation, increased 0.8 percent (not annualized) in Q3 2018, according to the Bureau of Labor Statistics. Wages rose 0.9 percent, while benefits fell 0.4 percent.
- **Light vehicle sales** increased 0.7 percent to 17.6 million annualized units in October, according to Autodata.

Annual Wage Growth Jumps to the Fastest Pace Of the Expansion



Source: Bureau of Labor Statistics

Headline Inflation Decelerates for the Second Straight Month



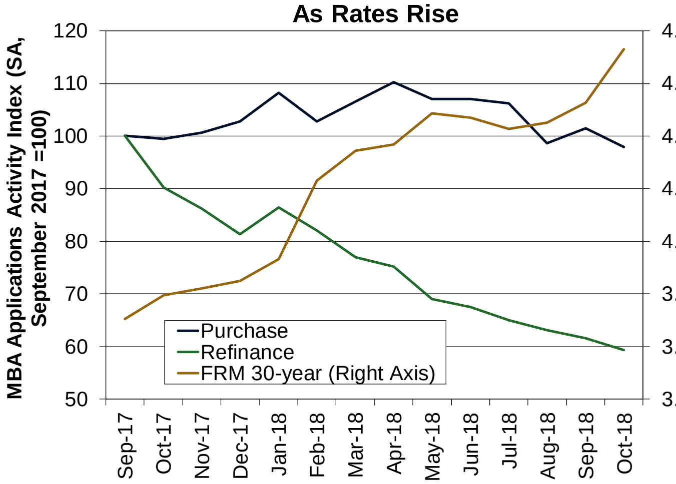
Source: Bureau of Economic Analysis

Housing: Single-Family Construction Growth Weakens

This week's releases covered demand, supply, and house price trends within the housing market, as well as updated information on the homeownership rate. Mortgage rates continued to climb in October and, as of this week, have risen 98 basis points since they began their most recent ascent in October 2017. Amid higher mortgage rates, average monthly mortgage applications for refinance and purchase both fell in October. Since mortgage rates began to climb last year, average monthly mortgage applications for refinancing have fallen substantially, while average monthly mortgage applications for purchase have been steadier, although they have fallen by more than 11 percent since April. House prices continued to climb over the past year, according to the CoreLogic Case-Shiller National Home Price Index, but the pace of year-over-year appreciation slowed for the fourth consecutive month in August. Although the homeownership rate continued to climb from its low in the second quarter of 2016, the Census Bureau reported that the one-tenth increase in the homeownership rate over the third quarter was not statistically significant. Interestingly, the upward trend in the overall homeownership rate since the 2016 trough reflects a rising rate among households with incomes below the median family income, but households with family income at or above the median have higher homeownership rates. Construction spending rose in September, reversing the decline in August as multifamily construction spending jumped and spending on home improvements grew for the third consecutive month. The gains in multifamily and home improvement spending were partially offset by a monthly decrease in single-family construction spending, which has now fallen for four consecutive months at a successively faster pace.

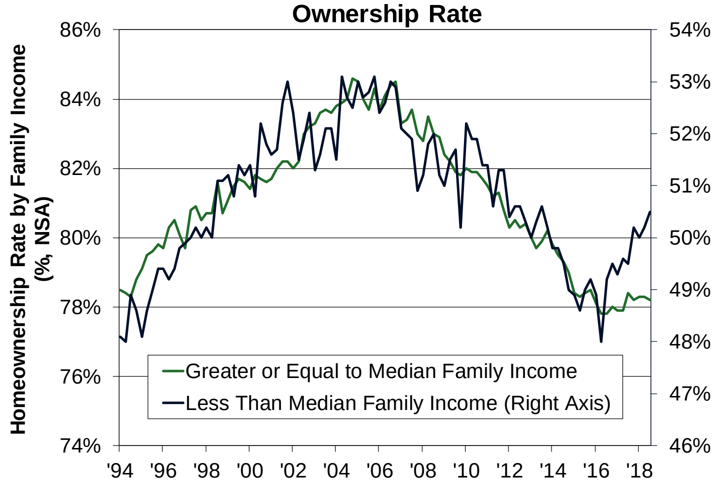
- **The Housing Vacancy Survey (HVS)** for Q3 2018 (not seasonally adjusted) showed that the homeownership rate rose to 64.4 percent, according to the Census Bureau. In the second quarter the homeownership rate was 64.3 percent; in the third quarter of 2017 it was 63.9 percent. Neither the 0.1 percent increase over the third quarter nor the 0.5 percent increase over the past year were considered statistically significant.
- **Private residential construction spending** rose 0.6 percent over the month of September according to the Census Bureau. Multifamily spending rose by 8.7 percent and home improvement spending edged up 0.1 percent, but single-family construction spending fell 0.8 percent. Over the past year, single-family construction spending rose 2.9 percent, multifamily spending increased 7.5 percent, and home improvement spending rose 4.8 percent.
- **S&P CoreLogic Case-Shiller National Home Price Index** (not seasonally adjusted) rose 0.2 percent in August. The annual gain moderated to 5.8 percent, its lowest rate of growth since July 2017.
- **Mortgage applications** fell 2.5 percent for the week ending October 26, according to the Mortgage Bankers Association. Refinance mortgage applications fell by 3.8 percent and purchase applications declined by 1.5 percent. For October, average purchase mortgage applications and average refinance mortgage applications both fell by 3.5 percent. The survey's average 30-year fixed mortgage rate was unchanged at 5.11 percent.

Refinance Applications Collapse As Rates Rise



Source: Mortgage Bankers Association, Freddie Mac

Lower Income Households Drive Up Home Ownership Rate



Source: Census Bureau

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