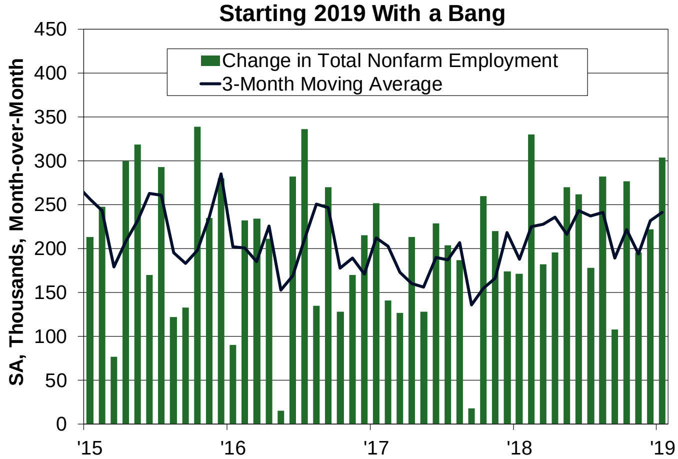
Weekly Note – February 1, 2019

Economics: The Fed Pledges to be Patient with Rate Hikes

This week featured the jobs report, which surprised on the upside for January hiring. Despite large net downward revisions in the prior two months, payroll gains over the past three months averaged 241,000, the strongest increase since last August. Annual wage gains edged down one-tenth from an expansion high but continued a six-month string of growth of at least 3.0 percent. The household survey showed an uptick in the unemployment rate, which partially reflected the government shutdown. The most positive aspect of the household survey was the rise in the labor force participation rate to 63.2 percent, the highest level since September 2013, boosted by an increase in the prime-age rate to 82.6 percent, the best showing since April 2010. The broadest measure of labor underutilization (U-6) jumped 0.5 percentage points to 8.1 percent, the highest level in almost a year, as the number of part-time workers who prefer full-time jobs surged, also likely a temporary result of the shutdown. Another highlight of the week included the Federal Open Market Committee meeting, which suggested a quite dovish turn for the Fed. In the main statement following the meeting, the Fed removed language signaling, "further gradual increases in the target range for the federal funds rate," and added that it "will be patient as it determines what future adjustments" need to be made to the rate. The Fed also removed its assessment, seen in prior statements, that risks to the outlook were "roughly balanced." In a separate statement, the Fed noted that it is prepared to adjust balance sheet normalization in light of economic and financial developments. We continue to believe that the Fed will hike rates only one more time in this tightening cycle, in June. Other news was mixed. The ISM Manufacturing Index rebounded in January but recouped only about half of the prior month's decrease. While two measures of consumer confidence dropped markedly in January, the declines likely reflected the government shutdown, and we expect confidence to rebound in coming months. Lastly, the Employment Cost Index, a measure of labor compensation, showed the annual increase for wages and salaries picked up one-tenth in the final quarter of 2018 to 3.0 percent, an expansion high.

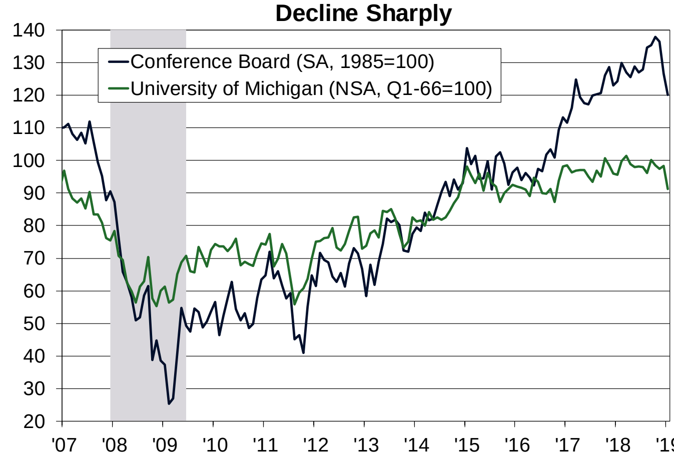
- **Nonfarm payroll employment** rose 304,000 in January, according to the Bureau of Labor Statistics. Downward revisions in the prior two months totaled 70,000. Average hourly earnings rose 0.1 percent from December and 3.2 percent from last January. The unemployment rate rose one-tenth to 4.0 percent.
- **The Employment Cost Index (ECI)** rose 0.7 percent (not annualized) in Q4 2018, according to the Bureau of Labor Statistics. Wages and salaries grew 0.6 percent. Benefits rose 0.7 percent from Q3 and 2.7 percent from Q4 2017.
- **The ISM Manufacturing Index** rose 2.3 points to 56.6 in January (any reading above 50 indicates expansion), following a 4.5 point drop in the prior month. New orders and production sub-components drove the increase.
- **The University of Michigan Consumer Sentiment Index** fell 7.1 points from December to 91.2, the lowest reading since October 2016, in the January final reading. The current economic conditions and the consumer expectations components fell by similar magnitudes. **The Conference Board Consumer Confidence Index** fell 6.4 points to 120.2 in January, marking an 18-month low. The decline reflected a 10.4-point drop in the expectations component to 87.3 and a modest decrease in the present economic conditions component.
- **Initial claims for unemployment insurance** jumped 53,000 from a 49-year low in the prior week to 253,000 in the week ending January 26, according to the Department of Labor. The four-week moving average rose 5,000 to 220,000. The bulk of the increase in claims were in California, likely reflecting a widespread teachers' strike. Increased filing by government contractors was also partially responsible for the rise in claims.

