HaMMR Digest

Stay current with economic and mortgage market trends.

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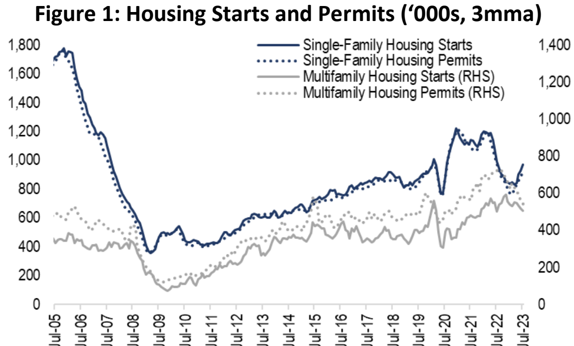
Weekly Wrap — Mind the Rip Tide

- Retail sales kick off the third quarter with a bang.
- Single-family construction activity maintained its uptrend while broader industrial production holds firm.
- This week's Jackson Hole Economic Symposium will be key to watch for any change in tone on monetary policy.

Economic momentum is firmly on the front foot. The Federal Reserve Bank of Atlanta's GDPNow estimate of 3Q23 real GDP growth stands at 5.8% at the time of writing, which most certainly overstates the case. Contributions are coming from all sectors with the majority of support coming from consumption and likely on the back of the bumper headline retail sales for July which rose 0.7% m/m (cons. 0.4%). On a three-month rolling average basis, real retail sales were up 2.1%, a clear upswing from the prior string of negative prints. Details were robust with strength in online sales, apparel and restaurants. However, several factors bolstered sales, including the Fourth of July holiday, Amazon Prime Day and back-to-school shopping, implying some giveback in August is expected instead of a new breakout to stronger growth.

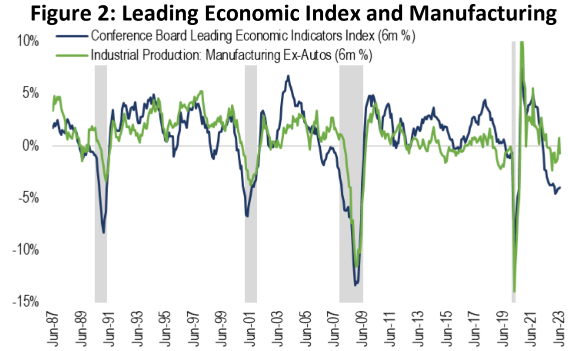
Total housing starts rose 3.9% m/m (cons. 1.1%) to a seasonally adjusted annualized rate (saar) of 1,452k, driven by a 6.7% uptick in single-family starts (Figure 1). Single-family permits were positive as well, rising 0.6% m/m and for the sixth consecutive month, setting the stage for residential investment to contribute to GDP in 3Q for the first time since 1Q22. However, the steady multi-month uptrend in mortgage rates has dented near-term housing prospects for buyers, sellers and builders. The August National Association of Home Builders (NAHB) Housing Market index backtracked to 50 (cons. 56), the first drop in eight months. Notably, the share of builders using incentives to bolster sales increased for the first time since March. Strong household formation, tight resale inventory, a steady labor market and an overall undersupplied market will likely keep the wind behind single-family construction's sails for some time.

Figure 1: Housing Starts and Permits ('000s, 3mma)



Souces: Census Bureau, Arch MI

Figure 2: Leading Economic Index and Manufacturing



Sources: Conference Board, Federal Reserve Board, Arch MI

Excluding construction, industrial output has been flat to marginally higher recently. July industrial production grew a sturdy 1.0% m/m (cons. 0.3%) with manufacturing up a healthy 0.5% m/m (cons. 0.0%), led by a 5.2% outturn in autos. The share of manufacturing industries expanding output month-over-month rose to 42% (three-month average) from 37% in May but remained below the long-term average of 55%. Industrial output is highly cyclical and tends to lag the Leading Economic Index (LEI), which declined for the sixteenth straight month in July, albeit at a slower pace than recent months. However, industrial output is holding up better than what the LEI would imply (Figure 2). The divergence is partly due to an over-reliance on "soft data" inputs to the LEI and the fact that a rebound in inventories and the undersupply in autos can keep production muddling along until other demand drivers improve on a sustained basis.

