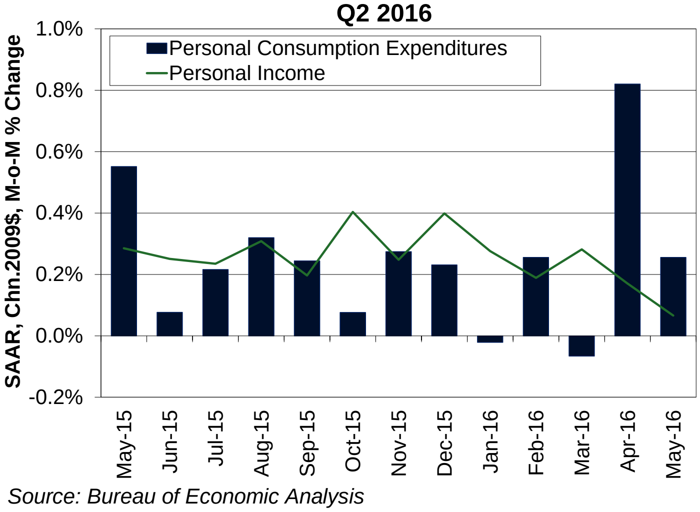
Weekly Note – July 1, 2016

Economics: Resilient Consumers Lead a Growth Rebound

This week's reports highlighted the strength of consumers amid signs of a gradual improvement in manufacturing. A solid gain in May consumer spending, combined with an upward revision that pushed April's increase to the biggest since August 2009, points to a pickup in real consumer spending growth in the second quarter to more than 4.0 percent annualized from the lackluster pace of 1.5 percent in the first quarter. The price index tied to consumer spending, the Fed's favored measure of inflation, showed muted inflation pressure in May. Consumers were much more optimistic in June, with the Conference Board Consumer Confidence Index rising to its highest level since last October. The survey closed before the U.K.'s vote to leave the European Union, however, and therefore it will be interesting to see if consumers will remain upbeat in July. A survey of manufacturing purchasing managers showed activity improved in June for the second consecutive month to the best level in 16 months. Initial jobless claims rose in the latest week, but their trend held steady at very low levels. Overall, this week's data suggest a rebound in economic growth in the second quarter from an anemic first quarter, which would mark the third consecutive year of this phenomenon.

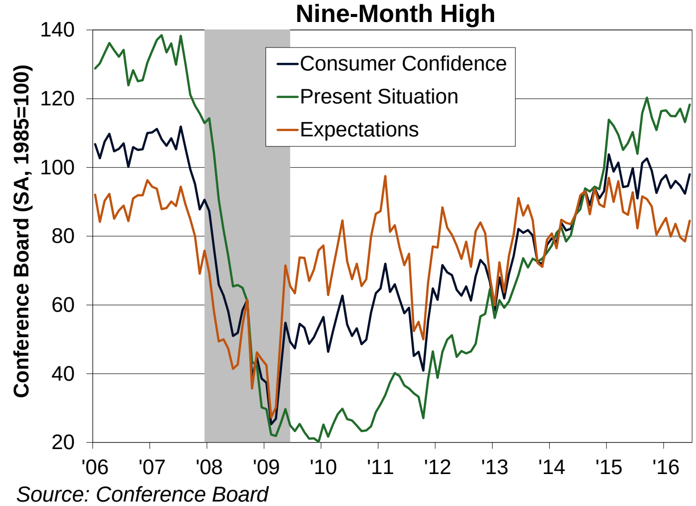
- **Gross domestic product (GDP)**, adjusted for inflation, was revised higher three-tenths to 1.1 percent annualized in Q1 2016, according to the third estimate from the Bureau of Economic Analysis (BEA). Real consumer spending growth was revised down sizably, from 1.9 percent to 1.5 percent. However, upward revisions in net exports and non-residential investment, especially in intellectual property, more than offset weaker consumer spending and residential investment.
- **Personal consumption expenditures (PCE)**, adjusted for inflation, increased 0.3 percent in May, according to the Bureau of Economic Analysis. All three components of spending — on durables, non-durables and services — showed gains for the second consecutive month, albeit slowing from the prior month's outsized increases. Real personal income edged up 0.1 percent in May. Both the headline and the core price indices (excluding food and energy) rose 0.2 percent. On a year-over-year basis, the PCE deflator moderated from 1.1 percent in April to 0.9 percent in May, while the core deflator held steady at 1.6 percent.
- **The Conference Board Consumer Confidence Index** jumped 5.6 points to 98 in June. The present situation index increased 5.1 points to reach 118.3, the highest reading since last September. Expectations rebounded strongly, gaining 6 points to 84.5, the best performance since January. Purchase intentions for autos, homes and appliances fell.
- **The Institute for Supply Management (ISM) Manufacturing Index** rose 1.9 points to 53.2 in June (any reading above 50 indicates expansion). This marks the highest reading since February 2015. Details showed that the forward-looking new orders index reached a three-month high as the employment index rose above the 50 mark for the first time since last November. Production and new exports orders also rose during the month.
- **Initial claims for unemployment insurance** increased 10,000 to 268,000 in the week ending June 25, according to the Department of Labor. The four-week moving average remained at 266,800.

