Fannie Thinks Economic Expansion Just Peaked

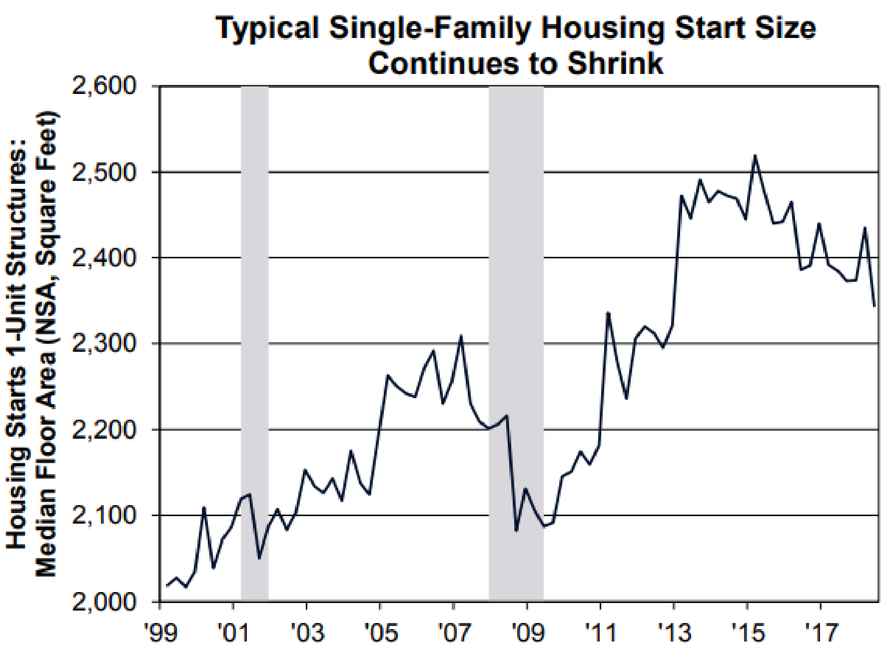
By: Jann Swanson | Mon, Sep 17 2018, 3:11 PM

The robust growth in the economy in the second quarter **may be the final peak** of this expansion according to Fannie Mae's Economic Development Report for September. Initial data indicates the 4.2 percent growth last quarter appears to be moderating to the estimated third quarter gain of 3.2 percent predicted in the August report. All factors considered, including inventory restocking and increased government spending leads Fannie's Economic and Strategic Research Group (ESR) to expect full-year 2018 growth of 3.0 percent before a slowdown to 2.3 percent in 2019 as the fiscal stimulus runs its course.

ESR expects consumer spending and business fixed investment growth to moderate but remain at a solid pace but expect that trade will drag on growth. Second quarter growth had benefitted in part by the frontloading of exports ahead of the July tariffs. The first month of the new quarter, showed a marked drop in agricultural exports which is expected to have continued, especially for soybeans, into August.

The group also expects that **residential investment** will subtract from growth for the third consecutive quarter, the first time during the expansion that a slump has been that protracted. The ESR refers to housing as "a wet blanket", saying the entire housing sector has been soft. Single family housing starts were up only slightly in July after the largest decline so far this year, 9.0 percent, in June. That same pattern played out with multifamily starts as well.

One **positive development** is an apparent response from home builders to strong first-time buyer demand by constructing smaller homes. The typical new single-family home size has been **falling since peaking in 2015**. The median square footage dropped sharply in the second quarter to the smallest reading since the end of 2012.



July also saw the slowest pace in new home sales since last October after the third decline in four months. **Demand remains strong**; over two-thirds of sales were of homes that were either under construction or not yet started, the highest share since the end of 2015.

According to the National Association of Home Builders Housing Market Index however, builders aren't feeling it. They indicate that demand is softening in their reports regarding sales expectation and buyer traffic. They are also **challenged** by pricing homes to cover material and labor cost increases. Fortunately, some material prices, such as for lumber, have started to ease. This could allow builders to offer more favorable pricing which might lead to an improvement in building and sales activity going into the fall.

The trend for existing home sales has been even worse than new home sales. They were down in July for the fourth month, making their worse showing since February 2016. Inventories have been up on an annual basis for the first time in three years but **remain at historic**

© Mortgage News Daily, LLC. - http://www.mortgagenewsdaily.com

lows. Pending sales, one leading indicator of existing home sales, fell for the third time in four months in July and another, purchase mortgage applications, dropped in August for the second straight month.

Home prices continue to outpace income growth and, along with a near **60 basis point increase in interest rates** since the first of the year, are weighing on affordability and home buying sentiment. Fannie Mae's Home Purchase Sentiment Index® has trended lower from its record high in May, with the net share of consumers saying now is a good time to buy a home sliding further in August to the second lowest reading in the survey's eight-year history.

Fannie Mae has now lowered its forecast for housing starts this year to **just under 900,000** but has kept its home sale forecast essentially unchanged at 6.12 million, reflecting a 6 percent increase in new home sales and a nearly 1 percent drop in existing home sales. Their outlook for purchase and refinance mortgage originations is little changed from August, with total single-family mortgage originations projected to fall about 9 percent to $1.67 trillion in 2018 and a refinance share of 28 percent.

The pop in annual wage gains in the August jobs report came on the heels of recent increases in broader measures of inflation. The Fed's preferred measure, the headline personal consumption expenditures (PCE) deflator, rose 0.1 percent in July, pushing it up to 2.3 percent on a year-ago basis. Since March, the annual increase in the PCE deflator has equaled or exceeded the Fed's 2-percent target and the annual rise in the core PCE deflator (excluding food and energy) accelerated one-tenth to 2.0 percent in July. These recent trends seem to support Fed Chair Jerome Powell's contention that raising interest rates too slowly could lead to **overheating**. Fannie Mae continues to expect September and December rate hikes consistent with what is implied in the "dot plot," showing fed funds rate projections by members of the Federal Open Market Committee (FOMC). This plot also implies three hikes next year, but Fannie Mae believes such a pace would be too aggressive given its forecast for slowing growth. The fed funds futures market has also turned more bearish and now implies the last rate hike for the cycle will occur in 2019.

View this Article: https://www.mortgagenewsdaily.com/news/09172018-fannie-mae-forecast

© Mortgage News Daily, LLC. - http://www.mortgagenewsdaily.com