Taking all the information together for 3Q23, the economy has solid momentum. Treasury yields have been climbing since the end of April alongside compression in high yield corporate credit spreads, a key sign of upgraded economic expectations and reduced credit risk. Additionally, evidence keeps mounting that inflation is slowly receding on a sustained basis. It seems all the stars have aligned for a "soft landing" with the Fed at a critical juncture. Balancing the risk between over/under-tightening will be the "x-factor" determining the next phase of the business cycle. We are likely to gain some insight into the Fed's latest thinking on how long rates will remain elevated following this week's Jackson Hole symposium.

Recent Data Releases

Key economic and housing data releases over the last week:

Date	Indicator	Period	Actual	Consensus	Previous	Note
8/15/23	Advance Retail Sales m/m	Jul	0.7%	0.4%	0.3%	sa
8/15/23	Retail Sales Control Group m/m	Jul	1.0%	0.5%	0.5%	sa
8/15/23	Import Price Index y/y	Jul	-4.4%	-4.6%	-6.1%	nsa
8/15/23	Empire Manufacturing	Aug	-19.0	-1.0	1.1	index, sa
8/15/23	Business Inventories m/m	Jun	0.0%	0.1%	0.0%	sa
8/15/23	NAHB Housing Market Index	Aug	50	56	56	index, sa
8/16/23	MBA Mortgage Applications	8/11/23	-0.8%	--	-3.1%	w/w, sa
8/16/23	Building Permits	Jul	1,442	1,463	1,441	k, saar
8/16/23	Housing Starts m/m	Jul	3.9%	1.1%	-11.7%	sa
8/16/23	Housing Starts	Jul	1,452	1,450	1,398	k, saar
8/16/23	Building Permits m/m	Jul	0.1%	1.5%	-3.7%	sa
8/16/23	Industrial Production m/m	Jul	1.0%	0.3%	-0.8%	sa
8/16/23	Capacity Utilization	Jul	79.3%	79.1%	78.6%	sa
8/16/23	FOMC Meeting Minutes	7/26/23	--	--	--	
8/17/23	Initial Jobless Claims	8/12/23	239	240	250	k, sa
8/17/23	Continuing Claims	8/5/23	1,716	1,700	1,684	k, sa
8/17/23	Philadelphia Fed Business Outlook	Aug	12.0	-10.4	-13.5	index, sa
8/17/23	Conference Board Leading Index	Jul	-0.4%	-0.4%	-0.7%	m/m, sa

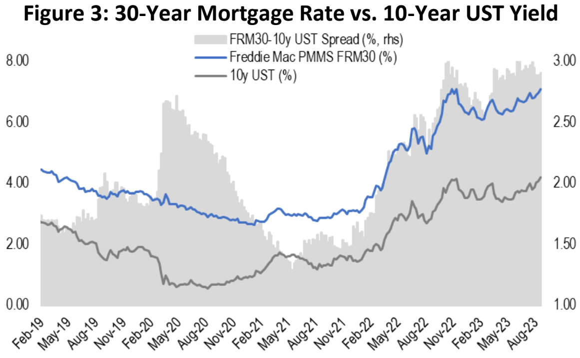
Sources: Bloomberg Consensus Survey of Economists, Arch MI

Green = beat expectations; **Red** = worse than expectations; (compared vs. prior if no consensus estimates available)