Consumer Spending Poised to Accelerate in Q2 2016



Source: Bureau of Economic Analysis

Consumer Confidence Jumps to a Nine-Month High



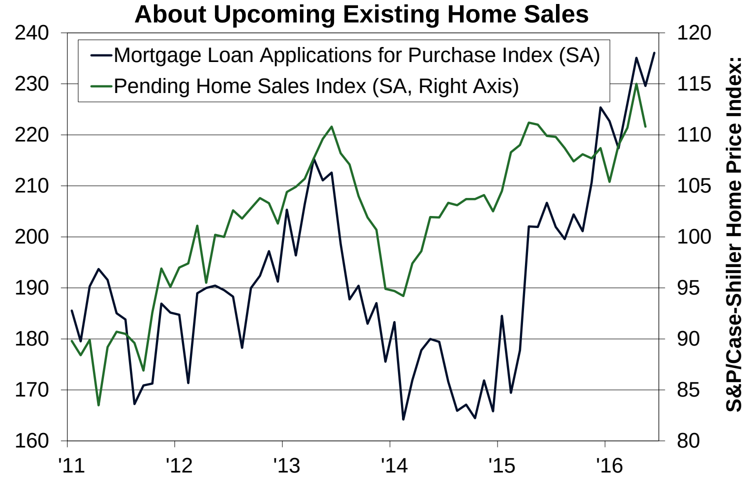
Source: Conference Board

Housing: Taking a Breather after a Strong Spring

Data released this week suggested the housing market took a breather after a robust spring. Private residential construction spending was unchanged in May, as a drop in expenditures on new single-family homes offset rises in multifamily and home improvement spending. New single-family construction spending has slowed markedly in recent months, posting three consecutive monthly drops and decelerating steadily on an annual basis since reaching its recent peak last August. Leading indicators for existing home sales are sending mixed signals. Pending home sales pulled back in May from a decade high reached in April, as all four regions fell during the same month for the first time since January. In addition, pending sales fell year-over-year for the first time in almost two years. Housing demand was perhaps pulled forward this spring, as brisk demand early in the season sizably reduced inventory. On the other hand, average purchase mortgage applications for June rose to the highest monthly reading since April 2010, boosted by the surge during the first week of the month. Purchase applications dropped in the last three weeks of June, however. Annual appreciation in the Case-Shiller National Home Price Index decelerated slightly for the third straight month in April, but has remained solid. The surprise British vote to leave the European Union led to declining mortgage rates during the last week of June as investors flocked to safety, pushing down the benchmark 10-year yield. The average 30-year fixed mortgage rate from Freddie Mac's survey fell eight basis points, the largest drop since early April, to 3.48 percent, the lowest level since May 2013.

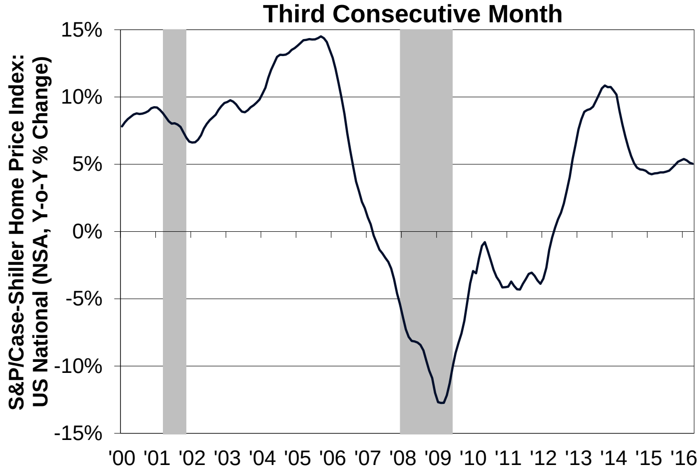
- **Private residential construction spending** was flat in in May, according to the Census Bureau. New single-family construction expenditures fell 1.3 percent, while multifamily spending rose 1.8 percent. From a year ago, new single-family and multifamily construction expenditures are 6.3 percent and 23.9 percent higher, respectively. Spending on home improvements rose for the fourth time in five months, increasing 1.4 percent. On an annual basis, improvement spending dropped 1.9 percent, marking the second consecutive decline.
- **The S&P/Case-Schiller National Home Price Index** (not seasonally adjusted) rose 1.0 percent in April. Annual home price appreciation slowed slightly to 5.0 percent, compared to 5.1 percent in March, but remained well above the 4.3 percent pace recorded a year ago.
- **The National Association of REALTORS® pending home sales index**, which records contract signings of existing homes and typically leads closings by one to two months, decreased 3.7 percent in May. The decline was nationwide, as all four regions saw a cutback in contract activity last month.
- **Mortgage applications** fell for the third time in five weeks, dropping 2.6 percent for the week ending June 24, according to the Mortgage Bankers Association. Purchase applications fell for the third consecutive week, decreasing 3.6 percent. Refinance applications dropped as well, falling 2.4 percent. Conventional and government applications saw declines in both the purchase and the refinance space. The average 30-year mortgage rate declined for the fourth consecutive week, edging down one basis point to 3.75 percent.

Leading Indicators Send Mixed Messages About Upcoming Existing Home Sales



Source: National Association of REALTORS®, Mortgage Bankers Association

Home Price Growth Slows Slightly For the Third Consecutive Month



Source: S&P/Case-Shiller

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