January Hiring Surpasses Expectations, Starting 2019 With a Bang



Source: Bureau of Labor Statistics

Consumer Confidence Measures Decline Sharply



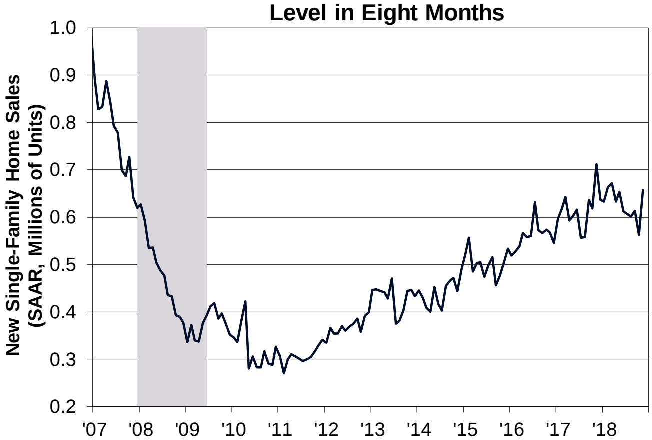
Source: U. of Michigan, Conference Board

Housing: Home Sales Up amid Weak Data Elsewhere

Housing data were mixed this week as new home sales jumped but pending sales declined. New home sales, which are recorded at contract signing, spiked in November after declining 8.3 percent in October. The November gain marks the largest monthly increase since January 1992 to reach the strongest annualized pace in eight months. The rebound likely reflected, in part, a recovery from Hurricane Michael, as sales in the South showed the largest gain. Sales in the prior three months were revised up by 44,000 units, which put year-to-date sales 2.8 percent higher than sales during the same period in 2017. While sales rose more than expected, the median sales price fell to the lowest level since February 2017, offsetting the benefits of higher sales to brokers' commissions and thus residential investment. Pending home sales, which measure contract signings of existing homes and lead closings by one to two months, fell for the third straight month in December and declined for the twelfth consecutive month annually, suggesting existing home sales will likely continue to struggle this quarter after falling every quarter in 2018. In November, private residential construction spending rose for the first time in four months as gains in multifamily and home improvement outweighed a decline in single-family spending. Annually, private residential construction spending fell for the third straight month with single-family spending falling for the first time since August 2011. On a positive note for affordability, annual home price appreciation slowed for the seventh month in November to the slowest pace in two years. In addition, mortgage rates stabilized in January. According to Freddie Mac, the average 30-year fixed mortgage rate edged up 1 basis point to 4.46 percent this week, staying within a tight range of 4.45 to 4.55 percent for the sixth straight week. Finally, both purchase and refinance applications fell last week for the second straight week; however, due to the spikes recorded during the first two weeks of the year, monthly purchase applications for January increased for the third straight month and refinance applications rose during the month for the first time in a year.

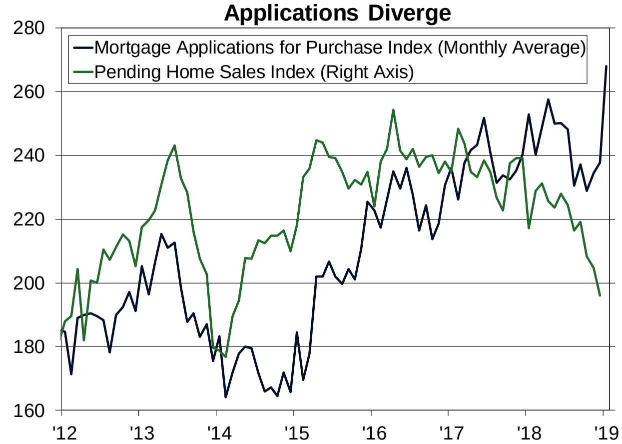
- **New single-family home sales** rose by 16.9 percent in November to a seasonally-adjusted annual rate (SAAR) of 657,000, according to the Census Bureau. Sales rose in every Census region but the West. The for-sale inventory (seasonally adjusted) increased 0.6 percent from October and 14.2 percent from November 2017. The months' supply fell from 7.0 months to 6.0 months, the lowest reading since June. The median price, which is not adjusted for the mix of sales, fell 11.9 percent from a year ago, the largest annual decline since February 2009.
- **The National Association of REALTORS® Pending Home Sales Index** fell 2.2 percent in December. Pending sales rose in the West but dropped in the other three regions. From a year ago, pending sales fell 9.8 percent.
- **Private residential construction spending** rose 3.5 percent in November but fell 1.1 percent annually, according to the Census Bureau. Spending on new single-family building decreased 1.8 percent, spending on multifamily building grew 2.6 percent, and home improvement spending spiked 12.1 percent. From a year ago, single-family construction spending fell 1.0 percent and multifamily spending rose 9.3 percent.
- **S&P CoreLogic Case-Shiller National Home Price Index**, reported on a seasonally-adjusted basis, rose 0.4 percent in November. From a year ago, the index increased 5.2 percent, slowing from October's pace of 5.3 percent.
- **Mortgage applications** declined 3.0 percent for the week ending January 25, according to the Mortgage Bankers Association. Purchase and refinance applications both fell 2.3 percent and 5.5 percent, respectively. The survey's average 30-year fixed mortgage rate rose 1 basis point to 4.76 percent.

New Home Sales Rebound, Reaching Highest Level in Eight Months



Source: Census Bureau

Pending Home Sales and Purchase Applications Diverge



Source: Mortgage Bankers Association, NAR®

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