MORTGAGE PURCHASE APPLICATION ACTIVITY INCHED LOWER

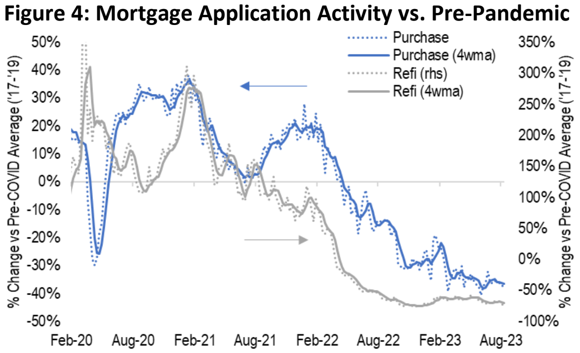
According to the MBA Weekly Applications Survey, the average contract conventional mortgage rate rose 7bps to 7.16% during the week ending Aug. 11 while the FHA contract mortgage rate declined -9bps to 6.93%, resulting in a -16bps contraction in the spread between the FHA and conventional mortgage rate to -0.23%. Freddie Mac's more recent Primary Mortgage Market Survey (PMMS) for the week ending Aug. 16 indicated that the 30-year fixed-rate mortgage (FRM30) jumped 13bps w/w to 7.09% (Figure 3) as the yield on the benchmark 10-year U.S. Treasury (UST) also jumped 11bps to an average of 4.19% over the same period. Accordingly, the spread between the PMMS FRM30 and the 10-year UST widened 2bps to 2.9%, about 120bps wider than its typical non-stressed level prior to the pandemic and still close to the recent peak just above 300bps. We expect rate volatility and mortgage spreads to remain wide until more clarity is gained around the path of inflation and monetary policy, which is not likely to occur until later this year.

Figure 3: 30-Year Mortgage Rate vs. 10-Year UST Yield



Sources: Freddie Mac Primary Mortgage Market Survey, Federal Reserve Board, Arch MI

Figure 4: Mortgage Application Activity vs. Pre-Pandemic



Sources: Mortgage Bankers Association, Arch MI

The MBA Weekly Applications Survey for the week ending Aug. 11 declined -0.8% w/w, leaving the index down -29% year-over-year and down -58% compared with pre-pandemic levels (i.e., the average of the same week in 2017, 2018 and 2019). The weekly decline was driven primarily by a -1.9% decline in refinancing applications, which remained down -35% y/y and -76% below the pre-pandemic level (Figure 4). Purchase applications declined -0.3% w/w and were down -27% y/y and -37% relative to pre-pandemic levels. Given the recent surge higher in rates, we expect application activity to remain cool in the weeks ahead.

NEW HOME CONTRUCTION KEEPS RISING BUT BUILDERS SIGNAL CAUTION

Total housing starts for July rose 3.9% m/m (cons. 1.1%) to a seasonally adjusted annualized rate of 1,452k (cons. 1,450k), maintaining the uptrend that began early this year. After taking a -9.0% m/m dip in June, single-family starts rebounded by 6.7% m/m and are up 22% from November's cycle trough. Multifamily starts declined for the second straight month, ticking down -1.7% to 469k saar, the slowest pace since September 2021. We hold a more positive outlook for single-family construction. given low resale inventory and positive demographics. We expect multifamily construction activity to continue to slow, given the elevated pipeline of multifamily units that are slated for delivery over the coming years. However, that positive outlook does not mean smooth sailing for new home sales. Builder confidence pulled back for the first time in eight months, falling 6pts m/m to 50 (cons. 56) in August (Figure 5). All three index sub-components fell on the month largely due to the impact of higher rates on buyer affordability and financing costs for new development. Indeed, the NAHB reported the first increase since March for the share of builders using price cuts to bolster sales in August, highlighting the fact that affordability still matters.

Figure 5: NAHB Housing Index and Housing Starts

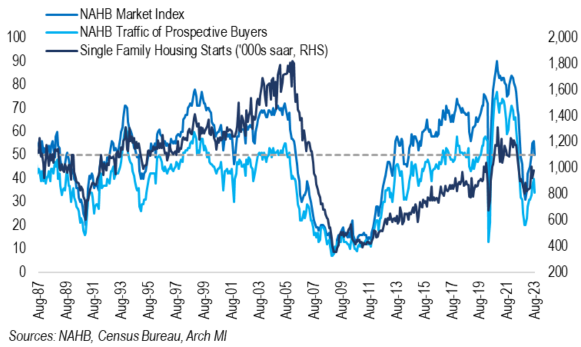
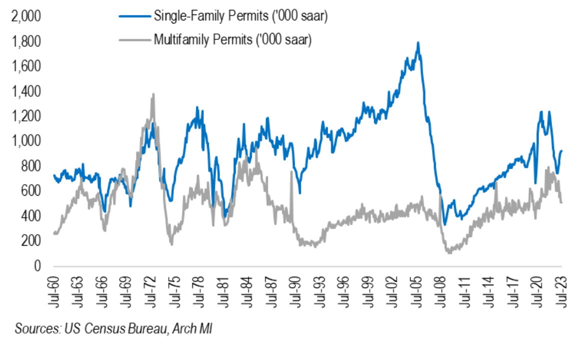


Figure 6: Housing Permits by Type



Single-family permits rose for the sixth month in a row, increasing 0.6% m/m but remained down -25% from last January's peak (Figure 6). Multifamily permits fell -1.0% m/m, maintaining the downtrend in place since last June. Total completions declined -11.8% m/m with the year-over-year measure down -5.4% amid pronounced weakness in the multifamily segment — down -39% m/m, compared to single-family completions up 1%. Single-family completions rose 1.4% y/y and after a year's long stretch, the gap between starts and completions has essentially closed (Figure 7). Improving supply chains and easing labor market conditions have allowed builders to start chipping away at the elevated count of 1,681k units under construction (Figure 8). Single-family units under construction have been declining since May and were down -17% y/y in stark contrast to the 16% y/y increase in the multifamily segment.

Figure 7: Housing Completions

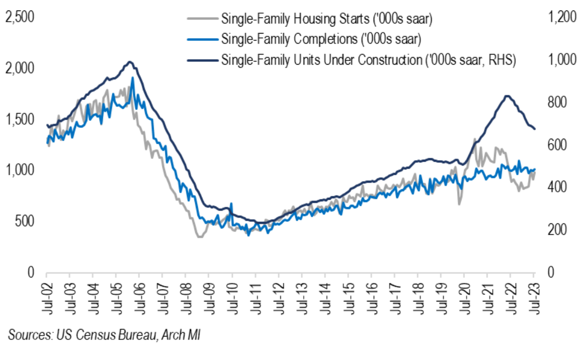
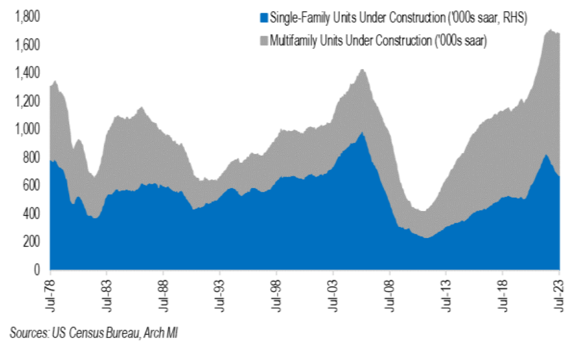


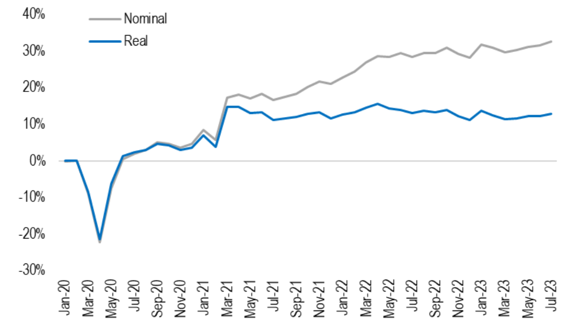
Figure 8: Housing Units Under Construction



RETAIL SALES START 3Q WITH A BANG

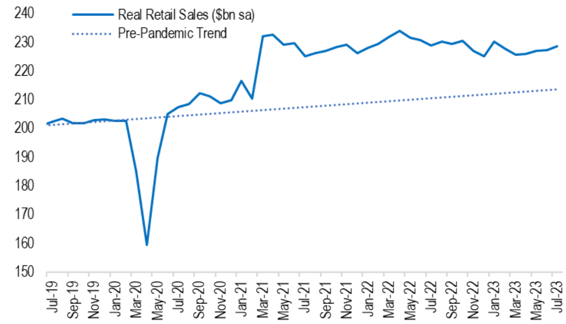
July nominal retail and food services surged to 0.7% m/m (cons. 0.4%) following a 0.3% gain in June. Auto sales declined -0.4% m/m from 0.6% last month but on a real basis, sales were up given the multi-month drag seen in new and used vehicle pricing. Gasoline sales rose for the first time in eight months with grocery sales rising a strong 0.8% m/m. Online sales (1.9%), apparel (1.0%), and general merchandise (0.8%) were strong as well. Several factors in July, namely the Fourth of July holiday, Amazon Prime Day back-to-school shopping and the general increase in food and energy prices bolstered topline sales. Retail sales, excluding autos, rose 1.0% m/m while the important control group (excluding food, autos, gasoline and building materials), which feeds directly into the GDP report, also rose by 1.0% (cons. 0.5%).

Figure 9: Retail & Food Service Sales (Change from Feb '20)



Sources: Census Bureau, Arch MI

Figure 10: Real Retail & Food Services Sales



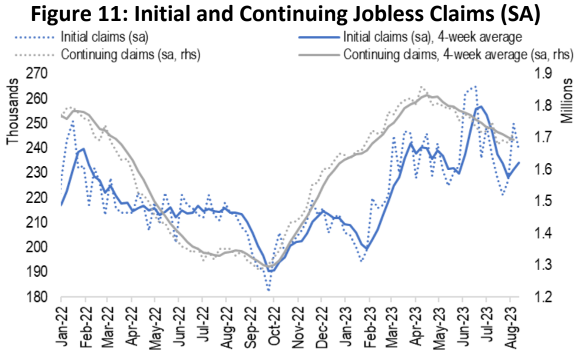
Sources: Census Bureau, Arch MI

Adjusted for inflation, retail sales increased 0.6% m/m (Figure 9), lifting the year-to-date gain to 1.7%. Real control group sales have performed slightly better over the same time frame and suggest that while consumers have pulled back a bit on their spending, they have yet to completely shut their wallets. In fact, real retail sales remained 13% above February 2020 levels and 8% above the pre-COVID-19 trend, suggesting consumption is gradually normalizing from an elevated level (Figure 10).

JOBLESS CLAIMS REVERSE SOME OF PRIOR WEEK'S SPIKE

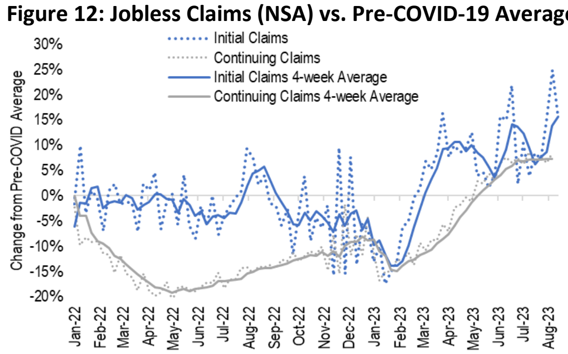
Initial jobless claims declined by -11k to a seasonally adjusted (sa) 239k (cons. 240k) during the week ending Aug. 12, but the four-week average moved up to 234k from 232k (Figure 11). The four-week average of non-seasonally (nsa) adjusted initial claims also moved up to 15.7% above its pre-COVID-19 average (i.e., 2018 to 2019) from 13.8% the week before and up from -10% below at the beginning of 2023 (Figure 12). Continuing claims (i.e., repeat filers for unemployment insurance) climbed by 32k during the week ending Aug. 5 to a seasonally adjusted 1,716k (cons. 1,700k), but the four-week average moved down to 1,693k from 1,701k. Meanwhile, the four-week average of non-seasonally adjusted continuing claims also moved down to 7.2% above its pre-COVID-19 average from 7.3% the week before but remains up notably from -10% below at the beginning of the year.

Figure 11: Initial and Continuing Jobless Claims (SA)



Source: U.S. Department of Labor, Arch MI

Figure 12: Jobless Claims (NSA) vs. Pre-COVID-19 Average



Source: U.S. Department of Labor, Arch MI

The Week Ahead

This week will continue the updates on the housing market, along with some survey data. July existing home sales will kick off the week, but likely with a dud of a report given the expected decline of -0.2% m/m (sa) according to the Bloomberg Consensus Survey of Economists. Resurgent mortgage rates through July presented a strong headwind for existing home sales an inventory and the continuation of the surge in rates into August has continued to weigh on activity. On the other hand, incentives offered by homebuilders have blunted some of the impact of higher rates, which is partly why new home sales are expected to inch up by 1.4% m/m (sa) in July after a -2.5% decline in June. On the survey front, S&P Global's preliminary August Purchasing Manager Indexes (PMI) are generally expected to show little change compared to July, with manufacturing still modestly below the growth breakeven level of 50 and services still maintaining a healthy clip.

While not a data release, this week's biggest update could well come on Friday following the Jackson Hole Economic Symposium, which is effectively an offsite for dozens of central bankers, policymakers, academics and economists from around the world, where participants discuss economic issues, implications and policy options. The topics for this year's symposium revolve around "Structural Shifts in the Global Economy" and participants are thus slated to dig into "several significant, and potentially long-lasting, developments affecting the global economy." Chairman Powell will speak on Friday following the meetings and is expected to take a different tone from his "there will be pain" speech after last year's symposium. Instead, Powell is widely expected to discuss the possibility of a higher neutral rate of interest (or r* — read as r-star) or the rate that is considered to be neither restrictive nor stimulative to the economy, in part due to the surprising resiliency of the economy in the face of the most rapid rate hiking cycle in decades. We do not expect any meaningful insights from Powell on near-term monetary policy and expect the discussion to remain focused on the longer-term structural developments underway.

UPCOMING DATA RELEASES

Key economic and housing data releases for the coming week:

Date	Indicator	Period	Actual	Consensus	Previous	Note
8/22/23	Existing Home Sales	Jul	--	4,150	4,160	k, saar
8/22/23	Existing Home Sales m/m	Jul	--	-0.2%	-3.3%	sa
8/23/23	MBA Mortgage Applications	8/18/23	--	--	-0.8%	w/w, sa
8/23/23	S&P Global US Manufacturing PMI	Aug P	--	49.0	49.0	index, sa
8/23/23	S&P Global US Services PMI	Aug P	--	52.0	52.3	index, sa
8/23/23	S&P Global US Composite PMI	Aug P	--	--	52.0	index, sa
8/23/23	New Home Sales	Jul	--	707	697	k, saar
8/23/23	New Home Sales m/m	Jul	--	1.4%	-2.5%	sa
8/24/23	Initial Jobless Claims	8/19/23	--	240	239	k, sa
8/24/23	Continuing Claims	8/12/23	--	1,690	1,716	k, sa
8/24/23	Chicago Fed Nat Activity Index	Jul	--	--	-0.32	index, nsa
8/24/23	Durable Goods Orders	Jul P	--	-4.0%	4.6%	m/m, sa
8/25/23	U. of Mich. Sentiment	Aug F	--	71.2	71.2	index, nsa
8/25/23	U. of Mich. 1 Yr Inflation	Aug F	--	--	3.3%	nsa
8/25/23	U. of Mich. 5-10 Yr Inflation	Aug F	--	--	2.9%	nsa

Sources: Bloomberg Consensus Survey of Economists, Arch MI